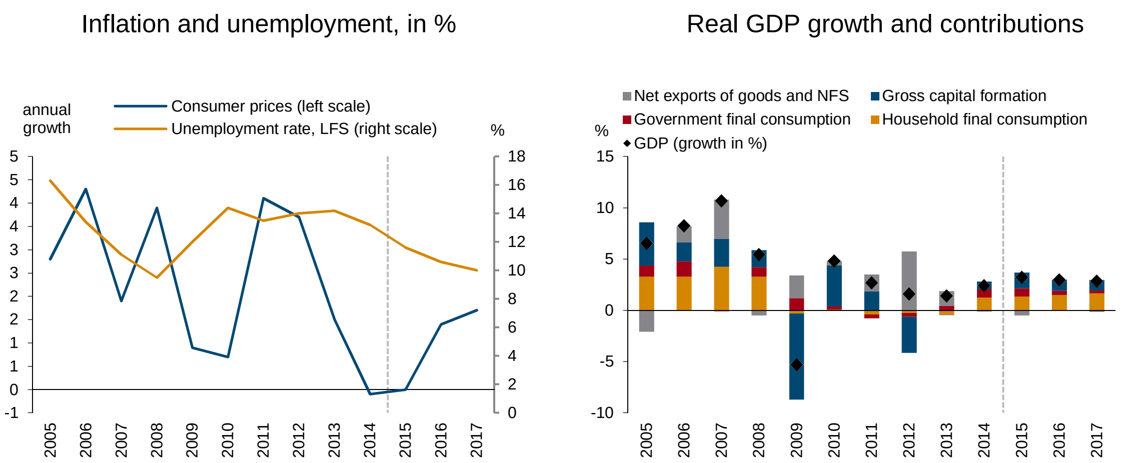
SLOVAKIA: Investments spurring growth

DORIS HANZL-WEISS

In 2015, surging investments will boost Slovak GDP growth, which is expected to reach 3.2%. Better conditions on the labour market will encourage household consumption and imports. At the same time, global uncertainties will restrain export growth, resulting in net exports contributing negatively to economic growth. Over the next two years we expect annual real GDP growth in the order of 3%.

Figure 59 / Slovakia: Main macroeconomic indicators



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

After recording a rise of 2.4% in 2014, GDP growth accelerated further in the first half of 2015 and reached 3.2% year-on-year. Gross fixed capital formation continued its strong upward trend and increased by 8.5% over the first half of 2015 year-on-year. This has been due to the speeding-up of EU structural funds spending, the drawing period ending this year. Government consumption rose by 2.9%, household consumption by 1.9% in the same period. Still this is below the levels implied by labour market improvements. Employment rose dynamically, unemployment declined by almost 2 percentage points and real wages increased by 2.5%. In addition, consumer prices did not increase, but fell by 0.3% in the first half of 2015. Net exports, which had been the main growth driver in the previous years, lost momentum: while exports of goods and services grew by 4.4% in the first half of 2015, imports increased by 5.2%. Exports of goods to Germany, which is the most important trading partner for Slovakia, grew by 6.6%, while exports to the Czech Republic, the second most important trading partner, stayed constant. Exports to Russia and China, previously two promising markets for the Slovak car industry, collapsed and fell by 35% and 26% respectively in the first half of the year.

Looking at sectoral growth trends, industrial production increased by 5.5% in the first seven months of 2015 year-on-year. Monthly growth rates, however, fluctuated heavily, peaking in March and July (+11%, +12%). This was due to the fluctuations in the sectoral performance of the transport equipment sector, the largest sector of Slovak manufacturing. The transport equipment sector finally took over its role as the main growth driver in June, after showing subdued performance in the second half of 2014 and the first months of 2015. Recently the Slovak government has signed a letter of intent with Jaguar Land Rover for building a new car assembly plant. If built, this would add about 150,000-300,000 cars made in Slovakia. In 2014, the three main car companies in Slovakia produced about 970,000 cars, of which Volkswagen Bratislava manufactured 394,000 cars, PSA Peugeot-Citroën 255,000 and KIA 324,000. The construction sector, which suffered from a six-year decline since the outbreak of the crisis, has finally recovered and increased by 15% over the first seven months as compared to the same period a year earlier. The services sector recorded a small increase in value added.

