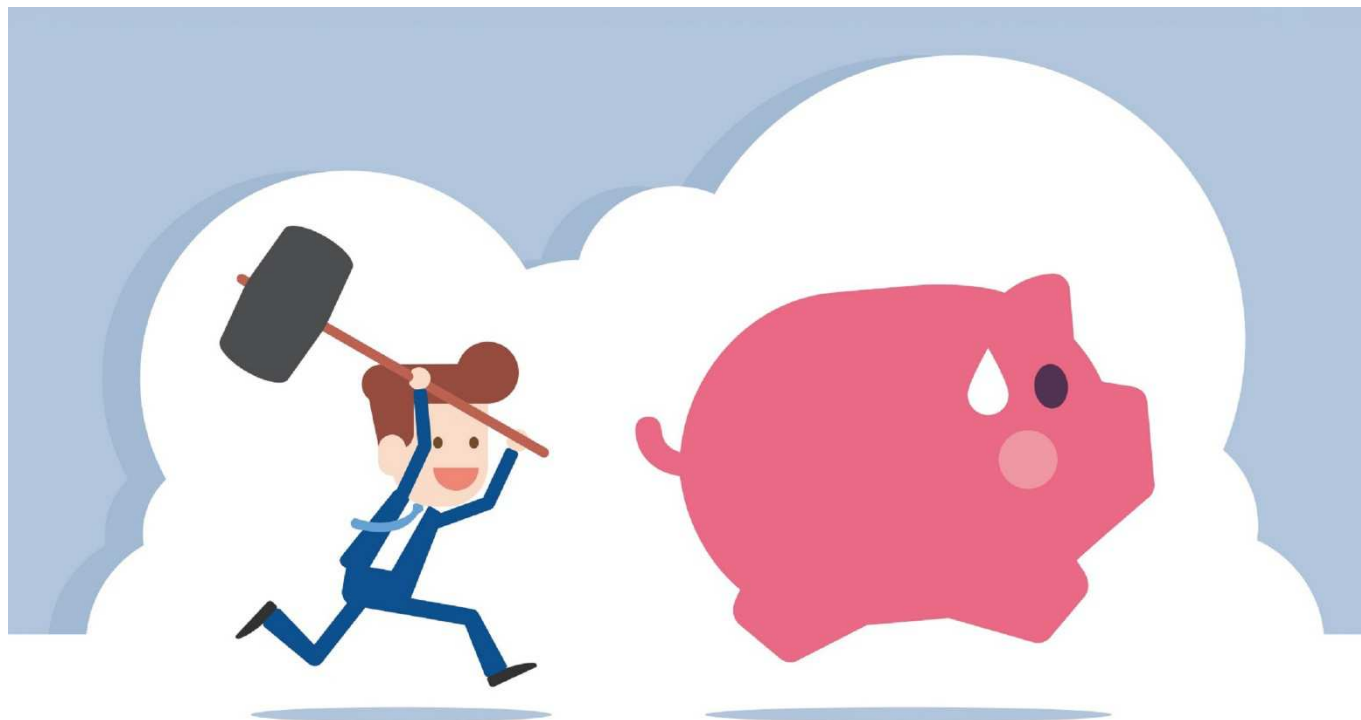


Quarterly report

Czech Economic Outlook

A new era of fiscal dominance



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■ **Following a temporary slowdown, we expect the economy to pick up again next year** In 2H25, we forecast a significant deterioration in Czech economic performance, as the impact of US tariffs shifts from positive to negative. However, we expect economic growth in 2026 will be supported by a strong fiscal stimulus from the likely new government. We forecast GDP growth of 2.1% this year, driven by what was a very solid 1H25, before slowing to 1.6% in 2026.

■ **Inflation to fall below 2% in 2026 before rising above the CNB's target again** We expect lower energy and fuel prices, including the effect of the planned transfer of payments for renewable energy sources from households to the state, to push inflation below the central bank's 2% target next year. However, subsequent price developments are likely to be affected by a recovery in domestic demand driven by expansionary fiscal policy. We estimate inflation of 2.4% in 2025 and 1.5% in 2026.

■ **The central bank is unlikely to lower rates further due to the expected fiscal expansion** We no longer expect further cuts in the CNB's repo rate, which is likely to remain at the current 3.5% for an extended period. The CNB board lists fiscal policy among the main inflationary risks, although we estimate that its recent impact on the economy was roughly neutral.

■ **Fiscal stimulus set to push market interest rates up** The economic slowdown should temporarily halt the upward trend in koruna's interest rates. Next year, fiscal policy easing at national and international levels will contribute to the resumption of this trend.

■ **The koruna set to take a breather** The koruna's current overvaluation, combined with the economy's near-stagnation in 2H25, should prevent further strengthening. However, we expect this to resume with the revival of economic activity over the course of next year.

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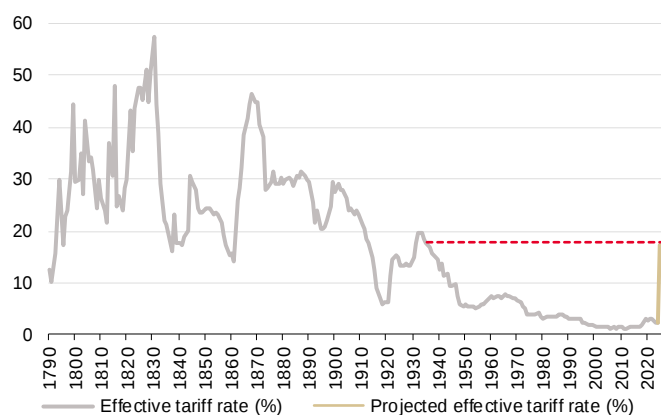


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Custom duties actually are being collected, and Czech industry is suffering

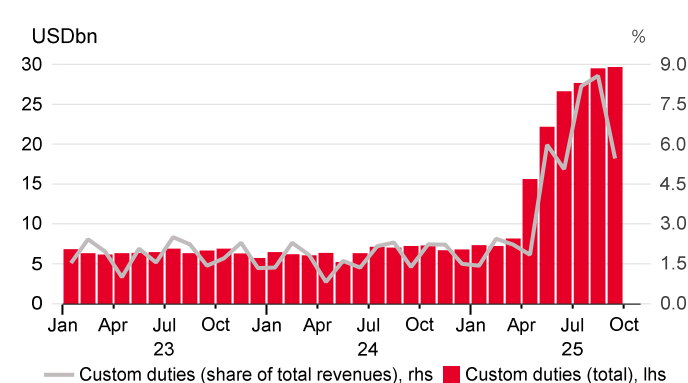
In the space of three months, the editorial of the summer edition of our *Czech Economic Outlook*, released under the heading *Tariffs actually will hit the economy*, has turned out to be almost prophetic. **While the market consensus and indeed the CNB expected the overall strong economic momentum to continue or even accelerate, we at KB warned of significant slackening ahead. Our warning has basically materialised.** And not only because of the introduction of custom duties on imports into the US, which became applicable for European countries on 7 August with a 15% tariff on most goods, but also because of the frontloading effects. Before the tariffs were introduced, US companies and households stockpiled imported goods before they became more expensive due to the tariffs, but the opposite occurred as soon as the tariffs came into effect.

The current average effective tariff rate for US imports is the highest since 1934



Source: The Budget Lab at Yale, Economic and Strategy Research, Komerční banka

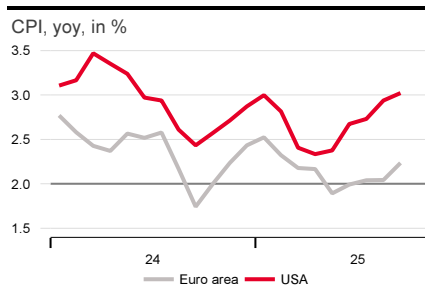
Tariffs are rapidly raising revenues for the US federal budget



Source: Macrobond, Economic and Strategy Research, Komerční banka

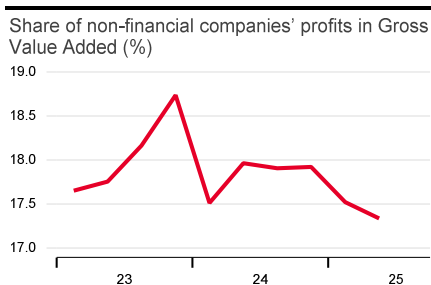
The increase in tariff revenues in the US is significant. At the beginning of the year, the monthly tariff revenue was a few billion dollars, but this figure rose to almost USD30bn in August and September. Naturally, somebody somewhere must have paid these tariffs. There are basically three channels: 1) American consumers in consumer pass-through; 2) American businesses in the form of lower profit margins resulting from higher costs; and 3) exporters coming under pressure from American customers to lower prices, i.e. also at the expense of their profit margins. The indicators released to date suggest that the impacts were evident in all three channels.

US inflation outpacing the euro area since the spring of 2025



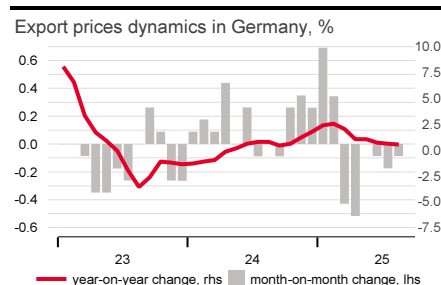
Source: Macrobond, Economic and Strategy Research, Komerční banka

US businesses' profit margins decreasing this year



Source: Macrobond, Economic and Strategy Research, Komerční banka

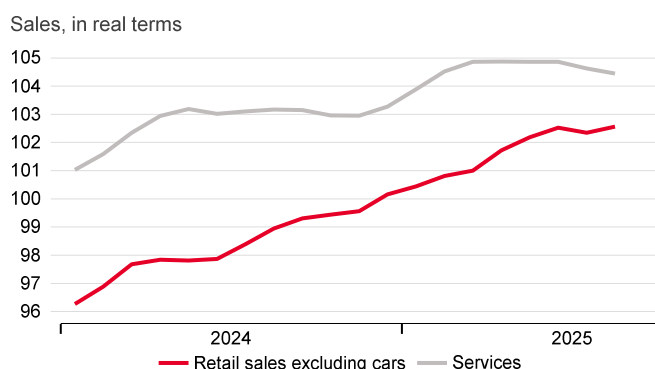
German export prices decreasing this year, but partly also because of the stronger euro



Source: Macrobond, Economic and Strategy Research, Komerční banka

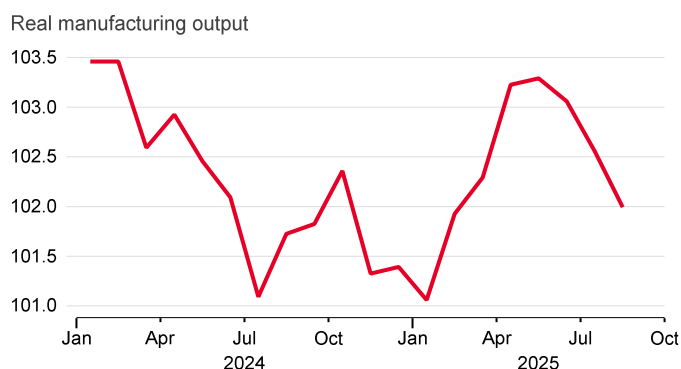
With its large industry sector, the export-oriented Czech economy was unable to avoid the impact of tariff implementation. Moreover, the first half of the year was favourably impacted by frontloading effects and robust domestic demand, with wage growth having surpassed expectations in the second quarter. However, economic activity cooled over the summer. So, while real GDP improved by 0.7% qoq and 0.5% qoq respectively in the first and second quarters, our estimates show that it ground to a halt in the third quarter. The strong wage growth in the second quarter appears to have been an isolated episode: slowing consumer demand dynamics caused retail sales and services revenues to weaken over the summer months. The situation in industry is even worse: in real terms manufacturing output had declined mom for four consecutive months since May.

Real revenues from service sales declined over summer; they remained roughly flat in retail trade (2019=100, SA, 3MA)



Source: Macrobond, CZSO, Economic and Strategy Research, Komerční banka

Manufacturing output recovered in early 2025 but is declining again now (2019=100, SA, 3MA)



Source: Macrobond, CZSO, Economic and Strategy Research, Komerční banka

The economy is slowing down and inflation is heading towards the target, which may generate pressure for rate cuts. Thus, the slackening of economic activity we predicted for the second half of this year has indeed materialised. At the same time, inflation has developed more or less in line with our July forecast, and is gradually heading down from a local peak of 2.9% yoy in June to the 2% target. The 2.3% in September provides promise that inflation will approach 2% at the end of this year. However, the core component remains elevated (2.8% in September), primarily due to higher services prices. Core inflation should also reach the target next year, but increase again later due to the fiscal impetus.

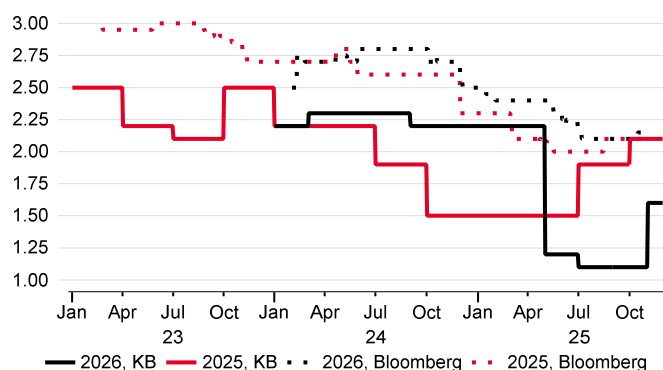
Economic growth and inflation are both currently below the levels projected by the CNB in August, and three months ago we therefore expected the CNB board to cut the rates again before the end of this year.

But the outcome of the recent general elections and the central bankers' rhetoric do not exactly encourage a further rate cut. Central bankers perceive pro-inflationary risks, particularly due to rising core inflation, increased inflation in services, and continued rapid wage growth. The minutes to the CNB board meeting in September¹ further note: *"Other upside risks and uncertainties were also discussed. Aleš Michl considered the persisting general government deficit to be the largest of these."* As noted in the section on fiscal policy, we are afraid that the currently ongoing consolidation effort, regarded by central bankers as insufficient anyway, will, on the contrary, lead to a relaxation of the budgetary responsibility rules. In a special box, Jaromír Gec quantifies the general qualitative and quantitative impacts of fiscal expansion on the most important macroeconomic and financial variables. According

¹ <https://www.cnb.cz/en/monetary-policy/bank-board-decisions/CNB-Board-decisions-1758717000000/?tab=record>

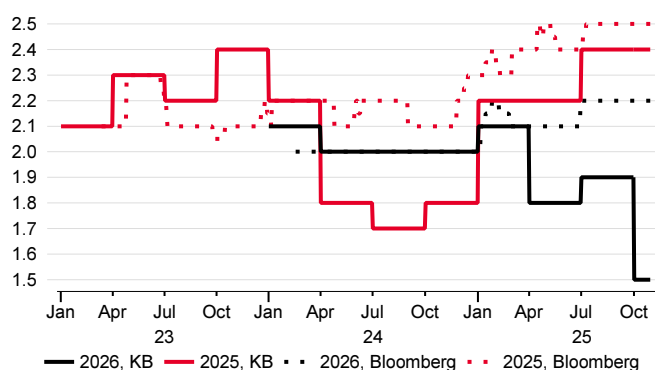
to this separate model, the main outcome is temporarily higher real GDP and inflation and, in response to that, also pressures for higher interest rates.

Growth prospects for the Czech economy (GDP, %, yoy)



Source: Bloomberg, Economic and Strategy Research, Komerční banka

Inflation prospects for the Czech economy (CPI, %, yoy)



Source: Bloomberg, Economic and Strategy Research, Komerční banka

While our expectation that economic momentum would slacken in the second half of this year is coming to fruition, we now see stronger growth prospects for both this year and next. For this year, we expect the economy to grow by 2.1% (0.2pp more than in the July forecast), which more or less matches the market consensus and results primarily from the strong first half of the year. However, we have also increased our 2026 growth forecast by 0.5pp to 1.6%, mainly to reflect our expectations for fiscal expansion to be implemented by the new cabinet and for public investment, which the most recent data suggests is developing promisingly. In spite of that, we remain below the market consensus.

We have not changed our inflation forecast for this year; inflation should be 2.4% on average. But we believe that it will be much lower in 2026, at 1.5% on average. The main reason for our revision is the likely transfer of payments for renewable energy sources, which are currently in the regulated component of the electricity supply price, from households to the government, and also further reductions in market prices of energy, as indicated by some energy suppliers. However, core inflation will stay above the 2% target. For 2025 and 2026, our inflation forecast is below the market consensus. Combined with the fiscal expansion we expect from the new government and the CNB's emphasis on the inflationary risks arising from the fiscal policy of the outgoing government, we have removed the assumption of further interest rate cuts by the CNB from our baseline scenario. Nevertheless, we still consider the risks to be biased in that direction.

Enjoy the autumn edition of Komerční banka's *Czech Economic Outlook*!

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External environment and assumptions



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Despite tariffs, recession unlikely in the US or eurozone

The key issue in the US is the cooling of the labour market, which should prompt the US Federal Reserve to continue cutting interest rates. We estimate the terminal rate at between 3.25% and 3.50%. Next year, US economic growth is set to slow, as the import situation normalises, tariffs negatively impact profit margins and wage growth slows. However, we do not expect a recession. The eurozone economy is likely to be buoyed by looser fiscal policy and a recovery in household consumption – bolstered by accumulated savings, relatively high real disposable incomes, and low unemployment. Inflation in the eurozone is set to slow significantly, to below 2% next year, on our forecasts. Concerns about the anchoring of inflation expectations will, in our view, prompt the European Central Bank to cut interest rates again in March. We expect the Polish and Hungarian central banks to ease monetary conditions as well.

US: labour market cools, Fed set to cut rates further

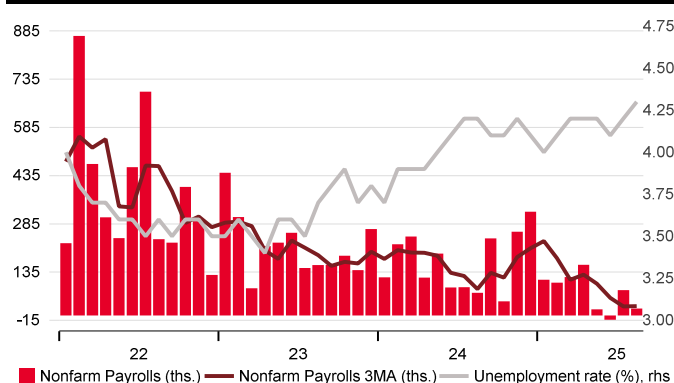
Government shutdown prevented publication of a range of data.

Although the US reached the debt ceiling, Republican lawmakers failed to secure sufficient support for financing the US federal government. This triggered a government shutdown, which has limited the operations of several federal agencies. Among other things, the shutdown has impacted the publication of statistical indicators, with most data not being published in October. The shutdown's economic impact will depend on its duration. The longest shutdown, which lasted 35 days at the turn of 2018/19, temporarily reduced GDP by 0.1% in 4Q18 and 0.2% in 1Q19.

Labour market data was disappointing.

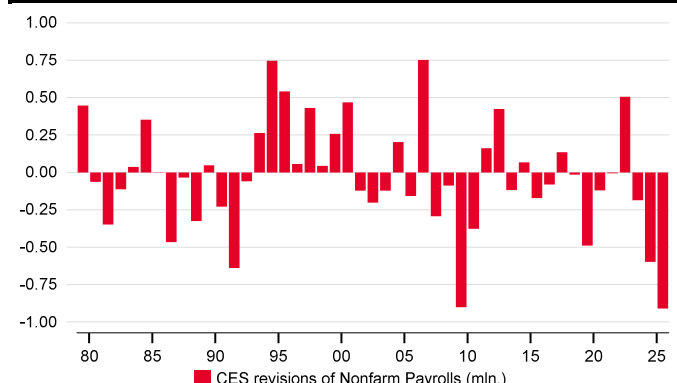
The labour market remains a key issue in the US. The data published thus far has been disappointing. For example, the August statistics on non-farm payrolls (NFP) showed only 22 ths. jobs created, whereas the market had expected 75 ths. Additionally, the June data on NFP was revised down, with jobs essentially disappearing. The annual preliminary revision of NFP data for the 12 months till March 2025 also came as a significant negative surprise. While the original report stated that the US economy created 1,758,000 jobs outside the agricultural sector during that period, the revised figure was only 847,000. This averages to 70.6 ths. jobs per month, rather than the originally announced 146.5 ths. The revision raises questions about the accuracy of the data published from March to the present too. Although these figures are already low, further downward revisions cannot be ruled out.

