

## NEWS SUMMARY OCTOBER 17 – OCTOBER 26

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## ECONOMICS &amp; FINANCE

## TIGHTER MORTGAGE CONDITIONS IN Q4 – 17. 10.

Czech banks expect tightening of lending standards for mortgages in the Q4<sup>1</sup> due to a new consumer credit act coming into effect and tougher recommendations on loan limits from the CNB.

Some banks also expect consumer credit loan standards to tighten while conditions for company loans to ease, the survey said. Banks widely expect increasing demand for loans in the Q4.

Record low interest rates are helping a mortgage boom in the CR,<sup>2</sup> driving up housing prices. The CNB tightened its recommendations to banks this month to lend no more than 95% of a property's purchase price.

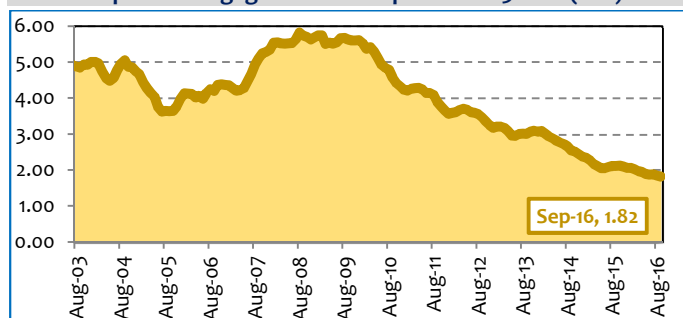
## MORTGAGE MARKET – 19. 10.

Mortgage rates continue to fall and again broke record levels.

The average interest rate on mortgages in August fell to a new record low of 1.82%, 1.84% in August.

Volumes climbed to CZK 19.607bn, an increase of CZ 1.468 bn in comparison with August.

Graph 6: Mortgage rate development 2003-2016 (in %)



## APPROVING DEBT-BRAKE MECHANISM – 19. 10.

The ChD<sup>3</sup> approved a debt-brake mechanism that would prevent future governments from borrowing and spending beyond their means. The bill sets a debt ceiling at 55% of GDP,<sup>4</sup> lower by 5% than that outlined in the EU's<sup>5</sup> fiscal compact. It also envisages the creation of a fiscal council which would monitor adherence to the criteria set down. According to the proposal regions and municipalities would also need to have balanced budgets. The bill, which still needs to be approved by the Senate and signed by the president, should come into force on Jan 1, 2017.

## ENDING OF CROWN CAP WILL BE TRANSPARENT – 19. 10.

The CNB<sup>6</sup>'s move to eliminate its cap on the value of the crown will be transparent, Vice-Governor Tomšík said, reiterating the policy is likely to end in mid-2017.

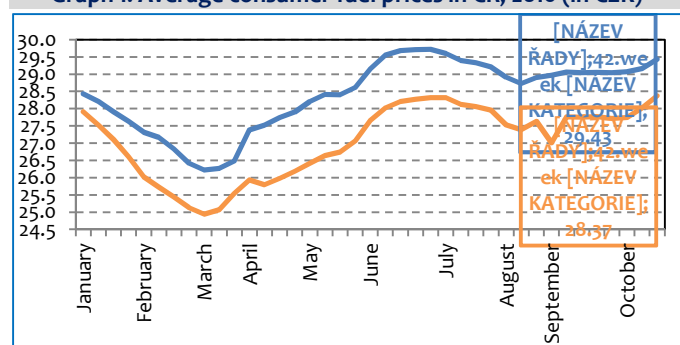
He also repeated the CNB's pledge that it would not end the crown commitment before the Q2<sup>7</sup> 2017 and said the preferred exit would be in a single move, but that other steps could not be ruled out.

He reiterated the bank would be prepared to intervene against excessive crown volatility after the exit.

## MAINTAINING WEAK CROWN POLICY TO 2018 – 20. 10.

The CNB could under certain circumstances maintain its policy of keeping the crown weak until 2018, its governor Jiří Rusnok said. He said, however, that the Q2 2017 was still the most likely date for ending the policy. It is, however, certain that it won't be discontinued before then, he said. Since November 2013 the CNB has spent nearly CZK<sup>8</sup> 600bn<sup>9</sup> on the currency markets keeping the crown at around 27/€. <sup>10</sup>

## AVERAGE CONSUMER FUEL PRICES – 21. 10.

Graph 1: Average consumer fuel prices in CR, 2016 (in CZK)<sup>11</sup>

## NOTIFICATION OF GOVERNMENT DEFICIT – 21. 10.

According to the CSO,<sup>12</sup> following consultation between Eurostat<sup>13</sup> and the CSO, the level of government deficit and debt was confirmed.

Table 1: CR, Notification table of government deficit and debt, 2012-2015 (in CZK mn, %)

	2012	2013	2014	2015
Surplus/Deficit	-159,552	-51,129	-83,063	-28,607
Consolidated gross debt	1,805,429	1,840,412	1,819,098	1,836,255
GDP	4,059,912	4,098,128	4,313,789	4,554,615
General government deficit	-3.93	-1.25	-1.93	-0.63

<sup>6</sup> CNB: Czech National Bank

<sup>7</sup> Q2: 2<sup>nd</sup> quarter of the year

<sup>8</sup> CZK: Czech Crown, the currency of the CR since 8 February 1993

<sup>9</sup> Bn: billion

<sup>10</sup> Euro: €, EUR, is the official currency of the Eurozone, which consists of 19 of the 28 member states of the European Union

<sup>11</sup> Consumer price indices calculated from the weekly price survey are not qualitatively adjusted and thus do not express the net price development applied at inflation measurement.

<sup>12</sup> CSO: Czech Statistical Office

<sup>13</sup> Eurostat: Eurostat is a Directorate-General of the European Commission. Its main responsibilities are to provide statistical information to the institutions of the EU and to promote the harmonisation of statistical methods across its member states and candidates for accession as well as EFTA countries.

