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Czech Economic Convergence: Glass Ceiling
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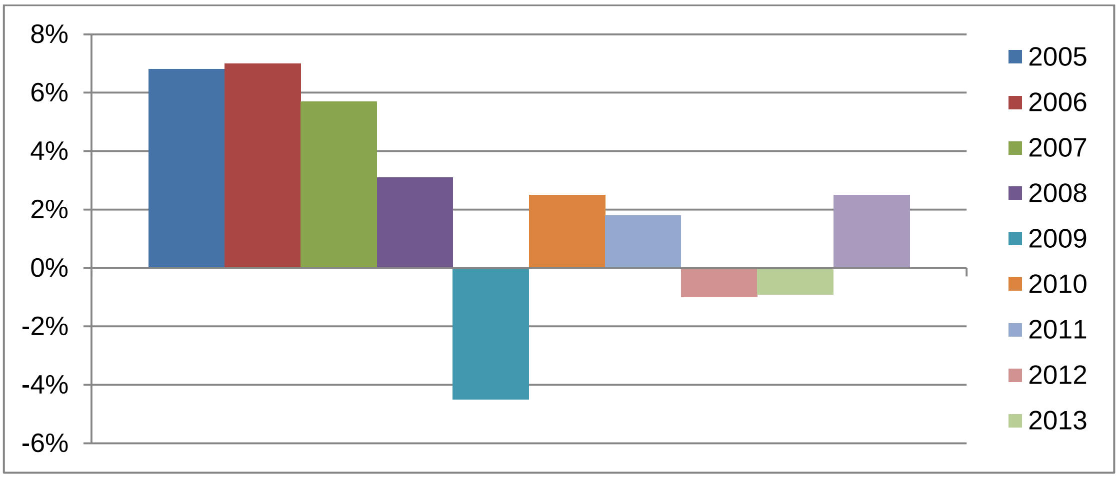
The stalled Convergence

At the beginning of transformation in the 1990s and after the dissolution of Czechoslovakia in 1993, economic indicators granted the Czech Republic an unquestionable first place within its region. The Czech Republic was also the first country form the Visegrad region which graduated from eligibility for World Bank lending (in fiscal year 2005, one year after Slovenia and two years before Estonia and Latvia).

The economic recession in the Czech Republic after the global financial crisis took shape of "W" with deep first "V" and a wide second "V". This contrasts with Polish continual growth over the whole previous decade and the situation in Slovakia, where only a simple "V"-shape recession occurred.

Figure 1. Czech GDP within the last 10 years										
Year	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014 (est.)
GDP growth (%)	6.8	7.0	5.7	3.1	-4.5	2.5	1.8	-1	-0.9	2,5



Source: Source: The World Bank [accessed: 28.1.2015]
2014 estimate by the Czech National Bank [6.11. 2014; accessed: 29.1.2015]

As a result, the long term difference between Czech and Slovak GDP per capita has now been almost fully erased. The commentaries on this fact mention that the Czech GDP per capita stalled roughly at the level of 80% of the EU average (already reached by the Czech Republic in the previous decade) and cannot progress significantly further.

Why the Glass ceiling?

The Czech Republic has several comparative advantages within its region, including relatively high level of savings, locality in the centre of Europe, high level of FDIs and relatively developed educational system (Office of Government, 2014).

Why are not those advantages transformed into swifter economic convergence to EU GDP per capita average?

Several possible answers:

- Frequent **changes of governments** (8 different prime ministers within last decade).
- Lack of lasting **structural reforms** (e.g. pension system, health care, justice).
- Frequent **changes of legislation** (including the completely new Civil Code which was subject to announced amendments even before its entry into force).
- Unfinished modern **infrastructure network** (highway, railway).
- Inability to tap EU **cohesion funds** (the worst situation in whole EU, estimate of 60 billion CZK of possibly untapped funding in the EU 2007-2013 Financial Framework).
- Bottleneck of the **state administration** (the Civil Service Act concerning the status of officials entered into force just on January 1, 2015).
- Increasing **red tape** (including the obligatory changes of incorporation documents due to reform of the corporate law in 2014).
- The unchecked scale of **Gold-Plating** together with Czech inability to secure, in reasonable cases, a proper wording of exceptions from **EU secondary legislations** that would be fitting to the Czech institutional framework.

Czech level of debt

The current level of the Czech Republic Government Debt is at 46% of GDP level (significantly lower than in most neighbouring countries, but despite the claimed austerity measures significantly higher in contrast to the 28% of GDP in the year 2008).

This relatively good result together with high level of capital available in Czech banks that seeks investments in government bonds provide the Czech Republic with significantly low costs on financing public debt (the annual interest rate on Czech ten-year bonds fell in November 2014 to a historic low of 0.87%, with better results in the EU for this instrument recorded only in Germany: 0.82%; and this positive trend has continued in the following months).

