

The Czech economy is facing a combination of exceptionally strong inflation pressures causing escalating broad-based price growth. Inflation in the domestic economy continues to hit new long-term highs in rapid succession.

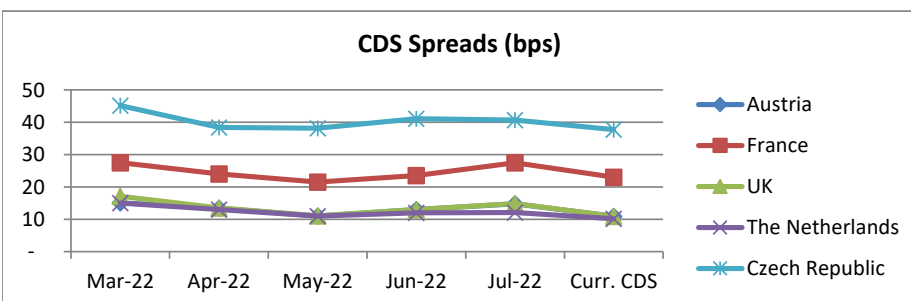
Consumer prices are being pushed up by rising costs, reflecting domestic and foreign factors, including higher energy prices, and growth in the margins of domestic producers, retailers and service providers amid a still solid income situation of households. A tight labour market will buttress private incomes, but weaker sentiment and rising prices will weigh on domestic demand. Inflation is expected to increase further, before gradually returning towards the tolerance band around the 2% target. Since June 2021, the Czech National Bank has cumulatively raised its policy interest rate by 550 basis points, to 5.75% in May 2022 and further rate rises are assumed until the summer of 2022. A gradual fiscal consolidation in structural terms is planned from this year onwards. We are affirming.

Annual Ratios (source for past results: IMF)

<b>CREDIT POSITION</b>	2019	2020	2021	P2022	P2023	P2024
Debt/ GDP (%)	37.8	47.1	48.4	54.4	60.4	65.9
Govt. Sur/Def to GDP (%)	1.0	-4.9	-5.3	-5.5	-5.7	-5.4
Adjusted Debt/GDP (%)	37.8	47.1	48.4	54.4	60.4	66.0
Interest Expense/ Taxes (%)	3.4	3.8	4.0	4.1	4.3	4.3
GDP Growth (%)	7.0	-1.7	7.5	2.3	2.3	2.5
Foreign Reserves/Debt (%)	150.6	132.9	127.1	111.3	98.0	87.6
Implied Sen. Rating	AA+	AA-	AA	AA	AA	AA

<b>INDICATIVE CREDIT RATIOS</b>	AA	A	BBB	BB	B	CCC
Debt/ GDP (%)	100.0	115.0	130.0	145.0	170.0	200.0
Govt. Sur/Def to GDP (%)	2.5	0.5	-2.0	-5.0	-8.0	-10.0
Adjusted Debt/GDP (%)	95.0	110.0	125.0	140.0	160.0	190.0
Interest Expense/ Taxes (%)	9.0	12.0	15.0	22.0	26.0	35.0
GDP Growth (%)	3.5	3.0	2.0	1.0	-1.0	-5.0
Foreign Reserves/Debt (%)	3.0	2.5	2.0	1.5	1.0	0.5

