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January 20, 2022

**Statement by Mr. Bevilaqua, Ms. Mahabir, and Mr. Velloso on Czech Republic
(Preliminary)
Executive Board Meeting
January 24, 2022**

Thanks to staff for the report and Messrs. Palotai and Marek for their helpful statement. The effects of the pandemic on the Czech Republic, although significant, were mitigated by the country's strong policy buffers. While growth is estimated to have returned, supply chain issues, pension reform, and financial sector risks need to be forcefully addressed going forward.

We take positive note that growth has returned to the Czech Republic. According to staff, growth returned in 2021 and is expected to gather momentum in 2022. This is welcome. However, as the recovery is predicated on the removal of most COVID-19 related restrictions amid steady progress with vaccination, risks to the outlook are not trivial. The services sector has benefited from the removal of restrictions, but some curbs were reintroduced on the hospitality sector and large gatherings at the end of November as infections spiked. In addition, exports and manufacturing activity have been adversely affected by supply chain bottlenecks. The automotive sector—which accounts for about one-quarter of the country's industrial output—has been significantly affected by supply issues, particularly the lack of microchips.

Fiscal support during the height of the pandemic was necessary but resulted in significantly higher fiscal deficits that need to be gradually brought under control. We support a cautious scaling back of fiscal support to businesses and households as the recovery becomes entrenched. The authorities' commitment to adhere to the EU budgetary rules provides a sound base for the implementation of necessary fiscal consolidation. Like staff, we are concerned with the long-term sustainability of the pension system, which is a challenge common to several countries facing an aging population. Staff has suggested sensible measures to improve over time the pension system's sustainability. *Could staff please indicate whether the Fund has provided or is planning to provide technical assistance*

to the country on pension reform? We are encouraged by the news that the government intends to undertake a thorough pension system reform by end-2023.

While the banking sector was resilient during the pandemic, risks to financial stability need to be carefully monitored and mitigated. Staff highlighted the residential real estate sector as one area of risk due to rising property prices. We take positive note that the authorities have recently tightened some macroprudential tools. Staff also stressed that regional financial system interlinkages expose the Czech banking system to potential regional spillover vulnerabilities. However, we note that the authorities view these interlinkages and contagion risks as limited. *We would be grateful if staff could please further elaborate on these interlinkages, their importance, the degree of potential spillover, and actions the authorities are taking to manage these risks.* As in many economies during the pandemic, the regulatory authorities enacted various measures to protect the financial system. We support the phasing out of such support measures as the economy recovers while monitoring and taking appropriate actions to deal with rising non-performing loans.

With these remarks we wish the Czech authorities success in their future endeavors.