

## Czech consumers shine amid a soft economic recovery

The Czech economic rebound continues, with the annual growth dynamic confirmed at 1.3%. The expansion remains relatively tepid, while solid consumer spending is set to foster inflation. The main question on our minds right now is whether the growth or inflation outlook will prove the bigger concern for policymakers

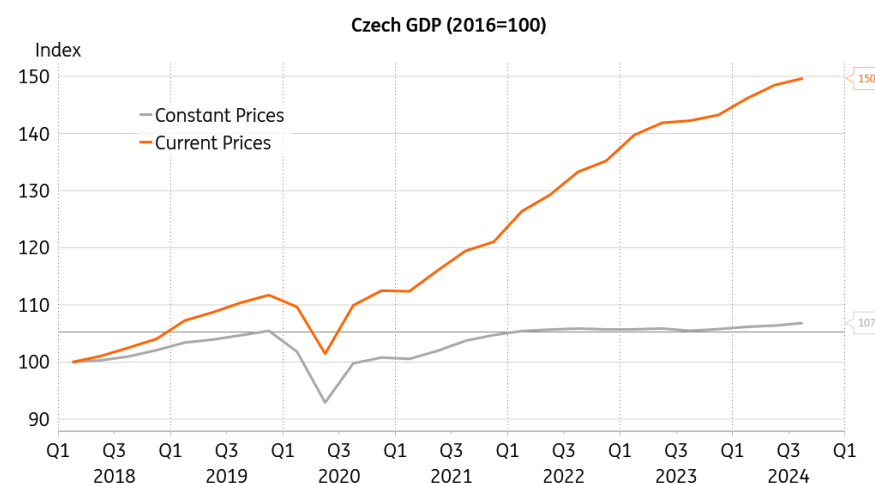


Rising household consumption was a key driver of the pick-up in quarterly GDP

Czech real GDP rose by 0.4% quarter-on-quarter in the third quarter, revised by 0.1ppt upward in the latest estimate at the cost of a downward revision in the previous quarter. Meanwhile, the annual dynamics remained unchanged at 1.3%, with household expenditure remaining the main contributor to the rebound.

Household consumption added 0.7% QoQ and picked up by 2.2% year-on-year. Government final consumption expenditure shed 0.1% QoQ but increased 3.0% YoY. Gross fixed capital formation has disappointed, falling 1.2% QoQ and declining by 0.8% YoY. Rising household consumption and the change in inventories were the main drivers of the quarterly GDP pickup in the third quarter, while gross fixed capital formation and external demand were a drag.

## Economic performance is not convincing

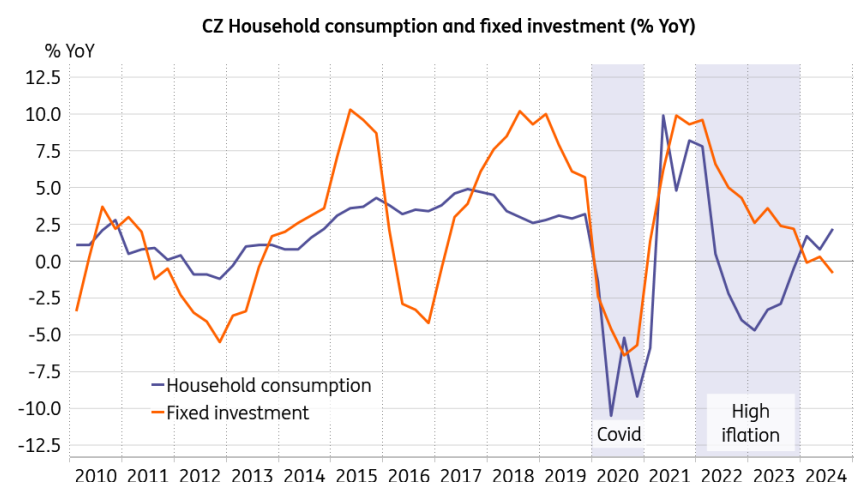


Source: CZSO, Macrobond

The Czech economy had hardly moved from its pre-pandemic levels until the beginning of this year, when its lukewarm recovery began. This is not a good outcome for an economy that used to expand by 2.5% on average between 2010 and 2019. Now, who is to blame?

It looks as though it could be the consumer, as household expenditure grew by a solid 2.2% on average in the decade after 2010 and shrunk by 0.7% annually after 2020. Sure, the pandemic years dragged consumption into the abyss – but the second hit was due to skyrocketing inflation, which has hit real purchasing power and real savings of Czech households.

## Consumption and investment flipping sides



Source: CZSO, Macrobond

In contrast, fixed investment did not perform as poorly post-pandemic, as its annual growth averaged above 2% in both periods. Meanwhile, households and firms have seen a shift in dynamics; consumption is driving the current rebound, but firms remain in doom and gloom.

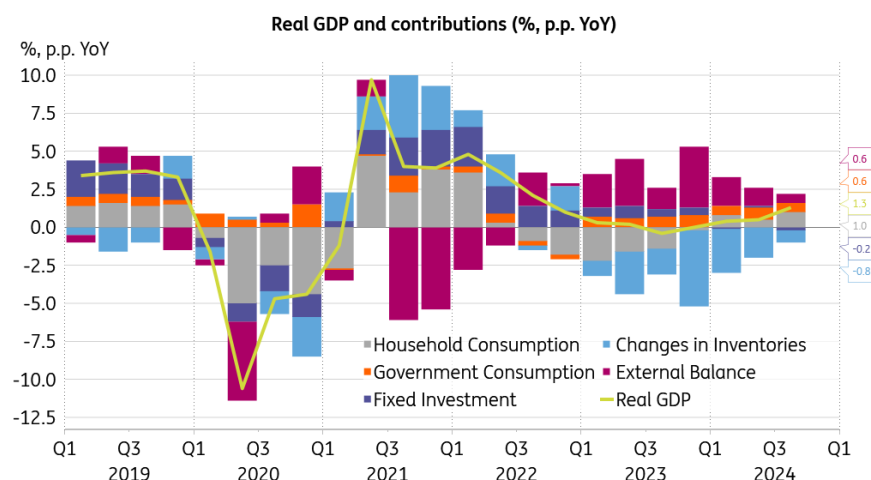
The question now is who will blink first in the medium term. Will firms enter opportunities for investment in Czechia and support the economic rebound, or will their focus be shifted elsewhere, eventually leaving Czech workers with fewer resources in the long term?

## Growth or inflation concerns – which takes the upper hand?

Overall, the dichotomy between strong consumers and the bleak industry continues in the third quarter, with continued robust consumer spending on the one hand and disappointing fixed investment on the other. The economic rebound should remain intact in the near term, but underinvestment represents a serious issue in the longer term. Still, the willingness to spend will likely turn into some price pressures in the consumer domain, as it will be met by a willingness to increase final price tags. This may be the case especially given the constrained supply side, particularly in the service sector.

Policymakers will consider this at their December meeting. Are growth concerns or potentially elevated inflation closer to their hearts? The first suggests further monetary policy easing at the December meeting, while the latter means a pause. The decision will be made under the current conditions of increased uncertainty surrounding potential tariffs that the incoming US administration could apply to European imports. Such a move would imply some negative impact on Czech growth, while the effects on prices are more ambiguous. That said, Czech consumers are rather sensitive to increasing price tags, so strong inflation could, in turn, undermine growth prospects anyway.

## Household spending rules them all



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