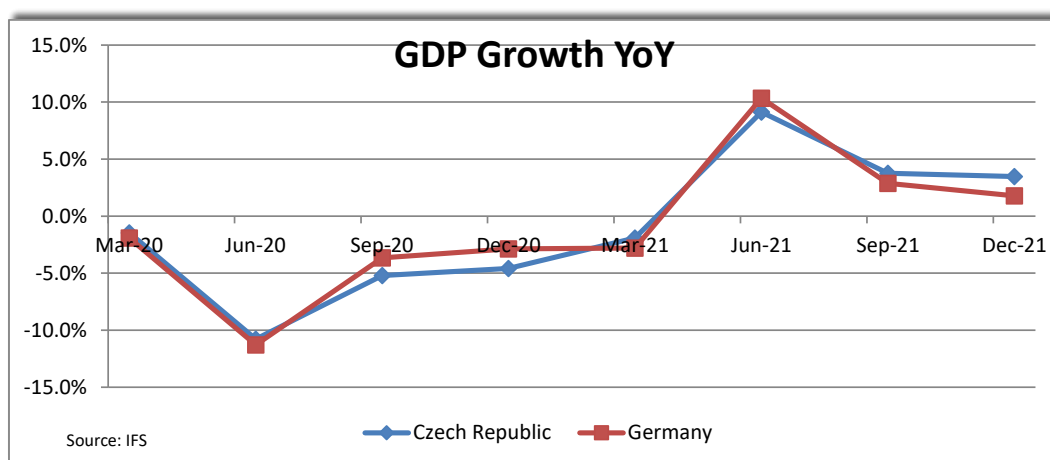
<b>PEER RATIOS</b>	Other NRSRO Sen.	Debt as a % GDP	Govt. Surp. Def to GDP (%)	Adjusted Debt/ GDP	Interest Expense/ Taxes %	GDP Growth (%)	Ratio- Implied Rating*
Federal Republic Of Germany	AAA	77.8	-3.6	77.8	2.4	6.0	AA
Kingdom Of The Netherlands	AA+	66.2	-2.5	66.2	2.2	7.6	AA-
Republic Of Austria	AA+	102.1	-5.2	102.1	4.0	6.2	A+
French Republic	AA	137.3	-6.0	137.3	4.6	8.2	A-
United Kingdom	AA	190.8	-8.9	190.8	9.4	7.8	BBB



Country	EJR Rtg.	CDS
Austria	A+	11
France	A+	23
UK	A+	11
The Netherlands	AA-	10
Czech Republic	AA	38

**Economic Growth**

Czech firms continue to face rapid growth in costs, driven largely by import prices. Besides rising foreign industrial producer prices, the growth in import prices is dominated by skyrocketing energy prices. The Czech economy will continue to operate amid persisting problems in global logistics and supplies of materials and components for production. Given its significant industrial orientation, these problems will dampen growth in total domestic economic activity until mid-2023. However, their impact on GDP will be smaller than last year and will gradually disappear next year. The Czech Republic's economy expanded by 0.2 percent seq. in Q2'22, slowing slightly from a 0.9 percent advance in the previous period while analysts expected it to contract 0.4 percent, preliminary estimates showed. On the expenditure side, support came primarily from higher domestic demand.



**Fiscal Policy**

Fiscal policy will reduce economic growth slightly this year, as the measures previously adopted to support the economy have been discontinued. Government expenditure to offset the impact of higher energy prices on households and firms and to support refugees will have the opposite effect. The general consensus assumes that fiscal policy will have a slightly expansionary effect next year, mainly due to continued provision of energy compensation.

	Surplus-to-GDP (%)	Debt-to-GDP (%)	5 Yr. CDS Spreads
Czech Republ	-5.26	48.39	37.71
Germany	-3.62	77.80	10.21
The Netherla	-2.53	66.21	23.02
Austria	-5.19	102.08	10.93
France	-5.97	137.28	10.16
UK	-8.88	190.85	10.93

Sources: Thomson Reuters and IFS

**Unemployment**

The unemployment rate remains very low and firms are facing labour shortages despite the rapid integration of many tens of thousands Ukrainian refugees into the labour force. The Czech unemployment rate ticked down to 3.1 percent in June of 2022 from 3.2 percent in the previous month, below market expectations of 3.2 percent. It was the lowest jobless rate since March of 2020 as the number of job seekers fell by 4.2 thousand from the previous month to 231.3 thousand.