Following developments in the real economy with some delay, trends in the labour market were very positive in the first half of 2015: employment rose by 2.6% and the unemployment rate (LFS) fell to 11.8%. Still, the unemployment rate remains rather high and especially problematic as much of it is attributed to a high share of long-term unemployed and youth unemployment, and high unemployment among the Roma minority population. A new law on vocational education came into force this year and could help to improve the situation.

In 2014, the Slovak budget deficit and public debt amounted to -2.9% and 53.6% as a share of GDP, respectively. Both figures are expected to decrease in the coming years but less than official figures suggest. The official targets defined in the Slovak Stability Programme (April 2015) are set at -2.6% in 2015, -1.9% in 2016 and -0.9% in 2017. The official debt to GDP ratio should fall below 53% in 2016. This is important because of Slovakia's Fiscal Responsibility Act since 2011, which defines various thresholds with certain consequences (at 50%, 53%, 55%, 57%, and 60% debt to GDP level).[58] However, additional spending seems likely this year, as the drawing of the EU structural funds for the period 2007-2013 will finish at the end of 2015, pushing up infrastructure investments. In addition, parliamentary elections will take place at the beginning of March 2016, tempting the (social-democratic SMER-led) government to spend more. The last measure of the first social package, announced in June 2014,[59] will be implemented this year. This encompasses a reduction of gas prices for households and might even include cash rebates. In May 2015, the second social package was announced including a reduction of VAT for selected foodstuffs (to 10%), aid to regions with high unemployment and various other social measures. A third package is scheduled just before the elections. On the revenue side, additional income stems from opening the second pension pillar (thus people have the possibility to exit the second pillar and join the first one) and the sale of a 49% share of Slovak Telekom to Deutsche Telekom for EUR 900 million.

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[58] Between 53% and 55%, the government must submit to the parliament a proposal of measures for debt reduction and the wages of government members are frozen to the level of the previous fiscal year. Between 50% and 53%, the Ministry of Finance sends a letter to the parliament explaining the reasons for higher debt and presenting measures to reduce it.

[59] Overall, the first social package included 15 measures such as free rail transport for students and pensioners, an increase of the minimum wage or the introduction of a minimum pension.

For this year, wiiw has revised its growth forecast for Slovakia upwards to 3.2%. Growth will be pulled by a strong surge in investment due to increased absorption efforts at the end of the drawing period of EU structural funds. In addition, government spending will rise dynamically owing to the upcoming parliamentary elections at the beginning of next year. No major changes are to be expected after these elections, either on the political side or for the economy: the Social Democrats (SMER), led by Robert Fico, lead in opinion polls, while the other parties are small and dispersed. A continuation of Fico's policy can be expected, including further debt reduction, a possible increase of state influence in the energy sector and selective social measures. Household consumption should speed up in the rest of this year as well because conditions of the improved labour market situation. However, this will also result in increased imports and, together with less dynamic exports, net exports will turn negative this year. For the next two years, we expect growth to decline slightly, reaching about 3% annually (meaning a downward revision). Investment and government consumption are expected to slow down, while household consumption should speed up. Missing export stimuli (e.g. from China or Russia) will limit improvements in the export dynamics and thus negative net exports will put a brake on faster growth. Furthermore, the recent Volkswagen scandal poses some risks for Volkswagen Bratislava too, which is Slovakia's largest company by turnover, as well as the country's largest exporter and one of its main employers.

