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Slovak Republic: 2009 Article IV Consultation—Staff Report; and Public Information Notice on the Executive Board Discussion

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2009 Article IV consultation with the Slovak Republic, the following documents have been released and are included in this package:

- The staff report for the 2009 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on May 25, 2009, with the officials of the Slovak Republic on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on July 2, 2009. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- A Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its July 20, 2009, discussion of the staff report that concluded the Article IV consultation.

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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SLOVAK REPUBLIC

Staff Report for the 2009 Article IV Consultation

Prepared by the Staff Representatives for the 2009 Consultation with the Slovak Republic

Approved by Anne-Marie Gulde-Wolf and Ranil Salgado

July 2, 2009

Executive Summary

Background: Slovakia adopted the euro in January 2009 after enjoying a period of rapid growth with few signs of overheating. Euro adoption, and an overall sound banking sector, helped Slovakia weather the global financial turmoil relatively well through 2008. However, economic activity tumbled in the first quarter of 2009, and the country is set this year to experience a recession for the first time since the early transition. Nonetheless, a recovery is projected to take hold in the second half of 2009.

Challenges: The immediate goal should be to curtail the extent and duration of the recession, while enhancing confidence and the foundations for future growth. This should be done by setting the fiscal deficit on a downward path to below 3 percent of GDP by 2011, while taking measures to maintaining high productivity growth.

Staff views: Fiscal policy that allows automatic stabilizers to operate is appropriate, but it should be anchored within a medium term credible framework that sets a declining deficit trajectory to below 3 percent by 2011. The financial sector will face a particularly challenging environment in the near future. However, the sector appears well-prepared, and the authorities' steps to increase monitoring and supervisory cooperation are appropriate.

Authorities' views: The authorities' goal is to maintain expenditure in 2009 within the budget envelope, while letting the automatic stabilizer on the revenue side operate fully. They are committed to fiscal consolidation and are searching for ways to reduce the deficit in 2010 with the goal of achieving the Maastricht criteria as soon as feasible.

Mission team: Mr. De Broeck (Head), Ms. Banerji, Mr. Konuki, and Mr. Mehrez (all EUR) visited Bratislava May 11–25, 2009 and held discussions with the Minister of Finance, the Governor of the National Bank of Slovakia, and other key central bank and government officials and financial sector, labor, and business representatives. Mr. Jakoby (Adviser to the Executive Director) also attended the meetings.

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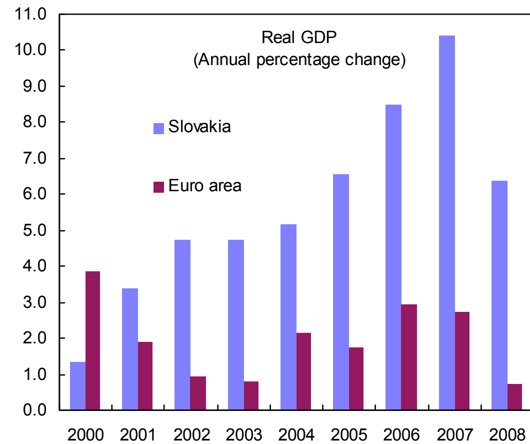
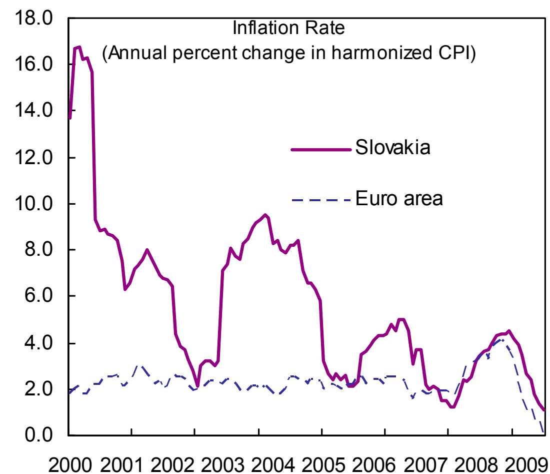
I. Context

1. **Slovakia has been among the best economic performers in central and eastern Europe in recent years.** During 2004–08, the country enjoyed a period of rapid economic growth guided by sound macroeconomic and structural policies, and buoyed by a vibrant export sector. Real GDP grew by an average 7.4 percent, which helped reduce the difference in GDP per capita between Slovakia and the EU average substantially. At the same time, the harmonized unemployment rate dropped by 10 percentage points to 9 percent (seasonally adjusted) by September 2008.



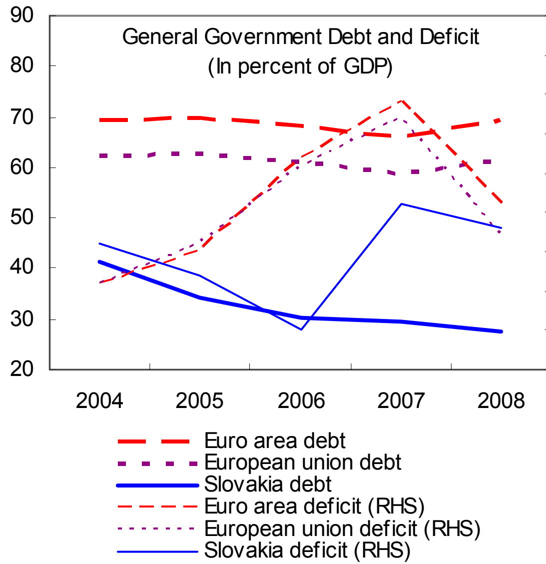
Source: Haver Analytics.

2. **The broad-based economic expansion did not instigate imbalances or unsustainable dynamics.** Inflation remained relatively low, and credit expansion, although rapid, was consistent with underlying convergence. Moreover, banks remained focused on traditional domestic activities and had no significant exposure to sub-prime lending or "toxic" structured products. The current account deficit has declined gradually to a level consistent with convergence. It was mainly financed by FDI, and hence external debt remained low. These favorable factors have facilitated a smooth transition to the euro on January 1, 2009, despite the global financial turmoil.

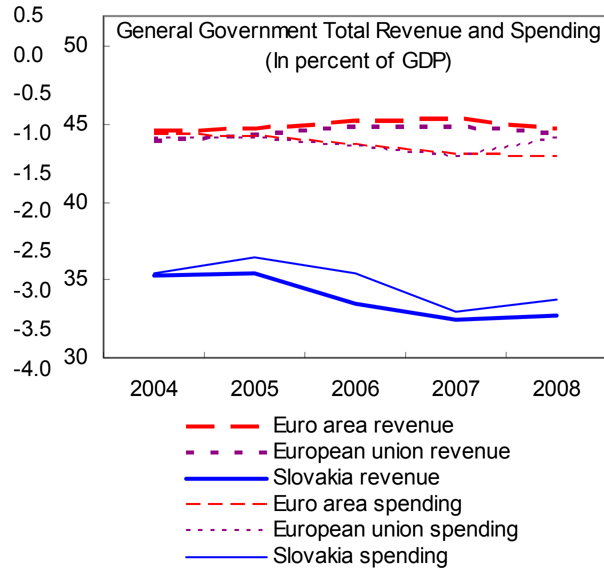


Source: Haver Analytics.

3. **Rapid growth helped bring down the government deficit and debt to comfortable levels.** The general government deficit, as a share of GDP, fell by about 1 percentage point to around 2 percent during 2006–08. This improvement was achieved despite a decrease in the tax revenue-to-GDP ratio to the lowest level among the EU countries. Reflecting smaller deficits and accelerating growth, the general government debt-to-GDP ratio declined to about 27 percent at end-2008.

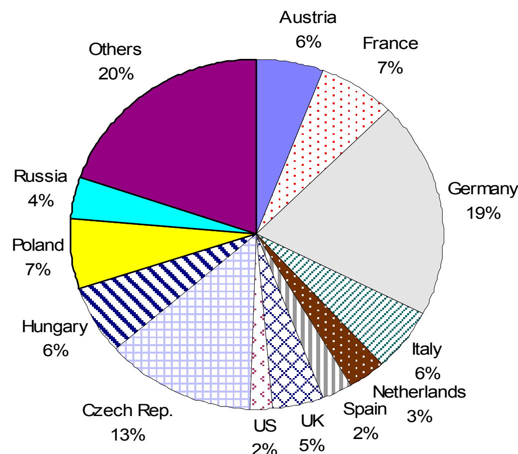


Source: Eurostat.



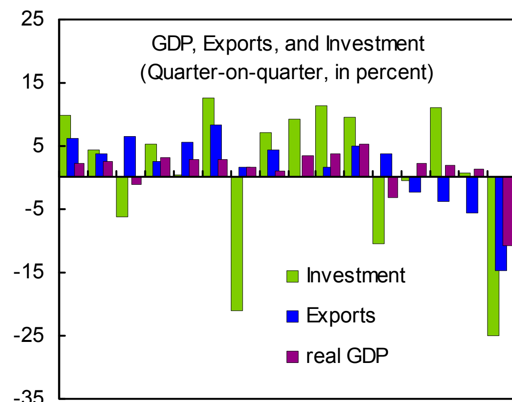
Source: Eurostat.

4. **However, Slovakia is highly influenced by external economic developments, and the global economic slump substantially affects its economy.** Strong economic fundamentals and a sound financial sector helped Slovakia weather the global crisis and contributed to maintaining the country's high growth throughout 2008. However, the magnitude and extent of the global slump, particularly the pronounced economic weakening in the euro area, led to a sharp decline in economic activity in the first quarter of 2009.



Source: IFS, Direction of Trade Statistics.

5. **Real GDP in the first quarter of 2009 fell by 11.4 percent (q-o-q).** Exports, which fell by 16.2 percent (q-o-q), led the decline, but domestic demand including private consumption contracted as well (by 2.8 percent). A one-off disruption of gas imports also contributed to a shift of production from the first to the second quarter. At the same time, the harmonized unemployment rate soared to 11.1 percent (seasonally adjusted) by April and inflation (y-o-y) decelerated rapidly to slightly above 1 percent.



Source: Haver Analytics, and IMF staff estimates.

