1. ECONOMIC DEVELOPMENT IN THE SLOVAK REPUBLIC

General Economic Environment

The year 1993 was the first year of the independent existence of the Slovak Republic. In that year the Slovak economy had to absorb even this, from the economic point of view, exogenous factor, having a profound impact on the imminent economic situation in Slovakia - together with the impact of the asymmetrically, and for the Slovak Republic, detrimentally distributed consequences of the abrupt liberalization of the economy and the restrictive stabilization policy of 1991-1992. As a result, the area of economic activity contracted and trade relations between Slovak and Czech enterprises partially disintegrated. The reallocation processes, existing in the former federation, ceased to exist and the establishment of the new state infrastructure incurred substantial costs.

Nevertheless, the political and economic sovereignty facilitated the harmonization of the country's economic policy with parameters of the internal economic environment and enabled the re-orientation of the economic policy so that it would stimulate the integration of the Slovak economy into international economic relations.

Freedom of action in this sphere is, for the Slovak Republic, especially important due to the fact that the structure of the Slovak economy has some unfavourable features, which form bottlenecks in the reform process. The main one is the excessive share of heavy industry and primary production in the industrial structure, coupled with the present difficult situation of large arms producers - their production represented 40% of the total output of the mechanical engineering sector in Slovakia during the late 80ties. Some of other particular features, such as soil and geographical characteristics of the country create unfavourable conditions for the development of farm production. In the past, these structural particularities of the Slovak economy determined, or predicted the preferred foreign trade orientation (both exports and imports) of Slovak enterprises towards the markets of former COMECON member countries; presently they complicate the commodity restructuring of Slovakia's foreign trade and the diversification of its territorial structure.

Underlining the structural particularities of the Slovak economy has by no means discredited the reform trend in economic policy and the achieved level of the transformation of ownership rights, price liberalization, and foreign trade. An additional systemic reform supporting the market orientation of the transformation process in the Slovak Republic has become effective on 1 January 1993. Of major importance were: the tax reform providing for a system of taxation conforming with the present standards used in market economies; the new system of health and old-age insurance; the improved mechanisms of the social security system. With the establishment of an independent central bank - the National Bank of Slovakia, a dynamic development began in the banking sector and the capital market.

It is very important that, despite a certain slow-down in the process of privatization, the small-scale privatisation has in fact terminated, the first phase of large-scale voucher privatisation has been completed, and the idea of an accelerated privatization has met with general support.

In addition to the above facts, which shape mainly the internal environment of the developing Slovak economy, the economic development in the Slovak Republic in 1993 was under the influence of the external environment characterized by continuing recession in developed economies and transition problems in most Central and Eastern European countries.
Development of GDP and the Main Sectors of the Economy

The establishment of an independent State necessitated a certain period of adaptation, which was accompanied by a deeper recession. The decline in economic performance was evident already in the first quarter of 1993; this falling tendency was partially overcome during the year (especially thanks to the development in the last months). With regard to the special economic situation in 1993, the 4.1% annual decline in GDP can be interpreted as a relatively auspicious result (by comparison: the GDP drop in 1992 was 7%). The absolute value of GDP in 1993 reached Sk 336.7 billion, or at constant prices (year 1984 = 100) Sk 172.2 billion.

Development of GDP in 1993 (at constant prices, change compared with the same period of the previous year)

The development of industrial production in 1993, marked by an annual decline of 13.5%, effectively illustrates the actual economic situation. Yet, in contrast to previous years, this decline was caused mainly by a contraction in external demand and only partially by a fall in domestic demand. However, exports still accounted for a relatively big share (i.e. 37.2%) of industrial sales.

The trend in the development of the industrial structure towards energy and material intensive production at a lower processing stage continued. This tendency was reflected in the different rates of decline in the output of mining and power industries (-8.4%), processing industries (-18.6%), and in a moderate decline in chemical (-6.8%) and metallurgical (-4.4%) industries and, on the other hand, in the plummeting output of mechanical engineering (-19.1%) and in other branches of final production. In 1993, an extreme decline (-42.3%) was recorded in petrochemical industry. The described discrepancy between the mining and power industries and the processing industries was markedly reflected in the generated profit: the mining and power industries accounted for Sk 28 billion, out of the Sk 45 billion profit generated in the whole industrial sector.

