SLOVAKIA: Domestic demand gaining importance

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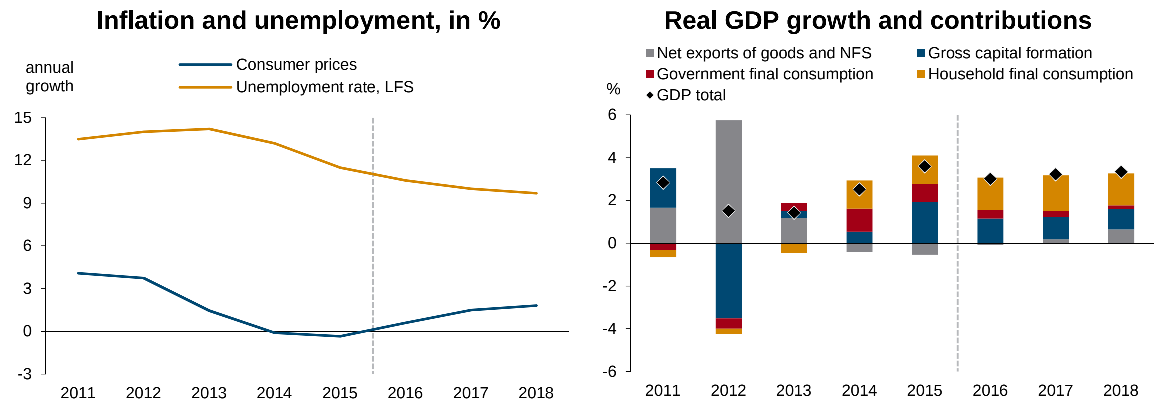
Strong growth in terms of gross fixed capital formation helped GDP to soar upwards by 3.6% in 2015. For the period 2016-2018, growth will range around 3%, with a slight upward trend in the latter years and backed by domestic demand.

Figure 54 / Slovakia: main macroeconomic indicators



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

Preliminary estimates show that Slovak GDP grew by 3.6% in 2015, the strongest increase in the past four years. This was due to a large surge in gross fixed capital formation (by 11% in the first three quarters; mainly in transport infrastructure), which benefited from the speeding-up of EU structural spending at the end of the drawing period of the 2007-2013 financial framework. In addition, household consumption grew as well (by 2.2%), but less than suggested by the pronounced improvements in the labour market and real wage growth. Consumer prices fell for the second year running, declining by 0.3% in 2015. In addition, government consumption contributed to growth. By contrast, net exports had a negative effect on growth. While goods exports rose by 5% (nominally) in 2015, goods imports increased by 7.5%. The trade balance was positive and reached EUR 3.3 billion but was 1.3 billion lower than in 2014. Together with a highly negative primary and secondary income balance (of about more than EUR 3 billion) this will push the current account into negative territory, after having achieved small positive figures in the previous three years. About 85% of goods were exported to the European Union, with goods exports to Germany – Slovakia's main export partner – rising by 8% (January to November 2015 as compared to the same period of 2014), and those to the Czech Republic, Slovakia's second most important export partner, by 2%. Deliveries to the former promising export markets Russia and China dropped by 30% each, while exports to the United States expanded by 17% (mainly cars).

Looking at sectoral trends, industrial production saw a pronounced surge in 2015 and increased by 6%. This was due to the automotive industry – the largest sector of Slovak manufacturing – taking over its role as a growth driver since mid-year again. The three main car manufacturers, Volkswagen Bratislava, KIA Motors and PSA Peugeot-Citroën, for the first time produced more than 1 million cars in 2015, boosting the country's position as the largest car producer per capita in the world (184 per 1,000 inhabitants). KIA raised car production by 4.4%, PSA Peugeot-Citroën by 19%. Despite the emission scandal striking Volkswagen in the United States in September 2015 and Volkswagen producing about 40% of all cars in Slovakia (about 400,000 in 2014), recent automotive industry figures of production and new orders have not shown signs of a slump – on the contrary, figures soared in November and December. In addition, another positive news was announced in December, when the final agreement for the arrival of a fourth car producer in Slovakia was signed: Jaguar Land Rover's new plant will be built near Nitra, the investment sum totals more than EUR 1 billion. Construction will start in 2016 and production should begin in late 2018. The initial annual production capacity will be 150,000 cars (up to 300,000 cars later on) while about 2,800 persons will be employed.

Declining for six years in a row, the construction sector finally recovered in 2015 and grew for the first time since the beginning of the economic crisis (by 18%, year on year). It was the main beneficiary of the speeding-up of EU structural funds towards the end of 2015. Overall, construction of civil engineering works increased by as much as 55% (data for the first eleven months of 2015), while construction of buildings grew only by 3%.