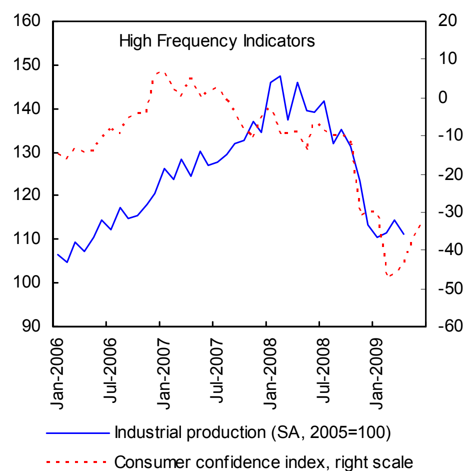
II. Policy Discussions

The policy discussions focused on the outlook; fiscal policy in response to the crisis and in the medium term; financial sector issues; and the medium-term challenges to competitiveness and to maintaining rapid and balanced growth.

A. Outlook

6. **The authorities and staff concurred that economic activity will decelerate significantly in 2009.** Staff projects that output will contract by close to 5 percent following the sharp decline in the first quarter. This projection falls within the range of forecasts from the private sector and the authorities. Reflecting its conservative character, the Ministry of Finance's projection, a 6.2 percent contraction this year, is near the lower end of the range. Growth is expected to resume in 2010 as Slovakia's major export markets will start bouncing back and short-term interest rates remain supportive. Growth would accelerate in 2011 and stabilize at around 4½ percent over the medium term, significantly below the 2004–08 average.

7. **Some high frequency indicators suggest that economic activity may be stabilizing, but the rebound will be slow.** Surveys of consumer and industrial confidence indicators also show some improvement, while remaining in negative territory. The linkages between Slovakia and the euro area have grown in recent years with the transformation of the country's economy. Thus, the pace and timing of the Slovak recovery would be in line with that in the rest of the euro zone (Box 1), which is projected to be only gradual. In addition, the recovery will be hampered by weak domestic demand reflecting the deterioration in employment during most of 2009, and banks' reining in of credit (see below).

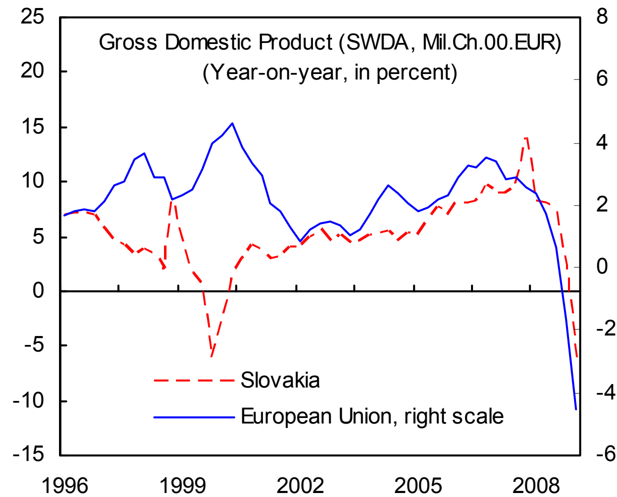


Source: Haver Analytics.

8. **The authorities and staff agreed that uncertainty is unusually large and risks to growth are broadly balanced.** The economy could rebound faster if the slump in the first quarter reflects mainly a one time adjustment of production to reduce inventories; if the euro zone recovers faster than projected; or if car incentives domestically and abroad benefit the Slovak automobile industry, which is more focused on small automobiles, more than proportionately. On the other hand, the recovery could be more subdued if the euro zone recovery will be weaker than envisioned or less beneficial to the Slovak economy than recent correlations suggest, or if banks' conditions deteriorate more than envisioned.

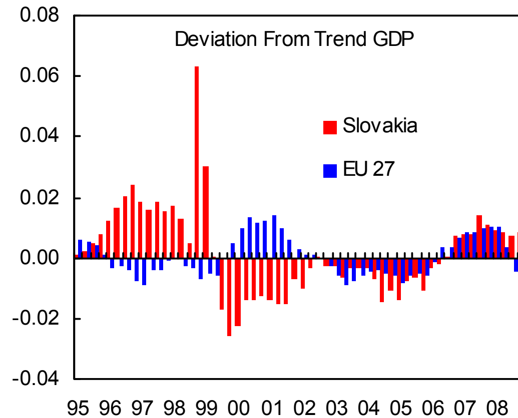
Box 1. Business Cycles Synchronization Between Slovakia and the EU

Business cycle correlation between Slovakia and other EU countries increased significantly in recent years as the Slovak economy shifted from demand-driven growth to supply- and external-driven growth. The data suggest that real GDP growth rates were uncorrelated prior to 2002, but became highly correlated after 2002.



Source: Haver Analytics.

An autoregressive estimation of Slovakia's real GDP deviation from its trend as a function of its lagged deviation and the deviation in the EU provides more quantitative results. It implies that if real GDP growth in the EU increases by one percentage point, growth in Slovakia will increase by about ½ percentage point during the same quarter, and the accumulated impact will reach about 2 percentage points.



Source: IMF staff estimates.

9. **Staff concurred with the authorities that underlying systemic vulnerabilities appear limited.** The projected increases in external and public debts are temporary and do not reflect structural imbalances or raise sustainability concerns. With Slovakia in the euro zone, gross external financing requirements on the order of 10 percent of GDP are expected

to be easily covered. The central government already has prefunded its financing needs for the remainder of 2009 and early 2010. Furthermore, corporate and household debt ratios are comfortable. Households' loan-to-value ratios are in the 50-60 percent range, and housing prices, except for commercial and high-end residential property, are broadly stable. The recession is not expected to give rise to social tensions either as social partners are cooperating, including through arrangements to increase working hour flexibility, which would limit the recession's impact on employment and welfare. Nevertheless, staff emphasized that financial conditions of households, firms and banks would come under additional stress. It was therefore essential that policies be prepared to deal with various contingencies, and be transparent, comprehensive and credible so as to maintain market confidence.

B. Fiscal Policy

10. **The fiscal position in 2009 is weakening rapidly because of revenues underperformance.** Central government tax revenue in the first six months of 2009 dropped by more than 13 percent compared with the same period last year. VAT revenue, in particular, plummeted reflecting a decline in domestic consumption and collapse in imports. Government spending, however, was kept in line with budget plans: a stimulus package (Box 2) was offset by reallocation and rationalization of spending. Overall, the central government budget deficit in the first six months of 2009 was already above its budgetary estimate for the year as a whole. The social security sector also is under pressure with collection of social security contributions falling short of targets and higher-than-expected spending on account of rising unemployment.

11. **The authorities intend to maintain the budgetary expenditure envelope in 2009, and let the automatic stabilizers on the revenue size operate fully.** They explained that keeping the deficit at 3 percent of GDP as envisaged in the budget would imply significant, unnecessary, pro-cyclical tightening. They emphasized their commitment to fiscal discipline—no new stimulus initiatives are planned for the remainder of 2009, and additional recession-induced social spending will be covered by sustained rationalization efforts. The revenue shortfall for the year as a whole is projected to reach about 2 percent of GDP. The general government deficit is projected to be about 5 percent of GDP, and could be larger in case of negative growth surprises.

Box 2. Fiscal Stimulus Package

The Slovak government in late 2008 and early 2009 introduced a range of fiscal stimulus measures. These include tax reduction and subsidies with annual budgetary impact of around ½ percent of GDP in 2009 and 2010,[1] measures to increase liquidity of the corporate sector, and steps to accelerate EU funds use. The main measures are:

- *Tax reductions.* A higher basic tax allowance on personal income tax and higher employee tax credit for low-income taxpayers, both expiring at end-2010.
- *Subsidies.* New incentives for corporate research and development, and a temporary car scrapping scheme.
- *Steps to improve the liquidity of the corporate sector.* A reduction in the period for VAT refunding from 60 to 30 days. Lending of around ⅓ percent of GDP to the railway freight transport and the railway infrastructure companies, which are confronted with a crisis-related large drop in transport activity.
- *Incentives to accelerate the use of EU funds.* A temporary simplification of legislative requirements for establishing and operating enterprises that employ disadvantaged workers.

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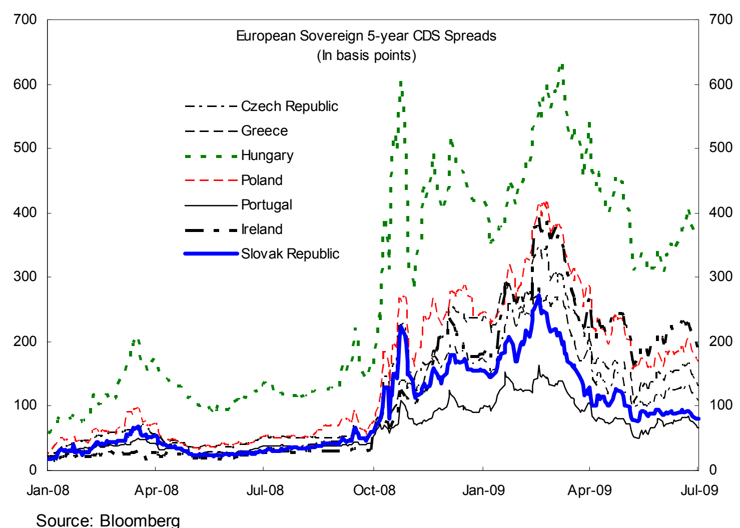
[1] A detailed description of the package, including a number of initiatives with a small budgetary impact (less than €50 million) which are not discussed here, can be found in the *Stability Programme of the Slovak Republic for 2008-2012*.