The poor performance of the construction industry in 1993 ended with a drop of 26.1% ensuing mostly from the overall economic recession, i.e. the decline in investment demand of both the enterprise and the budgetary sectors. Also the shrinkage of the operations platform of enterprises and the drop in the export of building capacities contributed substantially to the situation described. Nevertheless, the construction sector surpassed industrial production in the efficiency of the transformation process. Whereas small and medium-sized companies (mostly private or non-public companies) in 1993 accounted for 31.1% of the total industrial production, while in building and construction they accounted for as much as 51.7%.

The 1993 trend in agriculture showed some signs of stabilization and a moderate decline in production of about 7% compared with the development of industry and
construction. As a consequence of the faster growth in agricultural prices (an annual increase of 10.2%) compared with 1992 (a 6.5% increase), the position of agricultural companies slightly improved and the total loss in agriculture was pushed down to Sk 6.6 billion (compared with Sk 14.5 billion in 1992). The efforts made to slow down the divergence between input prices and output prices, which had characterized the whole period of transformation in the agricultural sector, were crowned with success in 1993.

The considerable increase in the importance of the services sector, accounting for one half of GDP generated in 1993, represents a positive element in the development of the structure of the Slovak national economy. Naturally, this had a positive effect on the relation between the added value and consumption in the process of GDP generation.

Price Developments

In 1993, the rate of consumer-price inflation reached 25.1%. The Slovak Republic again managed to maintain its position of a transition economy with a relatively low rate of inflation in spite of the fact that the development of consumer prices in Slovakia was exposed to a number of impacts during 1993. The major factors that considerably contributed to the price level increase were the introduction of value-added tax and the dissolution of the CSFR with the subsequent currency split.

As a result of the cumulative effect of these two factors, almost one half of the actual increase in consumer prices (i.e. 11.8%) was concentrated already in the first quarter of 1993, whereby the value-added tax accounted for the decisive part of this increase. Without the impact of VAT, the monthly rate of consumer-price inflation would have averaged about 1%, i.e. 12% to13% for the whole year. The inflation rate indicator for the prices of industrial producers (increased by 18.8%) and the prices of construction work (increased by 22.7%) - which showed more moderate dynamics under the continuing state control over energy and fuel prices, transport tariffs, etc. - would have been even lower.

Trends of Individual Prices (previous month = 100)
A characteristic feature of the price movements in 1993 was the fact that the rise in agricultural prices lagged behind the price increases in other areas, despite the accelerated growth in agricultural prices. Such a development can be explained by the effect of the prices of imported agricultural products on the demand-supply position of the relevant domestic farm product.

The factors that considerably influenced the month-to-month growths of inflation increments throughout the year are the devaluation of the Slovak crown (Sk) in July 1993 and the adjustment of VAT and other consumer taxes in August 1993, which caused an increase in the consumer price level of about 1% or 2%. The other factors were the partial adjustment of transportation and telecommunication tariffs, fees, and insurance premiums, as well as the increase in wholesale agricultural prices.

The development of consumer prices in 1993 caused a 24% rise in the costs of living, which was relatively equally distributed amongst the individual income groups of households.

**Labour Market**

In 1993, the rate of unemployment in the Slovak Republic reached 14.4%, representing a 4% increase compared with the figure for 1992. The development of unemployment differed according to sectors and time, but reflected the continuing economic decline. At the end of 1993, employment in industry dropped by 11%, in construction by 17%, while trade experienced an increase of 21% compared with the 1992 level. Within the scope of these development trends, employment in industry rapidly increased (by 49%) in the private sector, while an outflow of workers (17%) was recorded in building and construction including the private sector.

