NÁRODNÁ BANKA SLOVENSKA
EUROSYSTÉM

CHAPTER 2

MONETARY DEVELOPMENTS

2

2 Monetary Developments

Slovakia's economic fundamentals in 2009 were influenced by two factors above all others. Firstly, as from 1 January Slovakia joined the euro area and adopted the euro currency; at the same time, Národná banka Slovenska became a member of the Eurosystem. Secondly, economic developments were impaired by the persisting financial crisis, as global economic activity recorded its sharpest downturn since the Great Depression.

The adverse economic situation across the world had already affected the performance of Slovakia's economy in 2008, with growth slowing in the last quarter of the year. As a consequence of the financial crisis, Slovakia's real economy contracted by 4.7% in 2009, after growing by 6.4% in 2008. As regards GDP growth in individual quarters, however, the downturn gradually ameliorated, from -5.7% over the first three months to -2.6% in the last quarter. The effect of the global economic and financial crisis on Slovakia's real economy was seen above all in the slump in external trade. And just as external demand was slowing down, so too was domestic demand falling, particularly due to the decline in its investment component. The weaker external demand dragged down corporate profits, especially the profits of non-financial corporations, with the result that investment activities were scaled back substantially. Domestic consumption demand rose slightly owing to an increase in the final consumption of general government. The current account deficit of the balance of payments improved slightly in 2009 in comparison with the previous year, reflecting positive developments in the trade balance as well as in the income and current transfers accounts. But the fact that the trade balance was in surplus was due to imports declining more sharply than exports. Another repercussion of the economic downturn was rising unemployment and falling employment, particularly in industry. Amid the unfavourable economic conditions, both nominal and real wage growth slowed year-on-year. As for labour productivity, it declined on a year-on-year basis, in both nominal and real terms, owing to the sharp contraction in GDP. Unit labour costs, however, recorded an annual increase, largely because of the relatively high rise in nominal compensation per employee.

Price developments in Slovakia in 2009 were affected by the global economic downturn and the consequent decline in consumer demand. The inflation rate in Slovakia, as measured by the Harmonised Index of Consumer Prices, remained unchanged in December on a year-on-year basis. Compared to the year-on-year consumer price dynamics in December 2008, this represented a slowdown of 3.5 percentage points. The average inflation rate for 2009 came to 0.9%. The decline in the domestic price level was driven by lower prices of industrial goods, which in turn reflected a slower rise in energy prices and sharp drop in fuel prices. Food prices, too, were lower in the year-on-year comparison. Prices of services rose, but at a slower pace. For most of 2009, almost all producer prices were lower in comparison with the same point of the previous year.

In the field of interest rate policy, Národná banka Slovenska has been subject to the decisions of the European Central Bank since 1 January 2009, when it joined the Eurosystem. The ECB's main refinancing rate now functions as the base rate. In 2009, the main refinancing rate was cut on four occasions, and from May until the year-end it stood at 1.0%. Meanwhile, the euro's importance as a bulwark against the effects of the global financial crisis on Slovakia's financial sector and, indirectly, on its macroeconomic developments has increased substantially.

2.1 Economic Developments

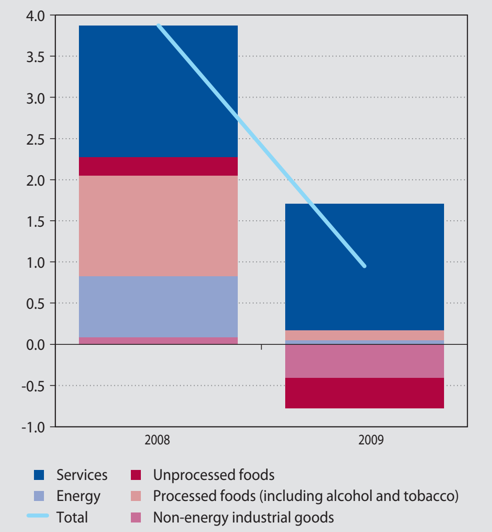
2.1.1 Price developments

Consumer prices

Inflation as measured by the Harmonised Index of Consumer Prices (HICP)