12. **Staff agreed that letting the deficit widen in 2009 in line with falling revenue was appropriate and would not raise investor concern.** The stimulus package and accelerated utilization of EU transfers will provide a welcome support of at least 1 percentage point of GDP. The wider deficit does not pose financing problems: the very successful issuance of a Eurobond in early May is a clear sign of continued investor confidence. Positive market sentiment toward Slovakia is also reflected in the relatively low government bond spreads versus Germany, and sovereign CDS spreads, which are significantly below those of the other central and eastern European EU members. Still, there is room



Source: Bloomberg

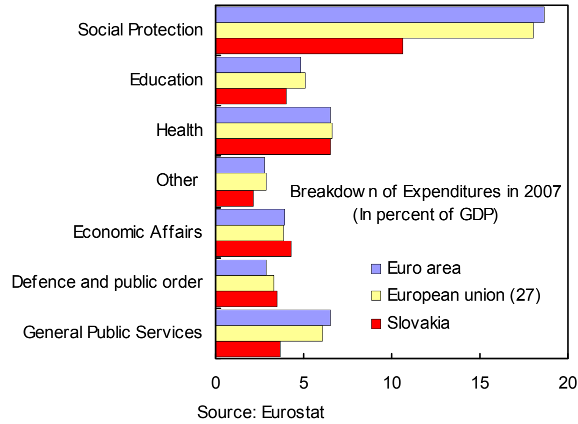
for further spread narrowing, and recent gains could easily be reversed. The mission accordingly supported the government's decision not to add to the stimulus package for the time being: additional discretionary loosening should only be considered in case a much worse-than-expected downturn were to prompt a coordinated EU initiative.

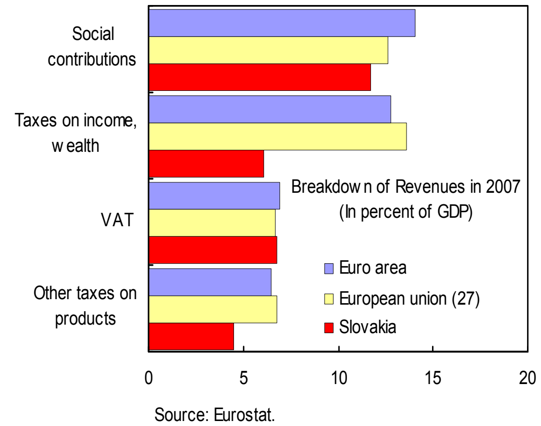
13. **The key challenge for fiscal policy will be to anchor an accommodating fiscal stance during the recession within a credible medium-term consolidation strategy.** Staff argued that deficits would persist in the 4-5 percent of GDP range even after the economy returns to potential in 2012, with upside risks related to expenditure growth in health care. The authorities acknowledged these unfavorable deficit and expenditure dynamics, but had yet to articulate a broader adjustment strategy and corresponding deficit targets. They were committed to sustained efforts to cut costs and improve the quality of spending, including in health care, and intended to broaden the base and simplify the rate structure of social security contributions. The mission welcomed these plans, but emphasized the need to embed them in a well-defined and credible medium-term consolidation strategy and to announce deficit targets for 2010–11.

14. **Staff recommended a strategy aimed at bringing down the deficit to about 4 percent of GDP next year and to below 3 percent of GDP by 2011.** This trajectory would take into account EU norms and avoid breaching the Maastricht ceiling in 2011, when the economy would be close to potential, and boost investor confidence. It also would smooth the adjustment effort and offer some welcome support for the still ongoing recovery in 2010. The authorities agreed with reducing the deficit to below the Maastricht norm as quickly as feasible, but did not specify a corresponding timetable or provide updated fiscal projections. They also wanted to raise spending in certain priority areas. Staff in this regard emphasized that targeted social spending and public investment should be among the spending priorities and be protected.

15. **To achieve the recommended deficit path, a combination of expenditure and revenue measures should be considered.** Sustained efforts to further cut costs and improve spending efficiency will be needed. In this regard, additional health care reform along the lines previously recommended by the IMF[1] and wage growth moderation in the public sector will be key. However, with room for further cost cuts diminishing, measures to boost revenue also will be needed. Authorities' plans to broaden the base of social security contributions while simplifying the rate structure will help. With Slovakia's tax burden among the lowest in the EU, staff and the authorities agreed that a realistic medium-term fiscal strategy would likely also require higher taxes on income.

[1] As discussed in IMF Working Paper No. 07/226 available at http://www.imf.org/external/pubs/cat/longres.cfm?sk=21329.0



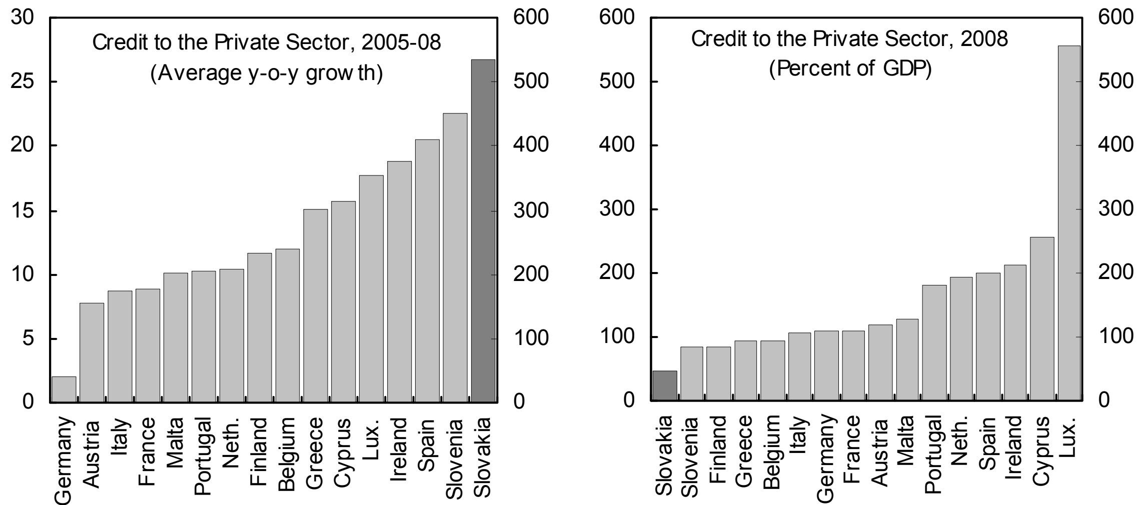


16. **To be credible and effective, the strategy should be supported by fiscal institutional reforms and enhanced transparency.** The mission recommended reforms to better align the annual budget process with the medium-term spending objectives, and steps to improve investment planning and execution and the capacity to expeditiously absorb related EU funding. The authorities acknowledged that meeting the 2009 budget targets on accelerated use of EU funds would be particularly challenging, in part due to the decentralized set-up of EU-funded programs within Slovakia. Noting the government's recent plans for Public-Private Partnerships (PPPs) for major road projects, staff and the authorities agreed that these initiatives should be accompanied by efforts to put in place a proper legal framework and establish arrangements for effectively monitoring and reporting related risks and contingent liabilities.

C. Financial Sector

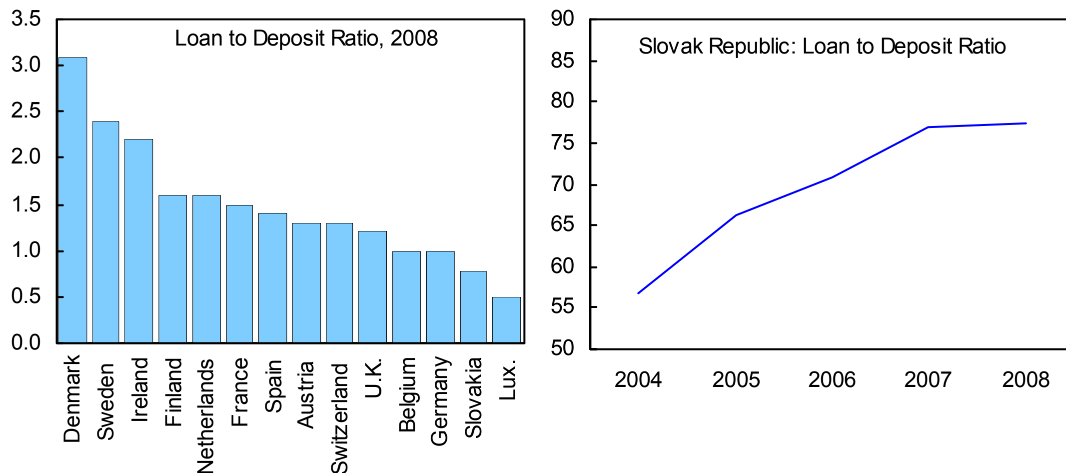
17. **Despite strong credit growth in recent years, credit to the private sector remains moderate and the financial system concentrated on traditional domestic banking activities.** Credit growth has been largely financed by rapid growth in domestic retail sources, and the loan-deposit ratio is around 0.8. Furthermore, bank lending has focused on the domestic private sector. Banks have no significant exposure to sub-prime lending, "toxic" structured products or exchange rate risks, have been resilient to adverse developments in parent banks, and are not dependent on deposits and loans from non-affiliated banks. Despite the growth of the system, concentration among commercial banks remains relatively high as three foreign owned banks dominate the market with a combined market share of around 60 percent of total assets.

18. **The euro adoption on January 1, 2009, went smoothly**. However, costs associated with the transition, and lost revenue from eliminated foreign exchange operations have reduced profitability. The transition to the euro also reversed speculative inflows in the running up to the adoption: foreign investor positions were unwound and deposits at the central bank dropped at end-2008.



Sources: IFS, and IMF staff estimates.

19. **Slovakia's banks have so far withstood the global crisis relatively well.** They are currently well capitalized, liquid, and properly provisioned owing to prudent regulation. The level of nonperforming loans is still low, albeit rising. In addition, the banking sector has been supported by a set of financial measures which the authorities pro-actively introduced when the global crisis hit Europe (Box 3).



Source: National Bank of Slovakia, IMF International Financial Statistics.

20. **Nonetheless, the financial sector is increasingly affected by the global crisis.** Although banks remained profitable, profits declined by 40 percent in January-May compared with the previous year. The share of non performing loans, albeit still relatively low, increased to around 4 percent in April 2009, and loan delinquency rates are on the rise. More importantly, the stress on banks is projected to intensify in the coming months as the impact of the recession deepens and more borrowers face financial difficulties.