![Unemployment Rate (in %)](image)

A characteristic feature of unemployment in the Slovak Republic is its evident regional differentiation: the lowest rate of unemployment was recorded in Bratislava and some other big cities, whereby in a number of districts, predominantly in southern and eastern Slovakia, the unemployment rate was as high as 20%.

The most unfavourable aspects of this development in 1993 were the above-the-average number of unemployed among young people and the growing share of long-term unemployment.
A fact that needs to be mentioned when describing the labour market in the Slovak Republic is the existing relatively extensive latent unemployment (or overemployment) in many large public enterprises or joint stock companies, which is one of the causes of the retarded privatization process (and vice versa) and of the overall malfunction of the labour market. Even in 1993, the insufficient functioning of the labour market was supported by the absence of wage control: in a liberalized, albeit far from competitive economic environment, the dominating tendency led to a continuous growth in nominal wages and an increase in labour costs. At an 18.5% annual increase in average nominal wages resulting both from the growing unemployment and an absolute rise in wages, the GDP wage-cost ratio in 1993 rose by 21.4% (representing Sk 0.65 per Sk 1 of GDP) compared with the 1992 figures.

The development of labour productivity reflected these trends in the labour market; from a cross-sectional view of the national economy (measured by the GDP level at constant prices per worker), labour productivity was down only by 0.9% compared with 1992. However, the fall in industry was 10.4%, or if including small businesses, about 7%. The most positive development in labour productivity was manifested by those industries where the production slow-down was accompanied by a rise in prices (food processing, oil refinery).

Foreign Trade

In 1993, the development of foreign trade in the Slovak Republic maintained the falling tendency of recent years, and the total volume of foreign trade dropped by 7.3% compared with the 1992 figure. The balance of foreign trade, resulting from the volume of exports (Sk 163.2 billion) and the volume of imports (Sk 195.2 billion), reached a deficit of Sk 32 billion.

Exports suffered a further year-to-year decline of 11.4%, hence the ability of covering imports through exports deteriorated as well as the export performance of the economy (measured as a ratio of exports to GDP), which reached a level of 49.5% compared with 64.4% recorded in 1992. A decline in exports was recorded in trade with all relevant regional blocks and countries (except Poland and Hungary) including the developing countries. The sharpest drop was recorded in exports to the Czech Republic and the former Soviet Union.

Structure of Imports  
Structure of Exports

The decline in imports (4.5%) was not as striking as in exports, however, the territorial differentiation was in the case of imports much more distinct. On the one hand, imports from EU and EFTA countries, and from the former Soviet Union, Poland, developing countries, and China increased. On the other hand, the volume of imports from the
Czech Republic substantially decreased probably as a consequence of an even more sluggish consumption and investment demand in the Slovak Republic, and also as a result of the continuing change in the orientation towards third countries, especially EU and EFTA countries, with regard to certain import items. The considerable weakening of foreign trade relations between Slovakia and the Czech Republic is evident from the fact that the level of trade between the two republics in 1993 reached only 68% of the 1992 level. In 1993, the balance of trade between Slovakia and the Czech Republic showed a surplus of Sk 1.3 billion.

No major changes were recorded in the commodity structure of the Slovak Republic's foreign trade in 1993: production with a low degree of completion continued to dominate exports, however, the proportion of machinery and equipment declined. On the contrary, commodities of this type were leading in imports.

Considering the described tendencies in the development of Slovakia's foreign trade, the identified key problem hindering the foreign trade from reaching a more favourable balance is the growing trade deficit with the countries of the former Soviet Union, which grew from USD 702 million to USD 892 million over the course of 1993.

The unfavourable level of the total foreign trade deficit of the Slovak Republic in 1993 was partly offset by the balance of services, which reached a surplus of Sk 12.8 billion.

**The Slovak Economy in a Central European Context**

The economic policy of Slovakia in 1993 continued the tradition of careful macroeconomic control, low inflation, low indebtedness, and continuing legislative and institutional reform. This made a significant contribution to the acceptable results of the Slovak economy, which managed to maintain its relatively favourable position compared with other reform economies.

