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Slovakia:
Export-led growth despite the EU crisis

Despite the EU crisis, export-led growth continued in Slovakia in the first quarter of 2012. The economy will expand by more than 2% this year. Growth will again be substantiated by the net exports, bolstered by still low unit labour costs and supported by the expansion of production in the automotive sector. The new government presumably will modestly stimulate private consumption. However, downward risks still prevail as resolution of the European debt crisis remains the crucial factor.

After a successful 2011, Slovak gross domestic product continued to grow in the first months of 2012 as well. Whereas GDP stagnated in the EU, growth in Slovakia in the first quarter 2012 was quite robust, reaching 3% year-on-year and 0.7% quarter-on-quarter. Slovakia thus recorded the fourth highest growth rate in the EU behind the Baltic countries and bucked the negative trend in the European Union. As in 2011, growth came primarily from net exports, with exports of goods and services increasing by about 2.6%, while imports declined by 1.3%. Exports to Slovakia's main trading partners – Germany and the Czech Republic – expanded most. In terms of export products, motor-car exports increased considerably. Consumption of households stagnated, while that of government increased slightly by 0.4%. Gross capital formation as well as gross fixed capital were negative (-4%, -3.9%) and thus did not contribute to GDP growth.

Industrial production grew by 8% in the first quarter of 2012 and that of manufacturing even more: 10%. The main Slovak sector, the automotive industry, which provides 27% of manufacturing output, expanded rapidly as well and displayed a growth rate of 25%. Two smaller sectors, textiles and leather, as well as electrical equipment, grew by 14% and 11%, respectively, while two other important branches, machinery and equipment and basic metals, expanded by 9.8% and 4.4%, respectively. On the other hand, output in the food, the wood-processing and pharmaceuticals industries declined during the period concerned. Apart from industry, small contributions to growth came also from services, while value added of agriculture and construction declined in the first quarter 2012.

In 2011 inflation rose to 4.1%: one of the highest rates in the EU. In the first quarter 2012, inflation still ran high at 4% year-on-year, but it is expected to decline over the course of the year.

Whereas the situation on the labour market deteriorated towards the end of 2011, it showed mixed results at the beginning of 2012. On the one hand, employment increased in the first quarter by 1.2% year-on-year; on the other hand, unemployment rose to 14.1%. The main problems are: (i) the high share of long-term unemployed, accounting for 67.7% of all unemployed (fourth quarter 2011); and (ii) the youth unemployment rate of 34.4%, which is well above the EU-average (23%, first quarter 2012). These problems are related to large regional disparities, with unemployment rates being higher in the eastern parts of Slovakia. The cabinet now plans to reshuffle funds of EU-supported operational programmes in favour of programmes tackling youth unemployment and boosting economic growth. Money will come from the operational programmes for the informatisation of society, education and transportation. Funds will also be forthcoming from the Ministry of Labour, Social Affairs and Family.

Public debt levels in the previous year rose more slowly than in the two years prior thereto, peaking at 43.3% which was well below the EU average. The budget deficit was reduced from about 8% in both 2009 and 2010 to 4.8% in 2011. This was a direct outcome of the consolidation programme introduced under the previous government headed by Iveta Radičová, which had set a deficit target of 4.9%. The difficulty of complying with that goal was however compounded by having to include the debts outstanding of both state-owned railway company and hospitals for the period 2008-2010. The main features of the budget consolidation programme included: (i) a temporary rise in VAT to 20%; (ii) an increase in selected excise taxes (e.g. tobacco); (iii) a reduction in the public wage bill; and (iv) a decline in government consumption of goods and services. The interim government still managed to pass the budget for 2012, in which the deficit is officially projected to reach 4.6% of GDP. A bank levy was introduced at the beginning of 2012.