Labour market developments have been very favourable in 2015. Employment rose by about 2%, the fastest growth since the outbreak of the global financial crisis. The unemployment rate declined to 11.5%, which is very low for Slovak standards but still high compared to neighbouring countries (Slovakia suffers particularly from high levels of long-term and youth unemployment). Large regional disparities exist (unemployment is highest in the East and Central-South parts of Slovakia, featuring also the highest shares of Roma population) and are targeted under Prime Minister Fico's second social package. Average monthly real wages increased by 3% in 2015, the minimum wage rose again by EUR 25 to EUR 405 at the beginning of 2016, and salaries of civil servants were raised by 4%. Nevertheless, teachers and nurses have protested since the end of 2015 for higher salaries and better conditions in the education and health care systems. Teachers went on strike in January 2016 and nurses handed in notices.

The Slovak budget deficit hovered between -2.6% and -2.8% of GDP in the last three years, with the debt to GDP ratio falling slightly below 53% in 2015. This is important with respect to Slovakia's Fiscal Responsibility Act, featuring a 53% threshold.[61] Revenues and expenditures in 2015 were strongly affected by the drawing of EU funds, as the drawing period for transfers under the 2007-2013 financial framework was coming to an end. Although the drawing was speeded up, Slovakia was less successful than other countries and may face a loss of EUR 1 billion as compared to the earmarked potential sum of EUR 11.5 billion. Government policies and expenditures are shaped by the approaching parliamentary elections on 5 March 2016. In December 2015, Fico announced the third social

[61] Between 53% and 55% of GDP, 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.

package.[62] It promises the creation of 100,000 new jobs, construction of apartments for young families and teachers, Christmas bonuses for pensioners, building of roads and security measures. At the beginning of 2016, a range of measures under the second social package became effective, comprising a reduction of the VAT rate of basic foodstuff from 20% to 10% (fresh meat and freshwater fish, butter, fresh bread and milk) and the introduction of free bank accounts and those for a monthly fee of 3 euro, respectively. Gas rebates will be paid out at the beginning of the year. New government investment projects in the pipeline include the repair of roads in Bratislava before July, when Slovakia takes over its first Presidency of the Council of the European Union, and the Bratislava ring road ('Bratislava bypass'). By the end of 2015, Italy's Enel sold its 66% stake in the Slovenské Elektrárne energy utility to the Czech EPH (the Slovak government was heavily interested in this deal and still has an option to increase its minority stake to 51% in the second stage of this deal).

For the period 2016 to 2018, Slovak growth is forecasted to range around 3% per year, with a slight upward trend in the latter years provided constant developments on global markets. The 2015 growth impetus of soaring gross fixed capital formation will not continue, as the effects of the next planning period for structural funds is going to take off only in the years ahead. However, private investment will be pushed up by the new plant construction by Jaguar Land Rover, while loans to corporations also started to increase at the end of 2015. Household consumption will be the main driver of growth in the following three years and should speed up, backed by favourable labour market developments. Strong growth of loans to households (above 13% in 2015, year on year) may be seen as one internal risk, but is being only slowly reflected in property prices. The upcoming parliamentary elections, to take place on 5 March, shape policies at the moment but no major changes are to be expected from these elections. The Social Democrats (SMER), led by Robert Fico, lead in opinion polls, while the other parties are small and dispersed. Thus, a continuation of Fico's policy can be expected (i.e., continuation of debt reduction, selective social measures and possibly increasing state influence in the energy sector). Net exports, which had been the major growth driver in the years after the crisis, have lost momentum and do not contribute to growth any longer. Imports are expected to increase with growing household consumption, while export growth is constrained by missing export locomotives. New capacities in the automotive industry might provide some impetus from 2018/2019 onwards, when the new Jaguar Land Rover plant will start car production.

[62] The first social package was announced in June 2014 (worth EUR 250 million), the second one in May 2015 (worth EUR 200 million). The third social package includes measures worth EUR 1 billion and should be introduced as of 2017.