The labour market is cooling



Source: Macrobond, Economic and Strategy Research, Komerční banka

Preliminary benchmark revision of NFP data (in millions)



Source: Macrobond, Economic and Strategy Research, Komerční banka

The US labour market is plagued by structural problems.

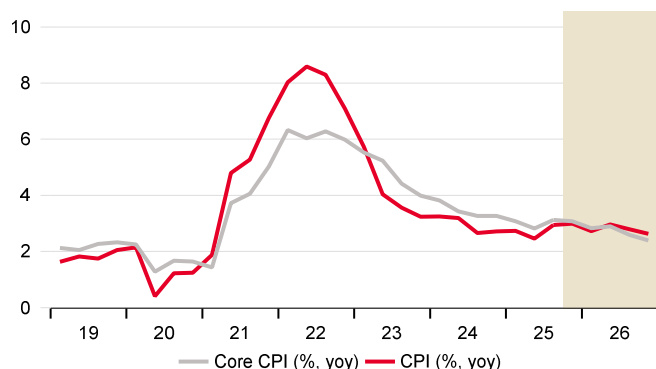
Not only is the labour market cooling, but it is also plagued by structural problems. The labour force participation rate for people over 16 has been gradually declining since the end of

2023, falling to 62.3% in August of this year. This is a full percentage point lower than in February 2020, when the labour market was first affected by the pandemic. This explains why the unemployment rate has only risen modestly so far, reaching 4.3% in August. Several factors are offsetting one another in the market. While trade wars lead to layoffs, unfavourable demographic trends and strict immigration policies reduce the available labour force.

The Fed is likely to continue to cut interest rates.

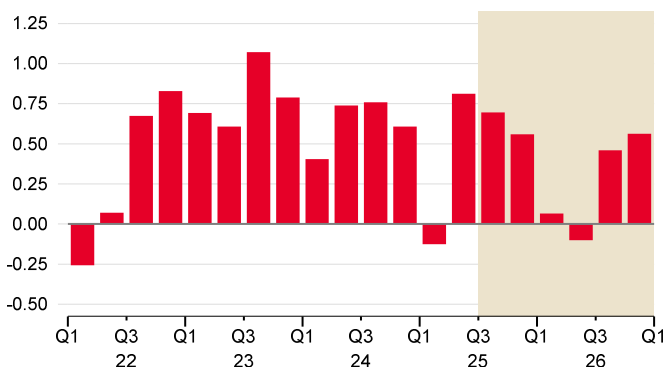
Concerns about further developments in the labour market now outweigh inflation risks, from the Fed's perspective. This was reflected in the resumption of the rate cutting cycle. In our opinion, the Fed will continue with cuts until the key rate reaches 3.25-3.50%. Financial markets expect an even lower final level, at 2.75-3.00%. However, our estimate is more cautious because we expect inflation to remain above the Fed's 2% target until the end of 2027. Therefore, unless the US economy slows considerably, we believe the Fed will not want to keep monetary policy significantly loose. On our forecast, the US central bank's key rate, adjusted for inflation, will be just above 1%. This would be a historically low value. Before the global financial crisis of 1990-2007, the average real key rate was 1.5%, even when including the period from 2001 to 2005 during which it was negative for three years. Previously, from 1990 to 2000, the average rate was 2.2%. The current level is 1.6%.

US: tariffs are pushing up inflation



Source: Macrobond, SG Cross Asset Research/Economics

We do not expect a recession in the US GDP (% qoq)



Source: Macrobond, SG Cross Asset Research/Economics

We do not expect a recession in the US at this time. We estimate 2% GDP growth this year (+0.2pp upward revision), but only 1.3% next year (-0.3pp compared to our July forecast). The data is set to remain volatile due to the tariffs introduced. These tariffs led to significant frontloading efforts in 1Q25, resulting in higher imports and a decline in the US economy. However, in the remaining quarters of this year, companies will import less, which will be reflected in higher GDP growth. Next year, on the other hand, we expect imports to return to normal levels, causing GDP growth to slow. Additionally, the cooling labour market will negatively impact overall sentiment, leading to slower wage growth. The tariffs will also cut into companies' profit margins.

China: further fiscal stimulus needed to achieve 2026 growth target

Chinese domestic demand is losing momentum.

The Chinese economy performed better than expected in the first half of this year, with GDP growing by 5.4% yoy in 1Q and 5.2% yoy in 2Q. The third quarter was also slightly better than the market consensus expected, with GDP growth reaching 4.8% yoy. Meanwhile, the government has approved support measures amounting to 0.7% of GDP. These measures should help kick-start fixed investment and enable China to achieve its 5% growth target this year.

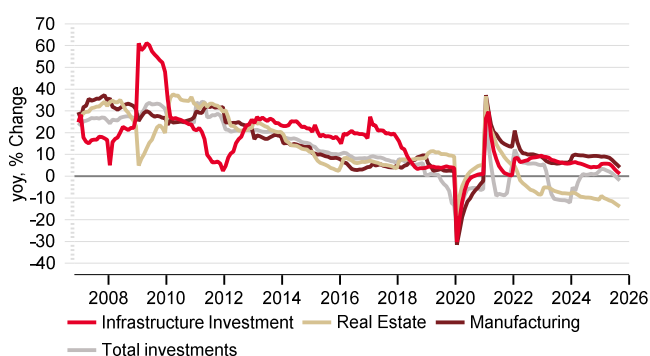
Chinese exports are still proving relatively resilient to the impact of tariffs.

September data from the real economy shows a mixed picture. Chinese retail sales grew at their slowest pace since November 2024 (3.0% yoy), as the positive impact of government support started to wear off. Meanwhile, industrial production accelerated from 5.2% yoy in August to 6.5% yoy thanks to resilient exports and growing production in higher-value sectors. Conversely, the government's efforts to curb overproduction are negatively impacting corporate investment, which fell by -0.5% yoy in September. Investment in real estate, the prices of which are falling, was also significantly lower. Overall, it is clear that domestic demand is losing momentum. On a positive note, the Chinese economy has been relatively resilient to the impact of US tariffs thus far. Although exports to the US have fallen by a third since April of this year, the total volume of exports has remained virtually unchanged. However, we expect the trade wars to have a greater impact next year. This means that further fiscal stimulus will be needed to achieve the 5% growth target in 2026.

Interest rates likely to be cut at the end of the year.

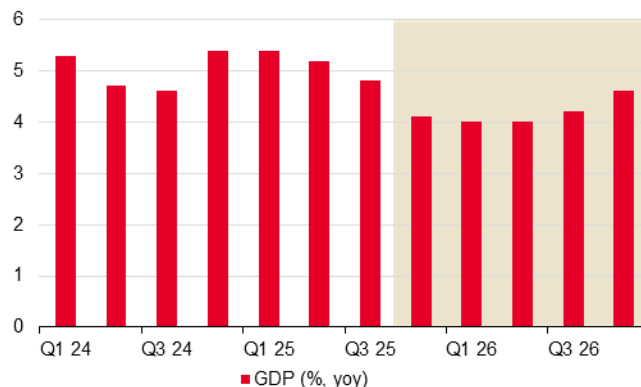
The Chinese central bank will also attempt to support the domestic economy. However, due to concerns about exchange rate developments, it has been cautious about easing monetary policy. The last rate cut was 10bp in May. We expect another 10bp rate cut by the end of the year, with the reserve requirement ratio decreasing by an additional 50bp. The Chinese central bank will likely continue managing the yield curve to prevent excessive volatility in the bond market. In addition to conventional measures, the bank will likely continue to allocate loans to support the technology, environmental, and consumption sectors. However, China has not yet won the fight against deflation. Inflation turned negative again in August and remained so in September (-0.3% yoy). Conversely, the decline in producer prices slowed from 3.6% yoy in July to 2.3% in September, which suggests that the government's efforts to curb overproduction may be bearing fruit.

Chinese investments have stalled



Source: Macrobond, Economic and Strategy Research, Komerční banka

Another fiscal stimulus will be needed to achieve growth target



Source: Macrobond, SG Cross Asset Research/Economics

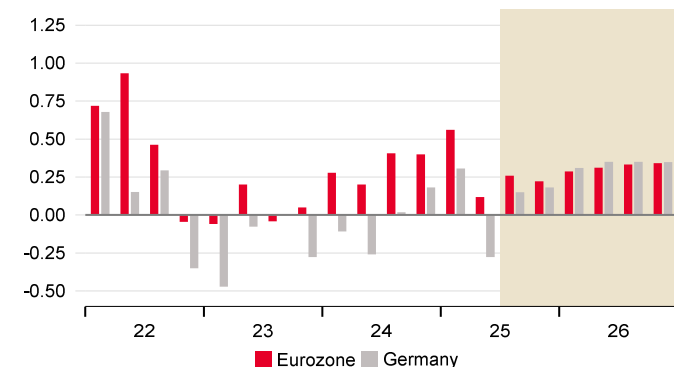
High real disposable income, low unemployment, and fiscal stimulus will support household consumption.

Eurozone: consumption – the engine of economic growth

Eurozone GDP grew by 0.1% qoq in 2Q, from 0.6% qoq in 1Q. In the coming quarters, household consumption should be the main driver of the economy. Robust wage growth resulted in a 2.4% increase in real disposable household income last year. We expect it to grow by 1.3% this year and next. The savings rate also remains high. In 1Q of this year, it was 2.7pp higher than the average for 2013-2019. Unemployment remained close to historical lows at 6.3% in August. These factors should lead to a recovery in household consumption. Investment, the main driver of growth in 2022-2023, fell by 2.1% last year. However, we expect the housing sector, which accounts for 6% of GDP, to stabilise this year. This could contribute 0.1-0.2pp to overall GDP growth after the negative impact in 2023-2024. Assuming reduced domestic political uncertainty, particularly in Germany and France, and increased

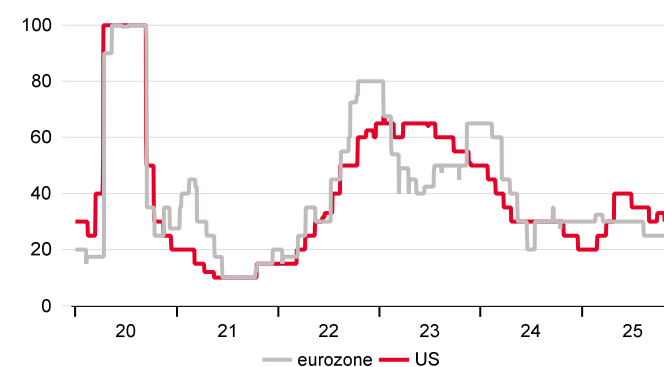
defence spending, we expect capital expenditures to grow by 2.2% this year. However, trade wars will slow down economic performance, due to the level of net exports. Overall, we forecast GDP growth of 1.4% this year and 1.1% next year.

Eurozone and Germany: GDP growth rate (% , qoq)



Source: Macrobond, SG Cross Asset Research/Economics

Recession probability in 1YR horizon (% , Bloomberg konsenzus)

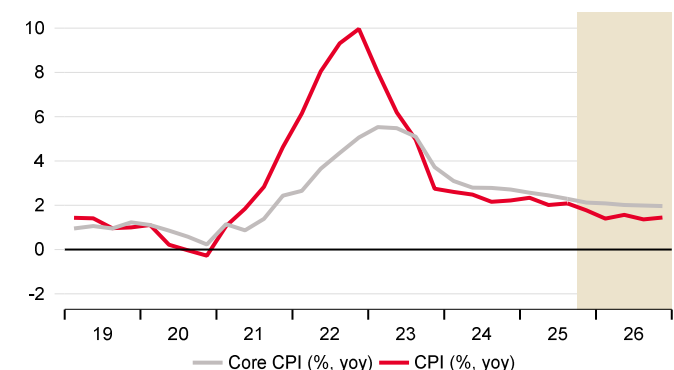


Source: Macrobond, Bloomberg consensus, Economic and Strategy Research, Komerční banka

We expect inflation to slow to an average of 1.5% next year.

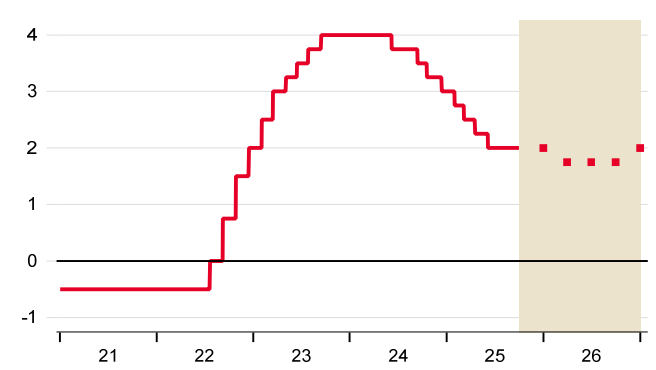
Inflation in the eurozone increased from 2.0% yoy in August to 2.2% in September. However, this was a temporary effect due to a low comparison base and energy price developments. Core inflation was 2.4% yoy in September. We expect it to remain slightly above 2% in the coming months due to elevated inflation in services (3.2% yoy in September). However, services inflation should gradually slow as well. Over the past 15 years, the pace of services inflation has lagged wage growth. We expect a slowdown in wage growth from 4.5% last year to 3.3% this year and 3.0% over 2026-2029, which would push inflation in services down to the 2-3% range. At the same time, inflation is likely to be affected by a stronger euro against the US dollar and falling energy prices. Thus, we expect inflation to slow to 1.6% by the end of this year, then to 1.4% yoy in 1Q26, and to average 1.5% next year.

Eurozone inflation likely to decelerate below the ECB target (% , yoy)



Source: Macrobond, SG Cross Asset Research/Economics

ECB to cut rates for last time in March (depo rate, %)



Source: Macrobond, SG Cross Asset Research/Economics

Further ECB rate cut in March 2026, in our view.

We forecast that the ECB will be concerned about the development of inflation expectations and will cut interest rates by another 25 basis points in March. This would bring the deposit rate to 1.75%, where we expect it to remain until the end of next year, at which time we anticipate the first interest rate hike. Overall, however, the ECB faces several challenges. European governments' plans to increase military spending, spending related to negative demographic trends, and necessary investments in structural reforms should lead to increased public deficits and put pressure on the long end of the yield curve. An increase

in average long-term yields to 4% (still significantly lower than the levels seen in 1999-2008) would result in an additional €140bn in debt per year. Maintaining the 3% public finance deficit target would be difficult without tax increases or significant cuts to social spending. Therefore, the question is whether the ECB will be able to continue reducing its balance sheet under current conditions, and at what pace in the coming years. The ECB's balance sheet currently stands at 40% of GDP, while the Fed's is at 22%.

We see better prospects for Germany only in 2026.

The German government has agreed on a package of reforms. This is to include restrictions on social benefits, support for active retirement, lower energy prices, a more attractive electromobility support system, and increased infrastructure and defence investments. However, no specific timetable or financial figures have been announced yet. The lack of concrete steps is the reason for the recent deterioration of leading economic indicators in Germany. Data from the real economy was also disappointing. Industrial production fell by 4.3% mom in August, marking the largest decline since March 2022. This was due to car factories closing for summer holidays and changes in production. The pharmaceutical industry fell by more than 10% mom, and production of computer, electronic, and optical products fell by 6% mom. This appears to reflect the negative impact of trade wars. Factory orders also fell sharply in August, marking the fourth consecutive month of decline. Thus, the German economy still appears to be facing cyclical and structural problems that should limit its performance in the coming months/quarters. On our forecast, GDP growth for the whole year will be 0.3%. Next year, however, we expect it to reach 1%.

CEE region: inflation outlook is favourable

We expect the National Bank of Poland to cut rates in November.

In early October, the National Bank of Poland surprised financial markets by cutting the key rate by 25bp to 4.50%. The bank justified its actions with a favourable inflation outlook. We expect a similar move at the November meeting, when central bankers will have a new forecast. This forecast will likely indicate that inflation is set to return to the central bank's tolerance band (2.9% yoy in August) within the next year. This would also be in line with our assumption, as we expect lower oil prices, a strong domestic currency (EURPLN 4.25 by the end of this year and in the first half of next year), and slowing wage growth to push inflation down. Therefore, we expect further easing of monetary conditions in March and May, which would bring the key interest rate to its neutral level of 3.75%.

We forecast a further rate cut in March 2026 in Hungary.

The Hungarian central bank left its key three-month deposit rate unchanged at 6.5% in October. The stability of the domestic currency remains the bank's main priority, and inflation is relatively high (4.3% yoy in September). Due to the favourable comparison base, the postponed increase in excise duty, and low repricing of regulated prices, inflation should return to the central bank's tolerance band in the first quarter of next year, in our view. We expect the central bank to respond in March by lowering the key base interest rate to 6.25%. We forecast that the Hungarian forint will trade in the range of EURHUF 390-400 in the next four quarters.

Macroeconomic forecast



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Major changes

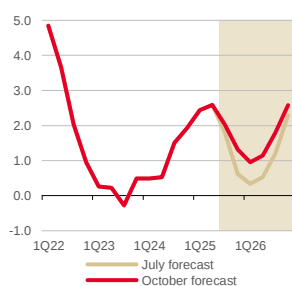
GDP:

We have raised our GDP growth forecast from 1.9% to 2.1% this year and from 1.1% to 1.6% next year. The upward revision for 2025 is mainly due to a strong recovery in government investment and construction output. Next year's forecast has been positively influenced by the fiscal stimulus indicated in statements from the likely new government.

Inflation:

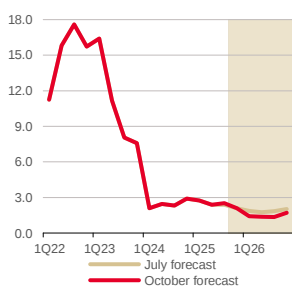
We have maintained our inflation forecast for this year at 2.4%, but reduced it from 1.9% to 1.5% for 2026. This is due to the likely new government's plan to transfer payments for renewable energy sources from households to the state. Along with further declines in household energy prices, this will result in inflation falling below the 2% target. However, our forecast includes an increased inflation outlook for subsequent years due to an expansionary fiscal policy.

Changes to GDP forecast (% , yoy)



Source: CZSO, Economic & Strategy Research, Komerční banka

Changes to CPI forecast (% , yoy)

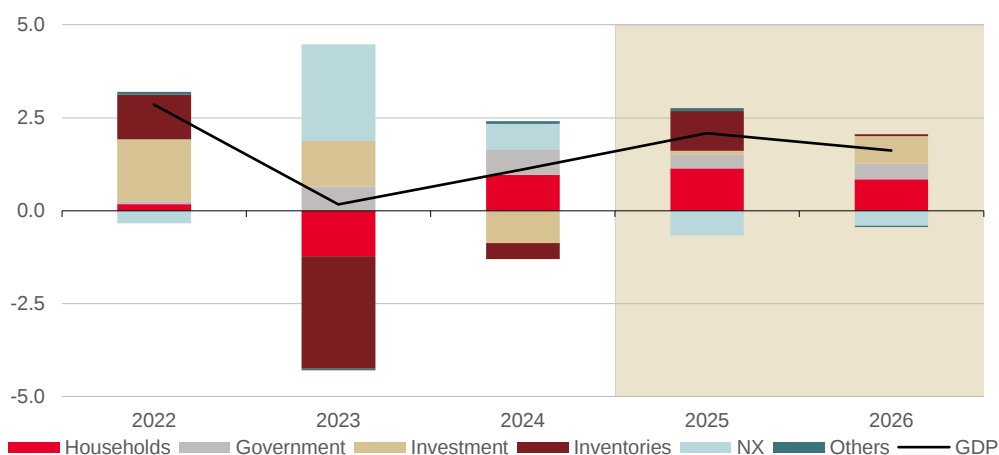


Source: CZSO, Economic & Strategy Research, Komerční banka

Fiscal stimulus is likely to alter economic and inflation trends

The Czech economy is unlikely to maintain its strong performance seen in 1H25. We expect a significant economic weakening and broadly stagnant growth in 2H25. This is due to a renewed decline in industrial production as the impact of US tariffs shifts from positive to negative. According to the latest data, household consumption has also slowed, though it should remain the main driver of economic growth this year and next. We expect this to be supported by continued wage growth and a tight labour market, with only modest increases in unemployment. Domestic demand is also likely to be boosted by government investment this year, with construction output rising strongly. Conversely, corporate investment and exports are likely to be weak due to subdued industrial activity. Nevertheless, we expect an economic and industrial recovery next year, when the substantial fiscal stimulus proposed by the prospective new government comes into effect. However, fiscal policy is also the main source of uncertainty in our forecast. The government's proposed measures to lower energy bills, alongside further reductions in household energy prices, are likely to push inflation below 2% next year. In contrast, we expect the expansionary fiscal policy to cause inflation to exceed the central bank's target in subsequent years.

