

## Country Report – Czech Republic

### 1. Economic and Financial Background

Table 1: Key Economic Indicators		
	2002	2003
Population (million)	10,189	10,211
GDP (EUR billions)	72,0	74,4
Real GDP growth (%)	2,0	2,9
Inflation rate (%)	1,8	0,1
Unemployment rate (%)	9,2	9,9
Stock market capitalization (EUR billions)	14,75	19,9
Stock market capitalization (% of GDP)	21	26,7
Bond market capitalization (EUR billions)	11,48	15,6
Bond market capitalization (% of GDP)	16,4	21
Household gross savings ratio (%)	6,1	5,6
Household financial wealth (EUR billions)	44,44	46,86
Average per capita financial wealth (EUR)	4320	4589

### 2. Key Trends in Global Market

Table 2: Net assets of the European Fund Industry (EUR billions)				
Year	Total assets under management	Of which:		
		UCITS nationally domiciled	Non-UCITS nationally domiciled	UCITS domiciled abroad and promoted by national providers
1999	2.796	1.491	1.305	N.A.
2000	2.577	2.136	0.437	N.A.
2001	2.303	1.916	0.387	N.A.
2002	4.401	3.142	0.159	1.100
2003	4.767	3.245	0.105	1.417

As can be seen from figures above the major rule are playing domestic open-ended mutual funds followed by funds domiciled abroad. Foreign funds are playing more important role on the market. Especially protected funds domiciled abroad are very popular among retail investors (till 1<sup>st</sup> May 2004 the Czech law did not allow establishment of protected funds in the Czech Republic). Distribution is the key factor, which funds will be successful on the market if domestic or funds domiciled abroad. At this moment about 90% of all sales are made through banks. There are no barriers (tax or administration) for foreign funds, which would go on the Czech market. At

the end of 2003 there was on the market about 50 domestic open-ended funds and about 800 funds domiciled abroad. The market is already consolidated and four the biggest domestic investment management companies are managing more than 90% of all assets of investment funds.

### 3. Key Trends in UCITS Market

Table 3: Number and net assets of UCITS					
Year	Number of UCITS	Fund Launches	Total net assets (EUR bn)	Average net assets by fund	Net sales (EUR m)
1999	64	8	1.491	0.023	479
2000	73	9	2.139	0.029	-168
2001	68	0	1.916	0.028	-356
2002	79	11	3.142	0.040	606
2003	60	5	3.245	0.054	81

Table 4: UCITS assets by fund type (EUR billions)										
	1999		2000		2001		2002		2003	
	Net Assets	% of total	Net Assets	% of total	Net Assets	% of total	Net Assets	% of total	Net Assets	% of total
Equity	0.008	0.5	0.045	2.1	0.064	3.3	0.042	1.3	0.097	3.0
Bond	0.172	11.6	0.094	4.4	0.196	10.2	0.577	18.4	0.805	24.8
Balanced	0.642	43.1	1.337	62.5	0.857	44.7	0.948	30.2	0.801	24.7
Money Market	0.661	44.3	0.629	29.4	0.772	40.3	1.556	49.5	1.531	47.2
Fund of Funds	0.009	0.6	0.034	1.6	0.028	1.5	0.019	0.6	0.012	0.4
Other	0	0	0	0	0	0	0	0	0	0
<b>Total</b>	<b>1.491</b>	<b>100</b>	<b>2.139</b>	<b>100</b>	<b>1.917</b>	<b>100</b>	<b>3.142</b>	<b>100</b>	<b>3.245</b>	<b>100</b>

Table 5: Net sales of UCITS by fund type (EUR millions)					
	1999	2000	2001	2002	2003
Equity	2.7	38.1	-9.3	-4.7	36.7
Bond	62.4	-15.8	78.3	214.9	199.9
Balanced	-32.4	-189.8	-499.2	-293.6	-229.3
Money Market	439.4	-33.1	76.0	692.1	70.5
Fund of Funds	7.9	32.2	-1.67	-2.5	3.4
Other	0	0	0	0	0
<b>Total</b>	<b>480</b>	<b>-168.29</b>	<b>-355.8</b>	<b>606.3</b>	<b>81.1</b>

Czech retail investors are very conservative and they prefer investment tools with lower level of the risk. Concerning this situation the money market funds are the most popular and they are used as substitute of saving account. The figures of money market funds (net sales) are distorted by institutional investor's out flow in the 2003 due to change in VAT system applicable on the Czech companies (this out flow represented about EUR 300 millions). Present assets under management in investment funds (both – domestic and domiciled abroad) are representing about 10% of all household savings. The mixed (balanced) funds are mostly former privatization funds and they are slowly changing their investment focus or they are merging together with other funds. These funds have still negative net sales because investors who invested in voucher privatization (10 years ago) are still continuing withdraw their investments. Only about 3% of assets are invested in equity funds but the growth rate is rapid.