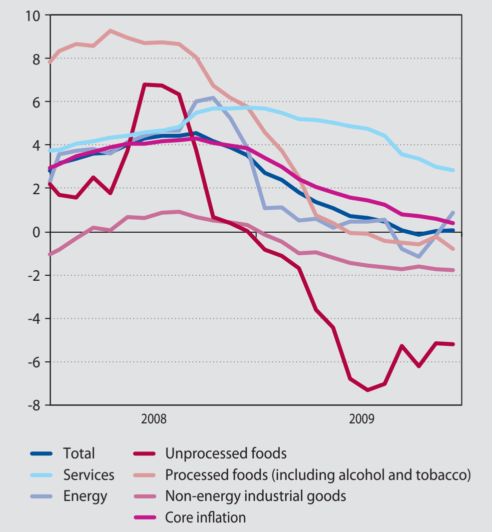
In December 2009, the HICP inflation rate stood unchanged on a year-on-year basis, and compared to the year-on-year consumer price dynamics in December 2008, this represented a slowdown of 3.5 percentage points. The average inflation rate for 2009 was 0.9% (compared with 3.9% for 2008) with prices of goods falling by 0.8% and prices of services rising by 4.4%. The

Chart 12 Structure of HICP inflation (contributions of components to the annual average rate; p.p.)



Source: SO SR and NBS calculations.

Chart 13 Year-on-year changes in HICP sub-components (%)



Source: SO SR.

year-on-year rate of core inflation (the headline rate excluding prices of energy and unprocessed foods) averaged 1.6% in 2009, which was 2.3 percentage points lower than in the previous year.

Price developments in 2009 were determined by external factors. The domestic price level was affected by the global economic downturn and the consequent downward pressure on world prices of energy commodities (oil) and non-energy (agricultural) commodities. Slovakia's inflation rate reflected these commodity price developments though a low increase in energy prices, a marked drop in fuel prices, and also a decline in food prices. The slowdown in consumer demand – stemming from uncertainty about future global developments (rising unemployment, falling employment) – dragged down prices of industrial goods, firstly from abroad and then from domestic producers. As for inflation in services prices, it began to slow down during the second half of 2009.

Goods

In the case of goods prices, the most substantial deflationary factor in 2009 was food prices, which reflected the falling trend in agricultural commodity prices recorded towards the end of 2008 and at the beginning of 2009. Food prices were lower on average throughout 2009, owing to a decline in unprocessed food prices and a slower rise in processed food prices. Prices of processed foods reflected also excise duties on cigarettes, which were raised in February 2009. This tax hike, however, only began to show up in consumer prices from September to December, since it had been preceded by substantial pre-stocking of cigarettes. The slowdown in energy price inflation was influenced by fuel prices and regulated energy prices. Fuel prices in 2009 fell by an average of 16.4%, after rising by 6.4% in 2008. Prices of non-energy industrial goods declined on average over 2009, with prices of durable industrial goods falling by an average of 7.6%. At the same time, however, prices of non-durable industrial goods rose by 1.3% on average.

Services

Inflation in services prices slowed only marginally in 2009, since it included sharp rises in prices of health services, dental services, bus fares and postal services. It was also the case that inflation in these prices did not start declining by a greater margin until the second half of 2009, when it reflected the impact of the crisis and the base effect. The most pronounced drop in prices within the services category was recorded by prices of telecommunications services and air transport.

Table 2 HICP inflation (average for the period; annual percentage changes)

	2008		2009				
	Dec.	Q1–Q4	Q1	Q2	Q3	Q4	Q1–Q4
Overall	3.5	3.9	2.3	1.1	0.4	0.0	0.9
Goods	2.5	3.5	0.8	-0.9	-1.5	-1.5	-0.8
Industrial goods	1.7	2.0	0.1	-0.6	-1.0	-1.2	-0.7
Non-energy industrial good	0.3	0.4	-0.5	-1.2	-1.6	-1.7	-1.3
Energy	3.8	4.5	0.9	0.4	0.1	-0.2	0.3
Foods	3.9	6.4	2.1	-1.4	-2.3	-2.1	-0.9
Processed foods (including alcohol and tobacco)	5.8	8.0	3.6	0.4	-0.4	-0.5	0.8
Unprocessed foods	0.0	3.0	-1.2	-5.0	-6.5	-5.5	-4.6
Services	5.7	4.8	5.5	5.0	4.2	3.1	4.4
Core inflation (overall inflation excluding energy and unprocessed food prices	3.8	3.9	3.0	1.8	1.2	0.6	1.6
Overall inflation excluding energy prices	3.5	3.8	2.6	1.2	0.4	0.0	1.1

Source: NBS calculation based on data from the SO SR.