Domestic demand, supported by a fiscal impulse, to be the main driver of GDP growth (% , yoy)



Source: CZSO, Economic & Strategy Research, Komerční banka

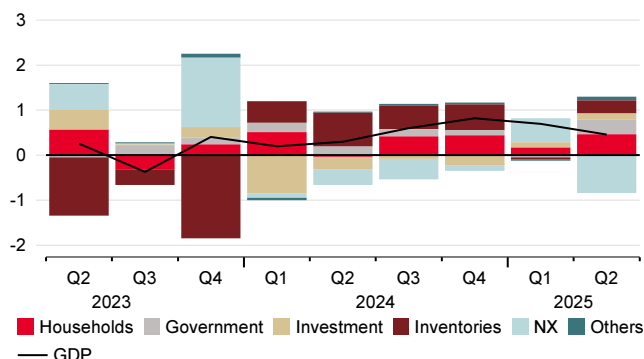
Czech economy to grow again in 2026 after stagnating in 2H25

Economic growth continued at a rapid pace in 2Q25, supported by domestic demand.

Czech GDP increased by 0.5% qoq, following a rise of 0.7% qoq in 1Q. In year-on-year terms, economic growth accelerated from 2.4% to 2.6%. This was broadly in line with our July forecast calling for increases of 0.4% qoq and 2.6% yoy. Strong domestic demand was the main driver of qoq GDP growth in 2Q. Household consumption rose by 1.0% qoq, accelerating from 0.4% qoq in 1Q. Nevertheless, it remained 1.3% below the pre-pandemic level of 4Q19. Government consumption grew significantly, at a rate of 1.6% qoq in 2Q. Domestic demand was also fostered by a 0.5% qoq increase in fixed investment. Its composition suggests that this was primarily due to government investment. Investment mainly rose in the category of other buildings and structures, which traditionally includes infrastructure investment financed from public sources. The positive impact of higher government investment is likely reflected in the strong growth of civil engineering since the beginning of the year. According to the latest data for August, its output was the highest since January 2010. In contrast, corporate investment likely remained weak, with only investment

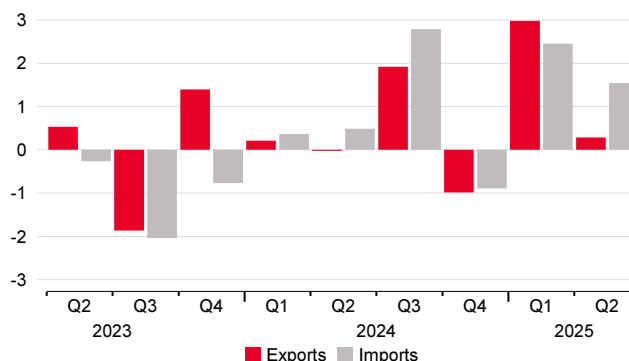
in transport equipment rising qoq. Inventories also made a relatively strong contribution to qoq GDP growth (+0.3pp).

The negative contribution of net exports to GDP growth in 2Q was offset by strong domestic demand (% , qoq, SA)



Source: CZSO, Macrobond, Economic & Strategy Research, Komerční banka
Note: NX denotes net exports.

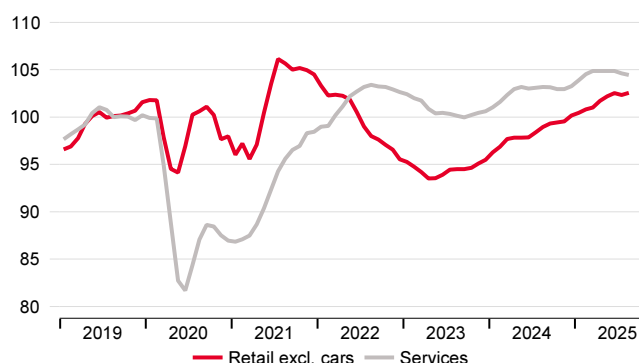
Real imports continued to grow rapidly in 2Q, while export growth was weaker but still positive (% , qoq, SA)



Source: CZSO, Macrobond, Economic & Strategy Research, Komerční banka

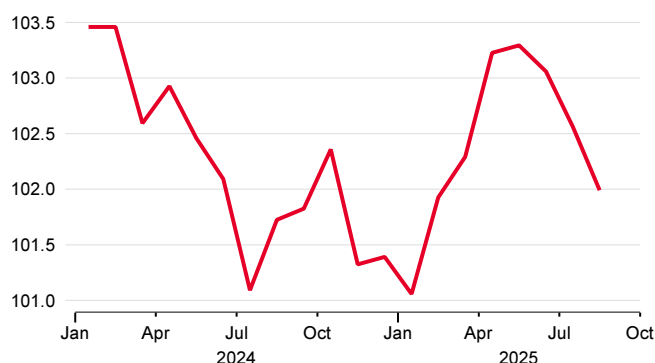
Despite the fall in net exports in 2Q, the volume of exports remained supported by US frontloading. While net exports added 0.5pp to qoq GDP growth in 1Q, they subtracted 0.8pp in 2Q. Imports continued to grow strongly, rising by 1.5% qoq in real terms in 2Q after +2.5% in 1Q. This was likely driven by growth in domestic demand. However, concerns about supply chain disruptions due to US tariffs and possible retaliatory measures may also have had an effect, prompting some domestic companies to stockpile inventories. The stockpiling was more evident among US companies and households looking to purchase imported goods before tariffs increased their prices. This was particularly noticeable in 1Q, but also impacted 2Q, with Czech exports rising by 3.0% qoq in real terms in 1Q, before slowing to just 0.3% qoq in 2Q. Although growth was significantly lower, it remained positive, likely due to the lingering impact of US frontloading. In line with this, Czech manufacturing output continued to grow strongly in 2Q, increasing by 0.7% qoq after +0.9% in 1Q, whereas it declined in all quarters of 2024. In fact, the entire European manufacturing industry recovered in 1H25.

Consumer demand growth weakened markedly, according to monthly real sales indicators (2019=100, SA, 3MA)



Source: CZSO, Macrobond, Economic & Strategy Research, Komerční banka

Manufacturing output recovered at the beginning of the year, but is now declining again (2019=100, SA, 3MA)



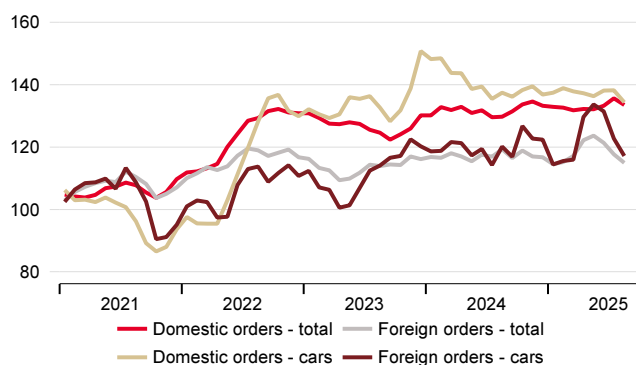
Source: CZSO, Macrobond, Economic & Strategy Research, Komerční banka

The monthly data indicate a significant slowdown in the Czech economy, which we estimate to have stagnated on a qoq basis in 3Q. The positive trend in industrial production observed at the beginning of the year was reversed following the announcement of steep US tariff increases in April. Since May, Czech manufacturing output has fallen steadily. According to the latest data for August, output was 2.7% lower than in April and the same as in January.

After a strong start to the year, we expect the economy to stagnate in 2H25. Economic growth should accelerate again in 2026 against the backdrop of substantial fiscal stimulus.

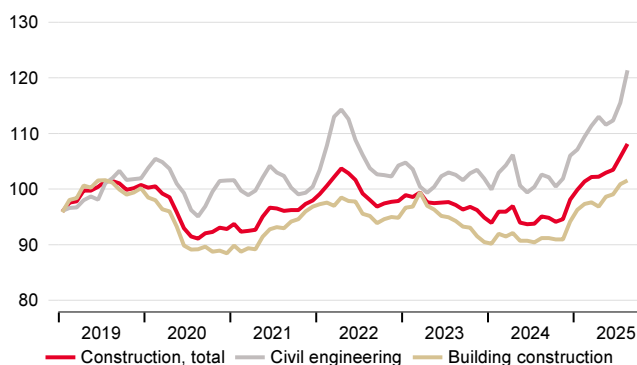
This confirms that the rebound in the industrial sector at the beginning of the year was only temporary, supported by the US frontloading rather than being a sign of cyclical recovery. Industrial indicators have also started to deteriorate again in other European countries, including Germany. The negative effects of US tariffs are likely playing an important role in this. We wrote more about our expected US tariff impacts on the Czech economy here: [https://bit.ly/US tariffs Czech economy EN](https://bit.ly/US_tariffs_Czech_economy_EN). Data on real sales in retail and services shows that households increased purchases of both goods and services in 1Q, but spent more on goods only in 2Q, which contributed to continued import growth. Sales of services remained unchanged qoq in 2Q. Closer analysis reveals that despite wage growth exceeding expectations in 2Q, growth in retail sales weakened significantly from May onwards. Overall, the monthly data from the real economy, which are currently available until August, indicate a slight qoq decline in services in 3Q, as well as only a slight increase in retail sales excluding cars. This would mark a sharp slowdown, given that retail sales excluding cars grew by a strong 1.5% qoq in 2Q. Therefore, it appears that not only has industrial activity weakened significantly in 3Q, but domestic demand has too. Conversely, the strong rise in construction output should support the economy. This reflects increased government investment in infrastructure and a revival in residential construction. However, this is still insufficient to meet the high demand for housing.

Foreign orders in the Czech industry have fallen after temporarily rising due to US frontloading (2019=100, SA, 3MA)



Source: CZSO, Macrobond, Economic & Strategy Research, Komerční banka
Note: Industrial orders are in nominal terms.

A substantial surge in civil engineering output is likely being fuelled by government investment (2019=100, SA, 3MA)



Source: CZSO, Macrobond, Economic & Strategy Research, Komerční banka

Given the prospect of a strongly expansionary fiscal policy, we expect economic growth to pick up next year. Compared to our previous forecast, we have raised our GDP growth estimate for 2025 from 1.9% to 2.1%. We had originally anticipated a slight contraction in the economy in 2H25, but now expect it to be broadly stagnant. This is due to positive developments in government investment and construction, as evidenced by the latest data. These should add to slightly rising household consumption and offset the expected decline in industry. Despite the fact that our forecast of a significant slowdown in 2H25 has come to pass, according to the available data, we have increased our GDP growth estimate for 2026 from 1.1% to 1.6%. The lower level of growth in 2026 continues to be influenced by the weak 2H25 and in the early part of next year. However, from 2Q26, our forecast incorporates the impact of a strong fiscal stimulus, as indicated by the plans of the likely future government and the election programmes of the parties likely to form the new coalition. In our view, this will manifest as higher government consumption and investment. Due to the gradual ramp-up, which may be due to a provisional budget, we expect this effect to be visible mainly in the 2027 full-year GDP statistics. We also expect a more expansionary fiscal policy to result in slightly faster growth in private consumption over the forecast horizon. However, we anticipate that the impact on real household consumption will be offset by higher inflation, which we predict as a result of increased government spending.

The uncertainties and risks surrounding our GDP forecast mainly relate to fiscal policy.

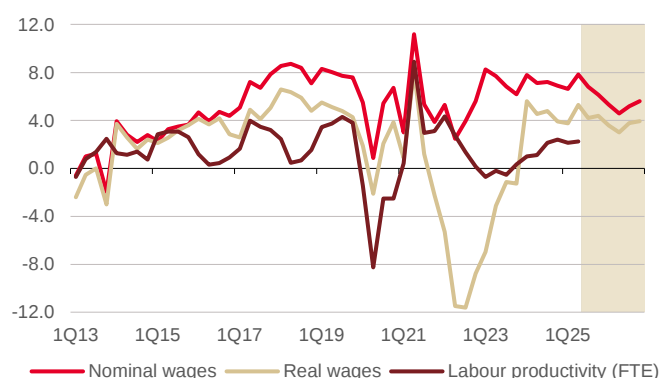
Strong fiscal expansion is a key part of our current forecast. If this does not materialise, economic growth is likely to be lower, particularly in 2026 and 2027. Continued subdued industrial performance could also contribute to weaker growth. After declining in 2H25, we expect industrial production to recover markedly next year thanks to fiscal stimulus at home and in Germany. Lower energy prices should also help. However, structural problems combined with intensifying Chinese competition in the European market could remain a strong counterweight. Conversely, stronger wage growth, particularly in the public sector, could pose a risk to higher growth.

Wage growth should support further increases in household spending

Surprisingly strong wage growth in 2Q25 was likely driven by one-off factors. Average nominal wages increased by 7.8% yoy, exceeding the 7.2% growth included in our July forecast. However, based on leading indicators, we estimate a slowdown to 6.8% yoy in 3Q. In spite of this, we have revised our 2025 wage growth forecast slightly upwards, from 6.5% to 6.8%. Given our expected fiscal stimulus and the associated faster GDP growth, we have also raised our estimate for 2026, from 4.7% to 5.2%. Nevertheless, we anticipate that wage growth will slow due to the temporary weakening of the economy and labour market, as well as the gradual convergence of real wages and labour productivity.

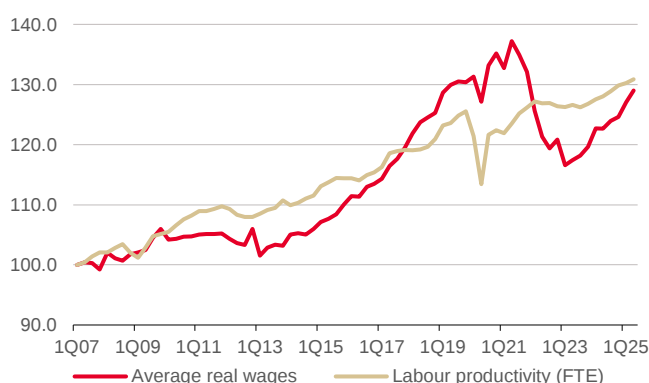
We anticipate a temporary easing of the labour market due to the economic slowdown in 2H25, although persistent labour shortages will still be an issue.

Wage growth to slow due to temporary weakening of the economy and labour market (% , yoy)



Source: CZSO, Economic & Strategy Research, Komerční banka

Real wages remain below labour productivity, but both are gradually converging (1Q07=100)



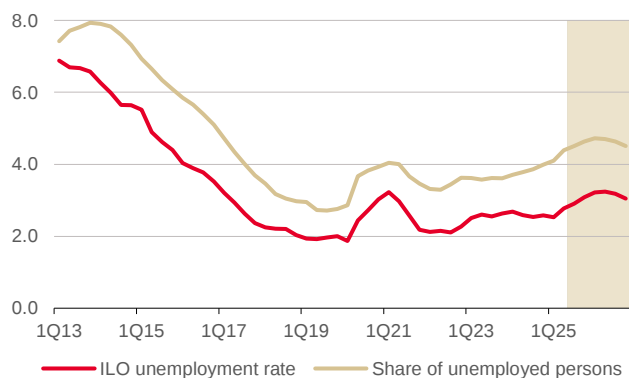
Source: CZSO, Economic & Strategy Research, Komerční banka

The labour market is set to partly ease. We expect the ILO unemployment rate to increase from 2.6% in 2024 to 2.8% in 2025 and 3.2% in 2026. This is due to a slowdown in economic activity in 2H25 and ongoing issues in the industrial sector. However, with the economy recovering, we foresee the unemployment rate to return below 3% in subsequent years. Employment (ILO) is likely to grow by more than 1% yoy in 2025 for the third consecutive year, driven by the inclusion of Ukrainian refugees. In line with the overall macroeconomic scenario, we expect employment to stagnate next year before resuming gradual growth. This will mainly be due to the influx of foreign workers, as the domestic labour force is very limited – a situation that will be exacerbated by an ageing population. The sharp decline in manufacturing employment is still being offset by job growth in other sectors of the economy. In the trade and services sector, employment remains around 2% below its pre-pandemic level. This offsets the impact of the industry downturn on the overall labour market and this trend should persist alongside the continued household consumption growth.

Despite the labour market partially easing this year and next, it is likely to continue suffering from a persistent labour shortage. This should lead to ongoing growth in real wages. However, we do not expect real wages and household consumption to reach

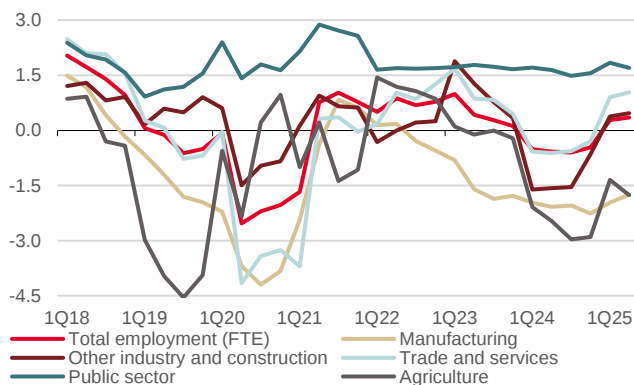
pre-pandemic levels until 1H26. As real wages have lagged behind rising labour productivity, the impact of their increases on inflation has been limited.

Unemployment is rising slightly and is likely to continue to do so for some time, thereby easing labour market tensions (%)



Source: CZSO, MLSA, Economic & Strategy Research, Komerční banka

While employment in the manufacturing sector is falling, the trade, services and public sectors are adding jobs (% , yoy)



Source: CZSO, Economic & Strategy Research, Komerční banka
Note: The graph shows full-time equivalent (FTE) employment.

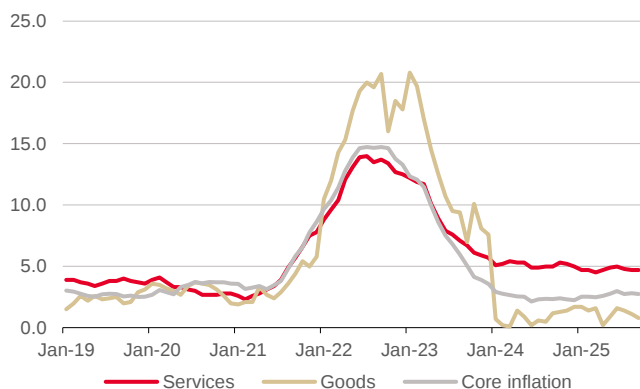
We expect lower energy and fuel prices to push inflation down to 1.5% in 2026, before price growth returns above the CNB target due to fiscal expansion.

Inflation is likely to temporarily fall below the 2% target next year

Consumer price growth slowed to close to the central bank's target in 3Q25. After reaching this year peak of 2.9% yoy in June, inflation steadily fell to 2.3% yoy in September. For 3Q as a whole, inflation averaged 2.5% yoy, which was only slightly higher than our July forecast of 2.4%. Food and fuel prices were higher than we forecast, while regulated prices showed slower annual growth. Excluding the impact of this year's increase in excise duties on alcohol and tobacco, monetary policy inflation stood at 2.1% yoy in September, essentially in line with the central bank's target. Core inflation averaged 2.8% yoy in 3Q, as in 2Q, in line with our forecast. Weighted imputed rents (10% of the CPI consumer basket), including the impact of rising house prices, continued to show strong month-on-month momentum. However, its annual growth did not accelerate further, as we expected. From June to August, growth in imputed rents stagnated at 4.9% yoy. Growth in paid rents slowed from 6.0% yoy in 2Q to 5.7% yoy in 3Q. Overall services inflation also eased slightly, from 4.9% yoy in 2Q to 4.7% yoy in 3Q. While the level remains high, it is offset by subdued growth in goods prices (1.1% yoy in 3Q).