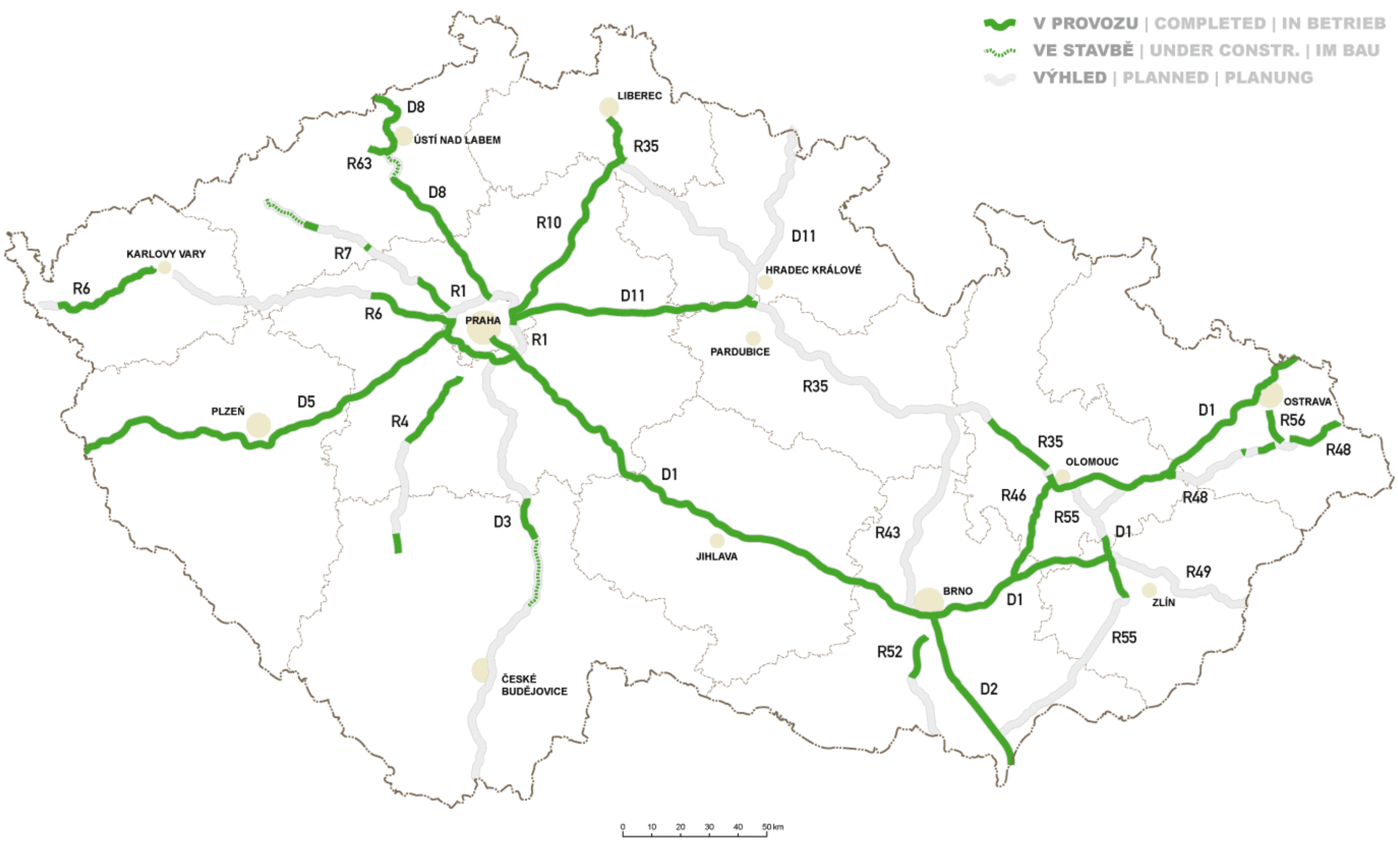
The Czech Republic and infrastructure

Highway infrastructure: Unfinished network including the main connection hubs

The actual length of highway network in the Czech Republic is 1,242 km, which is only slightly more than half of the whole planned network of approx. 2,180 km (ceskedalnice.cz).

Just these numbers show that the Czech highway network is unfinished. Several of its key parts are still missing, including the whole connection to Austria trough the biggest city in southern Bohemia České Budějovice (the planned D3) or northern horizontal connection through the country which would be parallel to the spinal and worn out southern D1 (Prague – Brno) highway. Also the outer circuit around Prague is missing which results in transit transport through the capital city.

Figure 2: Map of the Czech highway network (to January 1, 2013)



Source: www.ceskedalnice.cz.

Railway infrastructure: Densest network but three times slower than TGV

The Czech Republic has the second densest railway network worldwide. It is at the level of 199 km of railroad per every 1,000 km2 of land area, while the highest railway density worldwide is in Belgium 211 km (helgilibrary.com).

Modern high-speed train connection is however lacking. For instance, fastest available connection between the two biggest Czech cities Prague – Brno (2h 37m) takes almost three times more time than connection by TGV *Atlantique* on similar length of track between Paris – Le Mans (0h 57m). Similarly, fastest train connection Prague – Berlin (4h 38m) takes more than three times more of traveller's time than a trip on destination of similar length Paris – Brussels (1h 25m) with TGV *Thalys* (raileurope-world.com).

Infrastructure development: Right investment or corruption black hole?

The Czech Republic currently has comparatively low level of debt and one of the lowest interest rates on long term government bonds from the whole EU. This raises a question whether state should take an advantage of this situation and should invest (even with use of debt) to infrastructure projects, at least to finish the most important spinal highway connections. Under the given situation and after proper and conservative assessments of growth potential it may be considered as a sound investment by any entrepreneur. On the other hand, increase of debt in case of state is not safe from political risks, as other stakeholders, not just transportation sector, may seek increase of spending leading to spiral debt growth. There is also a risk of increased corruption in construction procurements. Finally, the primary reason for slow progress in the past was not lack of money but rather belated legal preparations, including land purchases, settlement of environmental claims and rights for use of countryside. Deep changes in legislation are therefore necessary before such large investments can even start to be considered.

Figure 3: Infrastructure investments with use of debt

Pros	Cons
GDP growth related to construction and better connectivity.	Risks of increased spending in other sectors through spillover.
Increase of mobility of population, removing transit traffic from cities, increased safety of transportation.	Risk of increased corruption in construction procurements.
	Necessary changes of legislation for development of the so called "linear constructions" still lacking.

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- organize educational projects;
- present critical assessment and comments on current events for local and international press;
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- support the interest in international relations among broad public;
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