

## **Aleš Michl: Remarks - 2024 Mexico City conference**

Remarks by Mr Aleš Michl, Governor of the Czech National Bank, at the Central Banking Autumn Meetings, Mexico City, 14 November 2024.

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### **Inflation**

When I became governor two and a half years ago, inflation was at its highest level since the transition from communism to capitalism 30 years ago, standing at 17.5%. We successfully reduced it to exactly 2% at the beginning of this year (Michl, 2024). This made us one of the first countries in Europe to hit the target. However, inflation is not dead; it has since risen to 2.8% in the Czech Republic in October.

After a period of high inflation, we are now entering a phase of higher inflation volatility around central bank targets, with an upside risk. The challenge stems from the fact that, prior to COVID, interest rates were near zero for over a decade, resulting in excessive money creation in the economy. This has led to persistent inflationary pressures (Michl, 2024). To address this, the policy mix should consist of two elements: firstly, maintaining interest rates higher than pre-COVID levels for a prolonged period; and secondly, governments must balance their budgets. Failure to do so could risk a second wave of inflation, with another cost shock potentially acting as a trigger.

In December 2023, we began reducing rates gradually – from 7% to the current 4%. Nonetheless, some degree of restriction is necessary to ensure low core inflation, which is critical for keeping headline inflation in check in a small and open economy like the Czech Republic. Looking ahead, core inflation may need to be slightly below 2%. Since this is not reflected in our current outlook, we are already discussing the appropriate time to pause rate cuts.

### **Payments**

Our vision is to enable individuals and businesses to conduct instant online payments seamlessly. With the Czech koruna, we've already achieved this through a new instant payment system in collaboration with banks, where transfers are completed within seconds. Instant payments are now widely accepted. Over the next two years, our focus will shift to enabling Czech clients to make instant payments in euros, not only domestically, but also with clients across the Eurozone.

We have also created a brand for instant payments.

### **Trade**

Before the Lehman Brothers collapse, automation, restructuring and offshoring of labour-intensive production significantly increased capital per worker in manufacturing. This was an area of strength for the Czech Republic. However, there is now a noticeable slowdown in total factor productivity growth in manufacturing as the global

economy shifts towards exporting services, with the export of goods relative to GDP in decline (Baldwin, 2023). For instance, in terms of engineering, Škoda Auto outperforms new competitors such as Tesla. However, when it comes to software, we are lagging behind. The emerging trend is clear: software and services are prevailing.

## AI

Productivity growth is all about maximising the return on labour and investment. **Third-generation AI (Deep Learning/Chat GPT, Grok-)** has the potential to deliver a one-off productivity boost by acting as an assistant – it enhances efficiency, saves costs and simplifies tasks. However, its role in long-term growth will depend on how well it is integrated into ongoing innovation cycles, business models, products and services. For AI to drive long-term productivity growth, it must help the Czech Republic in exporting services and fostering innovation.

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## References

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