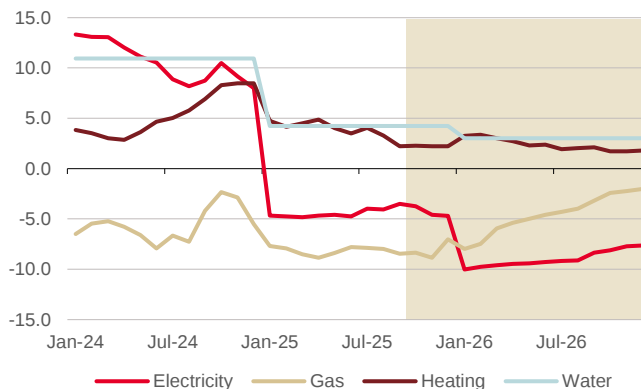
The energy component will push inflation below 2% next year. According to information published by energy suppliers, household electricity and gas prices will continue to decline for the rest of this year and into next year. This is due to favourable developments in the wholesale energy markets, with stable electricity and gas prices and suppliers yet to fully reflect their earlier decline in final household prices. Furthermore, our forecast takes into account the impact of transferring payments for renewable energy sources from households to the state within the regulated part of electricity prices. According to information from the likely new government, this will contribute to a 15% reduction in the regulated part of electricity prices, and should take place from January next year. Based on our calculations, this impact is realistic. Consequently, we expect the average household electricity price to decline by around 9% in 2026, following a likely fall of more than 4% in 2025. Household gas prices are likely to decline by about 8% this year and according to our estimates could fall by at least 4% next year. Lower energy prices are the main reason why we expect a 1% decline in overall regulated prices in 2026. According to the external assumptions in our forecast, oil prices will continue to fall due to increased production and subdued demand. Added to this will be the impact of the strong euro and Czech koruna. The energy component as a whole should therefore have a strong disinflationary effect in 2026, which could contribute to moderating the dynamics of other inflationary components.

High services inflation is balanced by subdued goods price growth (% , yoy)



Source: CZSO, CNB, Economic & Strategy Research, Komerční banka

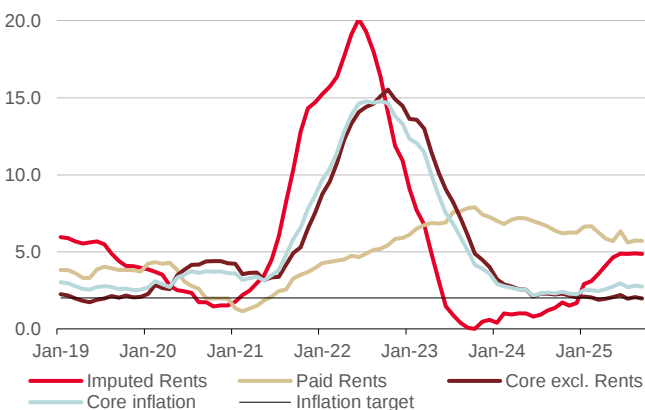
Household electricity and gas prices will continue to fall next year (% , yoy)



Source: CZSO, Economic & Strategy Research, Komerční banka
Note: Final household energy prices including both the market and regulated components.

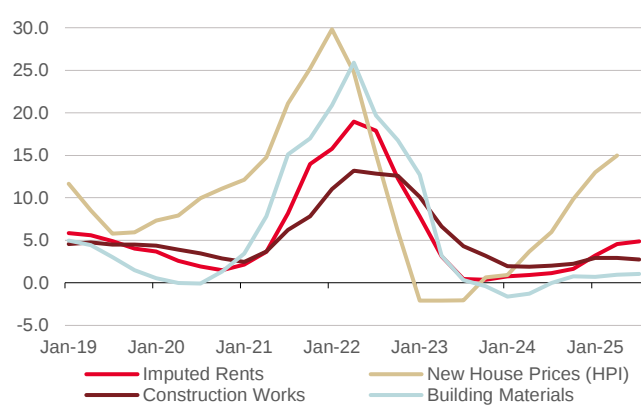
We expect inflation to fall from 2.4% this year to 1.5% next year, but it is then likely to return above the 2% target due to expansionary fiscal policy. Our estimate for 2025 remains unchanged from the previous forecast, but we have lowered the estimate for next year from 1.9%. This revision is mainly due to the outlook for energy prices. We expect core inflation to reach 2.7% this year and 2.1% next year. Compared to our July forecast, this year's estimate has remained unchanged, while next year's has increased slightly from 2.0%. In our view, the more expansionary fiscal policy will gradually boost domestic demand. After a temporary easing, we thus anticipate renewed pressure on core prices. Consequently, we expect core and headline inflation to accelerate again in 2027 (to 2.3% and 2.4%, respectively). We forecast that food price growth will slow from 3.4% in 2025 to 1.9% in 2026 due to the positive impact of a strong koruna, falling energy and fuel prices, and an improved local agricultural harvest.

Rent growth remains high but is not accelerating further, while core inflation excluding rents is on target (% , yoy)



Source: CZSO, CNB, Economic & Strategy Research, Komerční banka

Imputed rents also include the cost of construction work and materials, which has not grown as fast as house prices (% , yoy)

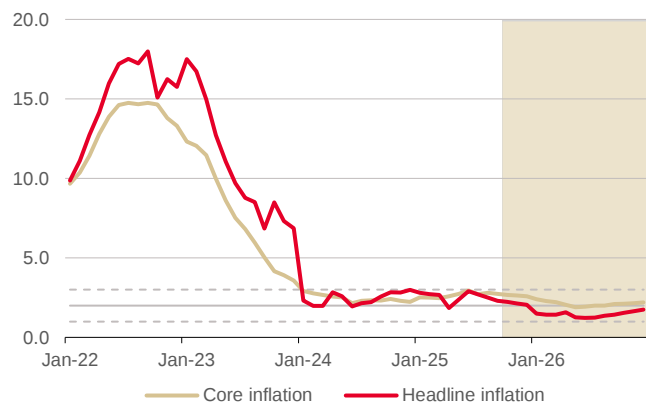


Source: CZSO, Economic & Strategy Research, Komerční banka

Our inflation forecast is also affected by the uncertainty surrounding fiscal policy. If fiscal spending does not increase significantly, providing no support for domestic demand, we believe that inflation may remain below the 2% target for a longer period. This could be further influenced by lower energy and fuel prices, as well as a stronger koruna exchange rate, spilling over into other components of inflation that are more closely linked to the domestic economy. If inflation remains below 2% for an extended period, this could also result in lower inflation expectations. Conversely, the inflationary risk to our forecast stems from the potential impact of introducing emission allowances for households and small businesses from 2027.

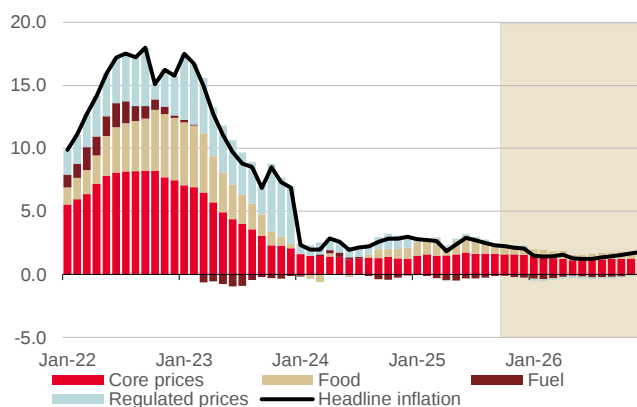
As the likely future government has consistently opposed the implementation of ETS 2 into Czech law, we have not included its impact in our current forecast. Dynamic house price growth and a potential resurgence of geopolitical tensions fuelling higher oil prices also represent inflationary risks to our forecast.

We expect headline inflation to fall below 2% next year, with core inflation near the central bank's target (%, yoy)



Source: CZSO, CNB, Economic & Strategy Research, Komerční banka

The downward pressure on inflation in 2026 will be driven by falling energy and fuel prices (%, yoy)



Source: CZSO, CNB, Economic & Strategy Research, Komerční banka

Monetary policy



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CNB rates to remain unchanged due to fiscal policy

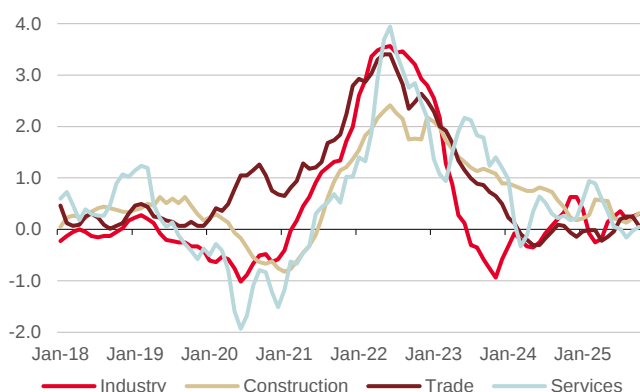
Although the Czech economy is developing in line with our disinflationary scenario, we have changed our call in regards to CNB policy. In our baseline scenario, we no longer expect further interest rate cuts, forecasting the repo rate to remain at 3.5% for some time. This is due to the anticipated shift in fiscal policy, as indicated by the results of the recent parliamentary elections. Fiscal policy is likely to become more expansionary on the monetary policy horizon, pushing inflation higher. Even when the impact of fiscal policy on the economy was, in our view, roughly neutral, the CNB board cited it as one of the main inflationary risks. Nevertheless, in terms of further possible rate movements, we still consider a cut to be more likely than a hike. If the scenario of a more expansionary fiscal policy does not materialise and the disinflationary trend in the economy continues, the CNB would likely have to resume cutting rates.

Higher interest rates and a stronger koruna than in the CNB forecast compensated for the faster wage growth in 2Q25.

Despite lower inflation, the Czech National Bank held interest rates unchanged in 3Q25.

Following the most recent cut in May, the key repo rate has remained at 3.5%, in line with our July forecast. However, CNB staff forecast an additional cut to the average repo rate of 3.2% in 3Q. By contrast, inflation at 2.5% yoy in 3Q was lower than the CNB forecast of 2.7%. The forecast deviation increased gradually during the quarter, with September inflation of 2.3% yoy already 0.3pp below the CNB forecast. This was almost entirely due to volatile food prices, while core inflation was in line with the central bank's view (2.8% yoy in 3Q). GDP developments in 2Q also met the CNB forecasts of an increase of 0.5% qoq and 2.7% yoy. Nevertheless, nominal wage growth of 7.8% yoy in 2Q significantly exceeded the CNB's estimate of 6.7%. This was offset by the stronger Czech koruna, which averaged EURCZK 24.50 in 3Q vs the CNB forecast of EURCZK 24.80, adding to the effect of higher interest rates.

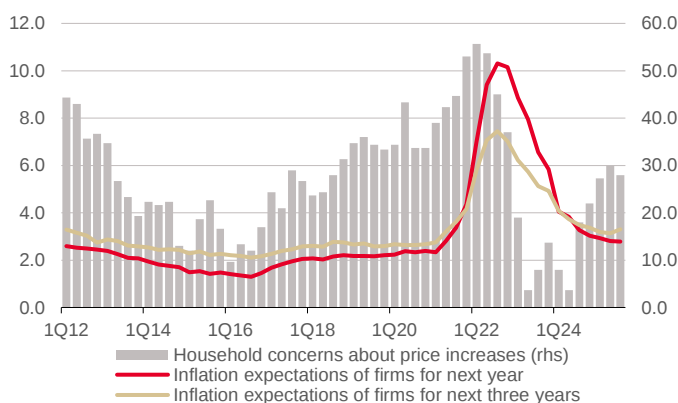
Price expectations stabilised at around their long-term average across the different sectors of the economy (z-score, SA, 3MA)



Source: CZSO, Economic & Strategy Research, Komerční banka

Note: Price expectations for a specific economic sector based on the CZSO survey. Z-scores are calculated using time series from 2003 and the graph shows their three-month moving averages.

Inflation expectations of non-financial firms are at 3%, whereas household fears of price rises are close to their average (%)



Source: CZSO, CNB, Economic & Strategy Research, Komerční banka

The scenario of economic acceleration in 2H25, as outlined in the CNB's August forecast, is unlikely to materialise. The central bank expects strong GDP growth of 0.6% qoq for both 3Q and 4Q25. This is a much more optimistic outlook than our own forecast of roughly stagnant economic activity in 2H25. Consequently, we estimate lower inflation of 2.1% yoy in 4Q, while the CNB foresees it at 2.7%. Forecasts for wage growth in 3Q do not differ significantly – we expect an increase of 6.8% yoy while the central bank expects 6.5%.

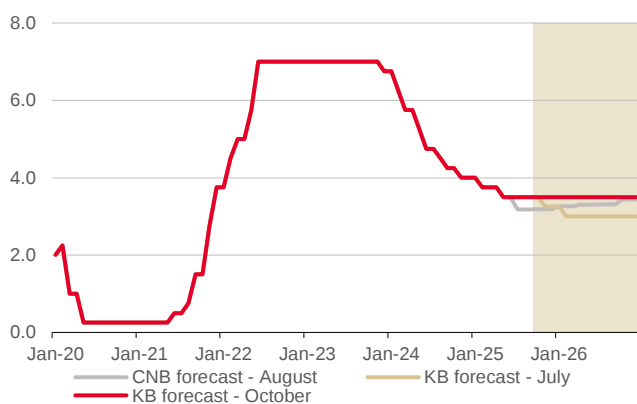
This suggests that the significant deviation from the CNB forecast in 2Q should not be too much of a concern for the central bank, as it was likely driven by one-off factors.

The prospect of a more expansionary fiscal policy is likely to prevent the CNB from making further rate cuts.

Despite our earlier disinflationary scenario materialising, we expect the CNB's interest rates to remain unchanged for an extended period due to fiscal policy. In our previous forecast, we called for a 25bp cut at the November and February meetings, which would bring the repo rate to its terminal level of 3%. However, we now consider the current level of 3.5% to be the end point of this monetary policy cycle. This is because we anticipate strong fiscal expansion, which is likely to alter the trend in economic and inflationary developments over the monetary policy horizon, i.e. at the turn of 2026 and 2027. Even more recently, when we had estimated fiscal policy to have a roughly neutral effect on the economy, the CNB board cited it as one of the main inflationary risks. The board has also used this as a reason for its cautious approach to lowering interest rates. If the bank board remains consistent in its stance, the outlook for an expansionary fiscal policy should result in stable rates over a longer period.

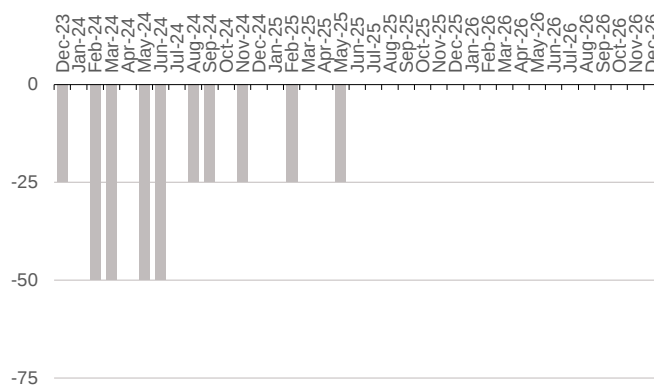
As we see the risks to our forecast being skewed to the downside, we still consider a further rate cut to be more likely than that of a hike. Once a new government is formed and the 2026 state budget is approved around the turn of the year, it will become clear whether a more expansionary fiscal policy will be implemented or not. If this does not happen, then the economy's disinflationary tendencies may persist next year, forcing the central bank to cut interest rates further. Therefore, as with our macroeconomic scenario, our CNB rate forecast depends heavily on fiscal policy prospects.

Repo rate to remain at 3.5%, in our view (%)



Source: CNB, Economic & Strategy Research, Komerční banka

We do not expect further CNB rate cuts in the near future (bp)



Source: CNB, Economic & Strategy Research, Komerční banka

Fiscal policy



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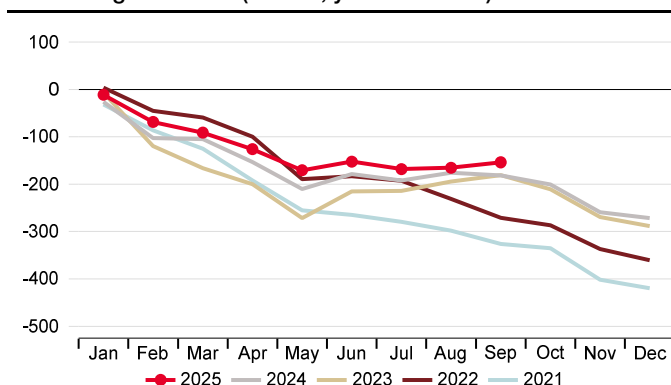
Fiscal easing in sight

As with previous parliamentary elections, we expect the new government to revise next year's budget. This will likely necessitate a provisional budget during the first quarter of 2026. Due to increased infrastructure investment and defence spending, we expect the cash deficit of the state budget to deepen to CZK320bn next year. On our estimates, this would imply an increase in the public finance deficit from 2.2% of GDP this year to 2.8% next year. Starting in the second quarter, when the provisional budget could end, we expect a gradual shift towards an expansionary fiscal policy, which would positively impact GDP growth and put upward pressure on inflation and interest rates. We do not expect public budget consolidation to resume in the coming years. This also means that domestic fiscal policy rules could be relaxed. Nevertheless, we expect the Czech Republic to continue meeting the Maastricht criteria for public finance deficits and debt levels within our forecast horizon.

Budget implementation indicates that this year's plan will be met

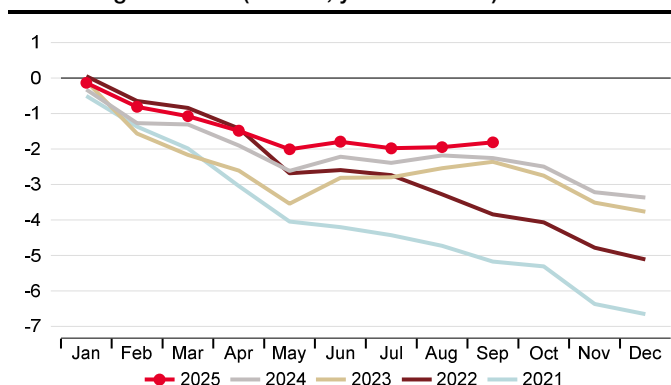
The state budget deficit reached CZK153.9bn by the end of September. This was CZK27.9bn lower than a year earlier. At 1.8% of GDP, the deficit for the first three quarters of this year was the lowest since 2019, the last pre-pandemic year. Overall, we do not believe the observed data indicate a risk of failing to meet the approved deficit for this year (CZK241bn).

State budget balance (CZKbn, ytd cumulative)



Source: Ministry of Finance, Macrobond, Economic & Strategy Research, Komerční banka

State budget balance (% GDP, ytd cumulative)

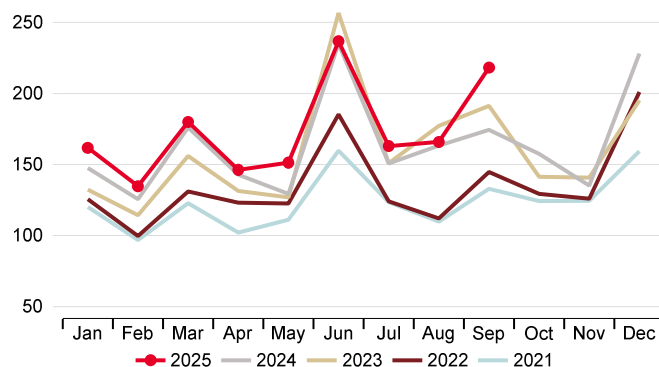


Source: Ministry of Finance, CZSO, Macrobond, Economic & Strategy Research, Komerční banka
Note: Nominal GDP in 2025 according to the KB forecast.

Year on year, expenditure increased by CZK85.2bn (+5.2%) by the end of September.

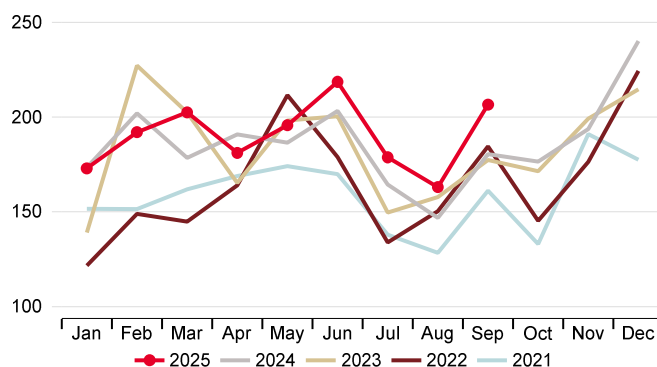
Compared with last year, current expenditures increased primarily due to transfers to local government budgets (+CZK21.2bn), which were allocated for education financing. Social benefits, the largest expenditure category, also contributed to the growth in total expenditure, increasing by CZK13.4bn. However, the increase in expenditure in these chapters was partially offset by lower non-investment transfers to state funds year over year. The 29.1% yoy increase in capital (investment) expenditure was mainly driven by higher investment transfers to the State Fund for Transport Infrastructure. **Revenues increased by CZK113.1bn (7.8%) yoy by the end of September.** As usual, the most significant revenue sources contributed significantly to this growth: social contributions (CZK39.9bn) and VAT (CZK22.4bn). The yoy growth rate of both items exceeds 7%, indicating continued robust consumer demand. Companies also remained in good shape, as evidenced by corporate income tax collection, which is likely to exceed the annual target this year.

