

## External economic relations

- ***The external balance of the economy is virtually unchanged year on year***

Already for the fourth year in a row, it is typical for the external balance of the Czech economy in the first quarters to have a surplus on the current account of the payment balance and a deficit on the financial account. The deficit result on the financial account was well covered by the surplus on the current account. The trends of the individual components of the current account remained basically the same -- its surplus was strengthened by foreign trade with goods and services and the return of the balance of current transfers into the positive territory. Conversely, it was weakened by the income balance.

The surplus of the current account (27 billion CZK) reached, on a quarterly basis, 3% of GDP in current prices and in comparison to the 1<sup>st</sup> quarter of 2007 was slightly higher (22.6 billion CZK, i.e., 2.7% of GDP). Foreign trade with goods and services contributed positively to it by 65.4 billion, mainly due to services - the balance of trade itself (41.7 billion CZK) was slightly weaker against a comparable period (45.7 billion CZK), but on the other hand the surplus of the balance of services (23.7 billion CZK) was double (12.1 billion CZK) year on year. The balance of income continued in its fall into the historically deepest deficit (-43.7 billion CZK). It was caused both by the growth of costs, as well as a non-traditional decline of income, which decreased by 4.7 billion CZK in a year on year comparison. The balance of current transfers was highly positive (+5.4 billion CZK), with the highest surplus since 2005.

- ***The deficit of the financial account was increased by the more moderate inflow of direct investments from abroad***

The financial account was in a deficit, as in every 1<sup>st</sup> quarter since 2005 - the deficit (7.4 billion CZK) was slightly deeper in comparison to the same period of 2007 due to the influence of a smaller net inflow of foreign direct investments (28.8 billion CZK against 37.2 billion CZK in the 1<sup>st</sup> quarter of 2007). On the other hand, direct investments of Czech companies abroad (7.9 billion CZK) were approximately double in comparison to the same period of 2007, as Czech companies provided capital to their foreign acquisitions. The item Other investments worked in the direction of the reduction of the financial account deficit, with a year on year more favorable balance (-15.2 billion compared to -24.1 billion CZK).

- ***Portfolio investments were especially in the name of sales***

The uncertainty on the capital markets manifested itself in the retreat from positions - in net terms, investors were selling - residents their foreign securities, non-residents their investments in the ČR (this occurred in a massive extent in March). This trend was evident mainly on stock markets - non-residents (net) sold Czech asset securities and participations for 10.9 billion CZK and bonds for 3.4 billion CZK. The result of net transactions by residents was the return of capital into the country, in combination of the purchasing of foreign stocks (9.4 billion CZK) and selling of foreign bonds (10.8 billion CZK). On aggregate, however, the balance of portfolio investments (-13 billion CZK) indicates a lower outflow of capital from the country in comparison with the 1<sup>st</sup> quarter of 2007 (-19.6 billion CZK).

- ***Foreign trade with goods slowed down its pace***

The dynamics of foreign trade with goods, after eight quarters of double digit year on year growths, decreased to one digit values. For January to March, exports grew by 5.7% and imports (in cif prices) by 7.2%.

Exports are showing an extraordinary linkage to EU 27 - during the first three months of 2008, 86% of Czech exports went there (for imports, the similar ratio was 68%). The highest year on year dynamics were exports to Russia (+27.5%). But in terms of value, exports to Germany were 13 times higher (+2%), which is the largest trading partner of the ČR. Czech exports to EU 27 grew somewhat slower than the dynamics of the total exports from the ČR - by 4.7% in comparison to the first three months of 2007. The year on year gain in imports (in cif prices) was higher in the 1<sup>st</sup> quarter in comparison with exports. Fastest, by a quarter, grew imports from Russia, the value of which was influenced by the price of oil (only partially compensated by the rapid strengthening of CZK to USD). Imports from China grew by one fifth.

- ***The price competitiveness of the Czech economy declined***

The change of the index of the real effective exchange rate of the Crown (REER) show a significant decline of the cost competitiveness of the Czech economy, in both the year on year, as well as - even stronger - quarter on quarter. But this is natural, with regard for the transfer of the country from a low-cost economy into the group of mid-income countries according to GDP per inhabitant in purchasing power parity.