Producer prices

For the greater part of 2009, almost all producer prices (except for construction work prices) declined on a year-on-year basis. This was largely due to the sharp drop in prices of oil and food products in world markets as well as to the base effect of their rapid increase in the previous year. Although the oil price rebounded from the beginning of 2009 (after plummeting from July 2008), it was not until November 2009 that it returned to the levels of the previous year. The decline in agricultural product prices culminated in the third quarter of 2009. Because of these factors, industrial producer prices fell in comparison with 2008 and agricultural product price recorded a substantial overall decline on a year-on-year basis. Also in 2009, prices of construction materials fell year-on-year and prices of construction work rose, on average, more slowly than in 2008.

Industrial producer prices

Year-on-year inflation in industrial producer prices had already been slowing down since the last months of 2008, and in April 2009 it entered negative territory. This trend became more pronounced in subsequent quarters as a result of persisting steep falls in refined oil products and decreasing energy prices.

The year-on-year slowdown in manufacturing output prices in 2009 reflected price deflation in all components and particularly in prices of refined oil products, which recorded an average decline of 34.7% (compared to a rise of 17.9% in 2009). Other prices that fell in 2009 on a year-on-year basis after rising in the previous year were prices of good products, rubber and plastic products, metals and metal products, and electrical equipment. The year-on-year decline in prices of transport vehicles slowed moderately in 2009 (by 5.5 percentage points, to -1.2%).

The decrease in energy price inflation in 2009 stemmed largely from prices for the production and pipeline distribution of gaseous fuels, which fell by 11.1% in 2009 after rising by 17.0% in 2008. Electricity production and distribution prices increased more slowly in 2009 on a year-on-year basis (3 percentage points lower at 7.1%), while inflation in prices of steam supply and cold air distribution accelerated year-on-year (by 1.4 percentage points, to 8.0%).

Construction work prices

Inflation in construction work prices slowed in 2009 in comparison with the previous year. Almost the same increases were recorded for prices of construction repairs and maintenance

Table 3 Producer prices – average year-on-year changes (%)

	2008	2009				
		Q1	Q2	Q3	Q4	Q1–Q4
Industrial producer prices	6.1	2.0	-2.2	-4.6	-5.4	-2.5
Raw materials prices	16.8	15.7	3.4	-10.3	-16.0	-2.6
Manufacturing output prices	2.0	-4.5	-6.7	-7.2	-5.4	-5.9
Energy prices	11.6	10.3	3.5	-1.3	-5.3	1.6
Water rates and sewage charges	5.9	4.9	4.0	4.3	5.0	4.5
Construction works prices	5.6	4.3	2.8	1.9	1.6	2.7
Construction materials prices	3.3	0.4	-5.8	-8.4	-9.0	-5.7
Agricultural output prices	5.9	-22.7	-27.7	-31.7	-16.1	-24.5
Plant products prices	19.7	-39.9	-41.6	-35.7	-14.8	-33.0
Animal products prices	5.3	-13.2	-22.8	-25.2	-18.3	-19.9

Source: Statistical Office of the SR.
Note: Data based on the revised statistical classification of economic activities (SK NACE Rev. 2).

(2.8%) and for prices of work on new constructions, on building modernisation and refurbishment, and on civil engineering construction (2.7%).

The prices of materials and products used in the construction industry (materials and products of domestic industrial producers) declined on average in 2009 in comparison with the previous year. This reflected a downturn in prices of materials used for construction repairs and maintenance (-5.4%) and in prices of materials used for new constructions and for building modernisation and refurbishment (-5.7%).

Agricultural output prices

Prices of agricultural products recorded a year-on-year decline in 2009, which was influenced mainly by falling prices of plant products and animal products.

As for plant products, the substantial year-on-year drop in their prices was largely related to developments since mid-2008 – when inflation in their prices began to slow sharply and then, in September of that year, entered deflationary territory, where it stayed for the duration of 2009. The main driver of this decline was prices of cereals and pulses, which recorded average annual falls of 33.9% and 35.5%, respectively.

As for prices of animal products, their overall decline on a year-on-year basis was primarily due to the downturn in prices of raw cow's milk (-33.1%), slaughtered pigs (-6.3%) and slaughtered poultry (-18.8%). There was also a year-on-year downward trend in the average prices of slaughtered cattle and veal (-0.4%) and chicken eggs for consumption (-2.3%).