Box 3. Financial Measures in Response to the Crisis

- Unlimited guarantee for all deposits by individuals and small enterprises until end-2010.[1]
- Support for small and medium-sized enterprises through state loan guarantees and higher loan volumes.
- Allowing more flexibility in restructuring retail loans including mortgages.
- Raising the capital of state-owned Exim Banka and of the Slovak Guarantee and Development Bank by €41.4 and €32 million, respectively, to strengthen support for export-oriented industries.
- Bank supervisors have stepped up the frequency and scope of their monitoring, including daily monitoring of banks' adherence to regulations regarding foreign banks' exposure to parent banks;[2] third party exposure of banks to problem banks and assets abroad, and liquidity indicators.
- A Standing Committee, launched in early 2008, comprising representatives of the Finance Ministry and the National Bank, has been meeting frequently (twice a month in 2008, once a month now) to discuss forward looking hypothetical scenarios and responses.
- The central bank has been dealing with cross-border supervisory arrangements and home-host country issues in the context of regular meetings of supervisory colleges.
- Legislation on banking sector stability is expected to come into force in 2009[3] establishing several forms of the state support to the real economy and the banking system on a precautionary basis. This legislation would allow the government to guarantee bank bonds, and inject capital in banks.

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[1] As at February 28, 2009, deposits covered by the deposit guarantee scheme are estimated at some €24 billion (63 percent of total deposits from non-banks).

[2] Under European regulations, foreign bank subsidiaries can only have an exposure to the parent bank of 20 percent of own funds.

[3] This legislation will lapse after 1½ years.

21. **Banks and the National Bank of Slovakia (NBS) appear well-positioned for further strains.** Banks have tightened lending requirements, while reducing the maturity of new loans and raising interest rates. In consultation with foreign owners, banks also reduced dividend payments and augmented capital, and sharply raised provisions. Exposure to foreign owner risk is mitigated by owners' clear commitment to stay fully engaged, limited reliance

on parent bank funding, and increased NBS monitoring of liquidity indicators and cross-border and third party exposures.[2] The supervisory and regulatory framework has been further improved, and the supervisor is appropriately proactive. While reassured, staff underlined that it was essential to remain vigilant and further strengthen the monitoring of credit risk. Staff also cautioned that the unlimited deposit guarantee, which had helped sustain deposit growth in the current difficult environment, in due course would have to be reconsidered, in line with EU-wide initiatives.

22. **The NBS has conducted stress tests under different scenarios that reflect the weakening of economic conditions.** The most pessimistic scenario assumes a particularly severe output contraction—which is currently not envisaged—combined with a surge in unemployment and jump in default rates. The stress test results, based on end-2008 bank balance sheets, suggest that it would take a highly unlikely further pronounced deterioration in the economic environment to push capital positions into danger zones. Capital adequacy ratios appear to be resilient to household risk and market (interest rate) risk in particular. The results also indicate that banks would be able to maintain adequate liquidity even after particularly severe shocks.

D. Structural Issues

23. **Wage growth in line with productivity gains has helped maintain competitiveness.** The real effective exchange rate has appreciated considerably since 2002 in CPI terms, but much less so in unit labor cost (ULC) terms. More importantly, relative profitability in the Slovak manufacturing sector vis-à-vis trading partners improved significantly over the past several years, and its market share in the world increased rapidly in recent years, outpacing that of neighboring countries.

24. **Additional measures of competitiveness suggest that Slovakia remains competitive.** The macroeconomic balance approach—which uses a normative approach—suggests that Slovakia's saving-investment balance is consistent with medium-term economic fundamentals. Likewise, the external sustainability approach, which calculates the saving-investment balance needed to maintain net foreign assets at their current level, implies that Slovakia is competitive. However, to that the extent that recent sharp currency depreciations in some neighboring countries are not reversed or not undone by higher inflation, Slovakia will have to make additional efforts to maintain its competitiveness edge.

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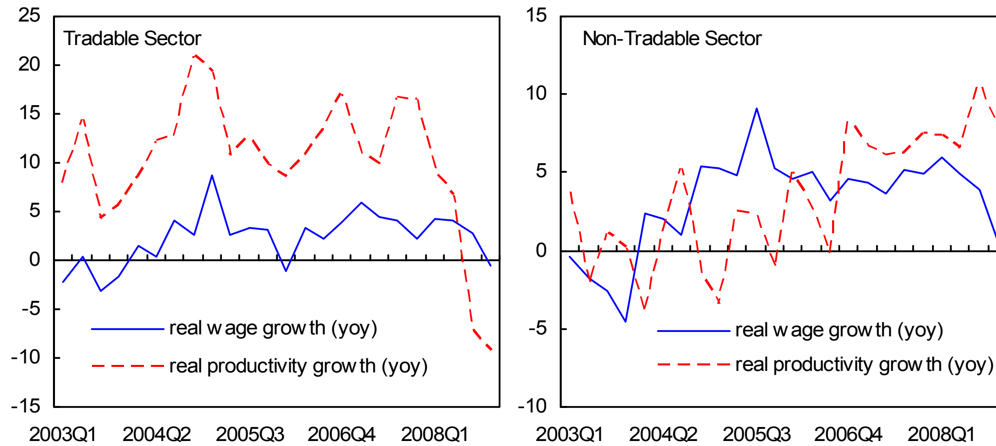
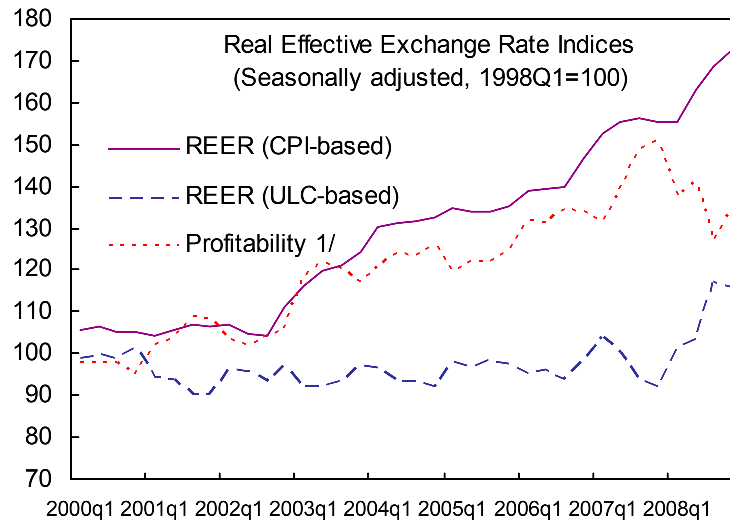
[2] In the event of a parent bank bankruptcy, the Slovak subsidiary would be considered a separate legal entity and its assets would not be considered part of the parent banks'.

Slovak Republic: Wage and Productivity Growth, 2003-2008





Source: Eurostat; International Financial Statistics; and IMF staff calculations.

1/ Unit labor costs in trading partner countries relative to those in Slovakia, adjusted for manufacturing producer price inflation—a rough indicator of developments in relative profitability.

25. **Looking ahead, staff emphasized that successful performance in the euro zone would require sustained efforts to enhance productivity**. Slovak inflation is projected to continue outpacing the euro zone average. As far as this differential is a symptom of underlying, productivity-driven convergence it is an equilibrium phenomenon. However, real exchange rate developments will need to be carefully monitored from this point of view, and further productivity gains relative to the rest of the euro zone will be essential to maintaining competitiveness. Although various measures of business conditions indicate that Slovakia is still outperforming its neighbors, the gap has narrowed in recent years. In this regard, labor market flexibility and education, especially at the post-secondary and vocational levels, stand

out as areas of concern. In a monetary union, enhanced labor market flexibility also will help improve the economy's capacity to respond to shocks.

III. Staff Appraisal

26. **Strong economic fundamentals, prudent macroeconomic policies, and a sound financial sector have boosted growth and helped pave the way for successful euro adoption.** The 2004–08 growth acceleration did not instigate domestic or external imbalances or unsustainable dynamics. While GDP per capita rose significantly and unemployment fell sharply, external and public debt remained low, and the current account deficit and inflation declined.

27. **However, Slovakia is highly influenced by external economic developments, and the economy is projected to shrink by near 5 percent this year.** The downturn is putting severe pressure on government revenue and is beginning to impact bank asset quality. Systemic vulnerabilities remain limited, however, and projected increases in external and public debts do not reflect structural imbalances or raise sustainability concerns.

28. **Fiscal policy is appropriately accommodating in 2009.** Reflecting the revenue shortfall, the general government deficit will widen to around 5 percent of GDP. Combined with stimulus of about 1 percent of GDP as a result of some reallocation of expenditure towards items with a higher multiplier and accelerated utilization of EU transfers, this would provide an appropriate counter-cyclical fiscal response and would not raise concerns involving funding or investor confidence.

29. **Without policy adjustments, the budget deficit will remain worrisomely high in 2010 and beyond.** The 2004–08 growth acceleration and related revenue boom have translated into expenditure growth that, if maintained over the medium term, could result in persistent deficits in excess of the Maastricht ceiling and loss of investor confidence.

30. **Anchoring the short-term fiscal response to the downturn within a credible medium-term consolidation strategy therefore will be key.** A fiscal strategy aimed at bringing down the deficit to about 4 percent of GDP next year and to below 3 percent of GDP by 2011 would offer a proper balance between facilitating full recovery and establishing the consolidation's credibility.

31. **To achieve the recommended deficit trajectory, sustained efforts to further cut costs, improve the quality of spending, and ensure adequate revenues will be essential.** The expenditure dynamics in health care is of particular concern, and needs to be addressed through structural reforms in line with IMF advice. With the scope for savings from further expenditure rationalization limited, higher taxation of income likely will be needed.

32. **The consolidation strategy should be supported by fiscal institutional reforms and enhanced fiscal transparency.** The medium-term expenditure framework incorporated

in Slovakia's three-year rolling budget should be strengthened to better align the annual budget process with underlying spending priorities. Investment planning and the capacity to accelerate the absorption of EU funds also need to be improved. And fiscal risks and contingent liabilities associated with PPPs should be properly monitored and disclosed.

33. **Banks appear to be overall well-positioned to cope with the downturn.** The recession and permanent reduction in revenue from foreign exchange transactions is putting severe pressures on the sector. Facing an inevitable further deterioration in asset quality, banks have appropriately responded by tightening lending standards, limiting dividend payouts and raising new capital. Maintaining adequate profitability while avoiding excessive risk taking will continue to be a challenge.