<sup>1</sup> Q4: 4<sup>th</sup> quarter of the year

<sup>2</sup> CR: Czech Republic

<sup>3</sup> ChD: Chamber of Deputies, the lower house of Parliament of the CR

<sup>4</sup> GDP: Gross domestic product

<sup>5</sup> EU: European Union

(in % of GDP)				
General government debt (in % of GDP)	44.47	44.91	42.17	40.32

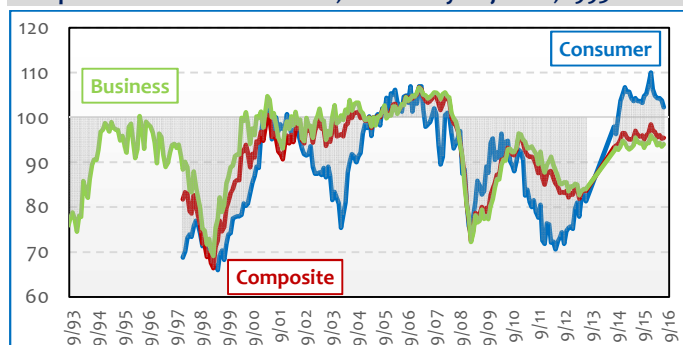
### VAT INCOME INCREASED TO – 24. 10.

In 2016 the VAT<sup>14</sup> income totalled CZK 248.88bn on October 14. At the end of the same period of 2015 it had totalled CZK 235.73bn. Collection of corporate income tax increased y-o-y<sup>15</sup> to CZK 131.04bn from CZK 115.96bn.

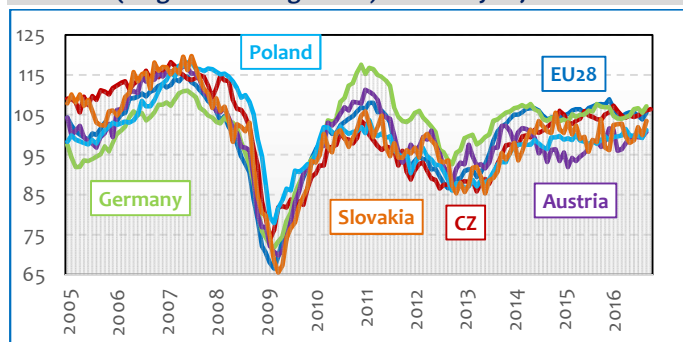
### BUSINESS CYCLE SURVEY – 24. 10.

Overall confidence in domestic economy increased slightly in October. The composite confidence indicator (economic sentiment indicator), that is stated by basic indices, increased slightly by 0.4 p.p.<sup>16</sup> to 97.5, m-o-m.<sup>17</sup> Confidence of entrepreneurs did not change and remained at the same value 95.2, compared to September. Consumer confidence indicator increased by 2.5 points to 108.9, m-o-m. Composite confidence indicator, entrepreneurs confidence indicator and consumer confidence indicator are higher, compared to October 2015.

Graph 2: Confidence Indicators, Seasonally Adjusted, 1993 – 2016



Graph 3: Economic Confidence Indicators - monthly data (long term average = 100) seasonally adjusted



### STATE BUDGET TO SHOW HIGHEST SURPLUS EVER – 25. 10.

The state budget will end in surplus this year, MF<sup>18</sup> Minister Babiš said. He said that it would be the best budget result since the CR<sup>19</sup> was founded in 1993. In addition, state debt has fallen for the 1<sup>st</sup> time since 2011. The minister chiefly attributed the positive figures to more effective tax collection.

This year's state budget was approved with a CZK 70bn gap. The budget surplus increased to CZK 82.3bn at the end of September from August's CZK 81.2bn.

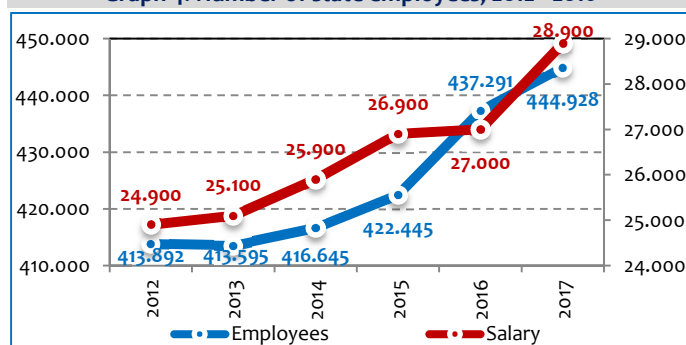
"We will have the best budget in the country's history - a surplus budget. We will lower the debt (below 40% of GDP) for the first time since 2011 thanks to (improved) tax collection," Babiš said.

### SOCIAL & HEALTH & EDUCATION

#### MARKED RISE IN STATE EMPLOYEES – 18. 10.

The number of state employees has grown by around 23,000 since 2012, according to data released by the MF. Nearly 440,000 people are now employed by the state in the CR, which has a population of 10.5mn.<sup>20</sup> Annual salaries for such workers have increased by CZK 16.6bn in the last 4 years to reach CZK 149bn. The average state employee receives CZK 27,000 a month.

Graph 4: Number of state employees, 2012 - 2016



#### RDI SPENDING – 26. 10.

Czech spending on RDI<sup>21</sup> continues to climb and is already at one of the highest levels per capita among new EU member states in CEE.<sup>22</sup> Last year RDI spending rose by CZK 3.6bn to CZK 88.7bn, according to the CSO. That represented a 4.2% increase on the previous year. Czech RDI spending has risen by 2/3 over the last 5 years. The proportion of spending per capita is 2<sup>nd</sup> in CE<sup>23</sup>, bettered only by Slovenia.

### AGRICULTURE & ENVIRONMENT

#### CZECH SUGAR PRODUCTION FELL LAST YEAR – 19. 10.

According to Report on Sugar beet by the MA,<sup>24</sup> in the sugar campaign, which ended in January this year, sugar production of the sugar factories in the CR went down by nearly a quarter to 451,87t.<sup>25</sup> It was due to drought and shrinking acreage on which sugar beet is grown. Production decreased despite record sugar content in sugar beet bulbs. In 2014, sugar production in the CR was the highest since the accession to the EU.

2.74mn t from 44.925 ha<sup>26</sup> area of sugar beet to produce sugar was processed. The yield amounted to 60.94t/ha as a reflection of a drought last year.

<sup>20</sup> Mn: Million

<sup>21</sup> RDI: Research, Development and Innovation

<sup>22</sup> CEE: Central and Eastern Europe, is a generic term for the group of countries in Central Europe, Southeast Europe, Northern Europe, and Eastern Europe

<sup>23</sup> CE: Central Europe

<sup>24</sup> MA: Ministry of Agriculture

<sup>25</sup> t: tonne, metric ton is a non-SI metric unit of mass equal to 1000 kilograms

<sup>26</sup> ha: hectare is a non-SI metric system unit of area equal to 10,000 m<sup>2</sup>

<sup>14</sup> VAT: Value-added tax

<sup>15</sup> Y-o-y: year on year

<sup>16</sup> P.p.: percentage point

<sup>17</sup> M-o-m: month-on-month

<sup>18</sup> MF: Ministry of Finance

<sup>19</sup> CR: Czech Republic

Last year, the area of sugar beet, from which not only sugar but also as biofuels or alcohol is produced, decreased for the first time since 2008. Beet was grown on 57,212 ha.