The course of producer prices in 2009 was to a considerable extent affected by the economic recession, although its repercussions varied in intensity from one sector to another and were felt after a certain time lag.

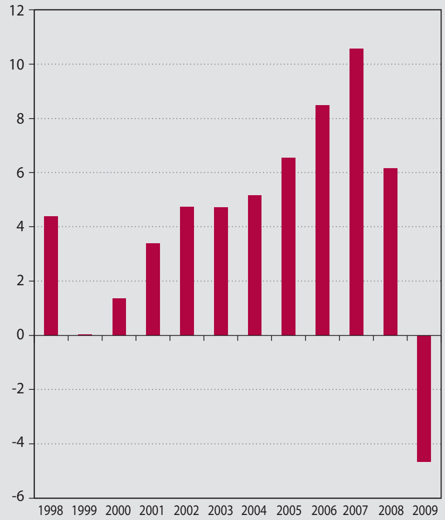
2.1.2 Gross domestic product

Slovakia's gross domestic product (at constant prices) contracted by 4.7% in 2009 on a year-on-year basis, according to the preliminary estimate from the Statistical Office of the Slovak Republic. In 2008, by contrast, GDP grew by 6.4%.

On the consumption side, the slump in GDP was attributable to the decline in external and domestic demand. On the production side, it was the sectors of industry and services that were the principal drag on growth. The nominal amount of GDP generated during the year represented €63.332 billion, which was 5.8% less than in the previous year.

Broken down by quarter, the downturn in real GDP gradually ameliorated over the course of the year, from -5.7% in the first quarter, to -2.6% in the fourth quarter.

Chart 14 Real GDP (annual percentage growth)



Source: SO SR.

After making seasonal adjustments, the only substantial quarter-on-quarter fall in GDP in 2009 was recorded in the first quarter. In subsequent quarters, economic activity was making a gradual recovery and GDP rose from one quarter to the next.

Supply side of GDP

GDP creation in 2009 was negatively affected by the value added component, which fell year-on-year by 4.6% at constant prices (compared to an increase of 6.9% in 2008), and it was also dampened by net taxes on products (value added tax, excise tax, and import tax, less subsidies), which fell by 5.6%, after dropping by 0.5% in the previous year.

The sectors in which the decline in value added was most pronounced were industry, construction and business services. By contrast, the agriculture, financial services and public services recorded growth in value added in 2009.

Table 4 GDP creation by component (index, same period a year earlier = 100, constant prices)

	2008	2009				
	Q1–Q4	Q1	Q2	Q3	Q4	Q1–Q4
Gross output	106.7	85.9	86.8	89.9	93.9	89.2
Intermediate consumption	106.6	81.8	81.6	85.5	91.5	85.2
Value added	106.9	93.0	94.9	95.8	97.8	95.4
Net taxes on products[1)]	99.5	108.8	90.1	88.0	93.9	94.4

Source: SO SR.
1) Value added tax, excise tax, and import tax, less subsidies.

Table 5 GDP by sector (index; same period of the previous year = 100; constant prices)

	2008 / 2007	Q1 09 / Q1 08	Q2 09 / Q2 08	Q3 09 / Q3 08	Q4 09 / Q4 08	2009 / 2008
GDP	106.2	94.3	94.5	95.1	97.4	95.3
of which:						
Agriculture	97.4	114.5	110.5	127.3	87.6	110.2
Industry	107.0	81.4	86.9	100.0	100.1	91.7
Construction	105.6	87.9	108.1	105.0	92.4	98.2
Trade, hotels and restaurants, transport	113.2	84.8	92.7	84.5	85.6	86.9
Financial intermediation, real estate activities	111.1	115.7	108.5	91.2	103.0	103.8
General government; education; health care; other community, social and personal services	95.2	106.8	92.7	100.5	111.7	102.9
Net taxes on products[1)]	99.5	108.8	90.1	88.0	93.9	94.4

Source: SO SR.
1) Value added tax, excise tax, and import tax, less subsidies.

Table 6 GDP by consumption (index; same period of the previous year = 100; constant prices)

	2008	2009				
	Q1–Q4	Q1	Q2	Q3	Q4	Q1–Q4
Gross domestic product	106.2	94.3	94.5	95.1	97.4	95.3
Domestic demand	106.0	96.1	93.3	93.8	93.4	94.1
Final consumption	105.8	99.6	101.9	99.7	99.4	100.1
Households	106.1	99.1	100.5	99.7	98.1	99.3
General government	105.3	101.3	106.9	99.8	102.9	102.8
Non-profit institutions serving households	101.6	98.3	98.1	98.5	98.4	98.3
Gross fixed capital formation	101.8	96.1	82.3	88.6	92.7	89.5
Exports of goods and services	103.2	74.8	79.7	85.0	94.8	83.5
Imports of goods and services	103.1	77.7	77.8	84.4	89.7	82.4

Source: SO SR.

