Slovak Republic

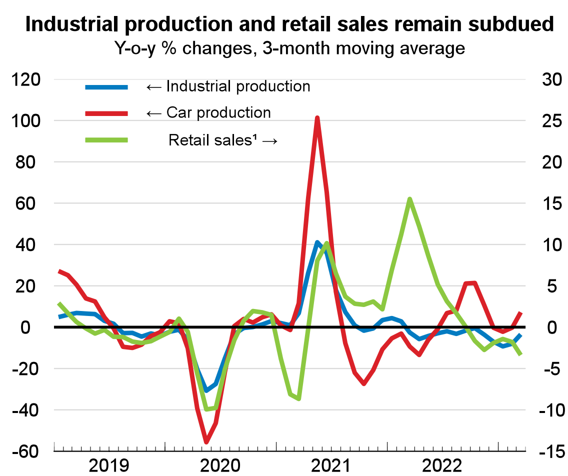
GDP growth is projected to be 1.3% in 2023 before picking up to 2% in 2024. High inflation will weigh on private consumption growth, although the impact is mitigated by substantial government support measures. Investment growth will be supported by the absorption of substantial EU funds in 2023. The recovery of global demand and continued easing of supply chain disruptions will boost export growth in 2024. The main risks to the projections are related to an escalation of Russia's war of aggression against Ukraine, which would weigh on foreign demand and could lead to a resurgence of global energy prices, increased inflation and lower growth.

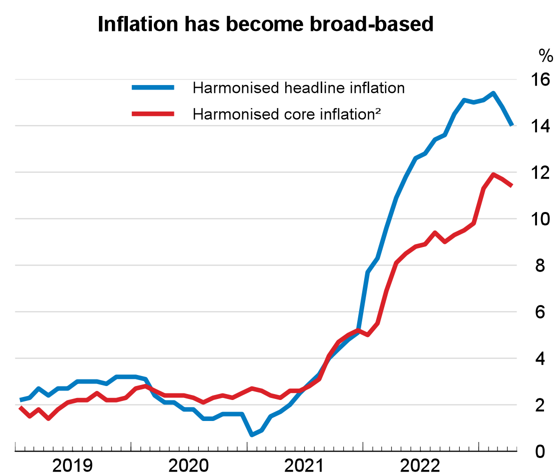
Fiscal support to households and firms to mitigate the rise in energy prices should be better targeted to limit additional demand pressures at a time of high inflation. Specific consolidation measures should be spelled out to ensure fiscal sustainability. Accelerating investment in the green transition, including improvements to the energy efficiency of buildings, will help enhance energy security and mitigate climate change.

Economic growth remains subdued

The economy continued to grow moderately in the first quarter of 2023, by 0.2% compared to the previous quarter. Domestic demand growth slowed, and net exports supported the economy on account of a significant drop in imports. Consumer and business confidence remained weak in April. Harmonised consumer price inflation is high (14.0% in April) and broad-based, with core inflation reaching 11.4% in April. The labour market has been resilient. The registered unemployment rate declined to 5.3% in April, close to pre-pandemic levels (5.2%).

Slovak Republic





1. Volume terms.
2. Core inflation refers to the overall index excluding food, energy, alcohol and tobacco.
Source: Statistical Office of the Slovak Republic; and Eurostat.