This year the area should be increased again, up to almost 61,000 ha. More than 1/84 of beet is being grown in the Central Bohemia, Olomouc, Hradec Králové and the Moravia-Silesia regions.

Production of molasses due to the drought experienced a further decline to another minimum of 54,800t. That is why Czech companies continue to buy molasses outside the CR. In the CR, there are 7 sugar mills, 2 of which are in Bohemia, 5 in Moravia. 4 of them are owned by 2 businesses having a decisive share of foreign capital.

Next year, EU sugar production quotas end and in this connection the AACR<sup>27</sup> has already expressed concern about the departure of some manufacturers from the CR.

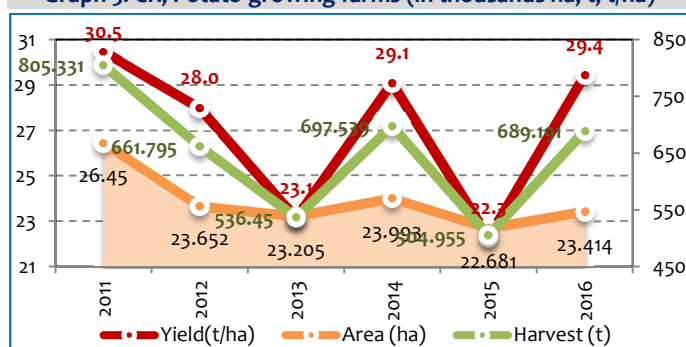
The MA seeks to support enlarging the areas of sugar beet. At the end of last year, for example, it included sugar beet among the so-called sensitive commodities on which higher subsidies can be drawn.



#### HARVEST OF POTATOES – 21. 10.

According to the latest estimate, growers in the CR will harvest around 689,000t<sup>28</sup> of potatoes this year. It is about 1/3 increase in quantity compared with the previous record low harvest.

Graph 5: CR, Potato-growing farms (in thousands ha, t, t/ha)



Potato harvest is comparable to the ten-year average because of good yield, although the size of potato fields in the CR declined in recent years. However, not this year's good harvest will not be enough to cover domestic consumption of potatoes. Domestic production covers the long-term needs from 70 to 80%. According to estimates, around 100,000t of potatoes will be imported to the CR from abroad.



#### DIESEL TAX REBATE PROGRAM – 21. 10.

The ChD has voted to extend a diesel tax rebate program to livestock farmers and other agricultural workers. Currently the program, under which farmers are able to reclaim 40% of the consumption tax they pay on diesel gas back from the state, applies only to grain farmers. Under the present amendment it should also apply to fisheries and forestry workers. The amendment, which still needs to win approval in the Senate, aims to raise the competitiveness of Czech farmers in the EU.

<sup>27</sup> AACR: Agricultural Association of the Czech Republic

<sup>28</sup> t: tonne, metric ton is a non-SI metric unit of mass equal to 1000 kilograms



#### CURBING BOOTLEG WINE PRODUCTION – 21. 10.

The ChD has moved to curb bootleg wine production. The proposed amendment to the law envisages fines of up to CZK 50mn, up from the present CZK 5mn, and sets down strict norms on the sale of barrel wine. If the bill wins approval in the Senate in its present form, barrel wine will only be able to be sold by wine producers and importers in special shops, so-called vinotekas, under strict conditions. MA<sup>29</sup> Minister Jurečka argues that in some ways the bill is excessively stringent and has said he will try to get the Senate to modify it. The country's small wine-makers also fear that the new conditions could be devastating for their business.



#### EGGS WARNING – 25. 10.

SVA<sup>30</sup> banned the sale of up to 3.5mn pieces of eggs from Poland from Femy Drobiu Wozniak Company. It could contain salmonella bacteria. Kaufland, Tesco and Ahold and manufacturing company Miloš Minařík from Opatovice has received them in the CR. The information on possible danger has come through the Rapid European RASFF alert. All retail chains withdrawn eggs from sale and offer customers return of money.

For example, the Netherlands, Norway, Croatia and the United Kingdom (Scotland) informed on the disease associated with eggs from this Polish supplier.

According to SVA, retailers could have up to 3.57mn pieces of eggs. Unsafe batches had a shelf life up to 22.10, 10.25, 10.31, 03.11, 11.04, 11.05, 11.06, 07.11, 08.11, 10.11, 13.11, 11.14 and 15.11 this year with code PL 30221304 or PL 30221321 on the packaging.

#### ICT & SERVICES



#### MERGERS AND ACQUISITIONS IN H1 2016 – 20. 10.

According to EY,<sup>31</sup> transactions worth USD 4.9bn were carried out on the mergers and acquisitions market in the CR in H1<sup>32</sup> 2016. Investors carried out totally 194 transactions. The CR was thus the biggest region in CEE in terms of value and number of transactions. Czechoslovak Group was the most active investor, having carried out 5 major transactions, involving e.g. the Avia and Prim brands. The top transaction in H1 2016 was the acquisition of online travel agent Invia.cz by Rockaway Capital for about USD 85mn.



#### PRICE OF FLATS IN PRAGUE RISING – 23. 10.

A real estate boom fuelled by low mortgage rates has sent up housing prices in Prague, making it one of the costliest cities to live in. Czechs with an average salary now have to work 11 years for a flat of approximately 70m<sup>2</sup>. An Austrian would need to work for 9 years to acquire a similar flat in Vienna, while a German would only need to work for 6 years

<sup>29</sup> MA: MasterCard Incorporated or MasterCard Worldwide is an American multinational financial services corporation. Throughout the world, its principal business is to process payments between the banks of merchants and the card issuing banks or credit unions of the purchasers who use the „MasterCard“ brand debit and credit cards to make purchases. MasterCard Worldwide has been a publicly traded company since 2006.