State budget revenue (CZKbn, non-cumulative)



Source: Ministry of Finance, Macrobond, Economic & Strategy Research, Komerční banka

State budget expenditure (CZKbn, non-cumulative)



Source: Ministry of Finance, Macrobond, Economic & Strategy Research, Komerční banka

The deficit will grow next year, Czech fiscal rules could undergo revision

We expect the state budget deficit to reach CZK320bn next year. The outgoing government approved a state budget with a deficit of CZK286bn. The provision of an interest-free loan for the construction of new nuclear power plant units in Dukovany and an increase in defence spending were expected to contribute to the yoy deepening of the deficit from approximately CZK241bn this year. However, according to a statement by the Czech Fiscal Council², the budget does not include the CZK37.2bn that the State Fund for Transport Infrastructure is counting on for next year. As was the case after the last parliamentary elections in 2021, we expect the new government to revise the current budget for next year. Therefore, a provisional budget is likely in the first months of 2026, governed by the previous year's budget (in this case, 2025), with a maximum of one twelfth of the expenditures allocated to each month. Given the new government's indication of further spending priorities, we see the risk as skewed towards an even deeper deficit.

We do not expect any further visible consolidation of the public finances in the coming years. This also means that the budgetary policy rules should be relaxed. The current version of the Fiscal Responsibility Act requires reducing the structural deficit by 0.5pp of GDP, capping it at 1.75% in 2026. The same reduction is included in the Act for 2027. Starting in 2028, the ceiling for the structural balance will be 1%. The only exception to these rules is defence spending; anything above 2% of GDP will not be included in the structural balance.³ Considering that 1) the Czech Republic is among the third least indebted EU countries with public debt of 43.3% of GDP at the end of 2024, 2) European fiscal rules are less strict than domestic ones, and 3) the emerging government is signaling the need for further increases in public budget expenditures without a proportional increase in revenues, we assume that consolidation of the structural balance will not resume in the coming years. Nevertheless, in line with the pre-election statements of the winning parties, we expect the Czech Republic to continue meeting the Maastricht criteria for public finance deficits and debt levels.

The impact of discretionary fiscal policy measures on the economy, given the expected increase in the structural deficit, will be expansionary in 2026 and then roughly neutral.

² <https://www.rozpovovarada.cz/en/ke-stazeni/statement-of-the-czech-fiscal-council-on-the-current-and-expected-work-on-the-state-budget-for-2026-the-process-of-its-preparation-and-the-outlook-for-public-finances-in-the-coming-years/>

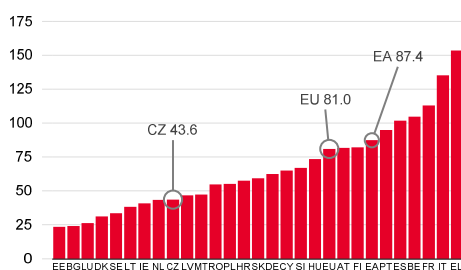
³ The 2026 budget approved by the outgoing government anticipates an increase of defense spending to 2.35% of GDP in 2026, but this is largely due to an increase in the transport infrastructure chapter, which may be problematic from the point of view of fiscal rules.

Following a visible reduction in the structural deficit of public finances last year, to which the consolidation package contributed, among other things, we estimate that fiscal restraint, measured by the approximate aggregate fiscal impulse, will completely disappear this year and will be offset next year by a renewed widening of the structural balance. The impact of fiscal policy on GDP and price dynamics is discussed in more detail in Box 1.

Box 1: Fiscal stimulus – temporary support for the economy, risk to price stability

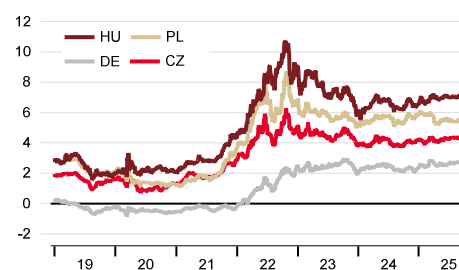
In our view, the likelihood of Czech fiscal policy easing remains high. This is primarily due to low overall debt in an international context and relatively strict national fiscal rules. The Czech Republic maintaining the best credit rating among Central and Eastern European countries is due in part to fiscal prudence. This has contributed to significantly lower financing costs for public debt and budget deficits compared to comparable countries with their own currencies. This box aims to describe the qualitative and quantitative impacts of fiscal expansion on key macroeconomic and financial variables.

Public debt in 2024 (% of GDP)



Source: Macrobond, Economic and Strategy Research, Komerční banka

10y bond yield (%)



Source: Bloomberg, Economic and Strategy Research, Komerční banka

Initially, fiscal expansion may lead to a temporary increase in economic activity. This is due to an improvement in aggregate demand.⁴ However, the associated inflationary pressures generally lead to a gradual increase in interest rates by the central bank and a rise in risk premiums on longer-term government bonds. The widening interest rate differential attracts additional capital into the country, strengthening the domestic currency on the foreign exchange market. Additionally, the exchange rate may appreciate in real terms due to domestic inflationary pressures, i.e. the inflation differential.

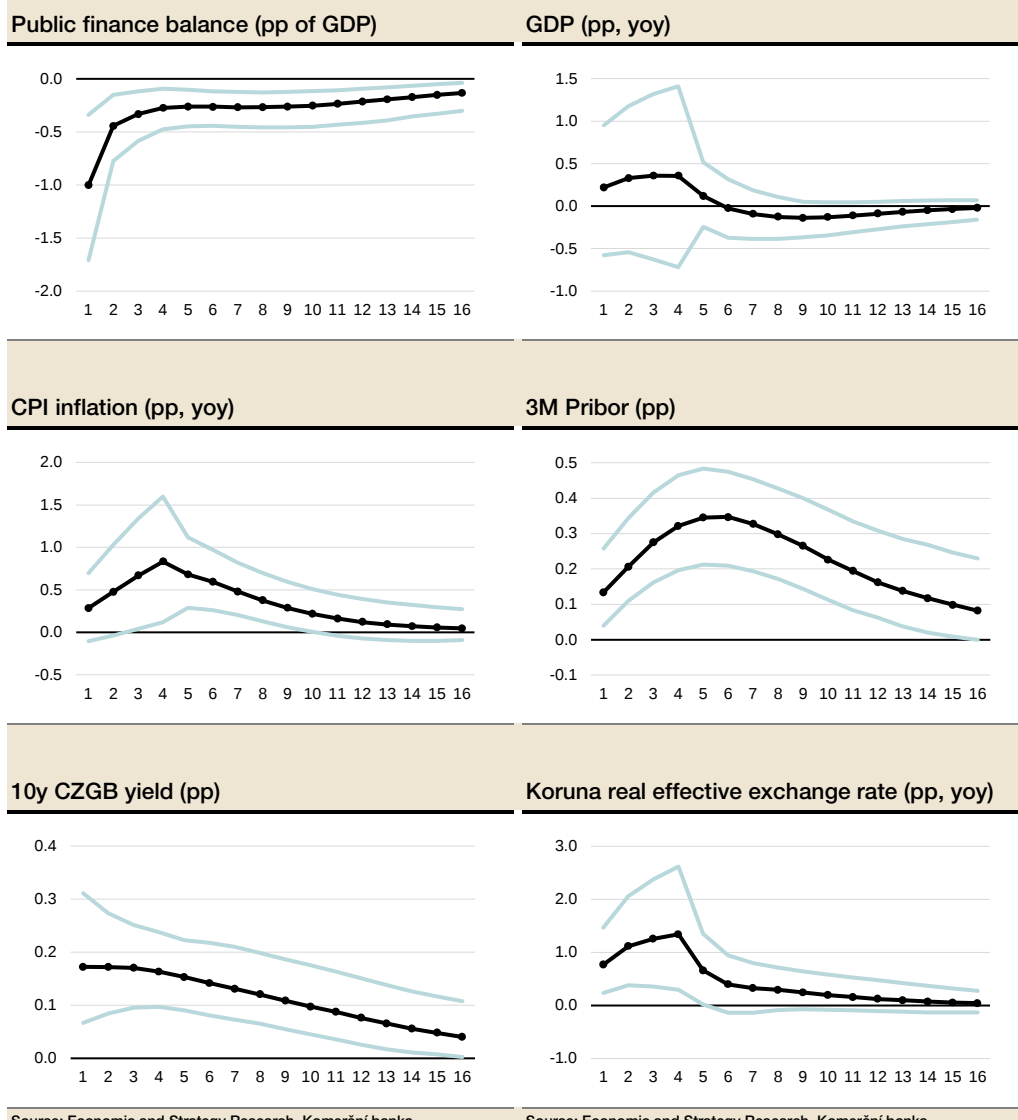
The positive effect on GDP fades over time and may eventually be completely offset. A combination of higher interest rates and a stronger real exchange rate restricts the economy. A stronger real exchange rate relatively reduces the competitiveness of domestic exporters in foreign markets while making imports cheaper. Higher interest rates also curb domestic demand, i.e. investment and consumption. Overall, fiscal expansion will likely only temporarily increase GDP and inflation.

The actual effect depends on the structure of the expansionary fiscal shock and the phase of the economic cycle. In general, investment (e.g. in infrastructure) tend to have more pro-growth (especially in the long term) and less pro-inflationary effects, while the opposite will be true for current expenditure. Research also shows that the size of the fiscal multiplier (the impact of fiscal policy on GDP) depends on whether the adjustment is on the revenue or expenditure side, with expenditure measures having a greater impact on economic activity. Furthermore, both within revenue and expenditure sides, the impacts of specific types of

⁴ Unless we assume the existence of so-called Ricardian agents, who would immediately start saving in response to fiscal expansion, because today's deficits = future taxes.

measures tend to differ.⁵ Some studies also point to higher fiscal multipliers, and thus the effectiveness of fiscal policy, during a recession.⁶ The impulse responses from the BVAR model⁷, which abstracts from these differences, are presented below. Therefore, these are responses to an unspecified fiscal shock in the form of a 1pp increase in the deficit/reduction in the public finance surplus relative to GDP. Given the quarterly frequency of the data and the estimated empirical persistence, this shock corresponds to an increase in the public finance deficit of around 0.5pp of GDP on an annual basis.

Impulse response functions of an expansive fiscal shock of 1pp of GDP from the estimated BVAR model (median and 68% credible intervals, x-axis – quarters)



Source: Economic and Strategy Research, Komerční banka

Source: Economic and Strategy Research, Komerční banka

⁵ For example: <https://www.cnb.cz/en/monetary-policy/monetary-policy-reports/boxes-and-articles/Partial-fiscal-multipliers-a-new-feature-of-the-CNB-forecast/>

⁶ For example: https://www.cnb.cz/export/sites/cnb/en/economic-research/galleries/research_publications/cnb_wp/cnbwp_2025_03.pdf

⁷ In addition to several exogenous variables, the BVAR used also includes six endogenous variables from the domestic economy, for which impulse responses are presented. With the exception of interest rates and bond yields, the variables were transformed into quarter-on-quarter (annualized) dynamics prior to estimation. The model works with quarterly data and contains four lags. The structural fiscal shock was identified on the basis of sign restrictions.

According to our simple empirical analysis, the positive impact of a more relaxed fiscal policy on GDP is debatable in the case of the Czech Republic, although it appears to be somewhat positive in the short term. Although the median response estimated on historical data is positive, the 68% credible interval shows that there is considerable uncertainty, not only about the size, but also the direction of the impact on real economic activity. Moreover, in the case of the median response, the cumulative impact on GDP converges to zero, which supports the hypothesis of a crowding-out effect of fiscal expansion. On the other hand, the positive response of inflation is significant. According to the model estimate, the central bank is also gradually responding to increased inflationary pressures by raising interest rates. As expected, the loosening of fiscal policy is also reflected in an increase in government bond yields and a real strengthening of the effective exchange rate of the koruna.

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We expect this year's public finances to end with a deficit of 2.2% of GDP. Next year, we anticipate the deficit to deepen to 2.8% of GDP.

Fiscal expansion should remain within the limits of the Maastricht criteria

Next year, we expect the public finance deficit to increase to 2.8% of GDP. Compared to the state budget, the public finance deficit as a whole will be reduced by the positive balance of local government finances, which have been in surplus since 2013. The public finance deficit should also be mitigated by continued financing for the completion of the nuclear power plant in the form of state loans. These loans are not included in the deficit in accrual (ESA) terms. In the coming years, the delayed positive effect of fiscal expansion on economic activity will contribute to a slight improvement in the balance relative to GDP. On our estimates, public sector debt relative to GDP will grow by an average of 1.1 percentage points (pp) per year from 2025 to 2029, reaching 48.7% of GDP in 2029.

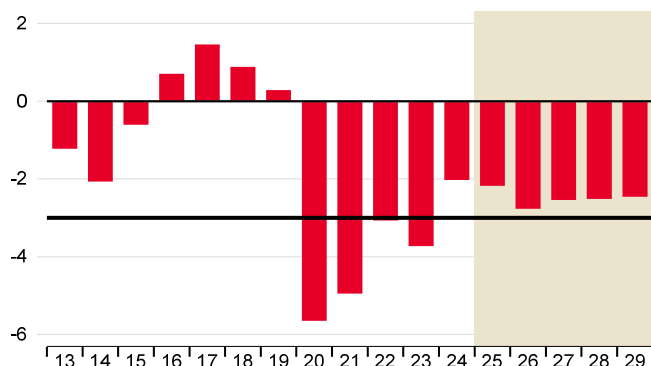
Public finance forecasts

	2024	2025f	2026f	2027f	2028f	2029f
Balance (% GDP)	-2.0	-2.2	-2.8	-2.5	-2.5	-2.5
Fiscal effort* (pp GDP)	0.5	-0.1	-0.7	0.0	0.1	0.2
Public debt (CZKbn)	3488.5	3728.5	4048.5	4348.5	4648.5	4958.5
Debt ratio (% GDP)	43.3	43.9	45.7	46.6	47.7	48.7

Source: CZSO, Macrobond, Ministry of Finance for published data, Economic & Strategy Research, Komerční banka

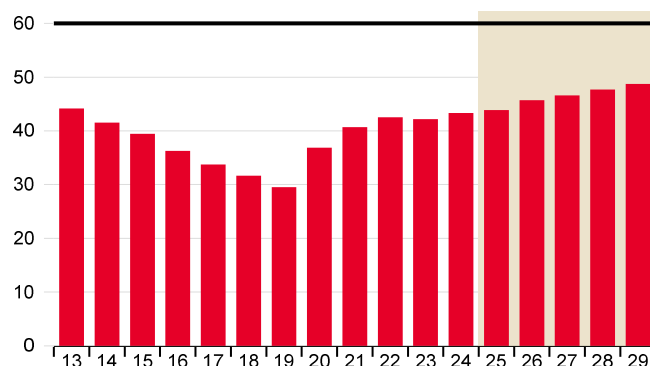
Note: fiscal effort is measured as the year-on-year change in the public finance balance, adjusted for the economic cycle and one-off operations on GDP in pp.

Public finance balance (% of nominal GDP)



Source: CZSO, Macrobond, Economic & Strategy Research, Komerční banka

Public debt (% of nominal GDP)



Source: CZSO, Macrobond, Economic & Strategy Research, Komerční banka

Summary forecast table

	Q1 25	Q2 25	Q3 25	Q4 25	Q1 26	Q2 26	Q3 26	Q4 26	2024	2025	2026	2027	2028	2029
GDP and its breakdown														
GDP (real, yoy, %)	2.4	2.6	2.0	1.3	1.0	1.1	1.8	2.6	1.1	2.1	1.6	2.8	2.1	2.3
Household consumption (real, yoy, %)	2.3	3.4	2.7	1.9	1.9	1.5	1.9	2.2	2.2	2.6	1.9	2.4	2.0	2.3
Government consumption (real, yoy, %)	1.9	2.6	1.4	1.1	1.6	0.8	2.4	3.2	3.2	1.8	2.0	2.6	1.9	2.1
Fixed investment (real, yoy, %)	-1.7	-0.2	1.0	2.6	2.7	2.7	2.6	3.1	-3.1	0.4	2.8	3.2	2.3	2.2
Net exports (contribution to yoy)	-0.4	-0.9	-0.7	-0.6	-1.4	-0.2	-0.1	0.0	0.7	-0.7	-0.4	0.3	0.2	0.2
Inventories (contribution to yoy)	1.8	1.3	0.9	0.2	0.3	-0.1	-0.1	0.0	-0.4	1.1	0.1	0.0	0.1	0.1
Monthly data from the real economy														
Foreign trade (CZKbn)	77.5	60.0	34.1	45.4	89.2	56.6	16.4	36.9	220.5	217.0	199.2	224.0	245.2	257.4
Exports (nominal, yoy, %)	6.1	3.0	0.7	-5.2	-3.9	-5.2	0.8	6.5	5.0	1.1	-0.6	6.0	5.9	5.4
Imports (nominal, yoy, %)	7.0	4.2	0.1	-5.9	-5.2	-5.2	2.4	7.6	2.8	1.3	-0.3	5.7	5.8	5.4
Industrial production (real, yoy, %)	0.5	1.2	0.0	-0.1	-1.3	-0.9	1.5	3.7	-1.0	0.4	0.7	3.5	2.9	2.7
Construction output (real, yoy, %)	7.3	10.3	0.7	12.8	9.6	8.0	0.8	2.0	-1.6	7.8	5.1	3.0	2.8	2.9
Retail sales (real, yoy, %)	3.4	4.8	3.4	2.6	2.1	1.1	1.6	2.3	4.5	3.6	1.8	2.8	2.4	2.3
Labour market														
Wages (nominal, yoy, %)	6.6	7.8	6.8	6.1	5.3	4.6	5.2	5.6	7.2	6.8	5.2	5.1	4.2	4.5
Wages (real, yoy, %)	3.8	5.3	4.2	4.4	3.6	3.0	3.8	3.9	4.7	4.4	3.6	2.6	2.0	2.4
Unemployment rate (MLSA, %)	4.3	4.2	4.5	4.6	5.0	4.5	4.6	4.5	3.8	4.4	4.6	4.3	4.4	4.7
Unemployment rate (ILO 15+, %)	2.6	2.7	3.0	3.0	3.3	3.2	3.2	3.0	2.6	2.8	3.2	2.8	2.9	3.3
Employment (ILO 15+, yoy, %)	0.5	1.5	1.4	1.2	-0.2	-0.1	-0.1	0.3	2.6	1.1	-0.1	0.7	0.2	0.0
Consumer and producer prices														
CPI Inflation (yoy, %)	2.7	2.4	2.5	2.1	1.4	1.4	1.3	1.7	2.4	2.4	1.5	2.4	2.2	2.0
Taxes (contribution to yoy inflation)	0.2	0.2	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.2	0.1	0.1	0.0	0.0
Core inflation (yoy, %) (*)	2.5	2.8	2.8	2.6	2.3	2.0	2.0	2.2	2.5	2.7	2.1	2.3	2.3	2.1
Food prices (yoy, %) (*)	4.2	3.8	3.2	2.3	2.1	1.8	1.8	1.9	0.7	3.4	1.9	2.2	2.3	2.0
Fuel prices (yoy, %) (*)	-4.4	-12.2	-6.8	-7.2	-10.6	-5.0	-5.9	-0.3	-0.9	-7.6	-5.5	4.4	0.6	0.3
Regulated prices (yoy, %)	1.2	0.9	1.1	0.6	-1.1	-1.2	-1.0	-0.7	6.3	1.0	-1.0	1.8	2.1	2.0
Producer prices (yoy, %)	0.0	-0.9	-0.9	-2.3	-1.2	-0.2	-0.6	-0.2	0.8	-1.0	-0.5	2.1	2.9	2.3
Financial variables														
2W Repo (% , average)	3.9	3.6	3.5	3.5	3.5	3.5	3.5	3.5	5.1	3.6	3.5	3.5	3.4	3.0
3M PRIBOR (% , average)	3.8	3.6	3.5	3.5	3.5	3.6	3.6	3.6	5.0	3.6	3.6	3.6	3.5	3.1
EUR/CZK (average)	25.1	24.9	24.5	24.4	24.4	24.3	24.2	24.1	25.1	24.7	24.3	24.1	24.1	23.9
External environment														
GDP in EMU (real, yoy, %)	1.6	1.5	1.3	1.2	0.9	1.1	1.2	1.3	0.8	1.4	1.1	1.3	1.2	1.2
GDP in Germany (real, yoy, %)	0.3	0.2	0.4	0.4	0.4	1.0	1.2	1.4	-0.5	0.3	1.0	1.3	1.1	1.1
CPI in EMU (yoy, %)	2.4	2.0	2.1	1.8	1.4	1.6	1.4	1.4	2.4	2.1	1.5	2.0	2.2	2.3
Brent oil price (USD/bbl, average)	75.0	67.3	69.5	60.0	59.0	57.0	53.0	52.0	80.8	67.9	55.3	60.1	66.7	70.9
EUR/USD (quarter eop, year average)	1.05	1.13	1.17	1.19	1.22	1.25	1.25	1.25	1.08	1.14	1.24	1.25	1.25	1.25

Source: CZSO, CNB, MLSA, Bloomberg, Macrobond, Economic & Strategy Research, Komerční banka
 Note: (*) these parts of inflation are adjusted for the primary effect of indirect tax changes

The Czech IRS market and government bonds



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Fiscal stimulus to push rates higher

In our view, the temporary slowdown in domestic economic activity and the resulting decline in market optimism could temporarily halt the upward trend in koruna market interest rates. However, we expect them to resume their upward trend next year due to fiscal policy easing both domestically and abroad. Despite a temporary decline in headline inflation below 2%, we believe that the CNB will respond to the risk of a more expansionary fiscal policy by keeping the rates unchanged next year. A deeper government budget deficit will also be reflected in higher CZGB issuance, increased yields and wider ASWs. If domestic fiscal rules are loosened and pension reform is canceled, there will also be a potential downgrade of the Czech Republic's sovereign credit rating.