	Unemployment (%)	
	2020	2021
Czech Reput	0.00	0.00
Germany	3.83	3.58
The Netherla	4.85	4.23
Austria	6.03	6.20
France	8.03	7.88
UK	0.00	0.00

Source: Intl. Finance Statistics

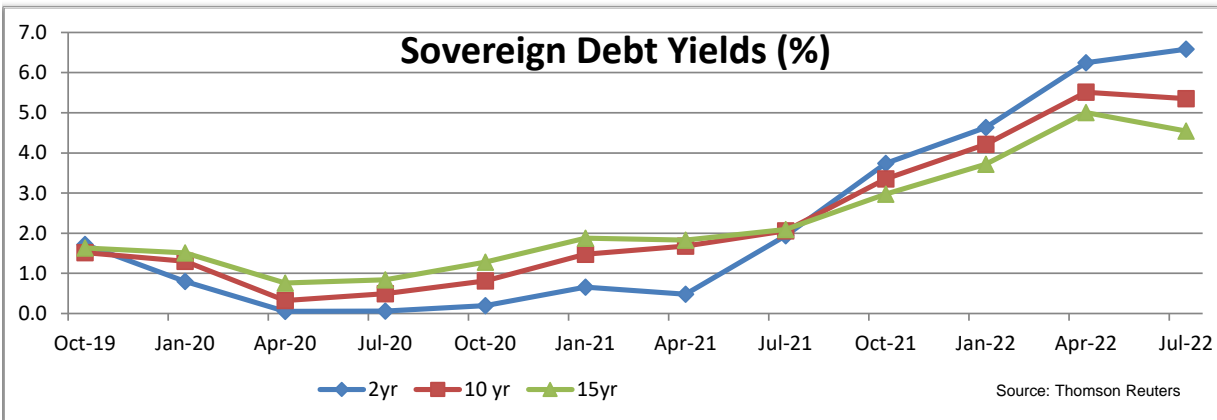
**Banking Sector**

The total assets of the Czech banking sector stood at CZK 9,662 billion at the end of June 2022, down by CZK 15 billion MoM. Loans to residents are the predominant asset item. Their volume reached CZK 6,602 billion. Deposits of residents, which are the most important item among banking sector liabilities, totalled CZK 6,220 billion. The volume of loans to resident households amounted to CZK 2,100 billion in June 2022 and increased by CZK 19 billion month on month.

Bank Assets (billions of local currency)		
	Assets	Mkt Cap/ Assets %
Komerční Banka	1,244.4	9.6
Total	1,244.4	
EJR's est. of cap shortfall at 10% of assets less market cap		5.6
Czech Republic's GDP		6,120.6

**Funding Costs**

In 2021, lending interest rate for Czech Republic was 3.2 %. Lending interest rate of Czech Republic fell gradually from 6.72 % in 2002 to 3.2 % in 2021. In May 2022, the Czech central bank raised its main interest rate by a larger-than-expected 75 basis points to 5.75%, the highest since 1999, as inflation soared on global price shocks and a tight domestic labour market. The Central Bank's decision still fell short of a rate increase assumed by the bank's new economic forecast which sees three-month interbank rates, a proxy for official rates, peaking at 8.4% in Q3'22.



**Ease of Doing Business**

Major factors for growing the economy are the ease of doing business and the economic freedom; although not the sole factor for determining economic growth, a country which makes it easy for businesses to operate and provides a reasonably free environment to conduct business has a good chance for growth. The chart on the right indicates that with an overall rank of 41 (1 is best, 189 worst) is above average.

The World Bank's Doing Business Survey*			
	2021	2020	Change in
	Rank	Rank	Rank
<b>Overall Country Rank:</b>	<b>41</b>	<b>41</b>	<b>0</b>
<b>Scores:</b>			
Starting a Business	134	134	0
Construction Permits	157	157	0
Getting Electricity	11	11	0
Registering Property	32	32	0
Getting Credit	48	48	0
Protecting Investors	61	61	0
Paying Taxes	53	53	0
Trading Across Borders	1	1	0
Enforcing Contracts	103	103	0
Resolving Insolvency	16	16	0

\* Based on a scale of 1 to 189 with 1 being the highest ranking.

**Economic Freedom**

As can be seen below, Czech Republic is above average in its overall rank of 73.8 for Economic Freedom with 100 being best.