<sup>30</sup> SVA: Czech State Veterinary Administration

<sup>31</sup> EY: Ernst & Young is a multinational professional services firm headquartered in London, United Kingdom. It is one of the „Big Four“ audit firms and is the 3<sup>rd</sup> largest professional services firm in the world, after PwC and Deloitte.

<sup>32</sup> H1: 1<sup>st</sup> half of year



to buy a one in Berlin. London, Paris or Brussels are more expensive. An average flat of 70m<sup>2</sup> in Prague costs approximately CZK 7.5mn. Just a year ago Czechs needed to work less than 10 years to acquire it.

### CCC AND SELLERS WARN OF LOSS – 24. 10.

The CCCT,<sup>33</sup> the CCC,<sup>34</sup> and the ACRE<sup>35</sup> warned that legislation passed this year – forcing large retailers to close their doors on 7 state holidays – will lead to a net loss in revenues of around CZK 4bn across the CR. Additionally, the grouping warned that the new law would lead to job losses, not just among cashiers or sellers but also cleaners and security. By contrast, the bill had support from the TUs<sup>36</sup> as it would allow employees in the service sector time off. October 28 is one of 7 state holidays when large retail stores will not be allowed to sell products.

### INDUSTRY & INVESTMENT

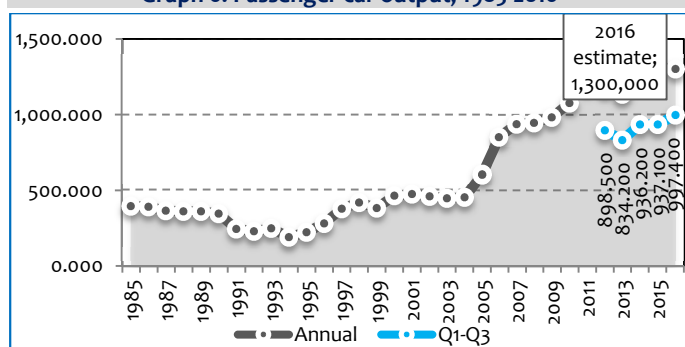
### EXPORTS TO GROW, BUT AT A SLOWER PACE – 19. 10.

The AMSP<sup>37</sup> expects that the CR's exports will increase in 2016 compared to 2015. However, the pace of growth has been slowing down from 7.5% at the end of 2015 to 5.1% in the first 4 months of 2016 and to 3.9% after 8 months of 2016. AMSP said the slowdown had been also caused by a lack of qualified workforce.

### PASSENGER CAR OUTPUT – 19. 10.

The passenger car output in the CR will exceed 1.3mn this year, beating last year's record which was closely below this level, AIA<sup>38</sup> said. This expectation can be confirmed by results of all car makers in the CR for the Q1-Q3<sup>39</sup> 2016, which are 7% higher than last year.

Graph 6: Passenger car output, 1985-2016



Škoda Auto's<sup>40</sup> output grew by 6% y-o-y in January-September and is expected to grow until the end of the year. Last year, Skoda produced nearly 737,000 cars. Sales of car companies last year reached the level of CZK 1tn<sup>41</sup>. This figure may be exceeded this year.

<sup>33</sup> CCCT: Czech Confederation of Commerce and Tourism

<sup>34</sup> CCC: Czech Chamber of Commerce

<sup>35</sup> ACREM: Atrium Czech Real Estate Management, managing the Flora shopping centre in Prague

<sup>36</sup> TU: Trade union, around 1/6 of all employees are union members in the CR.

<sup>37</sup> AMSP: Association of Small and Medium-Sized Enterprises and Crafts in the CR

<sup>38</sup> AIA: Automotive Industry Association, AutoSAP

<sup>39</sup> Q3: 3<sup>rd</sup> quarter of the year

<sup>40</sup> Škoda Auto: is a Czech automobile manufacturer founded in 1895 as Laurin & Klement. It is headquartered in Mladá Boleslav, Bohemia, Czech Republic. The car manufacturer was acquired by Škoda Works in 1925 and became a wholly owned subsidiary of the Volkswagen Group in 2000, positioned as the entry brand to the group. Its total global sales reached 1.04 million cars in 2014.

<sup>41</sup> Tn: Trillion

According to AIA, the sector as well as the government should nevertheless focus on the future, since the availability of workforce has started to be a problem. In addition, the CR lacks infrastructure and the car sector needs digital innovations. "The CR has to create better conditions for business. We cannot rely on having an advantageous geographical position. We are in a good condition but we must not rest on our laurels."

The TPCA<sup>42</sup> plans to raise its output by 2% to 224,000 vehicles this year and intends to keep producing around 200,000 cars annually in the following years as well. The plant's output has been growing for several years since 2013, when it dropped to a 10-year low of 185,127 vehicles. Last year, TPCA produced 210,054 cars.

Hyundai<sup>43</sup> plans to produce 350,000 cars this year, 8,000 more than last year. It has recorded a growing demand mainly for SUVs. While last year they accounted for 59%, this year it has reached 70%. The biggest demand for Hyundai SUVs is being registered in the Middle East.

The Kia's Slovak plant intends to produce around 338,000 cars this year, the same amount as last year. Last year's result was the highest in the plant's 10-year-history.

Kia is registering falling sales in Russia. While in 2013 it sold around 70,000 cars in Russia, this year it will sell there only 29,000 cars.

### ŠKODA STARTS PRODUCTION OF KODIAQ – 19. 10.

Škoda Auto's factory in Kvasiny started the series production of the new SUV model ŠKODA Kodiaq on October 18, 2016. The production has required investments in the extension and modernisation of the factory. The automaker plans to invest CZK 7.2bn in the factory by 2018. Its capacity will likely grow up to 280,000 cars a year. Besides the model ŠKODA Kodiaq, the Kvasiny-based factory manufactures also models Superb and Yeti. It manufactured about 142,000 cars in 2015.

### DNES BWI MANUFACTURING SHOCK ABSORBERS - 20. 10.

BWI<sup>44</sup> Group opened a new manufacturing plant for CZK 750mn in Cheb and will offer 300 new jobs, in the first wave. Prospectively, the number is expected to reach 500, perhaps 1,000.

The plant covers an area of 15,000 m<sup>2</sup> and will be manufacturing shock absorbers for luxury car manufacturers like BMW, Audi, Opel, or Volvo. Full production will start at the beginning of the next year.

The building project was financed and will be long-term rented by Accolade group.

The industrial zone in Cheb currently covers about 40ha. It employs 2,500 people. Thanks to the huge interest of investors, it has become one of the fastest growing industrial parks in the CR.