#### 4. Key Trends in Other Nationally Regulated Funds

Table 6: Net assets of other nationally regulated funds (EUR billions)					
	1999	2000	2001	2002	2003
Real estate					
Alternative management					
Special funds					
Other	0,94	0,29	0,3	0,11	0,1
<b>Total</b>	<b>0,94</b>	<b>0,29</b>	<b>0,3</b>	<b>0,11</b>	<b>0,1</b>

This part of collective investment has not been developed yet because the new act on collective investment, which allowed these kinds of funds has been in force from 1<sup>st</sup> May 2004. At the end of 2003 there were only 4 investment privatization funds and we supposed that all of them will change to open ended funds during 2004.

#### 5. Industry Structure

Table 7: Fund management companies		
Fund management companies	Assets under management of home domiciled funds (EUR bn)	Assets under management of home and foreign domiciled funds (EUR bn)
AKRO investiční společnost, a.s.	0,009	
ČP INVEST investiční společnost, a.s.	0,075	
ČSOB investiční společnost, a.s.	0,127	
Investiční kapitálová společnost KB, a.s.	0,734	
Investiční společnost České spořitelny, a.s. Investiční společnost České spořitelny, a.s. - ESPA fondy	1,479	0,096
J&T ASSET MANAGEMENT, INVESTIČNÍ SPOLEČNOST, a.s.	0,033	
Pioneer česká finanční společnost, s.r.o.		0,032
Pioneer česká investiční společnost, s.r.o.	0,087	
První investiční společnost, a.s.	0,514	
ŽB - Trust, investiční společnost, a.s.	0,187	
Non UNIS members -domestic comp.	0,094	
Non UNIS members – foreign dom. funds		1,289
<b>Top 5</b>	<b>3,042</b>	
<b>Industry Total</b>	<b>3,268</b>	<b>1,417</b>

#### 6. Legal & fiscal developments

6.1 How have the UCITS III Directives found their transposition in the national framework?

The Czech Republic will accede to the European Union on May 1, 2004. Many preparation processes have been undertaken in the Czech Republic and they should be all concluded by the accession date.

The process of preparation of two new acts that should supersede the existing fragmented arrangement of financial markets and its regulation in the Czech Republic has been going on since 2001. These acts are the Act on Capital Market Conduct and the Collective Investment Act, both supplemented with Amendments to the Bonds Act and so called "Amending Act" which amends number of pieces of legislation in relation to the adoption of the above-mentioned acts. The projected effective date of all the mentioned arrangements is the EU accession date.

The regulation that currently mainly governs area of collective investments is Act No. 248/1992 Coll. on Investment Companies and Investment Funds. Collective investments schemes will be newly arranged in the Collective Investment Act, which fully reflects EU regulations including UCITS III Directive; several new notices will be also adopted.

## 6.2. How have other EU Directives found their transposition in the national framework?

- E-commerce directive (deadline: 17 Jan. 2002)

*In particular the issue of home or host state control over incoming funds from other EEA jurisdictions.*

Directive 2000/31/EC on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market is implemented only partially. A bill on certain services of information society which shall provide full compliance of the Czech legislation with the E-commerce directive has been submitted to the Parliament. This bill includes general description of the home and host state control however it would be beneficial to include more specific regulation into the Collective Investment Act to reflect some specifics of the fund management business.

- Taxation of Savings directive (deadline: 1 Jan. 2004)

Taxation of Savings directive has been implemented by a major amendment to the Income Tax Act, which has been passed by the Parliament at the end of 2003 and which is the result of the ongoing harmonisation of Czech law with EU regulations. The amendment implements four EU tax directives into Czech tax legislation, all of which are prerequisites for accession: the parent/subsidiary directive, the merger directive, the savings directive, and the royalties/interest directive. These changes will take effect from the date of Czech accession to the EU, or in certain cases later.

- Distance marketing directive (deadline: 9 Oct. 2004)

*In particular any overlap with the UCITS Simplified Prospectus.*

Directive 2002/65/EC concerning the distance marketing of consumer financial services shall be implemented by the so called "Amending Act", which shall substantially amend existing Securities Act. UCITS Simplified Prospectus and its requirements shall be stipulated in the Collective Investment Act and especially in a more detailed notice issued by the Czech SEC.

Any investor should receive, before conclusion of the contract, prior information needed for conclusion of such contract and other information mentioned in the Act (some of them are the same as information provided in the Simplified Prospectus), however it is not precisely defined whether all information must be provided in the Simplified Prospectus or in any other form.

