

## Economics

3 January 2012 | 6 pages

# Czech Republic Macro Flash

## Fiscal deficit in 2011 brings positive buffer for painful 2012

- **Central government cash deficit is wider than planned, but narrower than recent expectations** — Central government deficit reached CZK142.8bn in 2011, likely 3.7% of GDP. This is wider than the approved CZK135bn, but narrower than recent expectations of CZK150bn due to the pending inflows of EU funds. Excluding this effect, the central government deficit reached CZK130bn. Moreover, the deficit would reach CZK119.5bn excluding unexpected negative effects (larger contribution to the EU budget and the decision of the Constitutional Court about the building saving scheme).
- **Drop in revenues was partly offset by drop in expenditures** — While the revenues slightly increased by 1.3%YoY in 2011, they lagged behind the plan by 5.3%. This was offset by virtually unchanged expenditures (see Figure 3), which represents a consolidation of 4% compared to initial plan for 2011.
- **MinFin estimates the general government deficit at 3.7% of GDP in 2011** (ESA methodology) — According to the MinFin, this is the pessimistic estimate and the result is likely to be better. If this materialises, it would be a significant improvement compared to initial expectations of the MinFin (-4.6% in Oct10 or -4.2% in Apr11); moreover, it would be a narrowing from -4.8% in 2010. Additionally, it creates a positive buffer for the 2012's target at -3.5% of GDP. Interestingly, this target was revised downward from -3.2% published in October's Fiscal Outlook. Our forecast of a mild recession in 2012 envisages the general government deficit at -3.9% of GDP in 2012 (in ESA95) with the central government cash deficit at CZK120bn (plan is CZK105bn).
- **Outlook on 2012 is negative, but manageable** — First, we understand that the pending EU funds could materialise later. Hence, there should be some revenue inflow later in 2012, but likely not up to the total pending amount of CZK12.8bn from 2011. Second, we feel that the government is ready to implement cuts in expenditures once the new, likely less optimistic, MinFin forecast is published (at end of January). However, the prospect of a recession could lead to hesitation over any additional austerity measures (for more see [Parliament finally approves 2012 Budget](#), 15 Dec).
- **Borrowing requirements are manageable in 2012 particularly, if foreign issuance materialises** — The MinFin expects issuance of bonds of around CZK167bn in 2012 after CZK181bn in 2011. This particularly reflects a plan of a larger issuance of T-bills and retail bonds (see Figure 4). In our view, any successful issuance of the Eurobond would offset a likely risk of wider deficit in 2012.
- **Wednesday 2Y bond (2.75%/2014) auction** — The MinFin plans to sell between CZK5-8bn in the competitive round (the total goal is likely at least CZK7bn, which is 4% of planned bond issuance this year). The outcome of the October auction of 2.5% bonds was a 2.9 bid-cover ratio with oversubscription of CZK12.9bn. The last auction (11Y floater) was not subscribed, when the MinFin sold only CZK3bn instead of planned CZK7bn.

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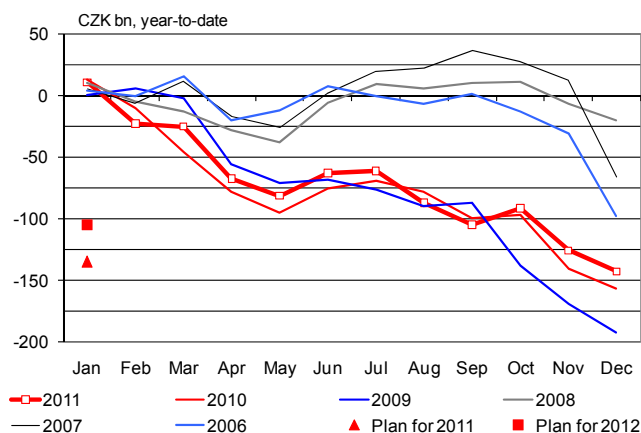
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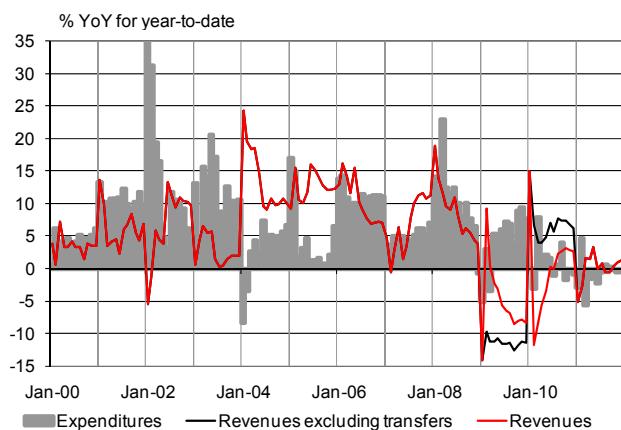
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Figure 1. Central government deficit – year-to-date and plans for 2011 and 2012



