CZECH REPUBLIC

Rating Analysis - 5/16/16

*EJR Sen Rating(Curr/Prj) AA/ AA
*EJR CP Rating: A1+
EJR's 3 yr. Default Probability: 1.0%

Strong recovery - The Czech economy has seen a solid growth since the second quarter of 2013, when the country finally ended its longest recession in history. Robust export performance and improved private spending drove up real GDP growth from -0.5% in 2013 to 4.3% in 2014, while public debt likewise alleviated as debt growth rate decelerated from +14.2% in 2012 to -1.12% in 2014. Budget deficit rose slightly on account of lessened fiscal austerity, while public debt dropped from 45.2% of GDP in 2012 to 42.8% in 2014, remaining low compared to the regional average.

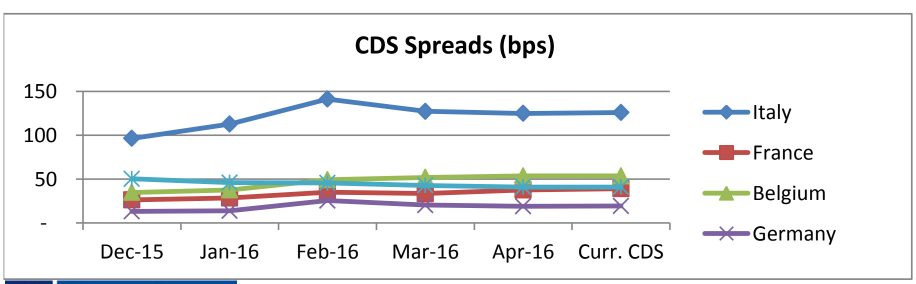
One major source of concern is the country's high reliance on export. While Czech's recent performance in face of the Russia crisis might have provided some assurance, the economy's resilience to external shocks remains to be tested. A potential decline in demand from one of its neighboring countries might pull down the economy and propel the public debt to increase at a rate above 10%, as seen in 2012 when the Czech government raised debt in an effort to revitalize the economy. We are assigning a rating of "AA".

Annual Ratios (source for past results: IMF)

CREDIT POSITION	2012	2013	2014	P2015	P2016	P2017
Debt/ GDP (%)	44.7	45.2	42.7	45.6	48.4	51.2
Govt. Sur/Def to GDP (%)	-4.7	-2.4	-2.8	-2.8	-2.8	-2.8
Adjusted Debt/GDP (%)	44.7	45.2	42.7	45.7	48.5	51.3
Interest Expense/ Taxes (%)	7.4	6.8	6.9	7.0	7.1	7.2
GDP Growth (%)	0.5	0.9	4.5	2.7	2.7	2.7
Foreign Reserves/Debt (%)	34.7	45.0	54.0	50.3	46.2	42.6
Implied Sen. Rating	AA-	AA	AA+	AA+	AA+	AA+

INDICATIVE CREDIT RATIOS	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

PEER RATIOS	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	75.2	0.2	75.2	7.7	3.4	AA
French Republic	AA	95.5	-3.6	95.5	7.5	0.7	A+
Kingdom Of Belgium	AA	106.3	-3.0	106.3	10.3	1.7	A+
Republic Of Italy	BBB-	132.2	-3.6	132.2	15.4	0.4	BBB
Portugal Republic	BB+	130.2	-8.1	130.2	19.5	1.9	BBB

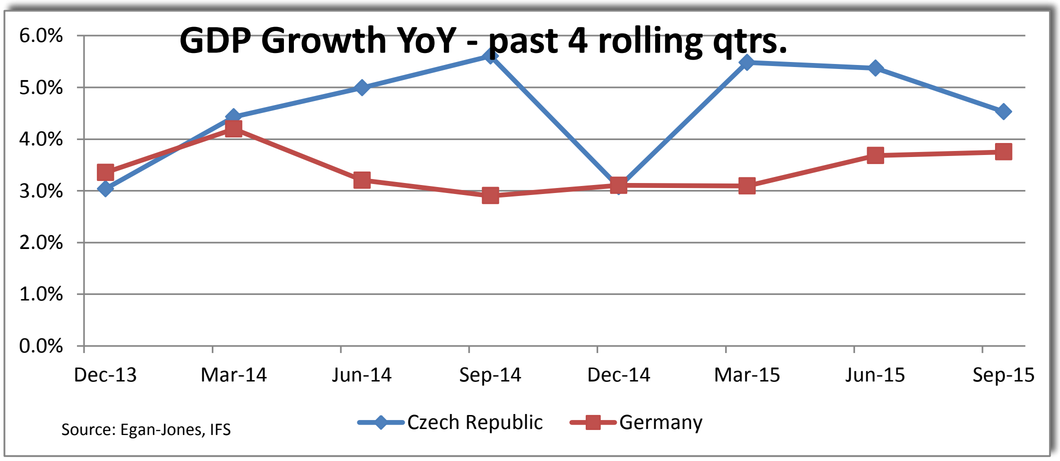


Country (EJR Rtg*)	CDS
Italy (CCC+)	126
France (BBB)	39
Belgium (BBB)	54
Germany (A)	19
Czech Republic (AA)	41