Table 24 / Slovakia: Selected economic indicators

	2011	2012	2013	2014 1)	2014	2015	2015	2016	2017
					January-June		Forecast		
Population, th pers., average 2)	5,398	5,408	5,413	5,419	5,417	5,421	5,424	5,429	5,434
Gross domestic product, EUR mn, nom. 3)	70,160	72,185	73,593	75,215	36,096	37,123	77,600	81,000	84,800
annual change in % (real)	2.7	1.6	1.4	2.4	2.4	3.2	3.2	3.0	2.9
GDP/capita (EUR at exchange rate) 3)	13,000	13,400	13,600	13,900	.	.	13,900	14,900	15,600
GDP/capita (EUR at PPP) 3)	18,900	19,600	20,000	20,800	.	.	.	.	.
Consumption of households, EUR mn, nom. 3)	39,583	40,770	40,995	41,867	20,681	21,060	.	.	.
annual change in % (real)	-0.7	-0.5	-0.8	2.2	2.6	1.9	2.4	2.7	3.0
Gross fixed capital form., EUR mn, nom. 3)	16,946	15,393	15,045	15,893	6,872	7,463	.	.	.
annual change in % (real)	12.7	-9.3	-2.7	5.7	3.9	8.5	6.5	4.5	3.5
Gross industrial production									
annual change in % (real)	5.3	7.9	4.9	4.0	6.5	4.5	5.0	4.0	4.0
Gross agricultural production									
annual change in % (real)	8.7	-5.7	6.7	0.9	.	.	.	.	.
Construction industry									
annual change in % (real)	-1.8	-12.5	-5.3	-4.1	-1.8	12.9	.	.	.
Employed persons, LFS, th, average 4)	2,351	2,329	2,329	2,363	2,342	2,404	2410	2430	2450
annual change in %	1.5	0.6	0.0	1.5	0.6	2.6	2.0	1.0	0.7
Unemployed persons, LFS, th, average 4)	368	378	386	359	370	322	320	290	270
Unemployment rate, LFS, in %, average 4)	13.5	14.0	14.2	13.2	13.7	11.8	11.6	10.6	10.0
Reg. unemployment rate, in %, end of period	13.6	14.4	13.5	12.3	12.8	11.6	.	.	.
Average monthly gross wages, EUR	786	805	824	858	839	858	880	910	940
annual change in % (real, gross)	-1.6	-1.2	1.0	4.2	4.5	2.6	2.5	2.0	2.0
Consumer prices (HICP), % p.a.	4.1	3.7	1.5	-0.1	-0.1	-0.3	0.0	1.4	1.7
Producer prices in industry, % p.a.	4.5	1.9	-1.0	-3.5	-3.5	-3.1	-2.0	1.5	2.0
General governm.budget, EU-def., % of GDP									
Revenues	36.4	36.0	38.4	38.9	.	.	37.9	36.9	36.9
Expenditures	40.6	40.2	41.0	41.8	.	.	40.7	39.5	39.2
Net lending (+) / net borrowing (-)	-4.1	-4.2	-2.6	-2.9	.	.	-2.8	-2.6	-2.3
Public debt, EU-def., % of GDP	43.4	52.1	54.6	53.6	.	.	53.4	53.5	53.0
Central bank policy rate, % p.a., end of period 5)	1.00	0.75	0.25	0.05	0.15	0.05	.	.	.
Current account, EUR mn 6)	-3,497	684	1,446	590	952	-16	-630	-970	-1,470
Current account, % of GDP 6)	-5.0	0.9	2.0	0.8	2.6	0.0	-0.8	-1.2	-1.7
Exports of goods, BOP, EUR mn 6)	54,673	60,159	62,145	62,658	31,530	32,468	65,200	67,800	70,500
annual change in %	17.6	10.0	3.3	0.8	3.3	3.0	4.0	4.0	4.0
Imports of goods, BOP, EUR mn 6)	54,709	57,653	59,097	59,309	29,273	30,944	63,000	66,200	69,500
annual change in %	17.4	5.4	2.5	0.4	3.2	5.7	6.2	5.0	5.0
Exports of services, BOP, EUR mn 6)	5,228	6,049	6,892	6,833	3,316	3,286	6,800	7,000	7,200
annual change in %	8.1	15.7	13.9	-0.8	1.2	-0.9	-1.0	3.0	3.0
Imports of services, BOP, EUR mn 6)	5,498	5,628	6,481	6,749	3,237	3,187	6,600	6,900	7,200
annual change in %	0.2	2.4	15.2	4.1	6.3	-1.5	-2.0	5.0	5.0
FDI liabilities (inflow), EUR mn 6)	3,961	1,356	757	27	254	1,583	1,700	.	.
FDI assets (outflow), EUR mn 6)	1,962	-958	976	184	828	1,374	1,400	.	.
Gross reserves of NB excl. gold, EUR mn	659	620	670	1,165	702	1,345	.	.	.
Gross external debt, EUR mn 6)	55,312	54,882	60,444	67,776	66,154	67,252	68,900	69,500	71,300
Gross external debt, % of GDP 6)	78.8	76.0	82.1	90.1	88.0	86.7	88.8	85.8	84.1
Purchasing power parity EUR/EUR	0.6872	0.6829	0.6794	0.6663	.	.	.	.	.

1) Preliminary. - 2) According to census May 2011. - 3) According to ESA 2010. - 4) From 2012 data according to census May 2011. -
5) Official refinancing operation rates for euro area (ECB). - 6) BOP 6th edition.

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