The position of Slovakia within the group of transforming economies is evident from comparison of the basic economic indicators of CEFTA (Central European Free Trade Agreement) countries, which include the Czech Republic, Hungary, Poland, and Slovakia.

In 1993, the decline in GDP continued at a slower rate with the exception of Poland, where increases have been recorded in the last two years.

<table>
<thead>
<tr>
<th>Year</th>
<th>SR</th>
<th>CR</th>
<th>Hungary</th>
<th>Poland</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
<td>85.5</td>
<td>85.8</td>
<td>88.1</td>
<td>92.4</td>
</tr>
<tr>
<td>1992</td>
<td>93.0</td>
<td>93.4</td>
<td>95.5</td>
<td>102.6</td>
</tr>
<tr>
<td>1993</td>
<td>95.9</td>
<td>99.7</td>
<td>98.5</td>
<td>103.8</td>
</tr>
</tbody>
</table>

Source: Central Statistical Office of the SR
1/ Preliminary data
2/ Calculated by using the conversion method
3/ Estimated figures
4/ Obtained by the ESA method, preliminary results, estimated index compared with 1991

The economic results achieved in Slovakia did not deviate from the general trend and were better than expected. There are signs of stabilization and a slight growth is expected in 1994.

In the group of countries analysed, inflation continued to decrease.
Consumer Price Index (last year = 100)\textsuperscript{1/}

<table>
<thead>
<tr>
<th>Year</th>
<th>SR</th>
<th>CR</th>
<th>Hungary</th>
<th>Poland</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
<td>161.2</td>
<td>156.6</td>
<td>135.0</td>
<td>170.3</td>
</tr>
<tr>
<td>1992</td>
<td>110.0</td>
<td>111.1</td>
<td>123.0</td>
<td>143.0</td>
</tr>
<tr>
<td>1993</td>
<td>123.2</td>
<td>1208</td>
<td>122.5</td>
<td>135.3</td>
</tr>
</tbody>
</table>

Source: Central Statistical Office of the SR

\textsuperscript{1/} Contrary to the indices used in the previous part of this chapter and in Chapter 2 (Monetary Development and Monetary Policy), the indices used here express the average price movement recorded in the relevant year compared with the previous one.

Price development in Slovakia (as well as in the CR) was largely influenced by systemic changes (particularly the introduction of VAT). In the comparison group, however, price movements in Slovakia remained in the zone of the slowest growth, and showed a clear tendency towards a further decrease.

Unemployment in general continued to increase.

### Unemployment Rate

<table>
<thead>
<tr>
<th>Year</th>
<th>SR</th>
<th>CR</th>
<th>Hungary</th>
<th>Poland</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
<td>11.8</td>
<td>4.1</td>
<td>8.5</td>
<td>11.8</td>
</tr>
<tr>
<td>1992</td>
<td>10.4</td>
<td>2.6</td>
<td>12.3</td>
<td>13.6</td>
</tr>
<tr>
<td>1993</td>
<td>14.4</td>
<td>3.5</td>
<td>12.1</td>
<td>15.7</td>
</tr>
</tbody>
</table>

Source: Central Statistical Office of the SR

Even though a relatively rapid rise in unemployment was recorded in Slovakia, the rate of unemployment does not exceed the average level recorded in the analyzed countries with the exception of the Czech Republic.

The development in public finance may be characterized by a tendency towards stabilization as far as the state budget deficit is concerned.