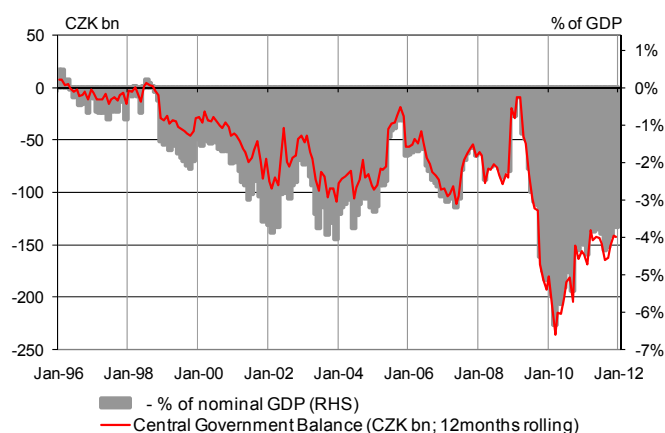
Source: Ministry of Finance and Citi Investment Research and Analysis

Figure 3. Revenues of central government budget improved in 2011, but lag behind the plan that was compensated by lower expenditures



Source: Ministry of Finance, Citi Investment Research and Analysis

Figure 2. Central government deficit – 12months roll



Source: Ministry of Finance, CZSO, Citi Investment Research and Analysis

Figure 4. Gross borrowing requirement and instruments for funding of the central government

CZK billion	2011		2012		2013	
	Plan	Predict.	Plan	Plan	Plan	Plan
<b>Net borrowing requirement</b>	<b>106.3</b>	<b>150.5</b>	<b>107.2</b>		<b>112.2</b>	
Redemptions on state debt, incl. buy-backs and switches within a budgetary year (1)	102.1	102.1	123.1		107.6	
Redemptions on loans from the EIB	1.1	1.1	3.1		1.1	
Buy-backs and switches of bonds due in following year (2)	10.0	2.0	10		10.0	
<b>Gross borrowing requirement</b>	<b>219.5</b>	<b>255.7</b>	<b>243.4</b>		<b>230.9</b>	
Net money market issuance (3,4)	30.0	48.7	50		40.0	
Gross government bonds issuance (5)	184.0	181.2	167.5		163.5	
of which at foreign markets	0.88	0.9	0.73			
Gross issuance of retail bonds	-	20.4	30		20.0	
Loans from EIB	5.5	5.4	5.9		7.4	
Net loans from the State Treasury	0.0	0.0	0		0.0	
<b>Funding of borrowing requirement</b>	<b>219.5</b>	<b>255.7</b>	<b>243.4</b>		<b>230.9</b>	

Note: (1) including redemptions on savings government bonds; (2) excl. operations with government bonds due within a budgetary year; (3) excl. revolving within a budgetary year; (4) net money market issuance on the market reached CZK 31.4 billion. The remaining CZK 17.3 billion was invested in the state financial assets; (5) nominal amount, ie. premiums and discounts are included in net costs on state debt not entering into net borrowing requirement

Source: Ministry of Finance (Debt & Funding Strategy for 2012), Citi Investment Research and Analysis.

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