<b>Heritage Foundation 2021 Index of Economic Freedom</b>				
<b>World Rank 73.8*</b>				
	<b>2021</b>	<b>2020</b>	<b>Change in</b>	<b>World</b>
	<b>Rank**</b>	<b>Rank</b>	<b>Rank</b>	<b>Avg.</b>
<b>Property Rights</b>	<b>76.2</b>	<b>76.8</b>	<b>-0.6</b>	<b>53.6</b>
<b>Government Integrity</b>	<b>56.8</b>	<b>64.2</b>	<b>-7.4</b>	<b>45.9</b>
<b>Judicial Effectiveness</b>	<b>64.4</b>	<b>49.9</b>	<b>14.5</b>	<b>45.4</b>
<b>Tax Burden</b>	<b>79.1</b>	<b>82.0</b>	<b>-2.9</b>	<b>77.7</b>
<b>Gov't Spending</b>	<b>51.4</b>	<b>52.7</b>	<b>-1.3</b>	<b>67.1</b>
<b>Fiscal Health</b>	<b>98.1</b>	<b>97.8</b>	<b>0.3</b>	<b>72.1</b>
<b>Business Freedom</b>	<b>68.8</b>	<b>69.7</b>	<b>-0.9</b>	<b>63.2</b>
<b>Labor Freedom</b>	<b>77.1</b>	<b>77.6</b>	<b>-0.5</b>	<b>59.5</b>
<b>Monetary Freedom</b>	<b>79.7</b>	<b>80.8</b>	<b>-1.1</b>	<b>74.7</b>
<b>Trade Freedom</b>	<b>84.0</b>	<b>86.4</b>	<b>-2.4</b>	<b>70.7</b>

\*Based on a scale of 1-100 with 100 being the highest ranking.  
 \*\*The ten economic freedoms are based on a scale of 0 (least free) to 100 (most free).  
 Source: The Heritage Foundation

**Credit Quality Driver: Taxes Growth:**

Czech Republic has seen a decline in taxes of 1.4% per annum in the last fiscal year which is disappointing. We expect tax revenues will decline by approximately 1.4% per annum over the next couple of years and 0.5% per annum for the next couple of years thereafter.

**Credit Quality Driver: Total Revenue Growth:**

CZECH REPUBLIC's total revenue growth has been less than its peers and we assumed a 0.4% decline in total revenue over the next two years.

Income Statement	Peer Median	Issuer Avg.	Assumptions	
			Yr 1&2	Yr 3,4,5
Taxes Growth%	11.6	(1.4)	(1.4)	0.5
Social Contributions Growth %	5.1	11.4	11.0	11.0
Grant Revenue Growth %	0.0	NMF		
Other Revenue Growth %	0.0	NMF		
Other Operating Income Growth%	0.0	8.0	(2.8)	(2.8)
Total Revenue Growth%	8.7	4.8	(0.4)	(0.4)
Compensation of Employees Growth%	3.5	6.7	6.7	6.7
Use of Goods & Services Growth%	10.8	2.3	2.3	2.3
Social Benefits Growth%	3.5	6.0	6.0	6.0
Subsidies Growth%	(4.8)	15.1		
Other Expenses Growth%	0.0			
Interest Expense	1.5	1.5	1.5	
Currency and Deposits (asset) Growth%	1.3	0.0		
Securities other than Shares LT (asset) Growth%	(3.0)	0.0		
Loans (asset) Growth%	(31.0)	(269.4)	(1.4)	(1.4)
Shares and Other Equity (asset) Growth%	(9.9)	(133.1)	2.0	2.0
Insurance Technical Reserves (asset) Growth%	0.0	7.4	7.4	7.4
Financial Derivatives (asset) Growth%	(16.1)	(56.9)	(10.0)	(10.0)
Other Accounts Receivable LT Growth%	(1.8)	(2.3)	(2.3)	(2.3)
Monetary Gold and SDR's Growth %	0.0	0.0	5.0	5.0
Other Assets Growth%	0.0	0.0		
Other Accounts Payable Growth%	2.2	20.7	3.0	3.0
Currency & Deposits (liability) Growth%	10.1	47.5	47.5	42.7
Securities Other than Shares (liability) Growth%	2.6	5.9	4.1	4.1
Loans (liability) Growth%	(3.7)	50.7	50.7	45.6
Insurance Technical Reserves (liability) Growth%	0.0	(14.4)	3.0	3.0
Financial Derivatives (liability) Growth%	0.0	363.5	363.5	327.2
Additional ST debt (1st year)(billions CZK)	0.0	0.0		

