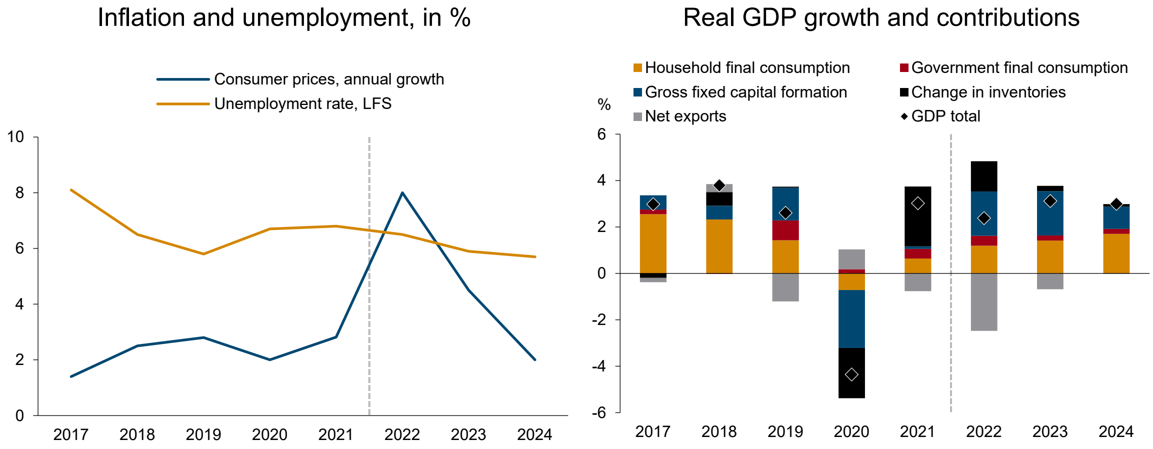
SLOVAKIA: Yet another blow to the automotive industry

DORIS HANZL-WEISS

By the end of 2021, Slovakia's GDP had still not fully recovered from the COVID-19 pandemic, showing annual growth of only 3%. Growth forecasts have been revised substantially downwards, reflecting the negative impact of the Russian war in Ukraine. Still, the inflow of EU funds should provide some growth impetus at a time of rising risk.

Figure 4.20 / Slovakia: Main macroeconomic indicators



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

The Russian invasion of Ukraine is sending shockwaves around the world and will also have repercussions for Slovakia, which has not yet fully recovered from the COVID-19 pandemic. Slovakia has been welcoming refugees from Ukraine, its immediate neighbour to the east: more than 300,000 crossed the border between 24 February and the start of April. The war will depress Slovak growth prospects through a combination of increased uncertainty and rising prices, and both consumers and investors are likely to be hit. Also, the important automotive industry will be exposed to another external shock – its third, following COVID-19 and the semiconductor shortage – and will see trade links disrupted further. Furthermore, the country's heavy dependence on Russian energy presents a threat to Slovakia's future prospects. A halt to energy imports would push Slovakia's growth into negative territory.

After the COVID-19-induced decline in 2020, GDP increased by 3% in 2021 – much less than expected. Still troubled by waves of the pandemic in the first and the fourth quarters, and by semiconductor shortages throughout the year (which affected the all-important automotive industry), the Slovak recovery in 2021 was less strong than expected. GDP increased by only 3% and has still not reached its 2019 value. If we look at the components of GDP, growth was supported by household consumption, up by 1.1% on the back of pent-up demand. Overall, however, growth was driven largely by an increase in inventories related to the supply-chain bottlenecks. Gross capital formation surged by 15%, while investment (gross fixed capital formation) increased by only 0.6%. Also, government consumption contributed to growth, rising by 1.9%. Net exports had a negative effect on growth: although exports of goods and services increased by 10.2%, imports of goods and services grew by even more (11.2%).

The important automotive industry still faces a rough ride in 2022. The main manufacturing industry in Slovakia – the automotive sector – was troubled by a shortage of semiconductors last year. It experienced ups (March) and downs (August) during the year, but overall grew by 4% year on year. The major automotive companies – Volkswagen Slovakia, KIA Motors Slovakia, Stellantis (previously PSA Peugeot-Citroen) and Jaguar Land Rover – had to either suspend production for several days, cut work shifts or drop certain production lines. Nevertheless, the output of passenger cars did increase slightly, compared to 2020, again reaching 1 million cars in 2021. In the neighbouring countries, passenger car production decreased. Slovakia thus retained its position as the world's number one producer of passenger cars per capita. The automotive industry faces tough conditions in 2022, too: the semiconductor shortage has still not been resolved and will last throughout 2022. Supply-chain disruptions could emerge as a result of outbreaks of COVID-19 in China. The war in Ukraine is also affecting supplies (in particular wiring harnesses) and raw materials. Volkswagen Slovakia, for example, had to suspend production for two days at the end of March, and Jaguar Land Rover for three days at the beginning of April. Thus, industrial production in the automotive sector fell by 3% in the first two months of 2022. In terms of exports, Slovakia has the largest share of its motor vehicle exports (NACE rev.2, 29.1) going to Russia (3.4%). Car parts (NACE rev.2, 29.3) have a lower exposure to Russia, however: only 2.5% of total car parts exports go to that country (compared to 4% to Czechia and Romania). That said, there are differences between the various companies, with KIA being the most exposed: 12% of its cars are exported to Russia.