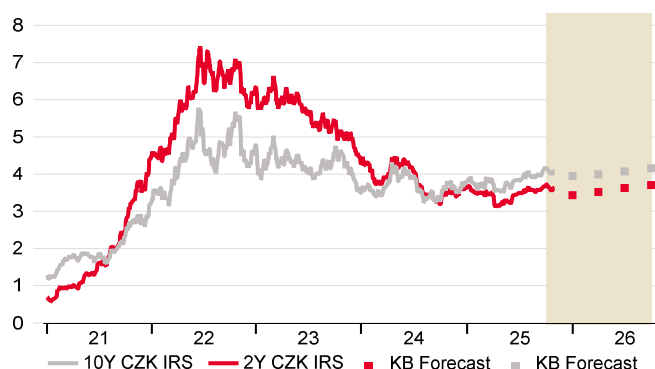
Market interest rates in Europe are reluctant to fall

In recent months, global market interest rates have not been in sync. While US dollar rates have fallen due to concerns about the negative impact of tariffs and shutdowns on the US economy, political uncertainty, the ECB's possible completion of its rate cut cycle, and the trend toward fiscal easing at the longer end of the curve have prevented a similar development in Europe. Additionally, the increased borrowing needs of European countries are colliding with weaker demand compared to the pre-pandemic period. There is no longer an important counterparty in the form of the ECB, which is no longer expanding its balance sheet by purchasing government bonds.

The CNB will not lower rates any further either this year or next. Fiscal stimulus will push up koruna market interest rates. Similar to our expectations, the koruna money market does not anticipate additional interest rate reductions in the near future. In the short term, we see room for market interest rates to fall, mainly in connection with a slowdown in the domestic economy in the second half of 2025. This slowdown could dampen the markets' still relatively optimistic assumptions about further (accelerating) growth in the Czech economy. However, fiscal expansion should become the dominant factor next year. We expect this to outweigh the temporary decline in headline inflation to the lower half of the CNB's tolerance band (due to cheaper energy) on the koruna market interest rate curve. In our view, the longer end of the curve will be driven primarily by the loosening of fiscal rules, which has already occurred in Germany and is part of our baseline scenario for the Czech Republic. Compared to our previous forecast, we have revised our outlook for koruna rates upward across the entire horizon due to the abandonment of the assumption of further CNB monetary policy easing, a less pronounced domestic economic slowdown, and a more expansionary fiscal policy.

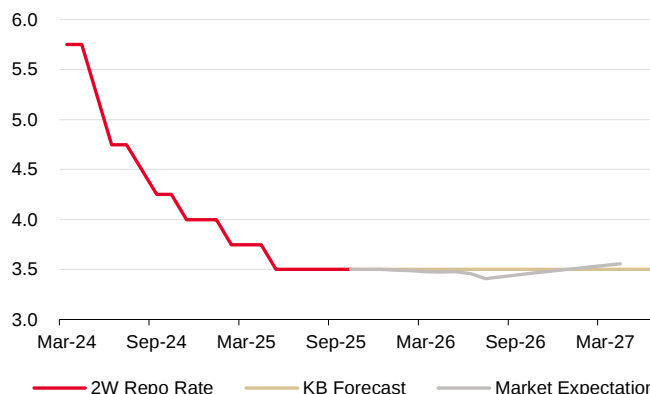
The increase in koruna rates should be temporarily prevented by a slowdown in domestic economic activity. However, fiscal policy easing should already be evident next year, pushing rates upwards.

IRS forecast (%)



Source: Bloomberg, Economic & Strategy Research, Komerční banka

Expected CNB key interest rate path as of 29 October 2025 (%)



Source: Bloomberg, CNB, Economic & Strategy Research, Komerční banka

CZK IRS outlook (end of period, %)

	4Q25f	1Q26f	2Q26f	3Q26f
2y	3.45	3.50	3.65	3.70
5y	3.70	3.75	3.85	3.95
10y	3.95	4.00	4.05	4.15

Source: Economic & Strategy Research, Komerční banka

Euro market consistently offers lower interest rates

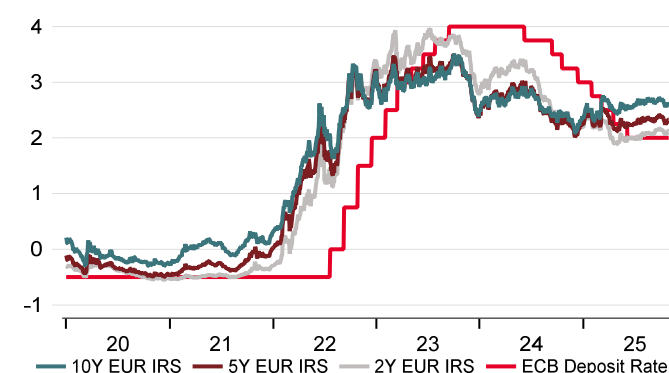
Interest rate hedging conditions on the koruna market have worsened as they are being influenced by foreign developments and the hawkish stance of the CNB. In our view, the economic slowdown could temporarily improve conditions. However, they should start to deteriorate again in 2026 as fiscal policy is loosened. The forward market offers higher rates across the curve compared to spot IRS. Interest rates in the eurozone remain significantly lower than those in the Czech Republic.

CZK forward interest rate swaps (% p.a., vs 6M Pribor, 1Y vs 3M Pribor)

	Maturity					
	1Y	2Y	3Y	5Y	10Y	
Spot	3.56	3.62	3.71	3.82	4.08	
3M	3.57	3.67	3.75	3.85	4.10	
6M	3.59	3.71	3.78	3.88	4.12	
9M	3.64	3.75	3.82	3.91	4.15	
1Y	3.70	3.80	3.85	3.95	4.17	
2Y	3.90	3.93	3.96	4.06	4.26	
3Y	3.97	4.00	4.06	4.17	4.32	

Source: Bloomberg, Economic & Strategy Research, Komerční banka, as of 29 October 2025

Euro area rates (%)



Source: Bloomberg, Economic & Strategy Research, Komerční banka

CZGB issuance to rise significantly next year

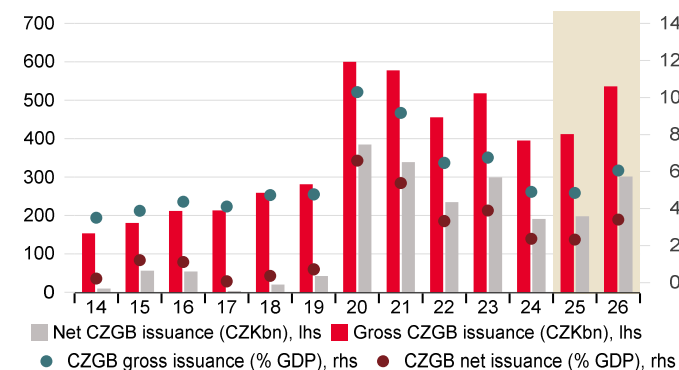
We expect the cash deficit of the state budget to reach CZK240bn this year and increase to CZK320bn next year. This year, combined with other financing needs, particularly repayments of maturing bonds and treasury bills, we estimate that gross issuance of koruna bonds will be in the upper half of the range indicated by the Ministry of Finance (MinFin). This assumes the issuance of CZK government bonds with a total volume of CZK350-450bn (CZK150-250bn in 2H25). Overall, the MinFin has already issued CZK318.8bn CZGBs on the primary market and CZK28.8bn on the secondary market as of 22 October this year. In addition, it has concluded switch operations for bonds maturing this year for another CZK17.9bn. So far in 2025, foreign currency issues have only been carried out on the secondary market and with a total amount of EUR250m. To a significant extent, treasury bills have also been used to cover borrowing needs so far this year. T-bills maturing next year have been issued in the amount of CZK45bn, supplemented by EUR1.0bn in bills maturing in 2026. **In 2026, both gross and net issuance will increase significantly.** In the case of gross issuance, this should be driven, among other things, by higher repayments of maturing T-bonds and T-bills (+CZK51.6bn) and a deeper cash deficit in the state budget (+CZK80.0bn). Net issuance should reach roughly the same level as in 2023.

Funding programme and issuance activity (CZKbn)

	2025		2026	
	MinFin	KB	MinFin	KB
State budget deficit	241.0	240.0	225.0	320.0
Transfers and other operations of state financial assets	7.4	7.4	2.5	2.5
T-bonds denominated in local currency redemptions	214.2	214.2	255.0	235.0
T-bonds denominated in foreign currency redemptions	0.0	0.0	0.0	0.0
Redemptions and early redemptions on savings bonds	20.4	20.4	15.7	15.7
Money market instrument redemptions	81.3	81.3	20.0	112.1
Redemption of T-bills		81.3		112.1
Redemption of other money market instruments		0.0		0.0
Repayments on credits and loans	3.2	3.2	26.5	26.5
Total financing needs	567.5	566.5	544.7	711.8
Money market instruments		112.1		110.0
T-bills		112.1		110.0
Other money market instruments		0.0		0.0
Gross issuance of CZK T-bonds on domestic market		411.9		536.5
Gross issuance of EUR T-bonds on domestic market/eurobond		6.3		24.3
Gross issuance of government savings bonds		1.3		1.0
Received credits and loans		20.0		20.0
Financial asset and liquidity management		15.0		20.0
Total financing sources		566.5		711.8
Gross borrowing requirement		551.5		691.8
Net CZGB issuance		197.7		301.5

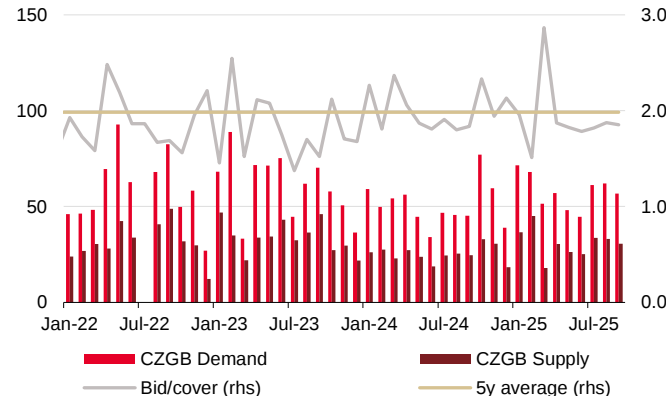
Source: MinFin, Economic & Strategy Research, Komerční banka

CZGB issuance



Source: MinFin, Economic & Strategy Research, Komerční banka

CZGB primary market (CZKbn)



Source: MinFin, CNB, Economic & Strategy Research, Komerční banka

Bond yields will rise more sharply than market interest rates

Government bond yields lagged behind the recent rise in IRS, resulting in a narrowing of ASW spreads and thus a relative richening. Given the expected fiscal expansion and loosening of domestic fiscal rules (see the *Fiscal Policy* chapter for more details) and the related increase in issuance activity, we expect the spread between bond yields and IRS to gradually widen over the forecast horizon. The increase in government bond yields should therefore be slightly more pronounced than in the case of koruna market interest rates.

CZGB yield forecast (end of period)

	4Q25f	1Q26f	2Q26f	3Q26f
2y CZGB yield (%)	3.40	3.50	3.60	3.70
5y CZGB yield (%)	3.80	3.85	3.95	4.05
10y CZGB yield (%)	4.30	4.35	4.45	4.60
10y CZGB ASW (bp)	35	35	40	45

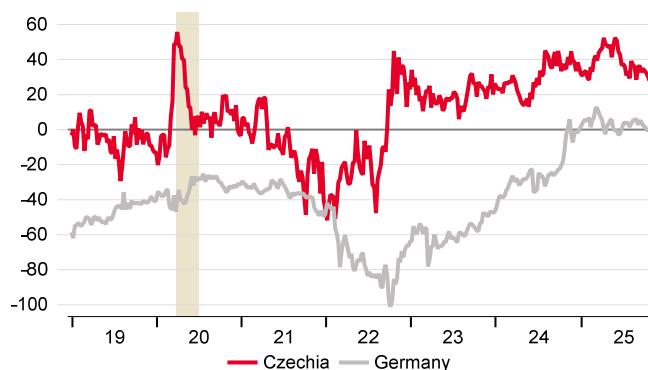
Source: Economic & Strategy Research, Komerční banka

CZGB yield forecast (%)



Source: Bloomberg, Economic & Strategy Research, Komerční banka

10y bond ASW (bp)



Source: Bloomberg, Economic & Strategy Research, Komerční banka

Note: ASW= 10y CZGB yield - 10y CZK IRS; shading indicates recessionary period in Czechia

The Czech Republic's credit rating remains unchanged (Aa3/AA-) with a stable outlook, but we believe that risks are increasing due to the expected fiscal expansion. The Czech Republic continues to have the best rating of all countries in Central and Eastern Europe. However, in their latest assessments, [Fitch](#) and [Moody's](#) made their current rating conditional on further consolidation or at least no deterioration in the condition of domestic public finances. At the same time, they point out that an important long-term challenge is the ageing population and the associated pressure on public finances. In our baseline scenario, we expect an increase in the public finance deficit, followed by a revision of domestic fiscal rules. In the medium term, the risk of a downgrade is also increased by the pre-election promise by some parties in the emerging government coalition to repeal the approved pension reform, which, among other things, gradually increases the retirement age after 2030 and slows the growth of pensions. The implemented reform should save around 1.5% of GDP per year in pension expenditure from the 2050s onwards compared with the scenario of maintaining the status quo.⁸

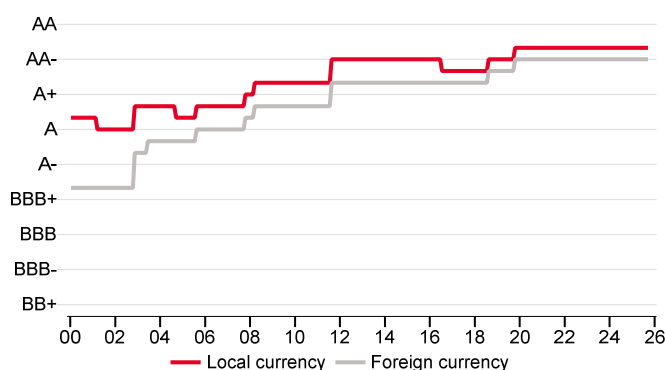
Sovereign rating overview

	Local currency	Outlook	Foreign currency	Outlook
S&P	AA	STABLE	AA-	STABLE
Moody's	Aa3	STABLE	Aa3	STABLE
Fitch	AA-	STABLE	AA-	STABLE

Source: Bloomberg, Economic & Strategy Research, Komerční banka

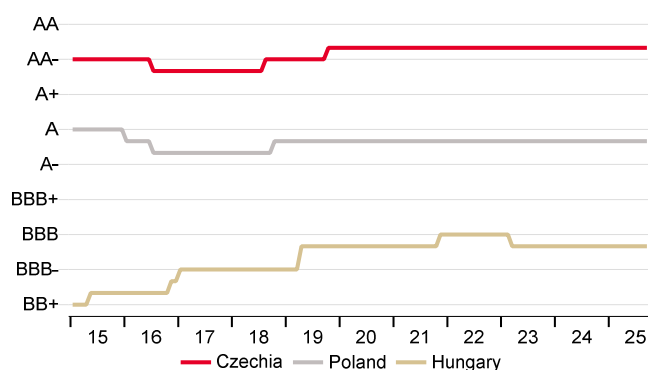
⁸ https://economy-finance.ec.europa.eu/document/download/f6fd1e81-2434-4729-bc36-28f9e6a79eb9_en?filename=CZ_final_2025.pdf

The Czech Republic's rating (average of Fitch, S&P and Moody's)



Source: Bloomberg, Economic & Strategy Research, Komerční banka

Rating in CE3 – local currency (avg. of Fitch, S&P and Moody's)



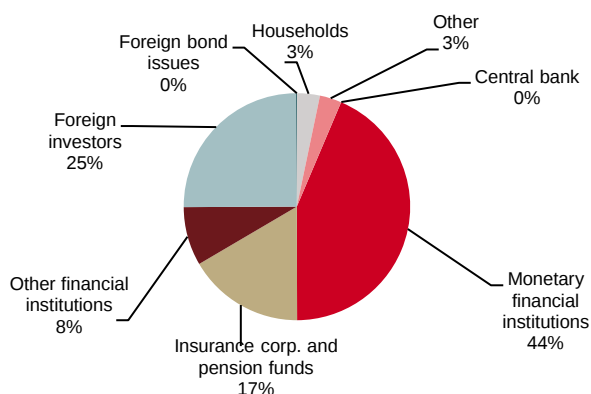
Source: Bloomberg, Economic & Strategy Research, Komerční banka

Government bond overview

Government bond overview										Rich-cheap analysis									
Bond	Dur.	Issued last 90D	Issuance limit	Yield	Δ1W	Δ1M	FX hedged	ASW	Δ1W	Δ1M	Min	90D	Max	Z-Score	Rank	Spline spread	Rank	Carry Roll 90D	Rank
6.00 Feb-26	0.3	0.0	71%	3.07	-10	-18	1.67	-49	-1	-11	-54		-13	-2.1	21	12.6	25	-173.3	25
1.00 Jun-26	0.6	0.0	100%	3.30	2	-2	2.01	-29	0	3	-32		-6	-1.1	11	-3.9	4	-15.5	24
0.25 Feb-27	1.2	0.0	108%	3.57	7	9	2.21	-8	2	14	-23		-2	0.5	2	-19.9	1	2.8	22
2.50 Aug-28	2.6	0.0	94%	3.61	1	-12	2.24	-14	-3	-2	-15		5	-2.1	20	1.0	18	3.8	19
5.50 Dec-28	2.7	0.0	88%	3.62	3	-6	2.25	-14	-3	3	-22		0	-0.6	6	4.9	23	3.7	20
5.75 Mar-29	3.0	0.0	103%	3.65	3	-10	2.30	-12	-2	-1	-16		4	-0.8	7	5.9	24	3.9	18
2.75 Jul-29	3.4	0.0	100%	3.75	3	-12	2.40	-6	-2	-2	-7		10	-1.7	17	0.2	15	4.5	13
0.05 Nov-29	3.9	0.0	61%	3.80	2	-12	2.43	-6	-3	-2	-4		11	-2.5	23	-0.1	14	4.6	12
0.95 May-30	4.3	0.0	100%	3.86	3	-15	2.50	-2	-4	-3	-2		13	-2.7	25	0.5	17	4.8	9
5.00 Sep-30	4.3	5.0	121%	3.91	0	-15	2.61	6	-4	-3	-1		18	-1.3	16	0.4	16	4.9	6
1.20 Mar-31	5.0	0.0	100%	4.01	3	-13	2.64	7	-3	-1	1		17	-1.7	19	-3.4	5	5.0	3
6.20 Jun-31	4.7	4.9	100%	3.98	1	-9	2.71	11	-3	3	-1		18	-0.1	3	2.5	21	5.0	4
1.75 Jun-32	6.0	0.0	100%	4.15	4	-12	2.79	13	-2	-1	5		22	-1.0	10	-2.5	7	5.0	5
4.50 Nov-32	5.9	5.8	127%	4.19	2	-13	2.89	21	-3	-2	12		31	-0.6	5	-2.4	8	5.0	2
3.00 Mar-33	6.3	6.1	70%	4.25	4	-13	2.91	21	-2	-2	16		31	-1.2	13	-4.8	3	5.1	1
2.00 Oct-33	7.1	0.0	100%	4.33	5	-13	2.95	22	-2	-3	14		32	-0.9	9	-6.9	2	4.9	8
4.90 Apr-34	6.7	6.9	113%	4.33	4	-14	3.05	28	-1	-3	19		36	-0.2	4	-1.9	9	4.9	7
4.25 Oct-34	7.3	12.9	47%	4.37	5	-13	3.07	28	-1	-2	22		39	-0.8	8	-1.8	10	4.7	10
3.50 May-35	7.8	0.0	101%	4.37	6	-17	3.05	22	0	-6	19		35	-1.7	18	3.8	22	4.4	14
5.30 Sep-35 *	7.6	13.2	16%	4.46	8	-9	3.20	35	0	1	28		37	1.0	1	-2.6	6	4.7	11
3.60 Jun-36	8.4	13.0	63%	4.50	7	-12	3.17	29	1	-3	26		43	-1.2	12	-1.1	11	4.4	15
4.20 Dec-36	8.3	0.0	100%	4.51	5	-11	3.20	30	0	-2	27		46	-1.2	14	1.5	20	4.3	16
1.95 Jul-37	9.9	0.0	62%	4.57	4	-11	3.16	24	-1	-3	24		41	-2.3	22	-0.7	12	3.9	17
1.50 Apr-40	12.0	0.6	64%	4.70	5	-11	3.25	24	0	-2	27		45	-2.6	24	1.2	19	3.2	21
4.00 Apr-44	12.2	2.3	15%	4.83	4	-2	3.51	43	-1	6	37		63	-1.3	15	-0.6	13	2.8	23