34. **The National Bank's proactive supervision is commendable.** Recent measures to strengthen bank monitoring and cross-border coordination have been well received by the banking sector and have helped shore up confidence and stability. While the results of recent stress tests are reassuring, continued vigilance by both the NBS and the banks and sustained efforts to strengthen risk monitoring and management will be essential.

35. **Productivity-enhancing structural reforms, wage discipline, and labor market flexibility should remain policy priorities.** To boost productivity, the government should continue to improve the business environment and place special focus on strengthening the education system. The recently reached tri-partite agreement to maintain real wage growth in line with productivity growth in 2009 will help maintain competitiveness, and similar arrangements should be envisaged for the coming years.

36. **It is recommended that Slovakia remain on a 12-month consultation cycle**.

Table 1. Slovak Republic: Summary of Economic Indicators, 2006-2014

				Projections					
	2006	2007	2008	2009	2010	2011	2012	2013	2014
	(Annual percentage change, constant prices, unless noted otherwise)								
Real GDP	8.5	10.4	6.4	-4.7	1.9	5.2	4.4	4.3	4.2
Domestic demand	6.1	5.8	6.6	-1.5	2.7	5.0	4.1	3.9	4.0
Public consumption	10.2	-1.3	4.3	4.1	2.7	2.2	1.0	0.7	1.6
Private consumption	5.9	7.1	6.1	0.2	3.0	5.5	4.8	4.5	4.5
Gross capital formation	4.1	8.1	9.1	-8.0	2.0	6.1	4.9	4.6	4.6
Net exports	3.3	4.9	-0.1	-3.0	-1.0	0.2	0.3	0.5	0.2
Exports of goods and services	21.0	13.8	3.2	-16.0	-1.3	8.8	8.0	6.7	6.2
Imports of goods and services	17.7	8.9	3.3	-13.0	-0.3	8.6	7.7	6.1	6.0
Prices									
Inflation (CPI)	4.5	2.8	4.6	2.3	2.9	3.1	2.5	2.5	2.5
Inflation (CPI, end of period)	3.7	3.2	4.4	3.9	3.8	3.1	3.1	3.1	3.1
Core inflation (end of period) 1/	1.5	2.1	2.0	2.0	2.0	2.0	2.0	2.0	2.0
Inflation (GDP deflator)	2.9	1.1	3.4	1.8	2.4	2.7	2.5	2.5	2.5
Employment and wages									
Employment (ESA95)	2.3	2.1	2.8	-2.4	0.1	0.8	0.6	0.5	0.5
Nominal wages	8.0	7.2	8.1	2.7	4.8	7.0	6.3	6.0	6.0
Productivity	6.1	8.1	3.5	-2.3	1.8	4.4	3.7	3.8	3.7
Real wages	3.3	4.3	3.4	0.4	1.8	3.8	3.7	3.4	3.4
Unit labor costs	1.8	-0.9	4.4	5.1	3.0	2.5	2.5	2.1	2.2
Unemployment rate (percent)	13.3	11.0	9.6	12.4	12.5	12.1	11.7	11.5	11.2
				(In percent of GDP)					
Public Finance									
General government balance	-3.5	-1.9	-2.5	-5.2	-4.5	-3.0	-2.4	-1.4	-0.7
Primary balance	-2.1	-0.6	-1.3	-3.7	-3.2	-1.6	-1.0	0.0	0.7
Primary expenditure	36.5	35.3	36.0	39.2	39.1	37.2	36.5	35.3	34.4
General government debt	30.4	29.4	27.6	33.7	36.7	37.0	37.0	36.0	34.4
Monetary and financial indicators									
Credit to private sector	39.6	43.4	45.7						
Lending rates 2/	8.0	8.3	8.4						
Deposit rates 3/	2.2	2.4	2.5						
Government bond yield	4.2	4.6	4.7						
				(In percent of GDP)					
Balance of payments									
Trade balance	-4.6	-1.2	-0.7	-1.3	-1.0	-0.8	-0.6	-0.3	-0.1
Current account balance	-7.0	-5.4	-6.5	-6.5	-5.9	-5.5	-4.9	-4.4	-3.7
Gross official reserves (US$ millions)	13,364	18,964	20,257	17,460	17,673	19,763	21,980	24,348	25,654
Gross external debt	54.7	52.0	50.3	50.3	49.8	48.9	48.1	47.3	46.4

Sources: National Authorities; and IMF staff calculations.

1/ Headline inflation minus the change in regulated prices.
2/ Average of interest rates on new loans to households and nonfinancial corporations.
3/ Average of interest rates on deposits from households and nonfinancial corporations.

Table 2. Slovak Republic: Fiscal Operations of the Consolidated General Government, 2006-11
Under the Scenario Suggested by Staff
(In percent of GDP)

				Projections		
	2006	2007	2008	2009	2010	2011
Total revenue	35.5	36.0	35.9	36.7	37.1	36.9
Tax revenue	17.1	17.2	16.5	16.5	16.5	16.5
Personal income tax	2.5	2.6	2.7	2.6	2.6	2.6
Wage tax	2.2	2.3	2.4	2.4	2.3	2.3
Self-employment tax	0.3	0.3	0.3	0.3	0.3	0.3
Corporate profit tax	2.9	3.0	3.0	2.8	2.7	2.7
Withholding tax on capital income	0.3	0.3	0.3	0.3	0.3	0.3
VAT	7.5	6.8	6.9	7.0	6.9	7.0
Excises	2.9	3.5	2.7	2.8	3.0	3.0
Import duties, property tax and other	1.0	1.0	0.9	1.0	1.0	1.0
Social contributions	12.8	13.0	12.9	13.4	13.8	13.8
Grants and transfers	1.7	1.6	1.6	3.0	3.9	3.8
Of which: from European Union	1.3	1.4	1.4	2.9	3.8	3.7
Other revenue	3.9	4.2	4.8	3.8	2.9	2.7
Of which: interest	0.3	0.3	0.2	0.2	0.3	0.2
Total expenditure	37.9	36.7	37.3	40.7	40.4	38.6
Current expenditure	33.8	33.0	32.9	36.0	35.6	34.0
Gross wages	6.6	6.3	6.4	7.0	6.3	5.9
Wages	5.0	4.7	4.8	5.2	4.8	4.4
Employer social security contributions	1.7	1.6	1.6	1.8	1.5	1.4
Goods and services	5.6	5.4	5.6	5.2	5.5	5.4
Subsidies and transfers 1/	20.1	19.8	19.6	22.3	22.4	21.4
Agricultural subsidies	0.7	0.7	0.9	1.0	1.0	0.8
Transport subsidies	0.8	0.8	0.9	0.7	0.7	0.6
Health insurance companies	4.5	4.5	4.7	5.3	5.4	5.3
Sickness benefits	0.3	0.3	0.4	0.4	0.4	0.4
Old-age and disability pensions	6.9	6.8	6.7	7.6	7.7	7.4
Active labor market policies	0.2	0.2	0.2	0.2	0.2	0.2
Unemployment benefits	0.1	0.1	0.1	0.1	0.1	0.1
State benefits and social assistance	2.0	1.8	1.6	2.0	1.9	1.9
Social security contributions on behalf of certain groups	2.0	2.1	1.8	2.2	2.2	2.2
Transfers to the EU	0.9	0.8	0.8	1.0	0.9	0.8
Other subsidies and transfers	1.6	1.8	1.5	1.9	1.9	1.6
Interest	1.5	1.4	1.2	1.5	1.3	1.4
Capital spending	4.1	3.7	4.4	4.7	4.8	4.6
Capital assets	2.3	2.3	2.3	2.2	1.9	1.9
Capital transfers	1.8	1.4	2.1	2.5	2.9	2.7
Revenue loss to the second pillar pensions	1.1	1.3	1.2	1.1	1.2	1.2
Fiscal balance	**-3.5**	**-1.9**	**-2.5**	**-5.2**	**-4.5**	**-3.0**
Memorandum items:						
Deficit excluding second pillar pension costs	-2.4	-0.7	-1.3	-4.0	-3.3	-1.8
Public debt, ESA 95 basis	30.4	29.4	27.6	33.7	36.7	37.0

Sources: Ministry of Finance; and IMF staff estimates and projections.

1/Table assumes that, in order to bring down the deficit during 2009-11 to the level it proposes, all necessary adjustment will take place on agricultural subsidies, transport subsidies, and other subsidies and tranfers.

Table 3. Slovak Republic: Medium-term Balance of Payments, 2005-14
(In millions of U.S. dollars, unless otherwise indicated)