Household consumption will be supported by an improving labour market, but is threatened by rising inflation. The situation on the labour market improved in the second half of 2021. Overall, however, employment fell by 1.4% in 2021. The services sector was still affected by the pandemic, and employment in accommodation and food services and in arts, entertainment and recreation fell by more than 10%. The unemployment rate declined throughout the year, but was on average slightly higher than in 2020 (6.8% compared to 6.7%). As the labour market reacts with a time lag, the situation will improve this year. There is a fear that the war in Ukraine will mean that Ukrainian workers will return home, leading to the loss of Ukrainian doctors in Slovak hospitals and of Ukrainian workers in the construction sector. The Ukrainian refugees are mainly women and children, and thus will not contribute to any easing of labour shortages. Inflation could threaten consumer sentiment and consumer spending. The Harmonised Index of Consumer Prices (HICP) was up 7.7% in January and 8.3% in February. The outlook for the whole year is grim, with inflation reaching about 8%. Producer prices have surged even more, rising by 21% in January and 28% in February 2022. The cost of electricity is regulated and electricity prices for households are frozen for three years, up to 2024. An 'inflation assistance' scheme is in preparation to help the most vulnerable groups. Another government support just established is financial support for anyone who provides accommodation for Ukrainian refugees.

The good export performance of 2021 – including in car exports – is threatened this year, while imports are skyrocketing as a result of higher prices. Together, these trends are pushing the current account into negative territory. In 2021, goods exports increased by 16.2%, while imports grew by 22.6% – both up on the 2019 figures (as measured by Slovak trade statistics data). Exports stood at a record high in 2021, having recovered from the COVID-19-induced slump of 2020. Car exports were also higher in 2021, despite the shortage of semiconductors hampering the industry that year. Trade in goods with the country's most important trading partners of Germany and the Czech Republic recovered in 2021: exports of goods to Germany increased by 12.5% and to the Czech Republic by almost 30%. Imports from those two countries likewise increased – by 21% and 14%, respectively. In 2021, imports from Russia surged by 63%, so that Slovakia recorded its second-largest trade deficit with Russia. If we look at trade with Ukraine and Russia in more detail, exports to those two countries are fairly limited, accounting for only 0.9% and 1.5% of total exports. While imports from Ukraine are also tiny (0.9%), imports from Russia are important and account for 6.4%. The main import products from Russia are crude oil, natural gas, nuclear fuel, iron ore and coal (used, for example, in U.S. Steel Košice). Slovakia's energy dependence on Russia is the second highest in the EU, with imports from Russia accounting for more than 50% of gross available energy in 2020.[42] Trade data available for January and February 2022 already show the main trends for this year: exports increased by 13.5% and imports by 25%, leading to a trade deficit of EUR 600m already in the first two months.

Inflows of EU funds should promote a recovery in investment, but there are still some problems. Slovakia should benefit this year (and in coming three years) from the increased inflow of EU funds. However, problems have recently emerged relating to projects for the previous programme period 2014-2020 (the final deadline for which is 2023) and concerning money for roads and railways. In addition, regional governors have expressed concern about the low allocation of funds under the new programme period 2021-2027. On the other hand, the chances are better for the disbursement of funds from the EU's Recovery and Resilience Facility: Slovakia's recovery plan is worth EUR 6.3bn, and the first payment request can be made at the end of April, once all the milestones and targets have been met. Of the 14 milestones, 13 have already been met, including university reform and the introduction of budget expenditure caps. Only the new court map, which is part of the judicial reform, is still missing.

The Russian war in Ukraine means that the forecasts for Slovakia have been revised downwards. The wiiw growth forecasts for Slovakia have been revised substantially downwards both for this year and for coming years, due to the growing uncertainty. Slovak GDP is expected to grow by 2.4% in 2022, 3.1% in 2023 and about 3% in 2024. This year, growth should come from household consumption, due to pent-up demand, and also from government consumption. Gross fixed capital formation, which has suffered badly over the past two years, should see a boost, helped along by the inflow of EU funds and the base effect. Net exports will continue to have a negative impact on growth, due to sluggish exports and growing imports. The risks are large and mounting: the Russian war in Ukraine means greater uncertainty, which could drag down consumer sentiment, consumer spending and also investment. The worst scenario would be a halt to energy imports from Russia, which would have severe implications for industry. Finally, the COVID-19 pandemic has moved backstage, but it still affected the economy in the Q1 2022 and is not yet over.