Economic Growth

The Czech economy has posted strong results for the last two years, benefiting from improved private consumption and solid monetary policy. Real GDP regained momentum as the quarterly growth improved from 1.1% YoY in Dec 2013 to 4.1% in Sept 2015. We expect the real GDP to grow at an annual rate of appromitely 2.5% for the next five year.

However, Czech's high dependence on export continues to be a source of risk for the economy. A number of scenarios might potentially erode demand and hamper the economic recovery, including the slowdown of China and the secondary effect from China's trade links with Germany (largest import and export partner), Greexit, as well as a prolonged weakness in the Eurozone.



Fiscal Policy

Czech Republic has a Debt-to-GDP ratio of 42.75%, 4.6% higher than in 2010 but still favorable compared to its neighbors. Deficit-to-GDP ratio rose slightly to 2.79% as the new government lessened fiscal austerity. 5-Year CDS Spreads is at 41.07 bps, above that of Germany and France but below that of Belgium. We expect the Debt-to-GDP ratio to drop slightly in the next coming years as the economy continues to recover from the recession, with a Deficit-to-GDP ratio that's safe below 3%.

	Deficit-to-GDP (%)	Debt-to-GDP (%)	5 Yr. CDS Spreads
Czech Republ	2.79	42.75	41.07
Germany	-0.19	75.22	19.33
France	3.60	95.51	39.17
Belgium	3.01	106.29	53.55
Italy	3.55	132.15	126.02
Portugal	8.05	130.17	258.03

Sources: Thomson Reuters and IFS

Unemployment

Czech's unemployment rate was among the lowest peer countries in 2013 and 2014. As shown in the chart, for 2014 the 6.12% unemployment was even lower than Germany's. The most recent data shows that the rate was 4.83% in September 2015, and Czech has been improving over couple of quarters. We do not consider the unemployment as a potential risk to Czech's economy.

Unemployment (%)

	2013	2014
Czech Reput	6.97	6.12
Germany	6.88	6.70
France	10.28	10.30
Belgium	8.45	8.53
Italy	12.13	12.65
Portugal	16.46	14.13

Source: Intl. Finance Statistics

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Banking Sector

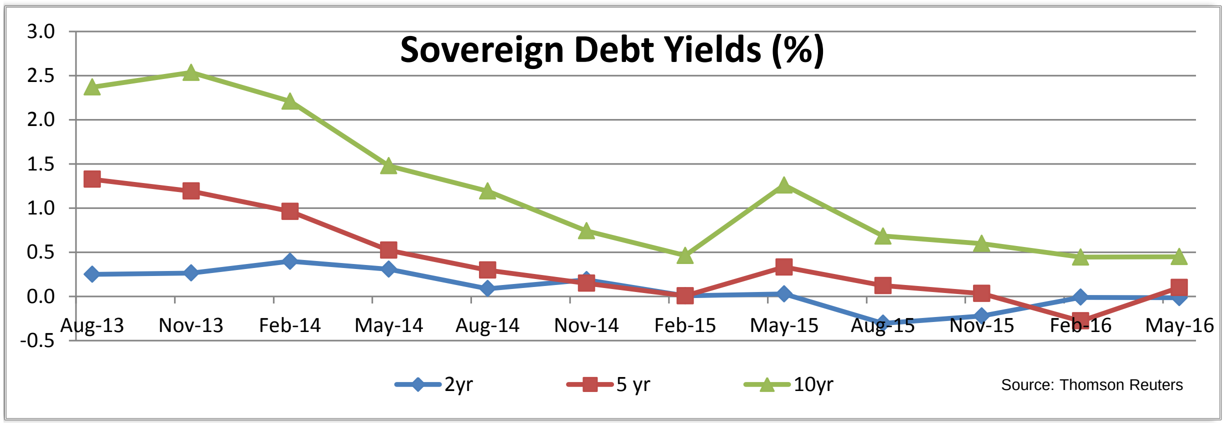
Komercni Banka is the 3rd largest bank in Czech. The top 5 banks' balance sheet is about 4 times of the shown amount, at around 84% of its GDP. Czech's exposure to its banking sector is within a normal level, as compared to Germany, where the top 5 banks have assets equal to 80.8% of GDP. As the liquidity level gradually rises, the risk in Czech's banking sector is minimal.