In the vicinity there is another industrial site, which has a chance to become a strategic zone of the CR. The proposal must be yet discussed by the Government.

<sup>42</sup> TPCA: Toyota Peugeot Citroën Automobile Czech (TPCA) is an automobile manufacturing company in Kolín, Czech Republic. It is a joint venture between Toyota Motor Corporation of Japan and PSA Peugeot Citroën of France.

<sup>43</sup> Hyundai CZ: Hyundai Motor Manufacturing Czech based in the Industrial Zone of Nošovice was founded in 2006.

<sup>44</sup> BWI: Beijing West Industries, a Chinese company



## JOINT STATEMENT TOWARD CHINA - 20. 10.

According to server Ekonomický deník, a possible explanation of joint statement of CR's top four leaders on a strong CR's friendship with China could be a prepared meeting of 16 CEE PMs<sup>45</sup> with the Chinese PM, which will be held on November 5-6 in Riga, Latvia.

According to the server Česká justice, also a bilateral meeting PM Sobotka with PM Li Keqiang is being prepared in Riga. Allegedly, this meeting might be compromised by meeting of MC Minister Herman the Dalai Lama and such a threat obviously should be avoided.

Negotiations will probably include the development of further cooperation in the transport industry, but also culture, banking. It includes not only road, rail and air transport, energy, the exploitation of mineral wealth, but also projects in the field of agriculture and the chemical industry. It was also repeatedly talked about the fact that CR could become the economic base of the „Chinese Dragon“ in Europe, from which it will expand to other regions.



## AEROHOLDING SELLS CSA – 20. 10.

Aeroholding<sup>46</sup> sold its remaining stake of about 20% in CSA<sup>47</sup> to state-run company Prisko.<sup>48</sup>

The value of the transaction, which was approved by the OPC<sup>49</sup> at the beginning of September, has not been disclosed.

“The price cannot be disclosed since it is non-public information,” MF said. Aeroholding head Řehoř indicated in May that the price would be markedly higher than what Korean Air and Travel Service had paid for their stakes.

Korean Air paid CZK68mn for its 44% in CSA 3 years ago. It was, however, entering a loss-making company at that time, while at present, CSA is posting profits.

The 20% stake is the last share in CSA owned by the Czech state. A majority of CSA shares is in the hands of Korean Air (44%) and Travel Service<sup>50</sup> (34%). The remaining 2.26% are owned by insurer Ceska pojistovna.

After the sale of CSA shares to Prisko, Cesky Aeroholding will merge with the Prague airport operator Letiste Praha, one of its biggest subsidiaries at present. CSA posted a

<sup>45</sup> PM: Prime Minister

<sup>46</sup> **Aeroholding:** Czech group Český Aeroholding, a company whose sole shareholder is the state, represented by the Ministry of Finance of the CR. The main task of Czech Aeroholding is to ensure coordination, financial management and implementation of synergies within the group. Group is gradually assuming control of aviation transport companies and firms providing related ground services at the Prague/Ruzyne International Airport. It employs 4,500 people, it comprises Letiste Praha, Czech Airlines Technics, which provides technical maintenance of planes, and Czech Airlines Handling, responsible for the ground handling of aircraft and passengers.

<sup>47</sup> **CSA:** Czech Airlines, the national airline of the Czech Republic with its head office on the grounds of Václav Havel Airport Prague in Ruzyně, Prague. Czech Airlines is the subsidiary of Czech Aeroholding.

<sup>48</sup> **Prisko:** Prisko was originally set up by the National Property Fund. Its main aim was to settle all obligations after privatisation of car manufacturer Skoda Auto. At present, Prisko's main activity consists in administering financial investments and providing loans.

<sup>49</sup> **OPC:** Office for the Protection of Competition, the central authority of state administration responsible for creating conditions that favour and protect competition, supervision over public procurement and consultation and monitoring in relation to the provision of state aid.

<sup>50</sup> **Travel Service:** Travel Service Airlines is an airline with its head office on the property of Václav Havel Airport Prague in Ruzyně, Prague. It operates charter flights and also wet and dry leases aircraft to other airlines. It has subsidiaries in Poland, Hungary and Slovakia. It also operates scheduled flights under the brand name SmartWings.

profit of CZK 72.4mn in the H1 2016, which was an annual rise of CZK 60mn and the best half-year result in 10 years. Its operating profit in H1 reached CZK47.3mn, compared to an operating loss of CZK154.1mn recorded in the same period a year ago.



## FIRMS PLAN TO INVEST, RAISE WAGES BY 2.7% - 21. 10.

According to survey carried out by the CI<sup>51</sup> and the CNB among domestic companies Czech industry's good condition is confirmed by the fact that a large portion of Czech firms want to continue with investments, in many cases beyond the framework of upgrades and reconstructions. The companies also plan to raise wages by the average of 2.7% in 2016. Companies plan to boost their employee bases by 0.6%.



## KARLOVY VARY'S CONTACTS WITH CHINA – 21. 10.

Karlovy Vary continues its contacts with China. Deputy Mayor will attend the 2<sup>nd</sup> ITFMRS,<sup>52</sup> while the most of travel and accommodation costs will pay Fujian Tourism Administration organizer. The Mayor has been already 2-times in China and now expects 2 Chinese delegations in Karlovy Vary. Another Deputy Mayor accepted 3 Chinese delegation.



## FACING CEILING FOR PRODUCTION GROWTH – 21. 10.

Czech car and vehicle production, accounting for just under 30% of the country's total industrial production, is heading by the end of this year for the record figure of 1.3mn vehicles manufactured in the CR.

And while there are signs for most manufacturers that the growth will continue into 2017, some, such as Kolín-based TPCA are already facing a downturn thanks to sharp competition at the bottom of the market. TPCA sees its production slipping in 2017 to 220,000 from this year's 224,000 target. And there are signs that the auto sector is already reaching the production ceiling. HN<sup>53</sup> pointed out that Hyundai's Czech plant is now producing at full capacity on three shifts a day; the biggest car maker Škoda Auto is searching for another 100 workers; and while bus maker Iveco has a new production hall ready it must really wait until a 26-kilometre missing link in the D35 motorway is completed until it can take full advantage of the new facility. Tatra,<sup>54</sup> which last year was making 3 lorries a day with that figure now shooting up to more than 7, says that some of its suppliers are having a hard time keeping up with the demand, especially in view of the fact that annual truck production is seen rising from 1,300 this year to 1,700 in 2017. And the situation could get even tighter with Jaguar Land Rover expected to start production of cars out of its new Slovak plant near Nitra from 2018. This week Toyota also announced plans to invest around €170mn in a new car

<sup>51</sup> **CI:** Confederation of Industry

<sup>52</sup> **ITFMRS:** International Tourist Festival Maritime Silk Road in Fuzhou lasts 4 weeks. It includes the Congress of Tourism Organizations of Maritime Silk Road, the International tourist Carnival, the International Fair of thermal baths, the Festival of Folklore and Culture Fuzhou 2016 and other events.