					Projections					
	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Current account balance	-4,090	-3,951	-4,071	-6,189	-5,573	-5,264	-5,268	-5,040	-4,810	-4,366
Trade balance	-2,450	-2,563	-929	-679	-1,125	-924	-737	-607	-303	-176
Exports, f.o.b.	32,026	41,723	57,815	70,191	54,271	53,265	59,697	64,992	69,789	74,375
Imports, f.o.b.	-34,476	-44,287	-58,744	-70,870	-55,396	-54,189	-60,433	-65,599	-70,092	-74,552
Services balance	320	755	541	-146	172	230	139	173	241	307
Receipts	4,407	5,404	6,871	8,125	7,608	7,792	8,370	8,905	9,455	10,020
Payments	-4,087	-4,649	-6,329	-8,271	-7,436	-7,562	-8,231	-8,732	-9,214	-9,712
Income balance	-1,976	-2,088	-3,227	-4,365	-4,439	-4,725	-5,238	-5,232	-5,393	-5,163
Receipts	1,620	1,955	2,373	2,536	2,194	2,233	2,239	2,643	2,929	3,087
Payments	-3,597	-4,043	-5,600	-6,901	-6,633	-6,958	-7,477	-7,875	-8,322	-8,251
Of which: Interest	-413	-545	-787	-790	-764	-939	-933	-954	-1,017	-469
Current transfers	15	-55	-456	-999	-181	156	568	625	646	667
Official	210	279	377	-107	765	1,130	1,600	1,720	1,806	1,896
Private	-195	-334	-834	-892	-946	-974	-1,032	-1,094	-1,160	-1,230
Capital and financial account balance	5,161	1,036	9,672	7,482	2,776	5,477	7,358	7,257	7,178	5,672
Capital account	-18	-41	422	435	489	547	594	644	697	755
Direct foreign investment	1,951	3,797	2,387	3,174	500	950	2,585	1,160	1,184	1,213
Reinvested earnings	1,219	801	1,074	1,986	200	350	383	406	428	457
Portfolio investment	-982	1,561	1,871	2,086	1,897	1,902	1,914	1,929	1,944	1,953
Other investment	4,245	-4,119	4,992	1,787	-111	2,078	2,266	3,524	3,353	1,751
Short-term	5,258	-4,747	4,309	1,133	-818	1,321	1,482	2,712	2,510	877
Long-term	-1,014	628	684	654	706	757	784	812	843	874
Reserve assets 1/	-568	2,116	-5,600	-1,293	2,797	-213	-2,091	-2216	-2368	-1306
Errors and omissions	-503	800	...	...	...	...	...	...	...	...
Overall balance	568	-2,116	5,600	1,293	-2,797	213	2091	2216	2368	1306
Financing	-568	2,116	-5,600	-1,293	2,797	-213	-2091	-2216	-2368	-1306
Gross reserves (negative indicates increase)	-568	2,116	-5,600	-1,293	2,797	-213	-2091	-2216	-2368	-1306
Memorandum items:	(In percent of GDP, unless otherwise indicated)									
Current account balance	-8.5	-7.0	-5.4	-6.5	-6.5	-5.9	-5.5	-4.9	-4.4	-3.7
Trade balance	-5.1	-4.6	-1.2	-0.7	-1.3	-1.0	-0.8	-0.6	-0.3	-0.1
Merchandise export volume (percent change)	13.7	21.7	15.0	2.8	-17.7	-1.6	12.1	8.9	7.4	6.6
Value (percent change)	15.9	30.3	38.6	21.4	-22.7	-1.9	12.1	8.9	7.4	6.6
Merchandise import volume (percent change)	15.5	16.1	8.8	0.5	-14.7	-2.3	11.2	8.3	6.6	6.1
Terms of trade (percent change from previous year)	-0.3	-1.4	-1.1	-1.6	2.5	0.3	0.0	0.0	0.0	0.0
Service balance	0.7	1.3	0.7	-0.2	0.2	0.3	0.1	0.2	0.2	0.3
Income balance	-4.1	-3.7	-4.3	-4.6	-5.2	-5.3	-5.4	-5.1	-4.9	-4.4
Current transfers	0.0	-0.1	-0.8	-1.5	-0.3	0.2	0.8	0.8	0.8	0.7
Total external debt	59.3	54.7	52.0	50.3	50.3	49.8	48.9	48.1	47.3	46.4
Short-term external debt (original maturity basis)	15,202	15,556	20,781	20,944	22,142	20,725	21,492	22,213	22,884	23,548
(in percent of GDP)	33.3	26.4	26.0	23.6	25.9	23.3	22.3	21.5	20.7	20.0
Short-term external debt (remaining maturity basis)	16,658	17,129	24,666	21,128	23,013	22,673	23,592	24,420	25,146	25,861
(in percent of GDP)	36.5	29.1	30.9	23.8	27.0	25.5	24.5	23.7	22.8	21.9
Reserves/short-term debt (percent, remaining maturity basis)	92.9	78.0	76.9	95.9	75.9	77.9	83.8	90.0	96.8	99.2
Reserves/broad money (percent)	58.5	41.3	45.0	37.6	36.3	35.4	36.6	38.0	39.2	38.7
External debt service/Exports of goods and services (percent)	11.7	4.7	3.8	3.4	4.2	4.8	4.4	4.2	4.1	3.3
GDP (US$ millions)	47,885	56,046	74,988	95,739	85,511	88,894	96,112	103,037	110,394	117,920

Sources: National Bank of Slovakia; and IMF staff estimates.

1/ Does not include the transfer of reserve assets from the NBS to the ECB which took place in 2009.

Table 4. Slovak Republic: Financial Soundness Indicators for the Banking Sector, 2004-09

(In percent, unless otherwise indicated)

	2004	2005	2006	2007	End-Sep 2008	2008	End-Mar 2009
Capital Adequacy							
Regulatory capital to risk-weighted assets	18.7	14.8	13.0	12.8	11.3	11.1	11.6
Regulatory Tier I capital to risk-weighted assets	18.9	15.0	13.2	12.3	11.1	10.7	11.2
Asset Composition and Quality							
Nonperforming loans to gross loans 1/	2.6	5.0	3.2	2.5	2.9	3.2	3.6
Nonperforming loans net of provisions to capital	3.1	6.4	7.9	8.0	8.2	8.8	10.1
Sectoral distribution of outstanding loans (in percent of total loans)							
Individuals	26.7	30.3	30.2	31.8	36.2	36.8	37.3
Government	8.3	5.0	2.5	4.9	4.0	4.3	3.9
Agriculture	1.6	1.6	1.3	1.1	1.7	1.3	1.4
Manufacturing	15.8	14.6	11.1	14.3	10.9	10.9	10.7
Construction	1.6	2.2	2.5	2.5	2.9	2.9	2.9
Wholesale and retail trade	13.5	13.0	11.9	12.5	13.7	13.2	13.0
Transportation	5.1	3.9	4.7	4.0	4.8	4.8	5.1
Financial services	8.7	10.3	18.3	14.8	7.0	6.7	6.0
Other	18.7	19.1	17.3	14.2	18.8	19.2	19.7
Earnings and Profitability							
Return on assets (after tax)	1.2	1.2	1.3	1.0	0.9	0.9	0.2
Return on equity (after tax)	11.9	16.9	16.6	16.6	14.6	13.8	2.8
Interest margin to gross income	73.3	65.4	66.4	70.5	67.8	69.3	74.1
Noninterest expenses to gross income	61.2	69.1	58.3	59.2	52.7	55.1	58.8
Liquidity							
Liquid assets to total assets 2/	13.3	33.5	36.5	30.7	29.7	29.3	18.3
Liquid assets to short term liabilities	40.3	40.3	45.6	36.6	36.6	36.3	23.3
Foreign Exchange Risk							
Net open positions in foreign exchange to capital (on balance sheet)	-80.0	-14.4	-1.2	-131.8	-111.3	-70.2	9.0
Net open positions in foreign exchange to capital (off balance sheet)	40.0	-24.2	44.2	102.3	44.9	11.3	-4.8
Foreign currency-denominated loans (percent of total loans)	22.8	28.2	27.1	23.6	21.5	21.9	2.2
Foreign currency-denominated liabilities (percent of total liabilities)	19.3	28.0	22.3	14.5	22.9	20.0	2.7
Other indicators							
Customer deposits to total (non-interbank) loans	166.4	136.3	130.2	118.4	…	119.6	…
Private sector credit growth	7.2	86.7	-17.3	22.3	…	15.3	…
Private sector credit (percent of GDP)	31.3	53.5	39.6	43.4	…	45.7	…
Real estate price growth	15.5	-10.3	16.8	23.9	…	22.0	…
Lending rates 3/	8.6	7.3	8.0	8.3	…	8.4	…
Deposit rates 4/	2.5	1.5	2.2	2.4	…	2.5	…
Loan to deposit ratio (non-interbank)	56.8	66.3	70.8	77.0	…	77.3	…
Loan to deposit ratio	88.7	113.4	99.4	108.0	…	114.5	…

Source: National Bank of Slovakia.

1/ A decline in the NPL ratio in 2006 is partly due to a change in the methodology for calculating NPLs.
2/ In 2006, liquid assets include government bonds in holding-to-maturity portfolio.
3/ Average of interest rates on new loans to households and nonfinancial corporations.
4/ Average of interest rates on deposits from households and nonfinancial corporations.