Bank Assets (billions of local currency)

	Assets	Cap/ Assets %
Komercni Banka	891.56	-9.97
Total	891.6	
EJR's est. of cap shortfall at 10% of assets less market cap		-88.9
Czech Republic's GDP		4,260.9

Funding Costs

Although Czech's sovereign debt yields slightly increased in May 2015, the overall rates have dropped since August 2013 and remained at a low level. As can be seen below, the 2-year and 5-year debt yields are near null and the 10-year debt yield is around 0.5%. As ECB holds the expansionary monetary policy and is unlikely to end it in short term, we are expecting Czech to maintain the low funding costs in the foreseeable future.



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 36 (1 is best, 189 worst) is above average.

The World Bank's Doing Business Survey*

	2015 Rank	2014 Rank	Change in Rank
Overall Country Rank:	**36**	**33**	**-3**
Scores:			
Starting a Business	93	90	-3
Construction Permits	127	126	-1
Getting Electricity	42	40	-2
Registering Property	37	35	-2
Getting Credit	28	24	-4
Protecting Investors	57	54	-3
Paying Taxes	122	123	1
Trading Across Borders	1	1	0
Enforcing Contracts	72	72	0
Resolving Insolvency	22	20	-2

* 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 72.5 for Economic Freedom with 100 being best.

Heritage Foundation 2015 Index of Economic Freedom
World Rank 72.5*

	2015 Rank**	2014 Rank	Change in Rank	World Avg.
Property Rights	75	70	5	42.2
Freedom from Corruption	48	45.3	2.7	41.9
Fiscal Freedom	81.5	81.7	-0.2	77.4
Government Spending	40.6	43.8	-3.2	61.7
Business Freedom	68.2	70.1	-1.9	64.1
Labor Freedom	82.9	84	-1.1	61.3
Monetary Freedom	81.2	79.4	1.8	75.0
Trade Freedom	88	87.8	0.2	75.4
Investment Freedom	80	80	0	54.8
Financial Freedom	80	80	0	48.6

*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

Valuation Driver: Taxes Growth:
Czech Republic has grown its taxes of 1.3% per annum in the last fiscal year which is disappointing. We expect tax revenues will grow approximately 1.3% per annum over the next couple of years and 1.3% per annum for the next couple of years thereafter.

Valuation Driver: Total Revenue Growth:
CZECH REPUBLIC's total revenue growth has been more than its peers and we assumed a 2.3% growth in total revenue growth over the next two years.

Income Statement	Peer Median	Co. Avg.	Assumptions Yr 1&2	Yr 3,4,5
Taxes Growth%	1.5	1.3	1.3	1.3
Social Contributions Growth %	1.0	3.6	3.6	3.6
Grant Revenue Growth %	0.0	NMF		
Other Revenue Growth %	0.0	NMF		
Other Operating Income Growth%	0.0	4.5	2.6	2.6
Total Revenue Growth%	0.7	2.6	2.3	2.1
Compensation of Employees Growth%	1.7	3.5	3.5	3.5
Use of Goods & Services Growth%	2.6	1.7	1.7	1.7
Social Benefits Growth%	2.4	2.5	2.5	2.5
Subsidies Growth%	6.9	3.9		
Other Expenses Growth%	16.9	16.9		
Interest Expense	0.0	3.1	3.1	
Currency and Deposits (asset) Growth%	0.0	0.0		
Securities other than Shares LT (asset) Growth%	0.0	0.0		
Loans (asset) Growth%	0.1	4.0	1.3	1.3
Shares and Other Equity (asset) Growth%	4.5	3.8	3.8	3.8
Insurance Technical Reserves (asset) Growth%	0.0	25.0	25.0	22.5
Financial Derivatives (asset) Growth%	0.0	0.0		
Other Accounts Receivable LT Growth%	1.6	3.8	1.3	1.3
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%	0.0			
Currency & Deposits (liability) Growth%	6.7	45.5	1.3	1.3
Securities Other than Shares (liability) Growth%	11.1	3.7	2.6	2.6
Loans (liability) Growth%	3.9	(3.3)	0.5	0.5
Insurance Technical Reserves (liability) Growth%	0.0	(29.2)	3.0	3.0
Financial Derivatives (liability) Growth%	0.0	(24.7)	(10.0)	(10.0)
Additional ST debt (1st year)(billions CZK)	0.0	0.0		

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ANNUAL INCOME STATEMENTS

Below are Czech Republic's annual income statements with the projected years based on the assumptions listed on page 3.