StatLink https://stat.link/9cwg7r

Slovak Republic: Demand, output and prices

Slovak Republic	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
GDP at market prices	94.4	-3.3	4.9	1.7	1.3	2.0
Private consumption	53.2	-1.4	1.8	5.1	0.6	1.6
Government consumption	18.5	-0.6	4.2	-3.2	0.2	0.5
Gross fixed capital formation	20.3	-10.8	0.2	6.5	9.9	3.8
Final domestic demand	92.0	-3.3	2.0	3.6	2.3	1.8
Stockbuilding[1]	2.2	-1.9	2.0	0.2	2.0	0.0
Total domestic demand	94.2	-4.8	4.3	3.7	4.0	1.7
Exports of goods and services	86.7	-6.5	10.6	1.2	3.0	4.4
Imports of goods and services	86.5	-8.3	12.0	3.3	5.7	3.9
Net exports[1]	0.2	1.7	-0.9	-2.0	-3.0	0.2
Memorandum items						
GDP deflator	_	2.4	2.4	7.5	9.4	4.9
Harmonised index of consumer prices	_	2.0	2.8	12.1	11.0	5.6
Harmonised index of core inflation[2]	_	2.4	3.3	8.2	9.5	4.9
Unemployment rate (% of labour force)	_	6.7	6.8	6.1	6.3	6.3
Household saving ratio, net (% of disposable income)	_	5.6	3.3	-1.8	0.2	1.6
General government financial balance (% of GDP)	_	-5.4	-5.4	-2.0	-5.8	-4.3
General government gross debt (% of GDP)	_	79.1	80.0	65.9	66.3	65.5
General government debt, Maastricht definition[3] (% of GDP)	_	58.9	61.0	57.8	58.2	57.4
Current account balance (% of GDP)	_	0.6	-2.5	-8.2	-10.2	-9.5

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 113 database.

StatLink https://stat.link/qlj74g

Slovakia has managed to reduce its high energy dependency on Russia. The recently signed agreement to purchase natural gas from the North Sea until 2024 will further improve energy security. Around 15,000 Ukrainian refugees found employment by the end of 2022 (about 0.5% of the labour force), mostly in low-skilled occupations with labour shortages. Tighter monetary and financial conditions have led to a decline in housing construction and new mortgage loans. House prices have been declining since June 2022.

The fiscal accounts will deteriorate sharply in 2023

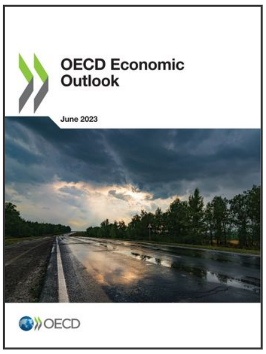
The government has adopted measures amounting to 2.5% of GDP to mitigate the effects of the energy crisis in 2023. For example, increases in gas and heating prices for households are capped. In addition, the government reimburses firms 80% (100% for small firms) of the gas and electricity costs above a certain price threshold. Permanent measures, such as higher tax allowances for families with children, significant wage increases for workers in the healthcare sector, and reduced VAT rates for catering, sports and tourism industries will add about 1.7% of GDP to the budget deficit. Slovakia can still draw unused 2014-20 EU Cohesion policy funds of about 4.3% of GDP in 2023, which together with funds from the EU Recovery and Resilience Plan (1.4% of GDP in 2023 and 2.3% in 2024) will boost public investment this year. Part of the unspent EU cohesion funds will be used to finance the energy support measures. Overall, the fiscal stance is expected to be strongly expansionary in 2023. Government fiscal plans foresee structural consolidation to start in 2024.

Growth in 2023 will be mainly driven by investment

High inflation will weigh on real wages and private consumption, but will be attenuated by government support measures. Real wages are projected to increase in 2024, which should support a pick-up in private consumption and some rebuilding of households' savings. Substantial EU funds will boost investment in 2023. The continued easing of supply chain disruptions will lead to an acceleration of exports and help regain some of the export market share lost in recent years, especially in the automotive sector. Headline inflation is projected to slow from the second half of 2023 due to reductions in global energy and food prices, while core inflation will decline more slowly due to the lagged pass-through of energy prices to other goods prices and the effects of nominal wage increases. The main downside risks to the projections are related to a prolonged war in Ukraine, which would weigh on foreign demand and could lead to the resurgence of global energy prices. Lower absorption of EU funds would negatively affect investment.

Better targeting and timely reduction of fiscal support is needed

Fiscal support for households and firms should be better targeted to limit additional demand stimulus at a time of high inflation and help preserve incentives to lower energy use. For example, support to households should target only those inadequately covered by the general social protection system. If resources allocated for energy support measures remain unspent, they should be used to reduce public debt. Consolidation measures for 2024 and beyond should be specified in line with recently adopted expenditure ceilings to ensure fiscal sustainability. The recovery plan allocates an important share of resources to the green transition, including improvements in the energy efficiency of the housing stock. Investment in these areas should be accelerated to reduce carbon emissions and improve energy security. Policies aimed at increasing labour force participation of mothers with young children, such as expanding the supply of high-quality and affordable childcare facilities, could boost labour supply and mitigate the effects of ageing.



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