42 https://ec.europa.eu/eurostat/statistics-explained/index.php?title=EU_energy_mix_and_import_dependency&stable=1 (data extracted 4 March 2022).

Table 4.20 / Slovakia: Selected economic indicators

	2018	2019	2020	2021 1)	2022	2023 Forecast	2024
Population, th pers., average	5,447	5,454	5,459	5,447	5,470	5,475	5,480
Gross domestic product, EUR m, nom.	89,430	94,048	92,079	97,123	107,400	115,700	121,500
annual change in % (real)	3.8	2.6	-4.4	3.0	2.4	3.1	3.0
GDP/capita (EUR at PPP)	21,170	21,750	20,950	21,960	.	.	.
Consumption of households, EUR m, nom.	49,683	52,334	52,748	55,075	.	.	.
annual change in % (real)	4.2	2.6	-1.3	1.1	2.1	2.5	3.0
Gross fixed capital form., EUR m, nom.	18,787	20,296	18,073	18,571	.	.	.
annual change in % (real)	2.8	6.7	-11.6	0.6	10.0	10.0	5.0
Gross industrial production							
annual change in % (real)	4.4	0.4	-9.0	10.4	2.0	5.0	3.0
Gross agricultural production							
annual change in % (real)	-2.4	-4.2	3.4	0.3	.	.	.
Construction industry							
annual change in % (real)	8.5	-3.6	-11.3	-2.0	.	.	.
Employed persons, LFS, th, average 2)	2,567	2,584	2,531	2,561	2590	2630	2660
annual change in %	1.4	0.7	-2.0	-1.4	1.0	1.5	1.0
Unemployed persons, LFS, th, average 2)	180	158	181	188	180	160	160
Unemployment rate, LFS, in %, average 2)	6.5	5.8	6.7	6.8	6.5	5.9	5.7
Reg. unemployment rate, in %, eop	5.0	4.9	7.6	6.8	.	.	.
Average monthly gross wages, EUR	1,013	1,092	1,133	1,211	1290	1370	1440
annual change in % (real, gross)	3.6	5.0	1.9	3.6	-1.5	1.5	3.0
Consumer prices (HICP), % p.a.	2.5	2.8	2.0	2.8	8.0	4.5	2.0
Producer prices in industry, % p.a.	2.3	1.9	-0.6	6.8	17.5	7.0	3.0
General governm. budget, EU def., % of GDP							
Revenues	38.8	39.3	40.1	40.4	40.0	40.0	39.5
Expenditures	39.8	40.7	45.6	47.5	45.1	44.1	43.0
Net lending (+) / net borrowing (-)	-1.0	-1.3	-5.5	-7.1	-5.1	-4.1	-3.5
General gov. gross debt, EU def., % of GDP	49.6	48.1	59.7	62.5	61.2	60.0	58.0
Stock of loans of non-fin. private sector, % p.a.	9.8	6.6	5.0	7.2	.	.	.
Non-performing loans (NPL), in %, eop	3.1	2.8	2.3	1.9	.	.	.
Central bank policy rate, % p.a., eop 3)	0.00	0.00	0.00	0.00	.	.	.
Current account, EUR m	-1,973	-3,163	330	-1,910	-4,200	-4,300	-4,000
Current account, % of GDP	-2.2	-3.4	0.4	-2.0	-3.9	-3.7	-3.3
Exports of goods, BOP, EUR m	75,142	75,522	70,011	81,464	83,900	87,500	91,900
annual change in %	6.6	0.5	-7.3	16.4	3.0	4.3	5.0
Imports of goods, BOP, EUR m	75,381	76,658	68,996	81,539	86,400	90,800	95,300
annual change in %	7.8	1.7	-10.0	18.2	6.0	5.1	5.0
Exports of services, BOP, EUR m	10,228	10,981	9,032	9,459	9,800	10,600	11,400
annual change in %	9.5	7.4	-17.8	4.7	4.0	8.0	8.0
Imports of services, BOP, EUR m	9,300	9,763	7,944	8,663	9,200	9,600	10,000
annual change in %	10.0	5.0	-18.6	9.0	6.0	4.0	4.0
FDI liabilities, EUR m	1,906	2,042	-214	818	.	.	.
FDI assets, EUR m	760	-162	1,683	1,097	.	.	.
Gross reserves of CB excl. gold, EUR m	3,426	5,002	6,050	6,850	.	.	.
Gross external debt, EUR m	102,870	106,016	110,925	133,057	113,000	110,000	110,000
Gross external debt, % of GDP	115.0	112.7	120.5	137.0	105.2	95.1	90.5

1) Preliminary and wiiw estimates. - 2) From 2021 the new LFS methodology is applied in line with the Integrated European Social Statistics Regulation (IESS). - 3) Official refinancing operation rates for euro area (ECB).

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