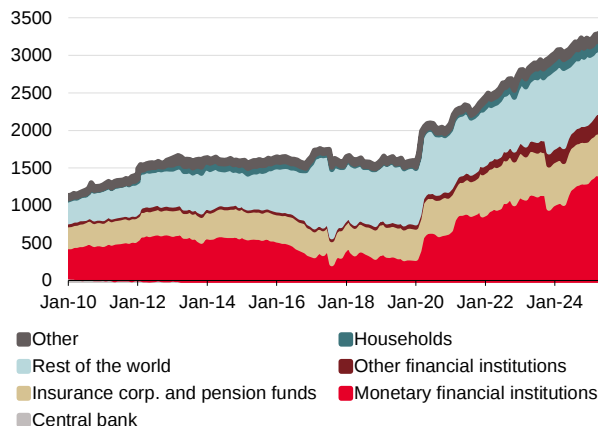
Source: Economic & Strategy Research, Komerční banka; Note: more details in CZGB Auction Alerts

Holdings of CZK government debt (August 2025)



Source: MinFin, Economic & Strategy Research, Komerční banka

Holdings of CZK government debt



Source: MinFin, Economic & Strategy Research, Komerční banka

Czech FX market



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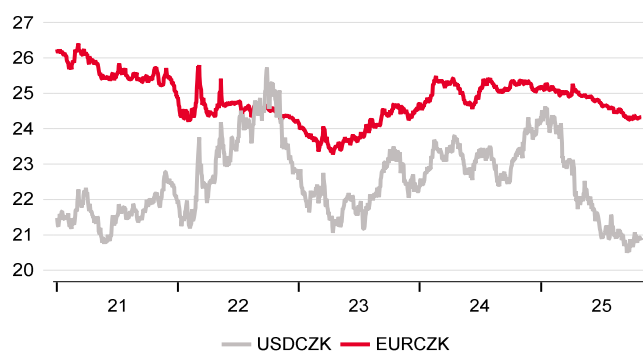
Koruna takes a breather

In recent months, the Czech koruna has continued to strengthen against the euro, despite the fact that the interest rate differential is no longer widening and the expected growth advantage of the Czech economy over the euro area is narrowing. In our view, the koruna's recent appreciation has been faster than what would be consistent with improving economic fundamentals. The koruna's main driver has been positive sentiment on global foreign exchange markets. While we anticipate continued weakening of the US dollar, the momentum of the domestic economy is slowing in the second half of this year. This should temper the still relatively optimistic market expectations regarding Czech economic growth. Therefore, before the positive effects of fiscal policy easing gradually kick in in 2026, we expect the koruna to temporarily interrupt its strengthening trend for the rest of this year and into next year.

The strengthening of the CZK is getting ahead of fundamentals

Supported by positive sentiment, the koruna strengthened further against the euro, reaching an almost two-year high. Given the CNB's consistently hawkish rhetoric, the interest rate differential no longer widened, so it was rather secondary to the koruna's spot rate during the summer. Positive sentiment became the main driving force behind the domestic currency, while the US dollar came under pressure on global markets. While our forecast anticipates continued dollar weakness, reaching EURUSD 1.25 by the end of next year, we estimate that other factors will offset the positive impact on the koruna's exchange rate against the euro.

CZK exchange rates



Source: Bloomberg, Economic & Strategy Research, Komerční banka

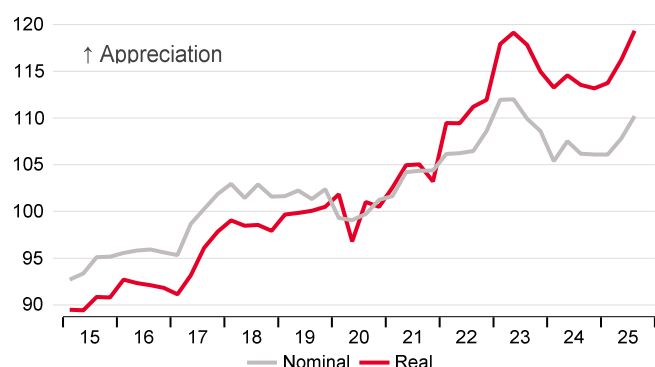
EURCZK and interest rate differential



Source: Bloomberg, Economic & Strategy Research, Komerční banka

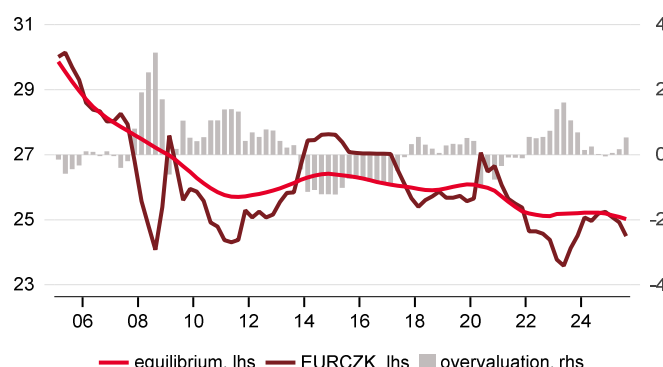
The overvaluation of the koruna is preventing further strengthening. Since August, the interest rate differential between the Czech Republic and the euro area has remained relatively stable. Markets remain convinced that the CNB will not cut interest rates further in this cycle and that the next change will be an increase. In our view, this leaves little room for the koruna to receive additional support from the interest rate differential. Our equilibrium exchange rate model indicates that the koruna is overvalued against the euro. The downward revision of expected GDP growth in 2026 will also negatively impact the koruna in the coming months. We believe this will be affected by the slowdown in domestic economic activity in the second half of this year, which markets have not yet fully accounted for.

Koruna effective exchange rate (2020=100)



Source: CNB, Macrobond, Economic & Strategy Research, Komerční banka
Note: Real effective exchange rate is deflated by GDP deflator.

Equilibrium EURCZK exchange rate

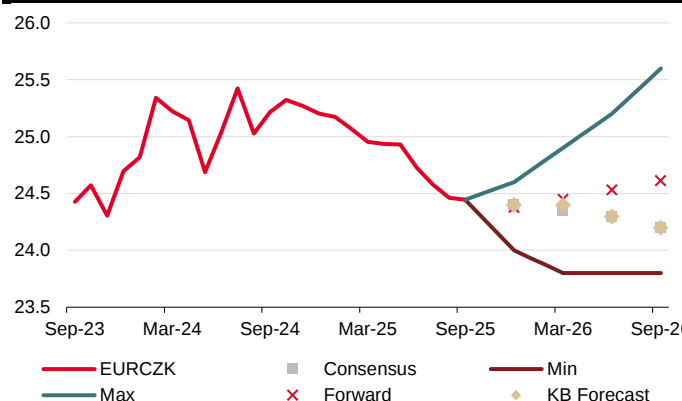


Source: Macrobond, Economic & Strategy Research, Komerční banka
Note: The estimated equilibrium exchange rate is based on a model of the economy's internal (output gap) and external (net export-to-GDP gap) equilibrium.

We have revised our forecast for the EURCZK exchange rate to significantly stronger levels. This is due to the continued resilience of the domestic economy, higher expected CNB rates, and more favourable global sentiment.

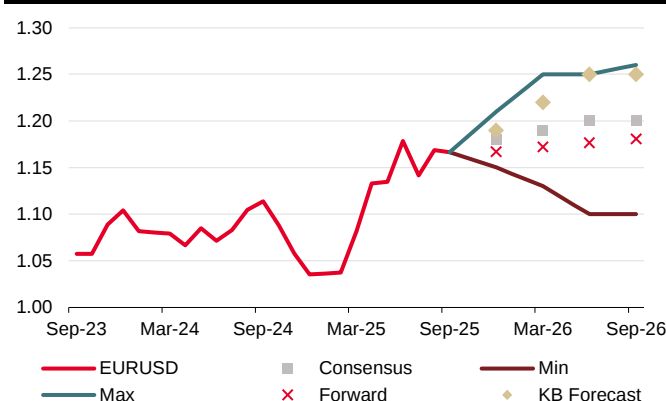
Overall, we do not expect the koruna to continue its recent appreciation against the euro in the coming months. We predict that the EURCZK exchange rate will reach 24.40 at the end of 4Q25 and 1Q26. Gradual strengthening should then resume, partly due to the easing of domestic fiscal policy (the response of the real exchange rate to fiscal expansion is discussed in *Box 1*). However, due to the domestic economy's lower growth potential compared to the pre-pandemic period, this strengthening will likely be gradual.

Expected EURCZK path, Bloomberg consensus (as of 29 October 2025)



Source: Bloomberg, Economic & Strategy Research, Komerční banka

Expected EURUSD path, Bloomberg consensus (as of 29 October 2025)



Source: Bloomberg, Economic & Strategy Research, Komerční banka, SG Cross Asset Research

Koruna exchange rate forecast (end of period)

	4Q25f	1Q26f	2Q26f	3Q26f
EURCZK	24.40	24.40	24.30	24.20
USDCZK	20.50	20.00	19.45	19.35
EURUSD	1.19	1.22	1.25	1.25

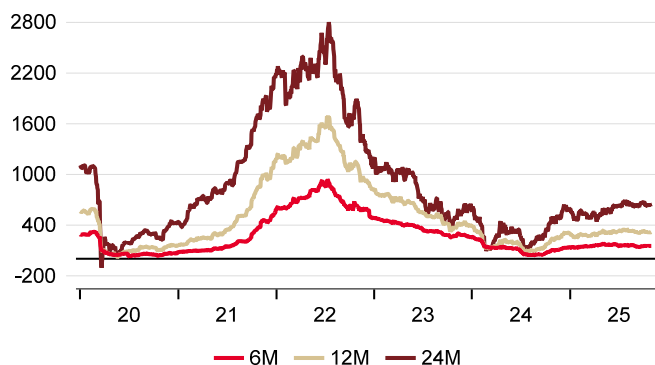
Source: Economic & Strategy Research, Komerční banka, SG Cross Asset Research

Further developments remain subject to considerable uncertainty

Compared to our baseline scenario, the risks are two-sided. They mainly relate to general uncertainty about the impact of tariff barriers on the Czech economy and the EU, and the monetary policy settings of the CNB and the ECB. The ongoing war in Ukraine also remains a source of uncertainty that could affect market perceptions of Central European currencies.

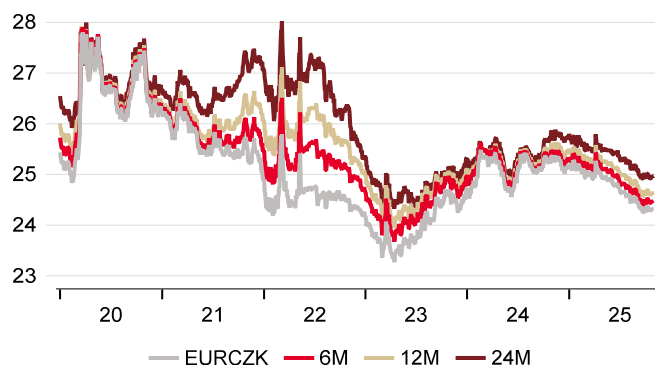
Markets do not expect any major fluctuations in the koruna exchange rate in the coming months. Implied volatility and the global currency market volatility index remain low. In our baseline scenario, conditions for hedging should not deteriorate significantly further for exporters with euro exposure until the end of this year, given the slowdown in domestic economic activity and the return of inflation to target.

Forward points



Source: Bloomberg, Economic & Strategy Research, Komerční banka

Forward vs spot exchange rate: EURCZK



Source: Bloomberg, Economic & Strategy Research, Komerční banka

Banking sector



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Credit activity gearing up for broader gains

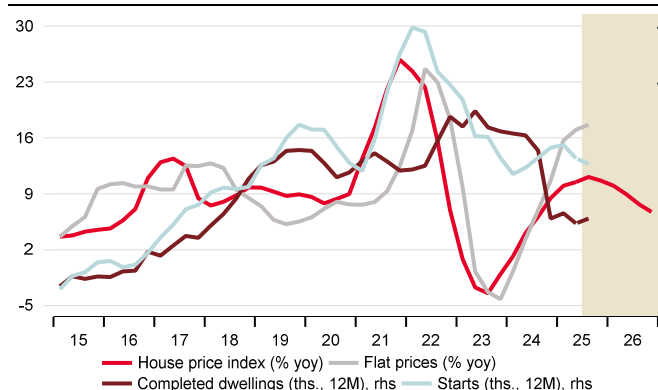
Credit growth remains two-tiered, driven by the retail segment, while business loans are lagging significantly behind. In 2026, we expect credit activity to exhibit solid growth across segments on the back of the fiscal boost and the related rise in aggregate demand. Growth in housing and consumer loans is set to remain strong, while business loan demand should pick up more noticeably. The housing and mortgage markets are overheating, and we believe that there is limited potential for an even stronger expansion. We expect house price growth to slow but remain high. Mortgage lending should continue to drive strong credit growth. Tightening financial conditions could slightly curb overall credit appetite. Nevertheless, it should improve in 2026 as the economy recovers from a temporary slowdown and returns to stronger growth. The slight cooling of the domestic economy should not prompt a major rise in credit risk on bank portfolios.

Housing and mortgage markets in overheat

The housing and mortgage market expansion is overheating. We do not expect house prices or monthly mortgage volumes to post stronger growth. However, growth in both areas should remain solid.

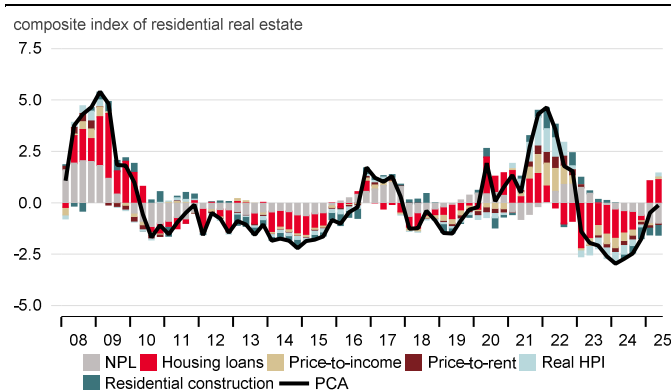
House price growth is set to slow but remain high. The House Price Index (HPI) shows house prices up 10.5% yoy in 2Q25. Although qoq growth stalled at 2.6%, it was slower vs 4Q24 (+2.9%). We expect sequential dynamics to eventually ease and estimate HPI growth at 10.6% in 2025, slowing to a still high 8.3% in 2026. However, signs of a slowdown are not yet clear cut. Asking prices of flats increased by 17.7% yoy in 3Q25 and grew at a similar pace qoq as in 2Q (+3.7%). Realised prices for flats showed a slowdown for second-hand apartments qoq, while growth accelerated qoq for new builds in Prague. *Flat Zone* data indicates a slowdown in yoy growth of Prague first-sale flats to 11.2% in 3Q, down from 13.2% in 2Q. We expect the overheating phase to slow as cyclical factors weaken – lower wage growth and the volume of households' excess savings, limited room for further decline in mortgage rates, and a cooling labour market. However, in the medium term, upward pressures dominate. These include demographic trends (immigration, *single* households, etc.), the relative tax advantage of real estate assets and insufficient residential construction. Nonetheless, we think that the pro-inflationary impulse from the housing market has largely been exhausted, and house prices are unlikely to push inflation up further.

House price growth could be near its peak



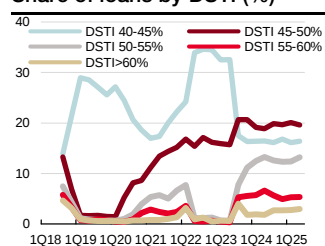
Source: CZSO, Macrobond. Economic & Strategy Research, Komerční banka
Note: data on dwelling completions and starts (as of August 2025) is extrapolated and only indicative for 3Q25. 12M denotes the 12-month trailing sum.

The housing market draws support from the mortgage boom



Source: Economic & Strategy Research, Komerční banka
Note: own calculations; PCA = principal component analysis vector. The composite housing index is the result of Principal Component Analysis (PCA). Construed as per Cár, M., & Vrbovský, R. (2019, March). *Composite index to assess housing price development in Slovakia*. https://www.nbs.sk/img/documents/publik_nbs/fsr/biatec/rok2019/03-2019/05_biatec19-3_car.pdf.

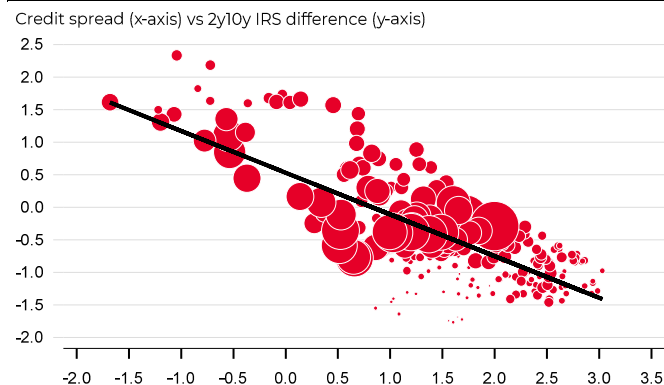
Share of loans by DSTI (%)



Source: CNB, Economic & Strategy Research, Komerční banka

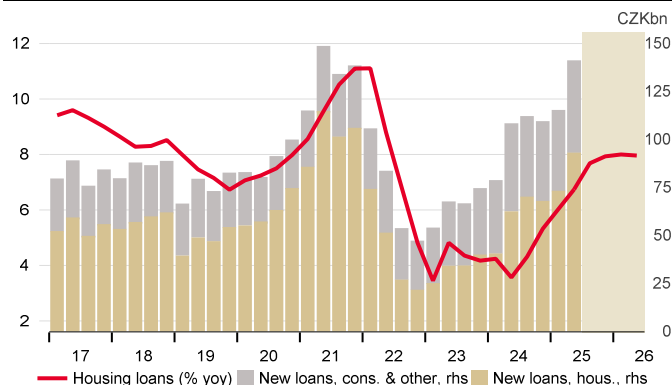
Mortgage lending should continue to drive loan growth. The volume of pure new housing loans was up 53% ytd as of August. The FY25 volume is likely to exceed our previous forecast of around CZK300bn. Moreover, growth in outstanding loans has also surprised us to the upside. We expect the housing loans market to grow 7.9% in 2025 and 7.2% in 2026.⁹ While we do not anticipate a slowdown, we also do not expect further acceleration in new monthly mortgage volumes. From a financial stability perspective, we do not see excessive risk accumulation due to mortgage activity and consider the reintroduction of DSTI and DTI limits in the near term as unlikely.

Mortgage credit spreads over IRS and IRS curve inversion (pp)



Source: CNB, Bloomberg, Macrobond, Economic & Strategy Research, Komerční banka
Note: The size of the bubbles represents the volume of new loans. Credit spread is computed as the difference between the realised interest rate on housing loans and the weighted average of corresponding market IRS (only an approximation).