Table 23 / Slovakia: selected economic indicators

	2011	2012	2013	2014	2015 1)	2016	2017	2018
							Forecast	
Population, th pers., average	5,398	5,408	5,413	5,419	5,424	5,429	5,434	5,439
Gross domestic product, EUR mn, nom.	70,444	72,420	73,835	75,561	77,900	80,700	84,500	88,900
annual change in % (real)	2.8	1.5	1.4	2.5	3.6	3.0	3.2	3.3
GDP/capita (EUR at exchange rate)	13,000	13,400	13,600	13,900	14,400	14,900	15,600	16,300
GDP/capita (EUR at PPP)	19,000	19,700	20,200	21,100	22,400	.	.	.
Consumption of households, EUR mn, nom.	39,667	40,868	41,083	42,010	42,900	.	.	.
annual change in % (real)	-0.6	-0.4	-0.8	2.4	2.4	2.7	3.0	2.7
Gross fixed capital form., EUR mn, nom.	16,946	15,405	15,292	15,766	17,100	.	.	.
annual change in % (real)	12.7	-9.2	-1.1	3.5	9.7	4.0	4.5	4.0
Gross industrial production								
annual change in % (real)	5.3	7.9	4.9	4.0	5.9	4.0	4.0	5.0
Gross agricultural production								
annual change in % (real)	8.7	-5.7	6.7	7.4	-4.8	.	.	.
Construction industry								
annual change in % (real)	-1.8	-12.5	-5.3	-4.1	17.9	.	.	.
Employed persons, LFS, th, average 2)	2,351	2,329	2,329	2,363	2,410	2450	2470	2490
annual change in %	1.5	0.6	0.0	1.5	2.0	1.5	1.0	0.7
Unemployed persons, LFS, th, average 2)	368	378	386	359	314	290	270	270
Unemployment rate, LFS, in %, average 2)	13.5	14.0	14.2	13.2	11.5	10.6	10.0	9.7
Reg. unemployment rate, in %, end of period	13.6	14.4	13.5	12.3	10.6	.	.	.
Average monthly gross wages, EUR	786	805	824	858	880	910	950	990
annual change in % (real, gross)	-1.6	-1.2	1.0	4.2	3.0	3.0	2.5	2.0
Consumer prices (HICP), % p.a.	4.1	3.7	1.5	-0.1	-0.3	0.6	1.5	1.8
Producer prices in industry, % p.a.	4.5	1.9	-1.0	-3.5	-3.0	0.1	1.0	1.5
General governm.budget, EU-def., % of GDP								
Revenues	36.4	36.0	38.4	38.9	40.8	39.3	38.5	37.9
Expenditures	40.5	40.1	41.0	41.6	43.5	41.7	40.5	39.7
Net lending (+) / net borrowing (-)	-4.1	-4.2	-2.6	-2.8	-2.7	-2.4	-2.0	-1.8
Public debt, EU-def., % of GDP	43.3	51.9	54.6	53.5	52.7	52.6	52.3	52.0
Central bank policy rate, % p.a., end of period 3)	1.00	0.75	0.25	0.05	0.05	.	.	.
Current account, EUR mn	-3,497	684	1,446	100	-897	-1,300	-1,700	-1,800
Current account, % of GDP	-5.0	0.9	2.0	0.1	-1.2	-1.6	-2.0	-2.0
Exports of goods, BOP, EUR mn	54,673	60,159	62,145	62,581	65,919	68,600	71,300	74,900
annual change in %	17.6	10.0	3.3	0.7	5.3	4.0	4.0	5.0
Imports of goods, BOP, EUR mn	54,709	57,653	59,097	59,722	64,029	66,900	70,100	73,600
annual change in %	17.4	5.4	2.5	1.1	7.2	4.5	4.8	5.0
Exports of services, BOP, EUR mn	5,228	6,049	6,892	6,833	7,184	7,400	7,600	8,000
annual change in %	8.1	15.7	13.9	-0.8	5.1	3.0	3.0	5.0
Imports of services, BOP, EUR mn	5,498	5,628	6,481	6,749	7,026	7,400	7,800	8,200
annual change in %	0.2	2.4	15.2	4.1	4.1	5.0	5.0	5.0
FDI liabilities (inflow), EUR mn	3,961	1,356	757	27	1,695	.	.	.
FDI assets (outflow), EUR mn	1,962	-958	976	184	1,147	.	.	.
Gross reserves of NB excl. gold, EUR mn	659	620	670	1,165	1,648	.	.	.
Gross external debt, EUR mn	55,312	54,882	60,444	67,776	70,900	72,600	74,400	76,500
Gross external debt, % of GDP	78.5	75.8	81.9	89.7	91.0	90.0	88.0	86.0
Purchasing power parity EUR/EUR	0.6873	0.6787	0.6741	0.6616	0.6417	.	.	.

1) Preliminary and wiiw estimates. - 2) From 2012 data according to census May 2011. - 3) Official refinancing operation rates for euro area (ECB).

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