### 6.3. Other regulatory developments at national level that impact fund management

There are number of pieces of legislation that will impact fund management business, among others amendment to the existing “Anti-Money Laundering” Act, amendment of the “Registry Office and identification numbers” Act and especially number of notices that should be issued by the Czech SEC in accordance with the Collective Investment Act and Act on Capital Market Conduct.

### 6.4. New tax rules at national level

(Up-date on discriminatory tax barriers will be dealt separately by FEFSI secretariat in co-operation with PwC and reviewed by the Tax Committee and national associations)

The general corporate income tax rate equals 31 % (with exception of pension, mutual and investment funds). There is an important change in taxation from January 1<sup>st</sup> 2004. Mutual funds and investment funds are newly subject to the corporate income tax, which equals 5 %! This rate is use for all types of funds including specialized funds.

Dividends from Czech securities are subject to 15% tax-deduction and are not liable to further taxation at the fund level. Dividends from foreign securities are an independent tax base with the same 15% rate.

Incomes from mortgage certificates are free of tax. Unrealised capital gains are not subject to taxation. .

Fund’s after-tax profit may be paid to shareholders in the form of dividends. This payment is subject to 15% tax-deduction, which is deducted and paid by the fund. The tax base for the deduction tax is proportionally reduced by fund’s incomes that are liable to tax-deduction, are an independent tax base (dividends from abroad) or are tax exempt. Funds may reduce their final tax liability by half of the tax deducted from the dividend payout in the taxable year.

There are no administrations or tax barriers for foreign fund operating in Czech Republic.

## 7. Corporate Governance

- UNIS is participant member of Corporate governance group for issuers which was established under supervision of Czech SEC.
- In Czech Republic at this moment the most of funds are open-ended mutual funds and there are no special rules for behavior of these funds. UNIS members – investment management companies are using corporate governance principles.
- UNIS members are providing very deep information about funds on the daily and weakly basis. Information describing behavior of the funds is widely extended by Czech newspapers; internet portals and. also by UNIS web pages.

## 8. Product development

There was no development in 2003 in this area because former law about investment management companies and investment funds had no allowed any other types of funds then open-ended mutual funds investing only into standardized investment tools. In 2003 UNIS participated on preparation of new law about collective investment, which is in force since May 1<sup>st</sup> 2004. We positively see possibilities for future development in area of specialized funds.

## 9. Standardization efforts

UNIS members already adopt wide range of standardization and they are providing many information about managed funds (fund performance, fund categorization, disclosure of fees, structure of assets, figures about sales and purchase of units of the funds, etc.). UNIS is distributing these dates and figures to the public trough network of cooperating newspapers and web portals. Adaptation of standardization is still in progress. UNIS supposes to fully adopt classification of fixed-income funds.

## 10. Development in fund based pension products

- Development of fund-based pension products in second and third pillar
  - Pension system in Czech Republic is fully paid out and only voluntary pension funds are present in 3<sup>rd</sup> pillar.
- Amount of retirement savings invested in fund based products (see Table 8 below)

<b>Table 8: Investment funds in European retirement provision</b> (EUR billions)					
	<b>Dedicated investment fund vehicles</b>	<b>Unit-linked life insurance contracts</b>	<b>Traditional life insurance schemes</b>	<b>Traditional pension funds</b>	<b>Other</b>
<b>Assets under management</b>	-	N.A.	1,267	2,370	N.A.
<b>Assets invested in investment funds</b>	-	N.A.	N.A.	-	N.A.
<b>Use in pension pillar (1<sup>st</sup>, 2<sup>nd</sup> or 3<sup>rd</sup> pillar)</b>	-	N.A.	-	2,370	N.A.

## 11. Other activities of the association

As the professional association of investment management companies and funds, the Union of Investment Companies of the Czech Republic endeavours to develop the capital markets and collective investment. Through its activities and self-regulating procedures, the Union aims to develop higher general awareness, knowledge, and confidence in collective investment. Membership in the Union represents a guarantee that a company fulfils certain standards of professionalism, integrity in managing assets, and acts in the best interests of investors and fund clients.

- Main issues at the center of your domestic lobbying activities
  - UNIS participated in process of preparation of the new law about collective investment
  - UNIS was successful in area of taxation of domestic funds. Due to UNIS activities Czech parliament reduce tax rate for all types of funds from 15% to 5%.
- Educational seminars & training courses
  - UNIS is partner of Czech SEC for long term project of education of investors on different levels. Educational seminars are hold for retail investors, distributors,

students from universities, teachers from high schools, employees of Civil Service etc.

- Publications (newsletters, reports etc)
  - UNIS with cooperation with Czech SEC issued publication – brochure for retail investors in total amount 175.000 pieces. This brochure is describing funds as efficient way for private investments and it is distributing by UNIS members and also by Czech Post.