Demand side of GDP

On the consumption side, the economy's downturn in 2009 reflected a decline in both domestic and external demand (which fell by 5.8% and 16.5%, respectively).

In the breakdown of domestic demand in 2009, investment demand recorded the sharpest fall, while rapid destocking also made a negative contribution to GDP growth. The consumption component rose only marginally, driven mainly by an increase in public consumption. Household consumption dropped by 0.7%.

Domestic investment demand

The downturn in external demand was reflected also in corporate profits and consequently in lower gross fixed capital formation. Among the component sectors, investment activities of financial and non-financial corporations recorded

Table 7 Structure of gross fixed capital formation in 2009 (current prices)

	Gross fixed capital formation (EUR million)	Share (%)	Index	
			2008/2007	2009/2008
Slovak economy – total	**14,943.2**	**100.0**	**103.8**	**89.4**
in which (by sector):				
Non-financial corporations	10,082.8	67.5	101.4	87.5
Financial corporations	179.9	1.2	108.3	63.4
General government	1,241.6	8.3	114.4	94.5
Households	3,394.0	22.7	108.1	95.9
Non-profit institutions	44.9	0.3	105.5	76.1
of which (by production):				
Machinery	**7,211.2**	**48.3**	**113.5**	**102.3**
of which: Other machines and equipment	5,510.5	36.9	114.5	105.6
Transport vehicles	1,700.8	11.4	110.7	92.8
Buildings	**6,578.9**	**44.0**	**100.0**	**79.4**
of which: Residential buildings	1,479.8	9.9	107.9	94.8
Other structures	5,099.2	34.1	98.4	75.9

Source: NBS calculations based on data from the SO SR.

Table 8 Investment and savings (%, current prices)

	2008	2009
Savings ratio[1)]	25.8	19.9
Gross investment ratio[2)]	28.1	20.6
Fixed investment ratio[3)]	24.9	23.6
Coverage of investments by savings[4)]	92.0	96.7

Source: NBS calculations based on data from the SO SR.
1) Ratio of gross domestic savings (GDP less total final consumption) to GDP.
2) Ratio of gross capital formation to GDP.
3) Ratio of gross fixed capital formation to GDP.
4) Ratio of gross savings to gross investments.

the sharpest fall. Fixed capital formation in the household and general government sectors was only slightly down.

In the breakdown by production, only investments in machinery increased on a year-on-year basis, according to revised data from the Statistical Office of the Slovak Republic. The most marked rise under this category was recorded by investments in other machinery and equipment. Investments in transport equipment and in buildings declined in 2009.

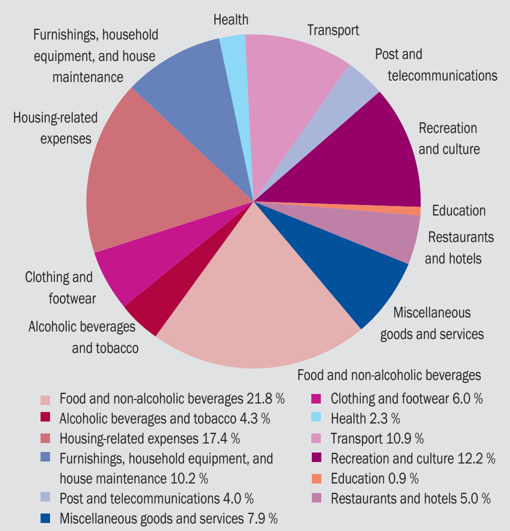
The share of domestic savings in the financing of investment demand increased in 2009. For every euro of gross investment in the economy there were 92.0 cents of gross savings, while in 2008 the figure was 96.7 cents. This difference was the result of gross investments falling more sharply year-on-year in comparison with the decline in savings.