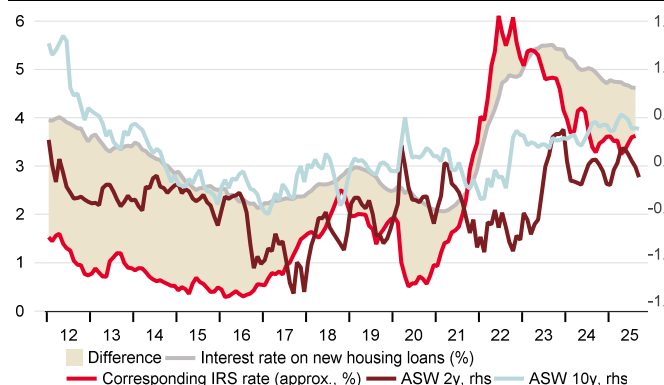
Growth in outstanding housing loans continues to accelerate



Source: CNB, Macrobond, Economic & Strategy Research, Komerční banka

There is little scope for further reductions in mortgage rates. The average mortgage rate reached 4.5% in 3Q. Given the slope of the yield curve and overall higher IRS levels, we think it could fall just a touch below this level. This year's roughly 20% share of refixations (on "new" loans) is narrowing the gap between rates on new and outstanding mortgages. A more significant narrowing is expected in 2026, when a large swath of 5y fixed rate mortgages from the record year of 2021 will be up for refixation. In most cases, interest rates could more than double, which could slow household consumption slightly.

Mortgage rate spreads over IRS (% , pp)



Source: CNB, Bloomberg, Macrobond, Economic & Strategy Research, Komerční banka
Note: ASW (CZGB-IRS) of corresponding CZGBs.

Surprisingly, the volume of consumer loans continued to rise



Source: CNB, Macrobond, Economic & Strategy Research, Komerční banka
Note: Pure new loans are loans or extensions to loans that enter the economy for the first time.

⁹ Unless stated otherwise, values refer to the end of period yoy growth.

Rising consumer financing reflects improved consumer sentiment and increased spending.

Consumer financing mirrors the robust growth in household consumption

Strong growth in consumer financing continued to exceed our expectations. In real terms, volumes are already well above pre-pandemic levels, and in nominal terms they were up 11% ytd as of August. The credit impulse of loans to households remains stable and strongly positive. However, we do not expect a further significant increase in the volume of new loans, so the credit impulse should not strengthen further. This should also be reflected in slower growth in consumer financing, which is set to reach 9.7% in 2025. For 2026, we expect it to slow to 8.5%. Relative to GDP, the volume of consumer loans should continue to increase, reaching 4.8% of GDP by end-2026. We have raised our forecasts for both consumer and housing loans for 2026, reflecting the fiscal boost which is likely to support growth in disposable income and credit demand at least to some extent. As in 2025, the retail market should remain the major driver of credit activity in 2026.

Bank loans and deposits (% , yoy)

	1Q25	2Q25	3Q25	4Q25	1Q26	2Q26	3Q26	4Q26	2024	2025	2026	2027	2028	2029
Bank loans														
Total	4.9	6.8	6.4	6.3	6.6	5.6	6.8	6.7	6.1	6.1	6.4	7.0	6.4	5.9
Households - real estate loans	6.0	6.7	7.7	7.9	8.0	8.0	7.5	7.2	4.4	7.1	7.7	6.6	6.1	6.0
Households - consumer loans	9.2	9.3	9.9	9.7	9.2	8.9	8.3	8.5	8.7	9.5	8.7	8.2	7.0	6.0
Corporate loans	4.1	5.9	4.2	4.2	4.5	3.7	6.2	6.0	7.5	4.6	5.1	7.2	6.6	6.0
Deposits														
Total	4.1	4.8	3.8	4.5	6.6	7.2	7.5	5.7	7.4	4.3	6.7	6.2	4.9	4.9
Households	5.8	4.8	5.3	5.5	5.7	6.4	6.1	6.1	8.0	5.3	6.1	5.9	5.1	4.8
Non-financial corporations	2.0	4.6	2.2	2.5	5.5	4.9	7.4	5.1	5.4	2.8	5.7	4.9	4.0	4.7
Others	2.9	4.9	2.5	4.4	8.7	10.2	9.9	5.4	8.0	3.7	8.5	7.6	5.3	5.1
Ratios														
Loans/GDP	56.9	57.5	57.4	57.4	57.6	58.0	58.8	58.8	57.0	57.3	58.3	59.4	60.3	61.3
Deposits/GDP	91.8	92.0	91.6	88.8	93.0	94.3	94.5	90.1	92.1	91.0	93.0	94.1	94.2	94.7
Loans/deposits	62.0	62.5	62.6	64.6	62.0	61.5	62.2	65.3	61.9	62.9	62.7	63.2	64.1	64.7
Interest rates														
Real estate loans	4.7	4.7	4.6	4.5	4.5	4.4	4.3	4.3	5.0	4.6	4.4	4.4	4.4	4.4
Consumer loans	8.2	8.0	8.0	8.0	8.3	8.4	8.6	8.7	8.8	8.0	8.5	8.7	8.9	9.5
Corporate loans	5.5	4.8	4.7	4.7	4.7	4.9	4.9	4.8	6.3	4.9	4.8	4.8	4.8	5.0
Share of NPL														
Real estate loans	0.7	0.7	0.7	0.7	0.8	0.8	0.9	1.0	0.7	0.7	0.9	1.1	1.3	1.6
Consumer loans	4.2	4.2	4.2	4.6	4.9	5.2	5.7	6.0	4.2	4.3	5.5	6.6	7.1	8.1
Corporate loans	2.6	2.6	2.5	2.5	2.6	2.7	2.8	2.9	2.5	2.6	2.8	3.2	3.9	5.1

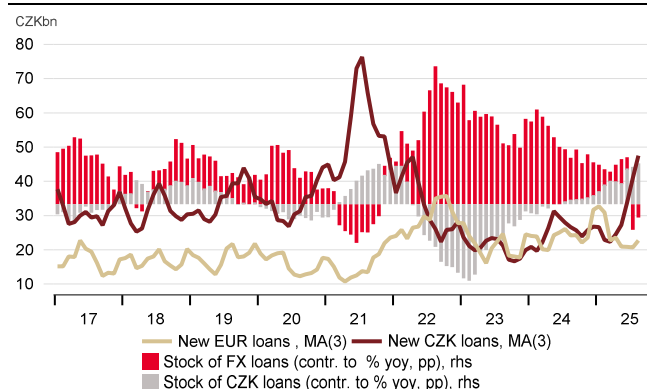
Source: CNB, CZSO, Macrobond, Economic & Strategy Research, Komerční banka
Note: quarterly values are end of period, full-year values are averages.

Uncertainty and US tariffs are holding back growth in outstanding NFC loans. We expect to see stronger growth in 2026 thanks to fiscal policy and the recovery in economic growth.

Investment appetite boosted by fiscal stimulus and stronger growth in 2026

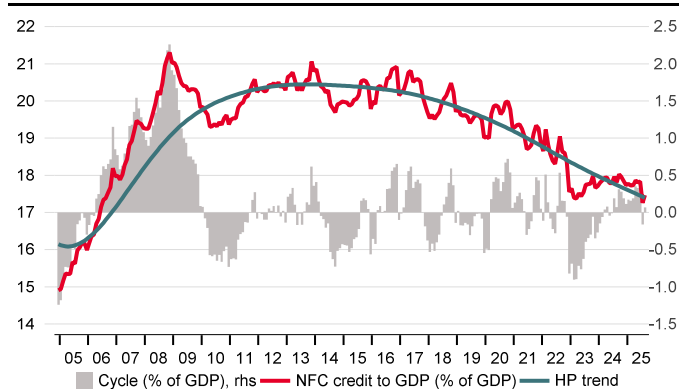
Monetary policy may not be significantly restraining the credit activity of non-financial corporates (NFCs), but uncertainty and the deteriorating situation in industry due to US tariffs could be holding it back. Growth in NFC credit remains low (+3.4% yoy in August). However, the volume of new CZK loans has soared since June and was up 28% ytd as of August, while the volume of EUR loans fell by 5% ytd. Notably, the exchange rate plays a role. According to our estimates, the stronger koruna reduced yoy NFC loan growth by 1.2pp in August. Given our EURCZK forecast, this effect could be more pronounced by the end of the year, reducing growth by almost 2pp. Nevertheless, both new and outstanding loans remain low relative to GDP, indicating that overall NFC credit activity is still rather subdued.

NFC credit activity soared since June



Source: CNB, Macrobond, Economic & Strategy Research, Komerční banka

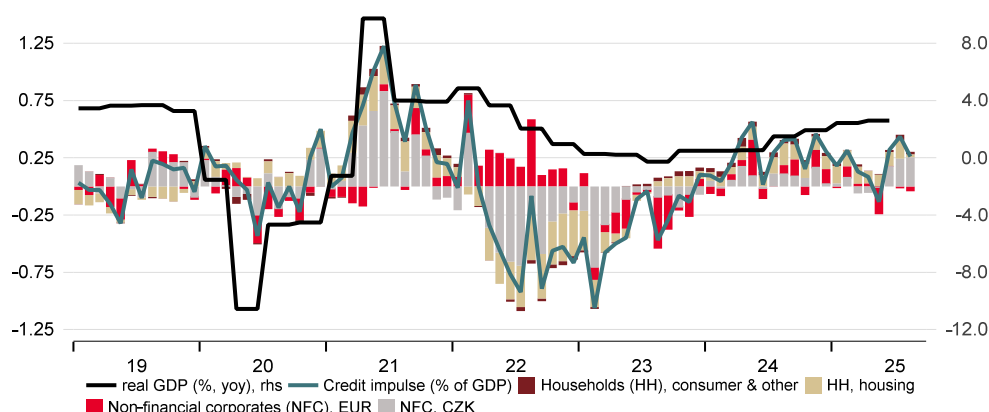
NFC credit-to-GDP ratio sticks to the downtrend



Source: CZSO, CNB, Macrobond, Economic & Strategy Research, Komerční banka

The traditional bank lending channel is likely being crowded out by alternative financing, such as bonds or intra-company financing. The ratio of NFC loans to GDP has essentially stagnated since 1H23, but we expect it to gradually rise in the coming years. The improved outlook for the domestic economy should boost credit demand. However, on the other hand, fiscal stimulus could, to an extent, crowd out private credit demand. We expect NFC credit growth to come in at 4.2% for 2025 and accelerate to 6.0% in 2026.

Credit impulse has temporarily slowed, but surprisingly supported the economy in 3Q



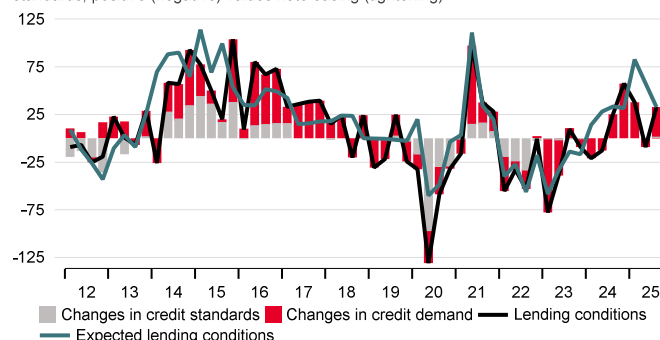
Source: CNB, CZSO, Macrobond, Economic & Strategy Research, Komerční banka

Note: Credit impulse is defined as the change in the volume of new borrowing, often given as a % of annual GDP. The presented credit impulse represents the yoy change in new borrowing of the non-financial private sector to trailing 12m nominal GDP. It is further broken down according to the use of the loan for households and the currency denomination for firms. As opposed to monthly credit indicators (as of August 2025), GDP (as of 2Q25) is a quarterly indicator.

The easing of financial conditions is mostly over. Monetary policy is set to remain slightly restrictive and market interest rate swaps are expected to rise (see *Rates* chapter). This should effectively tighten financial conditions in the market. Nevertheless, credit demand should strengthen in line with the rise in aggregate demand in the economy, boosted by fiscal stimulus. The relative advantage of EUR financing is likely to persist and could even widen at the start of the year in terms of key monetary policy rates, in view of our expectations of ECB rate cuts combined with stable CNB rates.

Lending conditions indicate higher credit demand

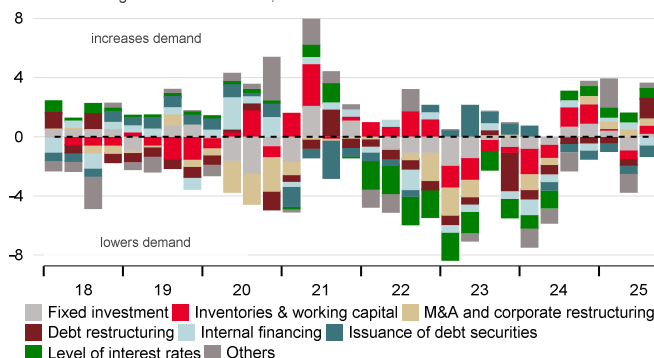
Lending conditions refer to the net increase in loan demand minus the net tightening of credit standards, positive (negative) values note easing (tightening)



Source: CNB, Macrobond, Economic & Strategy Research, Komerční banka
Note: Bank Lending Survey (CNB, 3Q25), loans to NFCs. Expected lending standards refer to questions regarding banks' expectations for the next three months.

Factors affecting NFC credit demand according to banks

Factors affecting NFC credit demand, z-scores



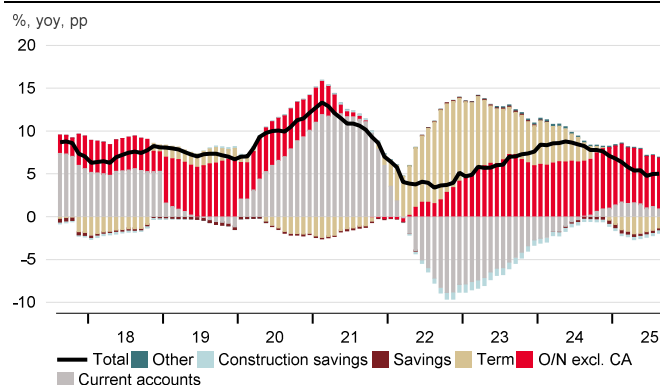
Source: CNB, Macrobond, Economic & Strategy Research, Komerční banka
Note: Stacking the z-scores in the bar chart is for presentation purposes only. *Others* refers to loans from other banks and non-bank institutions, issuance of equity and other.

In 2026, deposit growth is set to be supported by a fiscal boost and stronger credit activity.

Deposit growth slowing due to lower interest rates

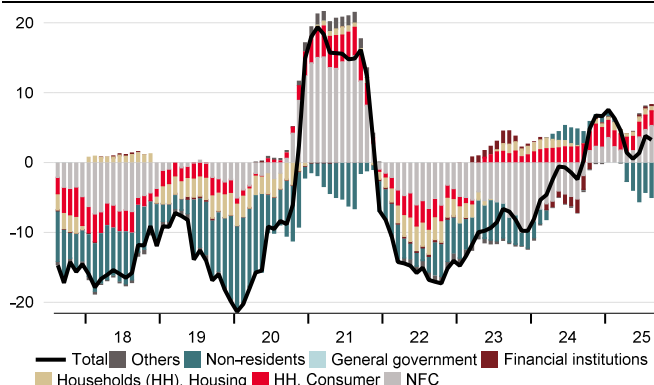
Despite stronger credit activity, deposit growth is likely to slow markedly this year compared to last due to lower interest rates. The fiscal stimulus, combined with stronger credit activity, should boost deposit growth in 2026. The overhang of deposits over loans has decreased significantly for households, while for businesses the loans-to-deposit ratio remains low at around 0.93x. The stabilisation of CNB rates and high excess liquidity in the banking system put downward pressure on deposit rates. Overall, the banks' funding bases should continue to grow at a solid pace. A strong deposit base and growth in banks' balance sheets could increase the absorption of government bonds, the issuance of which is set to increase. We estimate deposit growth in 2025 to average 4.3% and accelerate to 6.7% on average in 2026.

Household deposits are changing in reflection of lower rates



Source: CNB, Macrobond, Economic & Strategy Research, Komerční banka
Note: O/N = overnight; O/N excl. CA also includes non-term savings deposits

Non-performing loans growth not raising concerns (% , yoy)



Source: CNB, Macrobond, Economic & Strategy Research, Komerční banka

Credit risks remain moderate across all market segments. A slight slowdown in the domestic economy due to tariffs should not lead to major loan defaults.

Credit risks on bank portfolios remains well under control

The default rate (share of non-performing loans – NPLs) remains stable and close to historic lows. Despite the increase in credit activity, there appears to be no excessive accumulation of risk on bank portfolios so far. The economic slowdown due to tariffs combined with tighter financial conditions may lead to a slight increase in risk, especially sector-specific risks. Nevertheless, the higher volume of NPLs should have only a very slight impact on the overall NPL ratio. The volume of NPLs was up 3.3% yoy in August, but their share in total loans remained stable at around 2.6%. The latest *Bank Lending Survey* (CNB, 3Q25) shows that banks expect only a limited increase in credit losses in consumer and business loans.

Key economic indicators

Macroeconomic indicators – long-term outlook

		2022	2023	2024	2025	2026	2027	2028	2029
GDP	real, %	2.9	0.2	1.1	2.1	1.6	2.8	2.1	2.3
Inflation	average, %	15.1	10.8	2.4	2.4	1.5	2.4	2.2	2.0
Current account	% of GDP	-4.7	-0.1	1.7	0.1	0.3	0.3	0.4	0.5
3M PRIBOR	average, %	6.3	7.1	5.0	3.6	3.6	3.6	3.5	3.1
EUR/CZK	average	24.6	24.0	25.1	24.7	24.3	24.1	24.1	23.9
USD/CZK	average	23.4	22.2	23.2	21.8	19.5	19.3	19.3	19.1

Source: CZSO, CNB, Macrobond, Economic & Strategy Research, Komerční banka

Note: KB forecasts are in red

FX & interest-rate outlook

		28-10-2025	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26
EUR/CZK	end of period	24.3	24.40	24.40	24.30	24.20	24.05
EUR/USD	end of period	1.16	1.19	1.22	1.25	1.25	1.25
USD/CZK	end of period	20.9	20.50	20.00	19.45	19.35	19.25
3M PRIBOR	end of period, %	3.53	3.40	3.60	3.60	3.60	3.60
10Y IRS	end of period, %	4.08	3.95	4.00	4.05	4.15	4.20

Source: CNB, Macrobond, Economic & Strategy Research, Komerční banka, SG Economic Research

Note: KB forecasts are in red

Monthly macroeconomic data

		I-25	II-25	III-25	IV-25	V-25	VI-25	VII-25	VIII-25	IX-25
Inflation (CPI)	%, yoy	2.8	2.7	2.7	1.8	2.4	2.9	2.7	2.5	2.3
Inflation (CPI)	%, mom	1.3	0.2	0.1	-0.1	0.5	0.3	0.5	0.1	-0.6
Producer prices (PPI)	%, yoy	0.5	-0.1	-0.3	-1.3	-0.8	-0.7	-1.2	-0.8	-1.0
Producer prices (PPI)	%, mom	0.2	-0.1	-0.3	-0.8	-0.6	-0.2	0.1	0.0	-0.4
Unemployment rate	% (MLSA)	4.3	4.4	4.3	4.3	4.2	4.2	4.4	4.5	4.6
Industrial production	%, yoy, c.p.	-1.0	-1.5	4.6	-1.5	-0.7	3.2	4.9	-4.2	n.a.
Industrial sales	%, yoy, current.p.	0.8	-3.3	2.9	-2.4	-0.7	4.6	3.1	-5.7	n.a.
Construction output	%, yoy, c.p.	6.6	1.0	12.3	3.5	13.1	15.1	10.2	16.0	n.a.
External trade	CZKbn (national met.)	18.4	30.9	28.2	19.3	12.3	28.4	-0.6	5.6	n.a.
Current account	CZKbn	30.7	44.1	21.9	23.4	-16.0	-73.4	-14.9	-0.7	n.a.
Financial account	CZKbn	56.0	27.8	2.0	14.8	-4.4	-46.4	10.8	-22.4	n.a.
M2 growth	%, yoy	4.5	4.0	4.4	3.2	3.5	2.9	3.0	2.8	n.a.
State budget	CZKbn (YTD cum.)	-11.2	-68.6	-91.2	-126.1	-170.5	-152.4	-168.2	-165.4	-153.9
PRIBOR 3M	%, average	3.88	3.76	3.72	3.68	3.53	3.51	3.49	3.50	3.49
EUR/CZK	average	25.2	25.1	25.0	25.0	24.9	24.8	24.6	24.5	24.3
USD/CZK	average	24.3	24.1	23.1	22.3	22.1	21.5	21.1	21.0	20.7

Source: CZSO, CNB, MF, MLSA, Macrobond, Economic & Strategy Research, Komerční banka

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