**ANNUAL OPERATING STATEMENTS**

Below are Czech Republic's annual income statements with the projected years based on the assumptions listed on page 5.

	ANNUAL REVENUE AND EXPENSE STATEMENT					
	(BILLIONS CZK)					
	2018	2019	2020	2021	P2022	P2023
Taxes	1,106	1,179	1,137	1,121	1,105	1,090
Social Contributions	834	895	909	1,013	1,125	1,248
Grant Revenue						
Other Revenue						
Other Operating Income	<u>305</u>	<u>321</u>	<u>320</u>	<u>346</u>	<u>346</u>	<u>346</u>
Total Revenue	<u>2,245</u>	<u>2,394</u>	<u>2,367</u>	<u>2,480</u>	<u>2,576</u>	<u>2,684</u>
Compensation of Employees	521	576	633	676	722	770
Use of Goods & Services	326	339	346	354	362	371
Social Benefits	818	886	1,025	1,087	1,151	1,220
Subsidies	119	128	173	199	199	199
Other Expenses				197	197	197
Grant Expense						
Depreciation	209	220	232	244	244	244
Total Expenses excluding interest	<u>2,138</u>	<u>2,299</u>	<u>2,603</u>	<u>2,757</u>	<u>2,876</u>	<u>3,001</u>
Operating Surplus/Shortfall	107	96	-236	-277	-300	-317
Interest Expense	<u>40</u>	<u>41</u>	<u>44</u>	<u>45</u>	<u>46</u>	<u>46</u>
Net Operating Balance	67	55	-280	-322	-346	-364

**ANNUAL BALANCE SHEETS**

Below are Czech Republic's balance sheets with the projected years based on the assumptions listed on page 5.

Base Case	ANNUAL BALANCE SHEETS (BILLIONS CZK)					
	2018	2019	2020	2021	P2022	P2023
<b>ASSETS</b>						
Currency and Deposits (asset)	577	600	715	863	863	863
Securities other than Shares LT (asset)	14	13	15	16	16	16
Loans (asset)	-8	-5	-3	5	4	4
Shares and Other Equity (asset)	0	0	1	0	0	0
Insurance Technical Reserves (asset)	4	4	4	4	4	5
Financial Derivatives (asset)	1	0	1	0	0	0
Other Accounts Receivable LT	345	353	366	357	349	341
Monetary Gold and SDR's						
Other Assets					920	920
Additional Assets	<u>767</u>	<u>763</u>	<u>810</u>	<u>920</u>		
Total Financial Assets	1,699	1,729	1,908	2,164	2,156	2,148
<b>LIABILITIES</b>						
Other Accounts Payable	356	358	412	498	513	528
Currency & Deposits (liability)	9	5	11	16	16	16
Securities Other than Shares (liability)	1,629	1,685	2,129	2,254	2,346	2,443
Loans (liability)	172	139	126	190	536	900
Insurance Technical Reserves (liability)	5	4	4	3	3	3
Financial Derivatives (liability)	0	0	0	2	9	40
Other Liabilities						
Liabilities	2,171	2,191	2,683	2,963	3,301	3,657
Net Financial Worth	<u>-472</u>	<u>-463</u>	<u>-775</u>	<u>-799</u>	<u>-1,145</u>	<u>-1,509</u>
Total Liabilities & Equity	1,699	1,729	1,908	2,164	2,156	2,148

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#### **Comments on the Difference between the Model and Assigned Rating**

In this case, there has been little change in the recent results and therefore we have used our best judgement in making adjustments which are reflected in the results for the projected ratings. We have assigned a rating of "AA" whereas the ratio-implied rating for the most recent period is "AA"; we expect results to remain approximately the same.