Responsibility for continuing fiscal consolidation now falls on the new government formed by Robert Fico, whose leftist SMER party won the elections on 10 March 2012. Over the next four years, Slovakia will have a social democratic government that is bent on improving the living conditions of the disadvantaged segments of society. However, Fico has also announced that he would abide by EU-rules and pursue a pro-European course, including a reduction in the fiscal deficit to less than 3% in 2013. Although concrete measures are still missing, the new government’s proposed measures will focus mainly on revenues. The flat tax of 19% will be modified and higher personal income taxes will be introduced for people with high incomes. Corporate income tax will be increased to 23% and the taxable base for the bank levy will be extended, its rate will probably be raised. Further measures include a shift of contributions from the second pension pillar in favour of the first “pay as you go” system, as well as a special levy for certain companies in 2012 and 2013 equivalent to 4.2% of their earnings. The companies affected will encompass telecom companies, postal services and the energy sector. Apart from adhering to EU-rules, the new government programme includes somewhat broader topics ranging from mitigating the effects of the crisis to combating joblessness and improving social standards. It is now up to the government to put these agreeable ideas into practice and address the issue of structural reforms.

Foreign direct investment inflows recovered strongly in 2011 after the slump over the period 2008-2009; they amounted to EUR 1.5 billion. However, Slovakia still received less than half of the inflows it enjoyed in 2008. The three automotive companies in Slovakia – Volkswagen in Bratislava, PSA Peugeot-Citroën in Trnava and Kia in Žilina – recorded a successful year, with automotive production increasing by 14% to a total of 639,760 vehicles. Slovakia thus remained the number one car producer per capita in Europe. In 2011 investments were directed towards the manufacture of new models or the expansion of engine production (KIA) and in 2012 all three companies added a third shift: KIA introduced a third shift in January 2012; Volkswagen in March and PSA followed suit ahead of schedule in May (instead of June). Possible production numbers for 2012 range between 780,000 and 925,000 vehicles. While the news from the car manufacturers is positive, the number of newly announced greenfield projects declined significantly in the first quarter of the current year. Uncertainties about Fico’s policies and imponderables related to the crisis in Europe might delay new investment decisions.

Overall, wiiw has revised its growth forecasts upwards for the current year as the earlier negative scenarios it had previously assumed failed to materialize and the figures for the first quarter 2012 have been rather positive. We have thus reverted to our previous growth forecast of 2.2% for 2012. Growth will be again substantiated by the net exports, bolstered by still low unit labour costs and supported by the expansion of production in the automotive sector. Furthermore, private consumption might well start contributing, albeit modestly, to some GDP growth later in the year. The government might stimulate private consumption by cutting expenditures to a lesser extent than originally planned. That might yield greater growth and thus more tax revenues. Fico announced that his government would set priority on large-scale infrastructure projects, including the construction of motorways and the faster completion of the Mochovce nuclear power plant. Stimulation of household consumption seems now more probable and even strengthened by the outcome of the presidential election in France. However, downward risks still prevail since Slovakia is dependent on developments in Germany and the Czech Republic, its main trading partners which together account for 36.5% of Slovakia's exports. Resolution of the European debt crisis will be the crucial factor. The wiiw reckons with an acceleration of growth to 3% in 2013 and about 4% in 2014, backed by growth in private consumption and investment, as well as supported by net exports.