ANNUAL REVENUE AND EXPENSE STATEMENT
(BILLIONS CZK)

	2011	2012	2013	2014	P2015	P2016
Taxes	756	776	808	818	829	840
Social Contributions	593	600	607	629	651	675
Grant Revenue						
Other Revenue						
Other Operating Income	268	260	271	283	283	283
Total Revenue	1,616	1,637	1,686	1,730	1,763	1,798
Compensation of Employees	347	357	364	376	390	404
Use of Goods & Services	276	254	265	269	274	278
Social Benefits	651	663	678	695	713	731
Subsidies	91	91	96	99	99	99
Other Expenses	129	208	130	152	152	152
Grant Expense						
Depreciation	195	196	197	200	200	200
Total Expenses excluding interest	1,689	1,769	1,729	1,793	1,828	1,865
Operating Surplus/Shortfall	-73	-132	-43	-63	-65	-67
Interest Expense	53	58	55	56	58	60
Net Operating Balance	-126	-190	-98	-119	-123	-127

ANNUAL BALANCE SHEETS

Below are Czech Republic's balance sheets with the projected years based on the assumptions listed on page 3.

ANNUAL BALANCE SHEETS
(BILLIONS CZK)

Base Case

ASSETS	2011	2012	2013	2014	P2015	P2016
Currency and Deposits (asset)	396	526	0	400	400	400
Securities other than Shares LT (asset)						
Loans (asset)	115	115	129	134	136	138
Shares and Other Equity (asset)	721	671	628	652	676	702
Insurance Technical Reserves (asset)	2	2	11	14	18	22
Financial Derivatives (asset)						
Other Accounts Receivable LT	348	368	365	378	383	388
Monetary Gold and SDR's						
Other Assets					4	4
Additional Assets	16	15	508	4		
Total Financial Assets	1,598	1,697	1,642	1,582	1,617	1,654

LIABILITIES	2011	2012	2013	2014	P2015	P2016
Other Accounts Payable						
Currency & Deposits (liability)	3	9	7	10	10	10
Securities Other than Shares (liability)	1,498	1,803	1,816	1,883	1,932	1,982
Loans (liability)	195	195	195	189	311	438
Insurance Technical Reserves (liability)	8	9	11	8	8	8
Financial Derivatives (liability)	17	19	6	5	4	4
Other Liabilities	245	333	346	354	354	354
Liabilities	1,967	2,368	2,381	2,449	2,607	2,770
Net Financial Worth	-370	-671	-740	-867	-990	-1,117
Total Liabilities & Equity	1,598	1,697	1,642	1,582	1,617	1,654

Comments on the Difference between the Model and Assigned Rating

SEC Rule 17g-7(a) Disclosure

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+) other than those deep into speculative grade; for CC, C, and D there are no 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 methodology available in our Form NRSRO Exhibit #2 dated May 10, 2015 available via 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 page 3 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 dependant on numerous factors including the reliability, accuracy, and quality of the data relied used in determining the credit rating. The data is sourced from publicly-available 10Q and 10K statements, quarterly reports, 8K filings, earnings reports, and other similar sources. In some cases, the information is limited because of issues such as short operating histories, the lack of reported data, a delay in reporting data, restatements, inaccurate accounting, and other issues. Such shortcomings 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 10Q and 10K statements, quarterly reports, 8K filings, earnings reports, and other similar sources for ratings on publicly-traded issuers. In the case of private issuers, EJR relies on information provided mainly by 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 avail.

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%	1.3	5.3	(2.7)	AA-	AA-	AA-
Social Contributions Growth %	3.6	0.6	6.6	AA-	AA-	AA-
Other Revenue Growth %		(3.0)	3.0	AA-	AA-	AA-
Total Revenue Growth%	2.3	0.3	4.3	AA-	AA-	AA-
Monetary Gold and SDR's Growth %	5.0	3.0	7.0	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**

Mike Huang ………………………………………………………….. May 16, 2016 ……………………………………………

Mike Huang
Rating Analyst

Reviewer Signature: **Today's Date**

Caroline Ding ………………………………………………………….. May 16, 2016 ……………………………………………

Caroline Ding
Rating Analyst

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*EJR CP Rating: A1+
EJR's 3 yr. Default Probability: 1.0%

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.