#### **Changes in Indicative Ratios**

We have not made any adjustment in the indicative ratios at this time.



**SEC Rule 17g-7(a) Disclosure (Non-NRSRO)**

Below are the disclosures as required by Paragraph (a) of Rule 17g-7.

**1. The symbol in the rating scale used to denote the credit rating categories and notches within categories and the identity of the obligor, security, or money market instrument as required by Paragraph (a)(1)(ii)(A) of Rule 17g-7:**

For the issuer CZECH REPUBLIC with the ticker of 1040Z CP we have assigned the senior unsecured rating of AA.

There are three notches in our rating categories (e.g., A- A, and A+) except for AAA and those deep into speculative grade, i.e., CC, C, and D do not have notches.

**2. The version of the procedure or methodology used to determine the credit rating as required by Paragraph (a)(1)(ii)(B) of Rule 17g-7:**

We are using the Methodologies for Determining Credit Ratings (Main Methodology) version #15a available via [egan-jones.com](http://egan-jones.com) under the tab at the bottom of the page "Methodologies".

**3. The main assumptions and principles used in constructing the procedures and methodologies used to determine the credit rating as required by Paragraph (a)(1)(ii)(C) of Rule 17g-7:**

The credit rating assigned reflects our judgement regarding the future credit quality of the issuer. Regarding the specific assumptions used, please refer to projections on pages 1, 6, and 7 of this Rating Analysis Report.

**4. The potential limitations of the credit rating as required by Paragraph (a)(1)(ii)(D) of Rule 17g-7:**

Our rating pertains solely to our view of current and prospective credit quality. Our rating does not address pricing, liquidity, or other risks associated with holding investments in the issuer.

**5. Information on the uncertainty of the credit rating as required by Paragraph (a)(1)(ii)(E) of Rule 17g-7:**

Our rating is dependent on numerous factors including the reliability, accuracy, and quality of the data relied upon in determining the credit rating. The data is sourced from publicly available information from the IMF and other similar sources. In some cases, the information is limited because of issues such as the lack of reported data, a delay in reporting data, restatements, inaccurate accounting and other issues. Such issues are not always readily apparent. EJR aims to identify such shortcomings and make adjustments using its best judgement.

**6. Whether and to what extent third-party due diligence services have been used in taking the rating action as required by Paragraph (a)(1)(ii)(F) of Rule 17g-7:**

EJR does not utilize third-party due diligence services.

**7. How servicer or remittance reports were used, and with what frequency, to conduct surveillance of the credit rating as required by Paragraph (a)(1)(ii)(G) of Rule 17g-7:**

Servicer or remittance reports normally pertain to structured finance issuers; this report does not pertain to a structured finance issuer (EJR is not an NRSRO for structured finance or sovereigns/ municipal issuers). Regarding surveillance, the minimum time period for corporation issuers is normally one year.

**8. A description of the data that were relied upon for the purpose of determining the credit rating as required by Paragraph (a)(1)(ii)(H) of Rule 17g-7:**

EJR uses publicly available information from the IMF, governmental filings and other similar sources for ratings on sovereign issuers.

**9. A statement containing an overall assessment of the quality of information available and considered in the credit rating as required by Paragraph (a)(1)(ii)(I) of Rule 17g-7: The information is generally high quality and readily available.****10. Information relating to conflicts of interest as required by Paragraph (a)(1)(ii)(J) of Rule 17g-7:**

This rating is unsolicited.

**11. An explanation or measure of the potential volatility of the credit rating as required by Paragraph (a)(1)(ii)(K) of Rule 17g-7:**

Our rating aims to assess the probability of the payment of obligations in full and on-time. Factors which affect such probability, and in turn our rating, include changes in the operating performance of the issuer, changes in capital structure, and merger and acquisition events.