### State Budget Deficit (in % of GDP)

<table>
<thead>
<tr>
<th>Year</th>
<th>SR</th>
<th>CR</th>
<th>Hungary</th>
<th>Poland</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
<td>-3.9\textsuperscript{2/}</td>
<td>-2.1\textsuperscript{1/}</td>
<td>-4.9</td>
<td>-3.8</td>
</tr>
<tr>
<td>1992</td>
<td>-3.1\textsuperscript{3/}</td>
<td>-0.2\textsuperscript{3/}</td>
<td>-7.0\textsuperscript{1/}</td>
<td>-6.0</td>
</tr>
<tr>
<td>1993</td>
<td>-6.8\textsuperscript{4/}</td>
<td>0.1\textsuperscript{3/}</td>
<td>-6.8\textsuperscript{1/}</td>
<td>-2.8</td>
</tr>
</tbody>
</table>

Source: Central Statistical Office of the SR, NBS

\textsuperscript{1/} Preliminary data
\textsuperscript{2/} Estimated figures
\textsuperscript{3/} Calculated by the conversion method
\textsuperscript{4/} Calculated by the ESA method, preliminary data

The relatively unfavourable development in Slovakia should be viewed in connection with the elimination of transfers within the former federation and the increased state budget expenditure on the building of the state infrastructure.

The development in Slovakia’s foreign debt may be regarded as favourable. This applies to both the absolute volume of foreign loans and the amount of foreign debt per capita.

The relatively low level of foreign debt is a significant factor in Slovakia’s potential for further development.
Foreign Debt in 1993

<table>
<thead>
<tr>
<th></th>
<th>SR</th>
<th>CR</th>
<th>Hungary</th>
<th>Poland</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total debt</td>
<td>3.622</td>
<td>8.805</td>
<td>25.204*</td>
<td>46.169</td>
</tr>
<tr>
<td>(in USD billions)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Debt per capita</td>
<td>683</td>
<td>852</td>
<td>2450*</td>
<td>1199</td>
</tr>
<tr>
<td>(in USD)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Central Statistical Office of the SR

To sum up: the basic indicators in the Slovak economy do not deviate from those achieved by the leading transforming economies in Central Europe despite the numerous problems of economic development in Slovakia.

The short-term problems of Slovakia arise from the initial difficulties that accompanied its establishment as an independent state, and are partly a result of a "side effects" of the economic reform, which is, in some areas, in an earlier stage of development than in Poland and Hungary.

The medium- and long-term prospects for economic development in Slovakia depend mainly on the restructuring of the economy and its ability to meet keen international competition. In this field, Slovakia has relatively good preconditions within the framework of transforming economies. In addition to the trend towards stabilization and low foreign debt, Slovakia has a well-qualified and highly competitive labour force, strong research potential, and an advantageous geographic position at the heart of Europe.

1) The Empirica-Institute in Bonn carried out a study of all countries in Europe (except the former Soviet Union) analysing 404 regions from the point of view of their business potential. According to this study, the prospects of the Central European region are extremely favourable. Bratislava, the Capital of the SR, and its environs were seen as the region with the best prospects for economic development of all regions.
Prospects for Economic Development

The development of the Slovak economy in 1993 affected by new parameters defining the economic environment in the Slovak Republic after the introduction of important institutional reforms recorded again a decline and an eroded development of foreign trade. Economic development is summed up by the difficulties with the state budget (in 1993 the deficit of the state budget widened to Sk 23 billion, i.e. 6.8% of GDP), and the strained development in the balance of payment (effectively the closing account of the consolidated balance of payments for 1993 managed to maintain a surplus of Sk 1.7 billion).

The path representing a determined orientation in the economy of the Slovak Republic towards a recovery of economic growth is, in its systemic dimension, clearly defined by further embodiment of positive reform changes that have been enforced in the Slovak economy in spite of the problems encountered in its economic development in 1993. The underlying condition of the full enforcement of these transformation changes and a gradual formation of a standard market economy is an economically viable and socially long-term sustainable macroeconomic policy creating favourable conditions for market-orientated behaviour of the economic microsphere of both enterprises and individuals.

The microsphere requires a flexible competitive environment, i.e. primarily a need to accelerate the process of privatization. An inevitable requirement of structural adaptation is the fulfilment of the stated conditions and that, in its final effect, is crucial for increasing the performance of the Slovak economy to a level facilitating a more effective integration into international economic relations.