

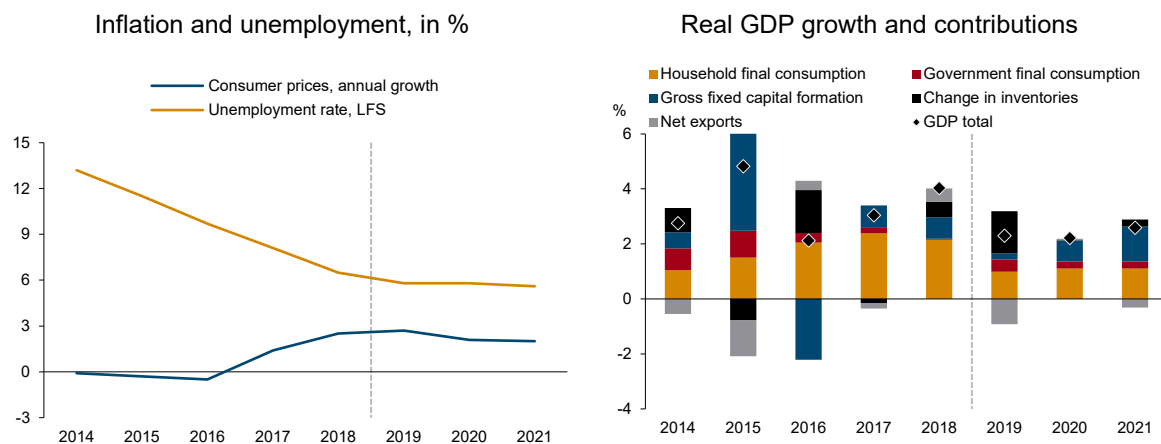


SLOVAKIA: Cooling due to external slowdown

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Slovakia's growth decelerated sharply in the second quarter of 2019 due to declining exports and investments. Growth in the key automotive industry turned negative in June. Growth will slow down in the coming years, with forecasts for this and next year amounting to 2.3% and 2.2%.

Figure 5.20 / Slovakia: Main macroeconomic indicators



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

Growth sharply decelerated in the second quarter. In the first half of 2019, Slovak GDP grew by 2.8%, compared to 4% for the whole year 2018. Overall, a strong decelerating trend became visible during the first half year: While in the first quarter of 2019, growth was robust and exhibited a y-o-y increase of 3.7%, the second quarter results came as a negative surprise when GDP grew by only 2%. While gross fixed capital formation and exports declined on the one hand, household consumption, government consumption and building up of stocks contributed to growth on the other.

Household consumption slightly recovered. In the first half of 2019, household consumption grew by 1.5%, markedly accelerating from the first to the second quarter from 1.1% to 1.9%. Still, this is very low taking into account the good situation on the labour market and the household saving rate rose further. Although employment growth slowed down in the second quarter, employment grew by 1.2% for the first half year. The employment rate now stands at 73%. The unemployment rate further declined and is now at a historical low level of 5.8%. Shortages of skilled labour persist but the tightness of the labour market started to ease as employers' expectations for employment growth (especially in manufacturing) went down recently.

Growing labour costs erode international competitiveness. In the second quarter of 2019, nominal wages edged up and rose by 9.7% - the strongest increase since the first quarter of 2008. For the first half year, nominal wages increased by 8.3%. As inflation reached 2.5% in that period, real wages were up by 5.8% and reached an average of EUR 1062 per month. As productivity increases were lagging behind wage increases, unit labour costs rose and steadily erode international cost competitiveness. High wage growth is driven by both shortages of skilled labour as well as government measures. State salaries went up markedly in both quarters; the minimum wage was raised by EUR 40 to EUR 520 in January 2019 (+8.33%) and will probably rise further to EUR 580 next year (+11.5%). In May, surcharges for night, weekend and holiday work rose for the second time; thirteenth salaries were paid out in the second quarter.

Investments declined significantly but stocks were built up. Investments declined by 1.2% in the first half of 2019 due to a strong fall in the second quarter. While gross fixed capital formation was still up by 2.1% in the first quarter, it fell by almost 4% in the second, also due to a strong base effect (the construction of Jaguar Land Rover plant was finished in the second quarter of last year). Construction output fell by 2.3% over the first seven months, also connected to problems in public motorway construction. Due to a strong built up of inventories, gross capital formation still rose by about 10% in the first half of 2019.