<sup>53</sup> **HN:** Hospodářské noviny Daily

<sup>54</sup> **Tatra:** a Czech vehicle manufacturer was founded in 1850 as the third oldest car maker in the world after Daimler and Peugeot. Production of passenger cars ceased in 1999, but the company still produces a range of primarily all-wheel-drive 4×4, 6×6, 8×8, 10×10 and 12×12 trucks.

engine plant in Poland. That step follows a similar move earlier in the tear by Mercedes. Many of CE's auto producers source the same local suppliers whether it comes to the basic raw materials or parts. It points out that the Czech joint venture car producer TPCA on average sources 2,300 separate parts from 234 suppliers.

And the transport logistics for shipping the materials and parts could also start coming under pressure it can no longer cope with, the paper adds.

And there is the human factor as well. While Czech car makers are continuing to recruit – new investments last year resulted in around 4,500 jobs – the companies are also facing a downturn in thanks to demographic trends in the pool of workers that they can draw on



#### CEFC WAS LOBBIED FOR BY CSSD – 22. 10.

The CEFC<sup>55</sup> that invests in the CR is not much transparent, Deputy PM and MF Minister Babiš said after a meeting with President Zeman, adding that it was lobbied for by ČSSD<sup>56</sup> linked people. Babiš said he and Zeman exchanged opinions on relations with China. He said he does not comment on Chinese investments in the CR and does not assess Czech investments in China. Babiš said his and Zeman's opinions differ. That is why Zeman promised him a list of Chinese investments worth a total of CZK 50bn, he added.



#### FOCUSING ON THE WEST – 22. 10.

According Deputy PM Bělobrádek (KDU-ČSL<sup>57</sup>), China is an interesting market, but not everything can be fitted into economic categories. „In this world is not possible to give up on certain principles and one of those principles is that we live in a free and sovereign country and we can discuss things here. I understand that the Chinese perceive it differently, have a different culture and I respect their opinion, but they must also respect our opinion.”

MA Minister Jurečka (KDU-ČSL) thanked the MC<sup>58</sup> Minister Herman (KDU-ČSL) for organizing a meeting with the Dalai Lama, which he unfortunately could not attend because of work obligations. Jurečka leaves in a few days on a 2-day ministerial working visit to China, but he does not fear that his words might arouse the indignation of his Chinese counterparts or thwart the negotiations. Instead, he is ready to repeat his words eventually. „I suppose we are talking as two sovereign states and act together on business matters,” he said. The main content of working visit should be an issue of veterinary certificates, as a purely professional matter.



#### CHINESE INVESTMENT – 22. 10.

Chinese investors spent almost CZK 2bn in the CR this year. Compared with investment in previous years, it is a significant increase. However, with regard to the March statement by the President Zeman of supply of nearly CZK 100bn in 2016, it is a negligible amount.

<sup>55</sup> **CEFC**: China CEFC Energy Company Limited, through its subsidiaries, engages in trading of oil, petrochemical products, and oil storage. The company is based in Shanghai, China.

<sup>56</sup> **ČSSD**: Czech Social Democratic Party, centre-left party

<sup>57</sup> **KDU-ČSL**: Christian and Democratic Union – Czechoslovak People's Party, centre party

<sup>58</sup> **MC**: Ministry of Culture

Participants signed about 30 trade agreements in various fields during the participation of the presidents of CR and China at economic forum in March. According to these agreement, Chinese should invest up to CZK 232bn in the CR by 2020. It should be a sum of CZK 95bn this year.

According to the CzechInvest,<sup>59</sup> the volume of Chinese investment did not exceed CZK 500mn annually up to 2014. The sum was CZK 1.15bn in 2015, and it nearly doubled after less than 10 months this year and is approaching CZK 2bn.

CzechInvest is currently negotiating with potential Chinese investors additional CZK 20bn, but it will likely not come close to the sum announced by President Zeman.

Around CZK 120bn flow annually to the CR. However, even some domestic enterprises are investing more than the Chinese. For example, the ČEZ<sup>60</sup>'s investment were around CZK 35bn last year.



#### NUCLEAR WASTE STORAGE TO BE CLOSE TO PLANT – 23. 10.

The SÚJB's<sup>61</sup> Chairwoman Drábová has suggested that a deep nuclear waste storage site should be built in the vicinity of one of the CR's NPPs<sup>62</sup>. Drábová said the MIT<sup>63</sup> had made a mistake in trying to find a new locality. Drábová said the inhabitants of villages near Dukovany had indicated an interest in geological tests in return for adequate compensation. The MIT's plans to conduct geological tests at 7 other localities raised a storm of opposition. The deep nuclear waste storage site should be built by 2065.



#### BIG CHINESE GAME – 24. 10.

The backbone of an ambitious project One Belt, One Road<sup>64</sup> is a creation of a main naval hub with the new maritime ports and the terrestrial hub, which envisages a construction of roads and railways. According Jan Bejtkovský of the Center for Asian Studies of University of Economics Prague, „Few people in the CR know that according to official documents, one of key projects is a better rail link between China and Europe, specifically the railway from Chinese Wuhan to Mělník and Pardubice“.

Moreover, speculations are that the Chinese are interested in buying Škoda Transportation.<sup>65</sup>

<sup>59</sup> **CzechInvest**: Business and Investment Development Agency CzechInvest, is an agency of the Ministry of Industry and Trade. Established in 1992, the agency contributes to attracting foreign investment and developing domestic companies through its services and development programmes. CzechInvest also promotes the Czech Republic abroad and acts as an intermediary between the EU and small and medium-sized enterprises in implementing structural funds in the Czech Republic.

<sup>60</sup> **ČEZ**: ČEZ Group is a conglomerate of 96 companies (including the parent company ČEZ, a.s.), 72 of them in the CR. It is involved in the electricity generation, trade, distribution and heat, as well as coal mining.