Table SK

Slovakia: Selected Economic Indicators

	2008	2009	2010	2011 [1)]	2011	2012	2012	2013	2014
					1st quarter			Forecast	
Population, th pers., average [2)]	5406.6	5418.6	5430.1	5397.3	.	.	5410	5430	5440
Gross domestic product, EUR mn, nom.	66842	62795	65744	69058	15853	16556	73000	77400	82900
annual change in % (real)	5.8	-5.0	4.2	3.4	3.4	3.0	2.2	3	4
GDP/capita (EUR at exchange rate)	11900	11600	12100	12700	.	.	13500	14300	15200
GDP/capita (EUR at PPP)	18100	17000	17900	18900	.	.	.	.	.
Consumption of households, EUR mn, nom.	37573	37640	37740	39018	9480	9897	.	.	.
annual change in % (real)	6.0	0.1	-0.8	-0.4	-0.2	-0.1	1	1.5	2.5
Gross fixed capital form., EUR mn, nom.	16576	13025	14616	15477	3564	3420	.	.	.
annual change in % (real)	1.0	-19.7	12.4	5.6	1.6	-3.9	2.5	3	4
Gross industrial production									
annual change in % (real)	3.1	-14.1	18.3	7.2	12.1	8.0	5	6	7
Gross agricultural production (EAA)									
annual change in % (real)	10.6	-12.3	-8.2	8.0	.	.	.	.	.
Construction industry									
annual change in % (real)	11.9	-11.2	-4.6	-1.8	-2.5	-9.2	.	.	.
Employed persons - LFS, th, average [3)]	2433.7	2366.3	2317.5	2351.4	2296.1	2324.7	2360	2400	2440
annual change in %	3.2	-2.8	-2.1	1.5	.	1.2	0.5	1.5	1.5
Unemployed persons - LFS, th, average [3)]	255.7	323.5	389.2	368.3	372.2	380.3	.	.	.
Unemployment rate - LFS, in %, average [3)]	9.5	12.0	14.4	13.5	13.9	14.1	14	13	12.5
Reg. unemployment rate, in %, end of period	8.4	12.7	12.5	13.6	13.1	13.7	13.5	13	12.5
Average gross monthly wages, EUR	723	745	769	786	746	770	.	.	.
annual change in % (real, gross)	3.3	1.4	2.2	-1.6	-0.4	-0.6	.	.	.
Consumer prices (HICP), % p.a.	3.9	0.9	0.7	4.1	3.5	4.0	3.5	3	3
Producer prices in industry, % p.a.	2.5	-6.6	0.1	4.4	5.3	2.5	3	3	3
General governm.budget, EU-def., % GDP									
Revenues	32.8	33.5	32.4	32.6	.	.	.	.	.
Expenditures	34.9	41.5	40.0	37.4	.	.	.	.	.
Net lending (+) / net borrowing (-)	-2.1	-8.0	-7.7	-4.8	.	.	-5	-4	-3
Public debt, EU-def., in % of GDP	27.8	35.5	41.1	43.3	.	.	46	47	47
Central bank policy rate, % p.a., end of period [4)]	2.5	1.0	1.0	1.0	1.0	1.0	.	.	.
Current account, EUR mn	-4021	-1627	-2278	38	156	388 I-II	700	300	0
Current account in % of GDP	-6.2	-2.6	-3.5	0.1	1.0	2.3 I-II	1.0	0.4	0.0
Exports of goods, BOP, EUR mn	49521	39721	48791	56408	13304	9156 I-II	60000	65000	70000
annual growth rate in %	17.2	-19.8	22.8	15.6	26.7	9.5 I-II	7	9	8
Imports of goods, BOP, EUR mn	50280	38775	48652	53967	12850	8509 I-II	57000	62000	67000
annual growth rate in %	17.2	-22.9	25.5	10.9	27.6	4.5 I-II	5.5	8	8
Exports of services, BOP, EUR mn	6001	4342	4398	4750	1066	821 I-II	5100	5700	6600
annual growth rate in %	16.8	-27.6	1.3	8.0	8.4	17.5 I-II	8	12	15
Imports of services, BOP, EUR mn	6488	5367	5140	5121	1194	803 I-II	5400	5900	6700
annual growth rate in %	36.6	-17.3	-4.2	-0.4	-5.2	3.8 I-II	5	10	14
FDI inflow, EUR mn	3323	-4	335	1541	309	803 I-II	1000	.	.
FDI outflow, EUR mn	376	652	250	353	42	-95 I-II	.	.	.
Gross reserves of NB excl. gold, EUR mn [5)]	12674	481	541	659	573	612	.	.	.
Gross external debt, EUR mn	37286	45338	49262	52934	51641	53891 Feb	.	.	.
Gross external debt in % of GDP	57.9	72.2	74.9	76.7	74.8	73.8	.	.	.
Average exchange rate EUR/EUR	1.0377	1.0000	1.0000	1.0000	1.0000	1.0000	1	1	1
Purchasing power parity EUR/EUR	0.6813	0.6810	0.6758	0.6770	.	.	.	.	.

Note: Gross industrial production, construction output and producer prices refer to NACE Rev. 2. Gross agricultural production refers to Economic Accounts for Agriculture (EAA).

1) Preliminary. - 2) From 2011 according to Census May 2011. - 3) Quarterly data according to Census May 2011. - 4) From 2009 official refinancing operation rates for euro area (ECB), two-week repo rate of NB before. - 5) From January 2009 (euro introduction) foreign currency reserves denominated in non-euro currencies only.

Source: wiiw Database incorporating Eurostat and national statistics. Forecasts by wiiw.