Industrial production is growing but the performance of the main automotive sector was disappointing. Regarding the sectoral structure of growth, industrial production increased by 4.6% in the first seven months of 2019. However, a major change in the growth pattern has become visible since June: The automotive industry – the key industrial sector in Slovakia – lost its main role as a growth driver and production has declined since then also due to a strong base effect. This came as a surprise as the new Jaguar Land Rover plant started production last October and should have provided a main growth impetus this year. Jaguar Land Rover plans to launch the second shift by the end of 2019 to order to produce 150,000 cars by then. Positive news also appeared when looking at the other main car manufacturers in Slovakia: PSA Peugeot Citroen showcased the electric Peugeot 208 model at the beginning of September, which it will only manufacture in Trnava. Overall, the company plans to produce 380,000 vehicles in 2019 (up from 350,000 in 2018). Kia Motors started the production of its new model, the Kia XCeed, at the beginning of August. Only VW Bratislava, which faces a loss of its small car segment (Škoda Citigo and Volkswagen UP!) at the end of 2021, has no assignment of a new car model thereafter yet.

Among other manufacturing sectors, positive contributions to growth for the first seven months came from the machinery & equipment sector, electrical equipment, the repair and the food sector. Otherwise, the basic metals & fabricated metal products sector saw a strong decline over the first seven months (due to troubles in the European steel industry which have also affected the U.S. Steel Košice company who announced plans to lay off 2,500 persons by 2021 – out of its 10,000 employees) as well as the refinery sector (due to a temporary shutdown of parts of the Slovnaft oil refinery).

Export declined unexpectedly. Export growth of goods and services turned negative in the second quarter of 2019 and declined by 2%, down from a very positive expansion of 7% in the first quarter. Imports of goods and services also slowed down from 6.4% to about 1% (at constant prices). Thus net real exports had a negative effect on growth. The National Bank of Slovakia cites declining exports to

the UK, Sweden, the Czech Republic and partly Poland as the main reason (Brexit; decline of auto part exports through value chains).

Upcoming parliamentary elections in February 2020 and lower growth jeopardize fiscal targets.

Government deficits and hence debt to GDP ratios have gone down in the last years, reaching -0.7% and 48.9% respectively in 2018. This year, however, the planned target of a balanced budget will not be reached. On the one hand this is due to lower than expected growth and thus lower tax revenues, and on the other, generous social actions before the upcoming parliamentary elections in February 2020. The deficit in 2019 thus is expected to reach -1.2% of GDP. Tax revenues might also decline over the coming years due to changes in taxes, i.e. lowering value added tax on certain food items, suggesting that the budget deficit may widen further.

30th anniversary of the Velvet Revolution in 1989 will be celebrated in mid-November,

accompanied by protests 'For a Decent Slovakia'. The protests symbolise the fight against corruption and a call for the rule of law and were brought to a head with the murder of the investigative journalist Ján Kuciak and his fiancée Martina Kušnírová in February 2018. The protests present a major challenge for Slovakia today.

Cooling down of the economy is already taking place this year. The wiiw-forecast for this year has been revised downwards due to surprising low growth figures in the second quarter of 2019. Household consumption will remain stable and thus be the main growth driver this year. Government consumption (parliamentary elections ahead) will also contribute to growth. The output of the key sector of Slovakia – the automotive industry - turned negative in June. For the coming years, household consumption will form the basis for growth, together with a revival of investments heading up with the end of the EU financing period. However, external risks are growing (trade wars, Brexit), which particularly affect the main automotive industry. Its major trading partner, Germany, is also facing troubles in its automotive sector.