<sup>61</sup> **SÚJB**: State Nuclear Safety Authority

<sup>62</sup> **NPP**: Nuclear Power Plant

<sup>63</sup> **MIT**: Ministry of Industry and Trade

<sup>64</sup> **New Silk Road**: Officially first announced in 2013 by President Xi Jinping, China's „one belt, one road” initiative aims to improve connectivity between China, Asia and Europe. The initiative merges both the land-based Silk Road (from China via Central Asia to Turkey and the EU) with the Maritime Route (via the Indian Ocean and Africa to Europe). Both routes were created with the intention of developing transportation infrastructure, facilitating economic development and increasing trade. The belt on land connects China, Central Asia, Russia, and Europe in the north and links China with the Persian Gulf and the Mediterranean Sea through Central Asia and the Indian Ocean in the south. The maritime route starts from China's coast to Europe through the South China Sea and the Indian Ocean in one route and to the South Pacific in the other – estimated to cover 4.4 billion people and US\$2.1 trillion gross production, respectively 63 percent of world population and 29 percent of world GDP.

<sup>65</sup> **Škoda Transportation**: a Czech engineering company headquartered in Plzeň. Its operations are in the area of transport engineering, manufacture of rail vehicles for urban and railway modes of transport, traction motors and drives for transport



**CHINESE CAPITAL FELL – 24. 10.**

Despite announcements of new Chinese acquisitions in the CR, Chinese capital in Czech companies decreased in volume this year, according to an annual report by the Bisnode.<sup>66</sup> Capital in Czech firms fell by around CZK 616mn to CZK 5.21bn, a decrease of around 10%. The total number of domestic companies with Chinese owners decreased by 137 to 2,086, according to analysis of ownership structure published by the agency; the volume of Chinese capital in Czech firms in 2014 and 2015 had reached historic highs: increasing by 110% from CZK 2.77 to CZK 5.83bn.

**TATRA TRUCKS CONTRACTS BY SEPTEMBER – 24. 10.**

Tatra Trucks had at the end of September 2016 fulfilled its 2016 contract plan, which totalled 1,300 vehicles. According to Tatra, the sales results are primarily owed to Tatra's regained reputation. Interest is growing in civilian series Tatra Phoenix, whose sales increased 65% y-o-y as well as in military, firefighting and rescue vehicles from series Tatra Force. The most important market remains the Czech-Slovak market with more than 435 vehicles. The 2<sup>nd</sup> is India (334 vehicles), followed by new markets Egypt and Jordan. A total of 130 vehicles will be supplied to each country. The brand current supplies production from its defence segment to these markets. In the future it wants to add the delivery of vehicles for the civilian sector.

**TEMELÍN'S 2<sup>ND</sup> UNIT TO BE OFFLINE AT END-2016 – 24. 10.**

Temelín NPP plans to shut down the unit 2 for a few days at the end of 2016. The 2<sup>nd</sup> unit, which was out of operation for several months, was restarted in the middle of October. Since then it has not yet reached its full performance as large vibrations occurred when the output of the reactor was raised to 100%. The reactor is currently running at 93% of its capacity.

After the lowering of the output, the level of vibration returned to normal. It is a non-standard situation and the turbine is really very sensitive. Now it is up to the producer to resolve the problem, he added.

In line with the schedule, the unit 2 will be taken offline before Christmas and its operation will be resumed at the beginning of January. Details are yet to be specified with the turbine's producer but the end of the year is suitable as electricity consumption goes down and it is easier to offset the missing output.

The 1<sup>st</sup> unit is not working because of a fuel replacement. Its planned shutdown began at the end of August.

Temelín NPP has also performed a test on one of its main diesel generators, which represent an important back-up source of energy which the plant would use to secure reactor cooling in the event of a blackout.

ČEZ invests CZK 3mn in the maintenance of diesel generators annually. The diesel generators are located in earthquake-resistant buildings. Their resistance is the same as that of the buildings protecting the reactor. This means

systems in the tradition of Škoda manufacturing plants. It has a strong footprint in the local and international market.

<sup>66</sup> Bisnode: a company that offers decision support in the form of digital business, marketing and credit information. Founded in 1989, Bisnode is present in 19 European countries and has its headquarters in Stockholm, Sweden

they can resist 5.5 Richter scale earthquake, which is about 100 times more than ever recorded in the plant's vicinity.

**CZECH-CHINESE FORUM SCRAPPED – 25. 10.**

President Zeman has information that a planned Czech-Chinese investment forum is to be cancelled due to MC Minister Herman's meeting with the Dalai Lama, and now he is doing his utmost for the forum to take place, his spokesman said.

**CHINESE INTERESTED IN DUKOVANY – 25. 10.**

Chinese firms are interested in taking part in the completion of nuclear power plant Dukovany, MIT Minister Mládek said after meeting of ministers for economic affairs with representatives of TUs and employers.

HN wrote that the Chinese demand a promise from the Czech government that some of the Chinese companies will gain a contract for the construction of a new nuclear unit in the CR automatically and without a tender.

"I do not know anything about that this should be without a tender. We are certainly not prepared for that," Mládek said. He conceded that such a course of action was theoretically possible. For example nuclear power plant Paks in Hungary is being built in this way. Russian firm Rosatom is completing this power plant.

Government commissioner for nuclear energy Jan Štuller said in August that talks with potential suppliers of technology for the construction of a new unit in Dukovany were beginning.

Suppliers in 6 countries - France, Russia, the USA, Japan, South Korea and China - have been addressed, Štuller said.

Ten projects are being considered, some of them international. The Czech side expects the answers by the end of October, according to earlier information.

Preparations for the construction of a new nuclear unit in Dukovany have a 3 to 4-year delay, Štuller said.

SÚJB chairwoman Drábová talked about roughly a 2-year delay last week. A change in legislation, that would accelerate the process with the permits, could help with the delays, she noted.

**LITHIUM MINING – 25. 10.**

Lithium should be purposefully extracted in the CR for the first time in the history during 3 years. Cínovecká deponie, which are majority owned fund RSJ Private Equity will acquire the lithium mica from the former tailings pond at Zinnwald. In September, the company acquired a mining permit from the Mining authority. It must prepare a project of the separation line that will separate the raw material for the production of lithium from the mined sand, which will take from 2 to 3 years, and then it will begin mining. The company, meanwhile, will try to get financial partner for the project.