**12. Information on the content of the credit rating as required by Paragraph (a)(1)(ii)(L) of Rule 17g-7:**

Regarding the historical performance of the credit rating, our rating transition matrix is available in our Form NRSRO, exhibit 1. The expected probability of default and the expected loss in the event of default is listed on the first page of this report.

**13. Information on the sensitivity of the credit rating to assumptions as required by Paragraph (a)(1)(ii)(M) of Rule 17g-7:**

Below is a summary of the impact of the 5 assumptions which independently would have the greatest impact on our "ratio-implied rating":

	Assumptions			Resulting Ratio-Implied Rating		
	Base	Optimistic	Pessimistic	Base	Optimistic	Pessimistic
Taxes Growth%	(1.4)	2.6	(5.4)	AA	AA	AA-
Social Contributions Growth %	11.0	14.0	8.0	AA	AA	AA
Other Revenue Growth %		3.0	(3.0)	AA	AA	AA
Total Revenue Growth%	(0.4)	1.6	(2.4)	AA	AA	AA
Monetary Gold and SDR's Growth %	5.0	7.0	3.0	AA	AA	AA

**14. If the credit rating is assigned to an asset-backed security, a description of: (i) the representations, warranties, and enforcement mechanisms available to investors; and (ii) how they differ from the representations, warranties, and enforcement mechanisms in issuances of similar securities, as required by Paragraph (a)(1)(ii)(N) of Rule 17g-7:**

This credit rating is not assigned to an asset-backed security.

**ATTESTATION FORM**

In compliance with the US Securities and Exchange Commission (SEC) Rule 17g-7(a), the Egan-Jones analyst who published the report is responsible for the rating action and to the best knowledge of the person:

- 1) No part of the credit rating was influenced by any other business activities,
- 2) The credit rating was based solely upon the merits of the obligor, security, or money market instrument being rated, and
- 3) The credit rating was an independent evaluation of the credit risk of the obligor, security, or money market instrument.

**Analyst Signature:**

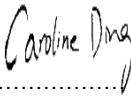
**Today's Date**

.....  
 Subramanian NG  
 Senior Rating Analyst

August 29, 2022  
 .....

**Reviewer Signature:**

**Today's Date**

  
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 Caroline Ding  
 Rating Analyst

August 29, 2022  
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## Sovereign Rating Methodology (Non-NRSRO)

**Scope and Limitations: Sovereign Issuer Credit Quality Ratings (CQR) are a forward-looking assessment of a sovereign's capacity and willingness to honor its existing and future obligations in full and on time. Sovereigns are assigned two CQRs: a Local-Currency CQR, which reflects the likelihood of default on debt issued and payable in the currency of the sovereign, and a Foreign-Currency CQR, which is an assessment of the credit risk associated with debt issued and payable in foreign currencies.**

**Key Rating Drivers: EJR's approach to sovereign risk analysis is a synthesis of quantitative and qualitative judgments. The quantitative factors EJR uses are:**

- Debt in relation to GDP.
- Surplus or deficit in relation to GDP.
- Debt plus potential under-funding of major banks in relation to GDP.
- Interest expense in relation to taxes.
- GDP growth.
- Foreign reserves in relation to debt.

Debt levels for many sovereign issuers have increased at an accelerating rate over the past decade, affecting implied ratings. EJR also considers unemployment levels and funding costs. EJR recognizes that no model can fully capture all the relevant influences on sovereign creditworthiness, meaning that the its sovereign ratings can and do differ from those implied by the rating model. Some of the qualitative factors that impact its ultimate assessment of credit quality include the flexibility, stability and overall strength of the economy, efficiency of tax collection, acceptance of contract law, ease of doing business, trade balances, prospects for future growth and health and monetary policy, and economic freedom. These subjective and dynamic qualitative issues are not captured by the model but affect sovereign ratings

*For additional information, please see Exhibit 2: Methodologies in EJR's Form NRSRO.*