Table 5. Slovak Republic: Macroeconomic Framework, 2005-14

					Projections					
	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
					(In percent of nominal GDP)					
Consumption	75.6	75.4	72.7	73.7	77.5	78.3	78.0	77.7	77.3	77.0
Nongovernment	55.6	55.5	53.5	53.9	55.9	56.5	56.9	57.2	57.5	57.7
Government	20.0	19.8	19.2	19.8	21.6	21.8	21.2	20.5	19.8	19.3
Gross capital formation	28.9	27.8	27.8	28.8	27.8	27.8	28.1	28.2	28.3	28.4
Nongovernment	26.5	25.5	25.5	26.5	25.6	25.9	26.2	26.3	26.4	26.5
Government	2.4	2.3	2.3	2.3	2.2	1.9	1.9	1.9	1.9	1.9
Fixed investment	26.5	26.5	26.1	25.9	26.2	26.2	26.4	26.6	26.6	26.7
Foreign saving 1/	8.5	7.1	5.4	6.5	5.7	5.0	4.5	3.9	3.5	3.0
Gross national saving	20.3	21.2	22.4	22.3	21.3	21.9	22.6	23.3	23.9	24.7
Nongovernment	21.0	23.1	22.7	23.2	26.2	28.2	28.2	28.4	28.1	28.1
Of which: Households	3.5	2.3	3.4	4.0	3.9	4.2	4.2	3.9	3.6	3.3
Government	-0.7	-1.7	-0.3	-0.8	-4.9	-6.3	-5.6	-5.1	-4.2	-3.5
Households' gross saving (percent of disposable income)	5.8	3.9	5.8	6.7	5.2	4.3	3.8	2.1	2.5	2.6
General government balance (ESA-95 basis) 2/	-2.8	-3.7	-2.2	-2.3	-2.1	-0.8	0.0	0.0	0.0	0.0
					(Percentage change in real term)					
GDP	6.5	8.5	10.4	6.4	-4.7	1.9	5.2	4.4	4.3	4.2
GDP, excluding the impact of tobacco stock piling	…	…	9.3	0.0	0.0	0.0	0.0	7.8	-2.7	1.9
Households' disposable income	6.6	3.8	9.2	7.2	-1.4	2.0	5.0	3.0	5.0	4.6
Domestic demand	8.6	6.1	5.8	6.6	-1.5	2.7	5.0	4.1	3.9	4.0
Consumption	5.7	6.9	4.9	5.6	1.2	2.9	4.7	3.9	3.6	3.8
Nongovernment	6.6	5.9	7.1	6.1	0.2	3.0	5.5	4.8	4.5	4.5
Government	3.3	10.2	-1.3	4.3	4.1	2.7	2.2	1.0	0.7	1.6
Gross capital formation	16.6	4.1	8.1	9.1	-8.0	2.0	6.1	4.9	4.6	4.6
Nongovernment 2/	17.5	5.2	8.1	9.4	-7.9	2.8	6.1	4.9	4.6	4.6
Government	3.9	-12.5	7.7	4.4	-10.4	-12.5	5.4	4.4	4.3	4.2
Fixed investment	17.6	9.3	8.7	6.8	-3.7	2.0	6.0	4.8	4.5	4.5
Change in stocks (Sk billion, constant prices)	23.9	13.1	20.5	27.9	9.0	9.0	9.0	9.0	9.0	9.0
Change in stocks (contribution to GDP growth)	0.0	-0.9	0.6	0.5	-1.2	0.0	0.0	0.0	0.0	0.0
Exports of goods and non-factor services	10.0	21.0	13.8	3.2	-16.0	-1.3	8.8	8.0	6.7	6.2
Imports of goods and non-factor services	12.4	17.7	8.9	3.3	-13.0	-0.3	8.6	7.7	6.1	6.0
					(Percentage change)					
Memorandum item:										
Inflation (CPI, period average)	2.7	4.5	2.8	4.6	2.3	2.9	3.1	2.5	2.5	2.5
Inflation (HICP, period average)	2.8	4.3	1.9	3.9	1.7	2.3	2.7	2.3	2.3	2.3
Inflation (HICP, end of period)	3.9	3.7	2.5	3.5	2.0	2.3	2.7	2.3	2.3	2.3
GDP deflator	2.4	2.9	1.1	3.4	1.8	2.4	2.7	2.5	2.5	2.5
Employment (ESA95)	1.4	2.3	2.1	2.8	-2.4	0.1	0.8	0.6	0.5	0.5
Nominal wages	9.2	8.0	7.2	8.1	2.7	4.8	7.0	6.3	6.0	6.0
Real wages	5.1	6.1	8.1	3.5	-2.3	1.8	4.4	3.7	3.8	3.7
Productivity 3/	6.3	3.3	4.3	3.4	0.4	1.8	3.8	3.7	3.4	3.4
Unit labor costs	3.9	1.8	-0.9	4.4	5.1	3.0	2.5	2.5	2.1	2.2
Unemployment rate (percent, annual average) 4/	16.2	13.3	11.0	9.6	12.4	12.5	12.1	11.7	11.5	11.2
Gross domestic product (Sk billion, current prices)	1,486	1,659	1,853	2,028	1,969	2,053	2,218	2,373	2,537	2,710
Export deflator (percent change)	8.0	11.8	10.0	15.9	1.7	-0.3	0.0	0.0	0.4	0.3
Import deflator (percent change)	9.9	10.6	9.8	19.7	2.1	0.1	0.3	0.3	0.6	0.3
Exchange rate (Skk per euro, period average)	37.8	34.6	33.7	30.1	30.1	30.1	30.1	30.1	30.1	30.1

Sources: Statistical Office of the Slovak Republic; and IMF staff estimates and projections.

1/ Negative of current account balance. For historical periods, foreign saving implied by national accounts data differs from the current account deficit reported in BOP statistics. The discrepancy is mainly due to different exchange rates employed in the calculations.

2/ After 2005, including second pension pillar costs.

3/ Employment on ESA 95 methodology and real GDP are used.

4/ Labor Force Survey.

INTERNATIONAL MONETARY FUND

SLOVAK REPUBLIC

Staff Report for the 2009 Article IV Consultation—Informational Annex

Prepared by the European Department

July 2, 2009

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Appendix I. Slovak Republic: Fund Relations

(As of May 31, 2009)

I. **Membership Status:** Joined: 01/01/1993; Article VIII

II. **General Resources Account:**

	SDR Million	Percent of Quota
Quota	357.50	100.00
Fund Holdings of Currency	311.50	87.13
Reserve Position	46.00	12.87

III. **SDR Department:**

	SDR Million	Percent of Allocation
Holdings	1.07	N/A

IV. **Outstanding Purchases and Loans:** None

V. **Financial Arrangements:**

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-by	07/22/1994	03/21/1996	115.80	32.15

VI. **Projected Obligations to Fund:** None

VII. **Exchange Rate Arrangement:**

The currency of the Slovak Republic is the euro, which was adopted on January 1, 2009.

The Slovak Republic has accepted the obligations of Article VIII and maintains an exchange system that is free of restrictions on the making of payments and transfers for current international transactions. The Slovak Republic maintains exchange restrictions for security reasons, based on UN Security Council Resolutions and Council of the European Union Regulations, that have been notified to the Fund for approval under the procedures set forth in Executive Board Decision No. 144–(52/51).

VIII. **Article IV Consultation:**

The consultation discussions were held in Bratislava during May 12–25, 2009. The mission met with Minister of Finance Počiatek, National Bank of Slovakia (NBS) Governor Šramko, Minister of Economy Jahnátek, other senior government and NBS officials, and representatives of financial institutions, think tanks, trade unions and employers' associations.

The mission comprised Messrs. De Broeck (head), Konuki, Ms. Banerji, and Mr. Mehrez (all EUR). Mr. Jakoby (Advisor to the Executive Director for Slovakia) participated in the discussions.

The mission's concluding statement was published on the IMF website on June 16, 2009. The authorities have agreed to the publication of the staff report.

The previous consultation with the Slovak Republic was concluded on June 6, 2007 (IMF Country Report No. 07/226).

IX. **FSAP Participation and ROSCs:**

An FSAP was concluded with the completion of the 2002 Article IV consultation on August 7, 2002 on the basis of missions that took place in February 2002 and April 2002. The FSSA report was published (IMF Country Report No. 02/198). An FSAP update mission was held in December 2006. The FSSA update report was circulated to the Executive Board together with the staff report for the 2007 Article IV Consultation and published on the IMF website on July 17, 2007.

The report on the Fiscal ROSC was issued in August 2002 (IMF Country Report No. 02/189) and updates were issued in August 2003 (IMF Country Report No. 03/236) and in March 2005 (IMF Country Report No. 05/73). The report on the Data ROSC was issued in May 2005 (IMF Country Report No. 05/161).

X. **Technical Assistance:** See the attached table.

XI. **Resident Representative Post:** None (closed at end-April 2004).

Slovak Republic: Technical Assistance, 2000–2007[1]

Department	Timing	Purpose
MFD	February 2000	Mission on pros and cons, and modalities of moving to an inflation targeting framework, operational issues (money markets and policy instruments), and dealing with potential problems posed by capital inflows for monetary operations
	December 2001	Long-term resident expert on banking supervision
	May 2002	Two missions on inflation modeling
FAD	April 2000	Tax administration
	February 2001	Tax administration (follow-up)
	April 2001	Public Finance Management (follow-up)
	August 2001	Tax administration: installation of resident expert to advise on establishment of Large Taxpayer Unit (LTU)
	August 2001–August 2002	Regular visits by FAD consultant on establishment of LTU
	December 2001	Tax administration follow-up, tax investigation/fraud issues
	June 2002	Mission to prepare Report on the Observance of Standards and Codes (ROSC), Fiscal Transparency Module
	February 2003	Tax policy
	March 2003	Tax administration
	May 2003	Expenditure policy
STA	February 2000	National accounts and price statistics
	March 2001	Multisector mission
	July 2003	Government finance statistics
	February–March 2004	Data ROSC Mission

[1]See Appendix I of IMF Country Report No. 05/71 for technical assistance during 1991–99.

Appendix II. Slovak Republic: Statistical Issues

1. Coverage, periodicity, and timeliness of data provided to the Fund are adequate for surveillance purposes. From the point of view of macroeconomic analysis and policy making, significant data improvements have been made in recent years, particularly in the national accounts. A data ROSC mission during February–March 2004 found that the integrity, methodological soundness, and reliability of the data were satisfactory, despite some shortcomings in the data revision policy. The main issues remaining are: (i) weaknesses in the data on prices and volumes of imports and exports; (ii) a lack of timely data on the general government operations; and (iii) slow compilation cycle of the annual national accounts and lack of proper benchmarking of quarterly data. The Slovak Republic subscribes to the Special Data Dissemination Standard (SDDS) since 1996 and observes or exceeds all related standards.

2. With regard to timeliness and public access, the authorities in general follow a free and open data publication policy. Data are promptly released to news services, and are also published regularly in various monthly and quarterly statistical publications, and on the Internet[2] according to a pre-announced schedule. Data on core surveillance variables are provided regularly to the Fund, and with minimal lags: a week or less for foreign exchange reserves; a day for monthly state budget implementation data; 10 days to a month for consumer prices, reserve money, broad money, and interest rates; two months for foreign trade data; and about three months for other fiscal, balance of payments, and national accounts data. However, the 2004 data ROSC mission reported some difficulties in fully reconciling the balance of payments with the national accounts, monetary, and government finance statistics.

Real Sector and Prices

3. Significant progress has been made in the compilation of the national accounts statistics. However, the quarterly national accounts data on expenditures exhibit weaknesses and there is a significant statistical discrepancy between the supply side and the demand side. An important outstanding issue is the compilation of reliable price deflators for imports and exports that would enable better decomposition into volume and price changes. The unit value trade price indices—on which the national accounts trade price deflators are based—are published with long delays and are not appropriately adjusted for quality changes. The statistical authorities are aware of these issues and improvements are pending.

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[2] Data are available on the website of the Slovak Statistics Office (www.statistics.sk), the National Bank of Slovakia (NBS) (www.nbs.sk), and the ministry of finance (MoF) (www.finance.gov.sk).

4. Following the fast development of chain stores, which are not fully captured in surveys, the authorities consider that retail sales and the level of consumption might be biased (especially if compared to VAT receipts), and wage statistics also might be biased.

5. In the enterprise sector, it would be very useful if the line ministries produced systematic accounts of the financial positions of the public enterprises under their purview.

Fiscal Sector

6. General government statistics are compiled annually in accordance with the methodology of the ESA95, and disseminated on the Ministry of Finance (MOF) website. In accordance with the EU *acquis communautaire,* the authorities report semi-annually on general government net lending/borrowing on ESA95 basis. Monthly reconciliation of government operations above and below-the-line is restricted to state budget transactions on a cash basis. A modern treasury system has been operating since January 2004. The new system has improved fiscal control and public debt management by allowing the recording of expenditures at the planning and commitment stages.