The tailings left after the former mining nonferrous metals hide 2,100 t of pure lithium. However, lithium carbonate is used in industry, for example in batteries, which can be produced from pure lithium in 5 times more quantity. Tone of carbonate is sold for around \$6,000 now. The company will not sell directly the lithium carbonate and down not

consider its production so far, that is why it will sell it at lower prices.

## SECURITY & POLITICS & POLLS & RANKINGS & OTHERS

### CONFLICT OF INTEREST BILL – 19. 10

The Senate has returned a conflict of interest bill to the ChD with a proposal that it should come into force as of September 2017 rather than the beginning of the year. The proposed change is based on the argument that the authorities will need more time to prepare a register of income and property declarations. The bill, which caused friction in the ruling coalition, would prevent people with large stakes in companies from becoming ministers, while firms more than 10% owned by cabinet members would not be allowed to enter public tenders. It is widely seen as targeting AN<sup>67</sup> leader and MF Minister Babiš whose powerful conglomerate Agrofert<sup>68</sup> involves 200 companies as well as several media outlets.

### COMBATING DISINFORMATION – 20. 10.

The CR must prepare to combat disinformation and hybrid threats, the MI<sup>69</sup> Minister Chovanec said speaking at a NATO<sup>70</sup> conference. He said the government needed to untangle the misleading information spread by „successful” disinformation websites. Speaking at the same conference, the chairman of the NATO Military Committee, General Petr Pavel highlighted the particular dangers of Russian and Islamic State disinformation. A new Czech centre focused on the fight against terrorism, hybrid threats and foreign propaganda is to be created in January.

### SANCTIONS ON RUSSIA – 20. 10.

The PM Sobotka says EU sanctions against Russia must remain in place in their current form unless progress is made in resolving the conflict in Eastern Ukraine. Speaking before flying to an EU summit in Brussels, he told the ChD's Foreign Affairs Committee that he would not support a tightening of the sanctions against Moscow as he did not possess an analysis of the possible impact of additional measures. He said supporting the sanctions had not been easy for the CR as the decision had negative implications for the country's economy.

### WJP RANKING 2016 – 20. 10.

The WJP<sup>71</sup> released the WJP Rule of Law Index® 2016, the annual report measuring how the rule of law is experienced by the general public worldwide.

<sup>67</sup> ANO: ANO 2011, centre-right party

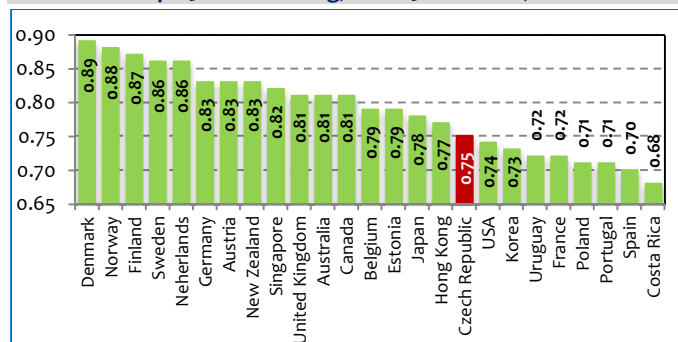
<sup>68</sup> Agrofert: an agricultural, food processing and chemical holding company based in CR. The holding consists of more than 230 companies mainly in CR, Slovakia and Germany. It is the 4<sup>th</sup> largest company in the CR by revenue with revenue exceeding CZK 117bn.

<sup>69</sup> MI: Ministry of the Interior

<sup>70</sup> NATO: the North Atlantic Treaty Organization, also called the North Atlantic Alliance, is an intergovernmental military alliance based on the North Atlantic Treaty which was signed on 4 April 1949. The organization constitutes a system of collective defence whereby its member states agree to mutual defence in response to an attack by any external party.

<sup>71</sup> WJP: World Justice Project, The WJP Rule of Law Index is the world's leading source for original data on the rule of law. The 2016 edition expands coverage to 113 countries and jurisdictions.

Graph 5: WJP ranking, TOP 25 countries, 2016



According to the Index, The CR's overall rule of law performance places it at 12 out of 24 countries in the EU/EFTA<sup>72</sup>/North America region, 17 out of 36 among high income countries, and 17 out of 113 countries and jurisdictions worldwide. The top three overall performers in the WJP Rule of Law Index 2016 were Denmark (1), Norway (2), and Finland (3); the bottom three were Afghanistan (111), Cambodia (112), and Venezuela (113).

### TEAM OF CYBER DEFENCE EXPERTS – 23. 10.

The MD<sup>73</sup> is building in secret a team of military agents who will be in charge of the country's cyber defence and who will be able to carry out a counter-attack if needed.

The MD has been looking for computing experts capable of protecting important information networks and databases, but also attacking enemy computers as hackers in case of a threat.

The construction of the NCFC<sup>74</sup> in Prague will start as soon as parliament passes an amendment to the VZ<sup>75</sup> law.

“We do not want to attack anyone, but of a concentrated attack were aimed at a target in the CR, the centre would have the ability to identify the attack and to carry out a counter-attack,” MD Minister Stropnický said.

If the state is capable of active defence, this will have a preventive effect and will discourage hackers from further attacks, president of the DSIA<sup>76</sup> Hynek said.

### WORLD BANK BUSINESS ENVIRONMENT RANKINGS – 26. 10

The CR has climbed the World Bank's annual rating of countries for their business environment. In the Doing Business 2017 survey, the CR is now placed 27<sup>th</sup>, up 9 places on its position a year earlier. The latest position is also the best ever for the country and an advance of 47 places compared with the placing in 2010. One black point in the survey is the red tape needed to get building permits where the CR's performance actually worsened from year to year.

### CANDIDACY FOR PRESIDENT – 26. 10.

MD Minister Stropnický is considering participation in the ANO potential primaries, from which candidate for

<sup>72</sup> EFTA: the European Free Trade Association is a regional trade organisation and free trade area consisting of four European states: Iceland, Liechtenstein, Norway, and Switzerland.[1] The organisation operates in parallel with the European Union (EU), and all four member states participate in the EU's single market.

<sup>73</sup> MD: Ministry of Defence

<sup>74</sup> NCFC: National Cyber Forces Centre

<sup>75</sup> VZ: Military Intelligence

<sup>76</sup> DSIA: Defence and Security Industry Association of the Czech Republic



president will emerge. ANO leader Babis suggested it to him  
at ANO Bureau meeting. ©

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