Table 5.20 / Slovakia: Selected economic indicators

	2015	2016	2017	2018 ¹⁾	2018 January-June	2019	2019 Forecast	2020 Forecast	2021
Population, th pers., average	5,424	5,431	5,439	5,447	.	.	5,450	5,455	5,460
Gross domestic product, EUR mn, nom. ²⁾	79,758	81,038	84,517	89,721	43,078	45,513	94,300	98,400	103,000
annual change in % (real)	4.8	2.1	3.0	4.0	4.1	2.8	2.3	2.2	2.6
GDP/capita (EUR at PPP)	22,500	22,400	22,800	23,900	.	.	.	.	.
Consumption of households, EUR mn, nom. ²⁾	42,416	43,904	46,473	49,395	23,624	24,575	.	.	.
annual change in % (real)	2.8	3.9	4.4	3.9	2.8	1.5	1.8	2.0	2.0
Gross fixed capital form., EUR mn, nom. ²⁾	18,919	17,019	17,965	19,050	9,101	9,177	.	.	.
annual change in % (real)	21.6	-9.3	3.9	3.7	13.7	-1.2	1.0	3.5	6.0
Gross industrial production									
annual change in % (real)	6.7	4.7	3.2	4.4	3.5	4.8	1.0	2.0	2.0
Gross agricultural production									
annual change in % (real)	-3.2	13.9	-6.1	-1.1	.	.	.	.	.
Construction industry									
annual change in % (real)	18.1	-10.7	3.0	8.5	7.0	-1.3	.	.	.
Employed persons, LFS, th, average	2,424	2,492	2,531	2,567	2,549	2,579	2590	2600	2600
annual change in %	2.6	2.8	1.5	1.4	1.2	1.2	0.9	0.3	0.0
Unemployed persons, LFS, th, average	314	267	224	180	188	157	160	160	150
Unemployment rate, LFS, in %, average	11.5	9.7	8.1	6.5	6.9	5.8	5.8	5.8	5.6
Reg. unemployment rate, in %, eop	10.6	8.8	5.9	5.0	5.4	5.0	.	.	.
Average monthly gross wages, EUR	883	912	954	1,013	980	1,062	1100	1170	1230
annual change in % (real, gross)	3.2	3.8	3.3	3.6	3.8	5.8	5.5	3.8	3.2
Consumer prices (HICP), % p.a.	-0.3	-0.5	1.4	2.5	2.6	2.5	2.7	2.1	2.0
Producer prices in industry, % p.a.	-2.9	-3.9	2.5	2.3	1.3	2.8	3.0	2.5	3.0
General governm.budget, EU-def., % of GDP									
Revenues	42.2	39.3	39.6	40.1	.	.	39.0	38.6	38.4
Expenditures	44.7	41.5	40.4	40.8	.	.	40.2	40.1	40.0
Net lending (+) / net borrowing (-)	-2.5	-2.2	-0.8	-0.7	.	.	-1.2	-1.5	-1.6
General gov.gross debt, EU def., % of GDP	51.8	51.9	51.2	49.2	.	.	48.2	47.8	47.5
Stock of loans of non-fin.private sector, % p.a.	9.7	9.3	9.9	9.8	10.2	7.2	.	.	.
Non-performing loans (NPL), in %, eop	4.8	4.4	3.6	3.1	3.5	2.9	.	.	.
Central bank policy rate, % p.a., eop ³⁾	0.05	0.00	0.00	0.00	0.00	0.00	.	.	.
Current account, EUR mn	-1,669	-2,221	-1,618	-2,371	-610	-495	-2,800	-2,800	-2,600
Current account, % of GDP	-2.1	-2.7	-1.9	-2.6	-1.4	-1.1	-3.0	-2.8	-2.5
Exports of goods, BOP, EUR mn	64,577	66,686	70,510	75,698	37,490	39,442	77,500	80,200	83,000
annual change in %	3.2	3.3	5.7	7.4	7.4	5.2	2.4	3.5	3.5
Imports of goods, BOP, EUR mn	63,779	65,432	69,913	75,919	37,016	38,975	78,300	81,000	84,000
annual change in %	6.6	2.6	6.8	8.6	8.0	5.3	3.2	3.5	3.7
Exports of services, BOP, EUR mn	7,324	8,350	9,339	10,209	4,802	5,053	10,700	11,200	12,000
annual change in %	6.3	14.0	11.8	9.3	8.2	5.2	5.0	5.0	7.0
Imports of services, BOP, EUR mn	7,196	7,967	8,457	9,284	4,313	4,494	9,700	10,200	10,600
annual change in %	7.2	10.7	6.1	9.8	6.6	4.2	4.0	5.0	4.0
FDI liabilities, EUR mn	1,357	4,326	3,749	2,158	824	729	1,500	.	.
FDI assets, EUR mn	1,266	3,684	1,367	1,354	1,107	850	1,000	.	.
Gross reserves of NB excl. gold, EUR mn	1,648	1,624	1,609	3,426	2,777	4,437	.	.	.
Gross external debt, EUR mn	67,398	74,917	94,188	101,914	95,866	103,455	105,000	110,000	110,000
Gross external debt, % of GDP	84.5	92.4	111.4	113.6	106.8	109.7	111.3	111.8	106.8

1) Preliminary. - 2) Half-year data unrevised. - 3) Official refinancing operation rates for euro area (ECB).

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