7. The MOF has converted its fiscal accounts to ESA95 standards. The MOF compiles Government Finance Statistics according to the *Government Finance Statistics Manual 2001* (*GFSM 2001*) analytical framework; data are available and disseminated on a cash basis for 1996–05, and on an accrual basis for 2003–08.

External Sector

8. External sector statistics are of good quality, and are reported on a timely basis to the Fund.

Monetary Sector

9. Monetary statistics are of good quality, and are reported on a timely basis to the Fund.

SLOVAK REPUBLIC: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE
(as of July 1, 2009)

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of Publication[6]	Memorandum Items:	
						Data Quality – Methodological soundness[7]	Data Quality – Accuracy and reliability[8]
Exchange Rates	07/01/09	07/01/09	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	06/24/09	06/26/09	W	W	W		
Reserve/Base Money	05/09	06/12/09	M	M	M	LO, LO, O, LO	O, O, O, O, O
Broad Money	05/09	06/09	M	M	M		
Central Bank Balance Sheet	05/09	06/12/09	M	M	M		
Consolidated Balance Sheet of the Banking System	04/09	06/09	M	M	M		
Interest Rates[2]	05/09	05/09	M	M	M		
Consumer Price Index	05/09	06/16/09	M	M	M	O, O, O, O	LO, O, LO, O, O
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	2008	04/2009	A	A	A	O, O, O, O	O, O, O, O, NA
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	06/09	07/01/09	M	M	M		
Stocks of Central Government and Central Government-Guaranteed Debt[5]	03/09	05/09	Q	Q	Q		
External Current Account Balance	03/09	06/30/09	M	M	M	O, O, LO, LO	O, O, O, O, O
Exports and Imports of Goods and Services	04/09	06/11/09	M	M	M		
GDP/GNP	Q1/09	06/03/09	Q	Q	Q	O, O, LO, LO	LO, O, LO, O, LO
Gross External Debt	03/09	06/30/09	M	M	M		
International Investment Position[9]	12/08	06/30/09	Q	Q	Q		

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A), Irregular (I); Not Available (NA).
[7] Reflects the assessment provided in the data ROSC (published on May 17, 2005, and based on the findings of the mission that took place during February 18–March 3, 2004) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O), largely observed (LO), largely not observed (LNO), or not observed (NO).
[8] Same as footnote 7, except referring to international standards concerning source data, statistical techniques, assessment and validation of source data, assessment and validation of intermediate data and statistical outputs, and revision studies.
[9] Includes external gross financial asset and liability positions vis a vis nonresidents.

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Public Information Notice

EXTERNAL
RELATIONS
DEPARTMENT

Public Information Notice (PIN) No. 09/90
FOR IMMEDIATE RELEASE
July 28, 2009

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2009 Article IV Consultation with the Slovak Republic

On July 20, 2009, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV Consultation with the Slovak Republic.[1]

Background

Following a period of rapid growth, economic activity tumbled in the first half of 2009 as a result of the global crisis. Strong economic fundamentals and a sound financial sector boosted economic growth in 2004–08, and shielded the economy from the global financial crisis until recently, while facilitating successful euro adoption at the beginning of 2009. However, the country is highly dependent on external economic developments, and the pronounced economic weakening in the euro area caused a sharp drop in output in the first quarter. The economy is projected to shrink by about 5 percent this year, and to return to growth on the order of 2 percent in 2010. Reflecting the broad economic downturn, the unemployment rate is projected to increase to more than 12 percent by end-2009, and remain high through 2010.
The fiscal position is weakening rapidly because of revenue underperformance. The shortfall in tax revenues and social security contributions deepened in the first half of the year, and is projected to reach about 2 percent of GDP for the year as a whole. Government spending, on the other hand, has been kept in line with budget plans. A package of stimulus measures was offset by reallocation and rationalization of spending elsewhere. Overall, the general government deficit is forecast to widen to about 5 percent of GDP, up from 2¼ percent in 2008.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

Slovakia's banks have so far withstood the global crisis relatively well. Reflecting the sector's focus on traditional domestic banking activities, banks have avoided sub-prime, structured products, and foreign currency denominated lending. They are currently well capitalized, liquid, properly provisioned and rely mainly on domestic retail deposits. Nonetheless, strains from the crisis are manifest: profits in the first half of 2009 are down sharply compared with the same period last year, and the share of non-performing loans is on the rise. Looking ahead, pressures on banks are expected to intensify in the second half of the year as an increasing number of borrowers will face financial difficulties.

Banks and the supervisor, the National Bank of Slovakia (NBS), have been preparing for further strains. Banks have tightened lending requirements, limited dividend payouts, raised capital and increased provisions. The supervisor pro-actively introduced a series of measures, including steps to safeguard domestic liquidity, when the global crisis hit Europe in the fall of 2008, and has stepped up the scope and frequency of bank monitoring. Cross-border supervisory coordination also has been strengthened.

Executive Board Assessment

Executive Directors noted that Slovakia's strong economic and policy fundamentals have contributed to rapid growth in recent years and successful euro adoption in the beginning of 2009. However, the global economic slump has led to a sharp contraction in the first quarter of the year and continues to deeply affect the Slovak economy. Directors agreed that the main challenge facing Slovak policymakers is to support domestic demand in the short run, while preserving and further strengthening the country's strong economic foundations over the medium term.

Directors considered fiscal policy to be appropriately accommodating in 2009. Freely operating automatic stabilizers and a contained stimulus package, financed by spending reallocations, will help support economic activity without hurting confidence. Directors welcomed the authorities' intention to accelerate the utilization of EU funds, and, in this context, underscored the importance of improving investment planning and implementation and absorption capacity. They also looked forward to the development of a proper legal, monitoring, and reporting framework to underpin the government's plans for Public-Private Partnerships.

Directors encouraged the authorities to formulate and announce a credible medium-term fiscal consolidation strategy, aimed at bringing down the general government deficit to within the Maastricht norm in a timely manner. They called on the authorities to move ahead with already identified consolidation measures, and observed that sustainable deficit reduction would require additional expenditure savings as well as revenue enhancing measures, including some tax increases. To preserve long-term sustainable public finances, they further recommended consideration of binding expenditure rules and moving forward with pension reform.

Directors noted with satisfaction that Slovakia's banks have withstood the global crisis relatively well. They commended the pro-active response by the supervisory authorities when the global crisis hit Europe, which has helped shore up confidence and stability. Continued vigilance will

nevertheless be required, along with sustained efforts to strengthen risk monitoring and management. In particular, loan losses are expected to intensify as the impact of the recession deepens. Directors were encouraged by results from recent stress tests showing that it would take very severe shocks to push capital and liquidity positions into danger zones.

Directors emphasized that external competitiveness will require sustained structural reforms and wage discipline. While standard indicators of competitiveness do not raise immediate concerns, continued close attention is warranted. Directors welcomed recent tripartite wage agreements aimed at keeping real wage growth in line with productivity growth. Such wage moderation will help Slovakia remain competitive, in combination with productivity-enhancing reforms. In this regard, Directors recommended further steps to improve the business environment and to strengthen education and human capital formation.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case. The staff report (use the free Adobe Acrobat Reader to view this pdf file) for the 2009 Article IV Consultation with the Slovak Republic is also available.

Slovak Republic: Summary of Economic Indicators, 2006-2011

				Projections		
	2006	**2007**	**2008**	**2009**	**2010**	**2011**
Real GDP	8.5	10.4	6.4	-4.7	1.9	5.2
Domestic demand	6.1	5.8	6.6	-1.5	2.7	5.0
Public consumption	10.2	-1.3	4.3	4.1	2.7	2.2
Private consumption	5.9	7.1	6.1	0.2	3.0	5.5
Gross capital formation	4.1	8.1	9.1	-8.0	2.0	6.1
Net exports						
Exports of goods and services	21.0	13.8	3.2	-16.0	-1.3	8.8
Imports of goods and services	17.7	8.9	3.3	-13.0	-0.3	8.6
Prices						
Inflation (CPI)	4.5	2.8	4.6	2.3	2.9	3.1
Inflation (CPI, end of period)	3.7	3.2	4.4	3.9	3.8	3.1
Core inflation (end of period) 1/	1.5	2.1	2.0	2.0	2.0	2.0
Inflation (GDP deflator)	2.9	1.1	3.4	1.8	2.4	2.7
Employment and wages						
Employment (ESA95)	2.3	2.1	2.8	-2.4	0.1	0.8
Nominal wages	8.0	7.2	8.1	2.7	4.8	7.0
Productivity	6.1	8.1	3.5	-2.3	1.8	4.4
Real wages	3.3	4.3	3.4	0.4	1.8	3.8
Unit labor costs	1.8	-0.9	4.4	5.1	3.0	2.5
Unemployment rate (percent)	13.3	11.0	9.6	12.4	12.5	12.1
			(In percent of GDP)			
Public Finance						
General government balance	-3.5	-1.9	-2.5	-5.2	-4.5	-3.0
Primary balance	-2.1	-0.6	-1.3	-3.7	-3.2	-1.6
Primary expenditure	36.5	35.3	36.0	39.2	39.1	37.2
General government debt	30.4	29.4	27.6	33.7	36.7	37.0
Monetary and financial indicators						
Credit to private sector	39.6	43.4	45.7			
Lending rates 2/	8.0	8.3	8.4			
Deposit rates 3/	2.2	2.4	2.5			
Government bond yield	4.2	4.6	4.7			
			(In percent of GDP)			
Balance of payments						
Trade balance	-4.6	-1.2	-0.7	-1.3	-1.0	-0.8
Current account balance	-7.0	-5.4	-6.5	-6.5	-5.9	-5.5
Gross external debt	54.7	52.0	50.3	50.3	49.8	48.9

Sources: National Authorities; and IMF staff calculations.
1/ Headline inflation minus the change in regulated prices.
2/ Average of interest rates on new loans to households and nonfinancial corporations.
3/ Average of interest rates on deposits from households and nonfinancial corporations.