Czech wage increases soften while real purchasing power remains strong

The average real wage in the Czech Republic decelerated in the second quarter of the year, coming in below market expectations. This reflected a softening in nominal wage increases and higher consumer inflation compared to the previous reading. Still, real purchasing power will provide support to spenders

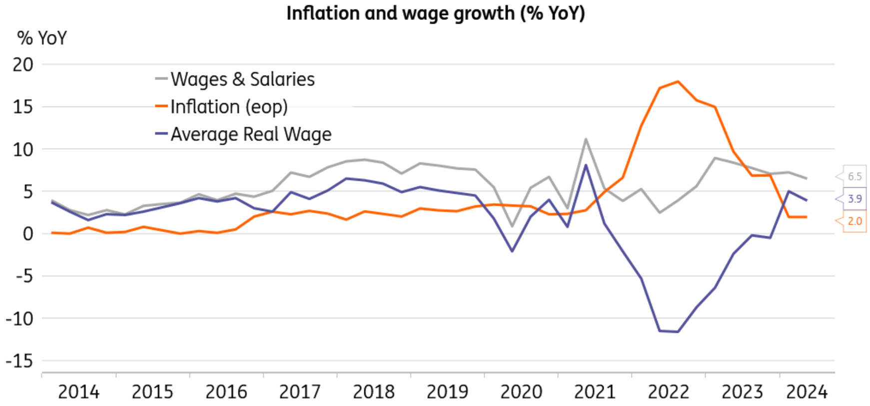
The Czech National Bank building in Pilsen

Real purchasing power continues to gain

Average nominal wages increased by 6.5% in the second quarter, representing a noticeable deceleration from the peak dynamic of almost 9% at the beginning of 2023. However, the return of consumer inflation back to the target from lofty heights is keeping real wage growth afloat.

After taking into account the impact of inflation, wages added 3.9% in real terms. However, employees in some sectors did not see real wages rise from the previous year. The median nominal wage increased 5.8% from a year earlier, showing that lower-income groups have fewer reasons to celebrate. Compared with the previous quarter, average nominal wages added 1.4% after seasonal adjustment.

Nominal and real wage growth decelerated



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Enough fuel to drive spenders

We see continued real wage growth as supportive of household spending, especially given the erosion of real purchasing power between late 2021 and 2023. However, annual real wage increases recorded during a fully-fledged economic upswing between 2016 and 2019 averaged 4.7%. Overall, the current 3.9% real wage growth will provide enough fuel for a continued recovery in household expenditure over the coming quarters. Considering the whole-year average, we expect wages to expand by 6% in nominal terms this year and by 3.9% when adjusted for inflation.

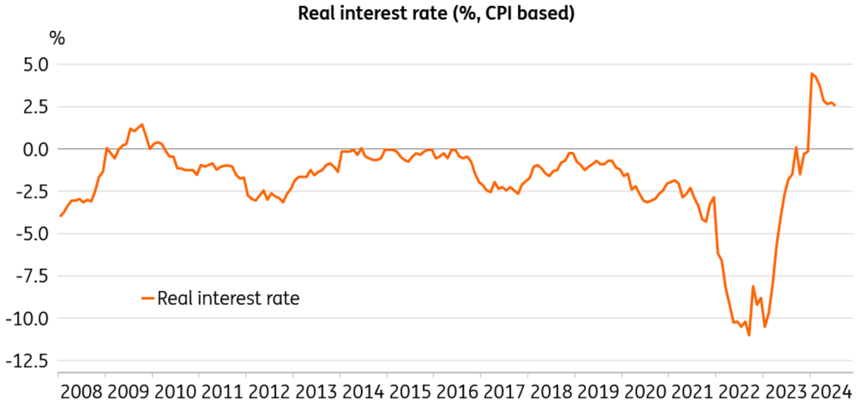
We would like to see a long-awaited turnaround in industrial performance so that firms remain keen to support solid wages. The tightness of the labour market and shortages of skilled workers support an outlook of continued robust wage dynamics. At the same time, consumer inflation is set to remain close to the target in the coming quarters. This seems good news for budgetary constraints when looking ahead. In contrast, the protracted weakness in demand from Czechia's main trading partners warrants some caution when it comes to overly optimistic scenarios. The PMI for August suggests further deterioration in manufacturing output, while the one-year-ahead confidence improved.

Wage growth below central bank forecast opens door to further easing

The Czech National Bank (CNB) expected nominal wages to increase by 7.2% and real wages to add 4.6% from a year earlier for the second quarter, while the observed wage dynamic of 6.5% and 3.9% respectively is well below the estimate. The lower-than-expected nominal wage increase implies less risk for a potential unfolding of a wage-price spiral, while the less buoyant real purchasing power gains suggest less support for consumer demand along with lower price pressures in the coming months.

Overall, the recent wage reading opens the door for further easing in monetary policy, which is restrictive compared to historical standards. We expect policymakers to proceed with two more rate cuts this year with a terminal rate of 4%. That said, the bank board has been rather hawkish and signalled that consumer inflation below the target is acceptable for some time. We also see some reluctance to compensate for structural weaknesses of the economy.

Monetary policy setup is restrictive



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