Domestic consumer demand

Final consumption expenditure increased only slightly in 2009 on a year-on-year basis, with most of the additional spending accounted for by general government consumption. The consumption of households and non-profit institutions serving households declined. Growth in general government consumption fell in comparison with 2008, largely due to a slower rise in intermediate consumption. Household final consumption in 2009 fell by 0.7% year-on-year in real terms, while its share of overall GDP rose to 54.1% (from 51.9% the year before). The downturn in private consumption was caused by the deteriorating situation in the labour market (falling employment, slowdown wage growth) related to a slump in manufacturing, as well as to waning consumer confidence. While household consumption was decreasing, the savings ratio was rising.

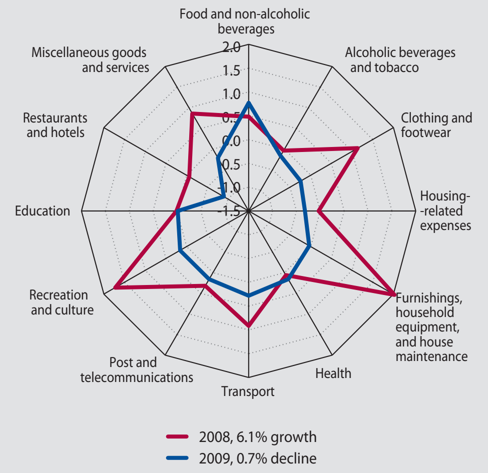
As for the different items of consumption expenditure, spending on food and non-alcoholic drinks accelerated more sharply than the rest, rising by 3.7% year-on-year (compared with 2.2% in 2008). The items on which spending fell included mainly furnishings and housing, recreation and culture, clothing and footwear, restaurants and hotels, and transport. As a percentage of total household consumption, the largest item continued to be food and non-alcoholic beverages (21.8%), followed by spending related to housing

Chart 15 Structure of household final consumption in 2009 (percentage shares)



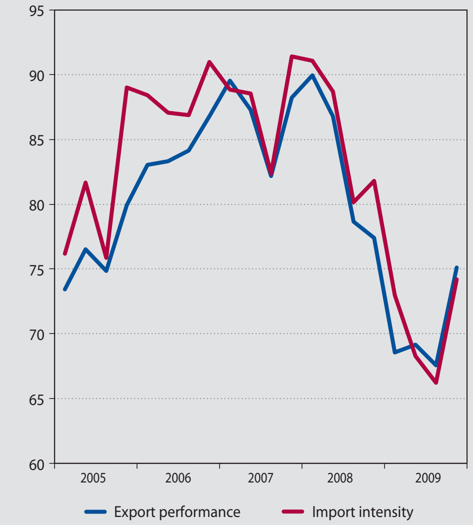
Source: SO SR.

Chart 16 Items of consumption expenditure by contribution to household final consumption growth (p.p.)



Source: NBS calculations based on data from the SO SR.

Chart 17 Export performance and import intensity (%)



Source: SO SR.

(17.4%). The combined share of these two items in total household consumption increased by 0.7 of a percentage point in comparison with 2008.

The year-on-year decline in household final consumption was driven mainly by spending related to restaurants and hotels and to housing, all of which fell as a natural consequence of the crisis.

Exports and imports of goods and services

As a consequence of the downturn in external demand, both exports and imports of goods and services slumped in 2009, with exports down by 20.4% and imports by 22.3% (at current prices). Because the fall in imports was more pronounced (reflecting also destocking and weaker domestic demand), nominal net exports recorded a moderate deficit of €138.6 million (compared to a deficit of €1,512.6 million in 2008). At current prices, exports fell by 16.5% and imports by 17.6%, which resulted in net exports making a positive contribution to GDP (accounting for 0.5 of a percentage point of GDP growth).

The export performance of the Slovak economy in 2009 deteriorated by 12.9 percentage points year-on-year, with exports of goods and services as a share of GDP (at current prices) reaching 70.1%. Import intensity weakened on a year-on-year basis, down to 70.4% (from 85.3% in the previous year).

The openness of the Slovak economy as measured by the ratio of exports and imports of goods and services to nominal GDP represented 140.5%.

Household income and expenditure

The current income[1] of households in 2009 came to €54.8 billion, representing a year-on-year nominal increase of 0.9% (and a real decline of 0.1%), according to preliminary data from the Statistical Office of the Slovak Republic. Compared with 2008, the nominal growth slowed by 9.6 percentage points. Among items of current income, social benefits recorded the sharpest rise (8.5%). The largest item of current income was employee compensation, which declined by 0.8% year-on-year.

As for the current expenditure[2] of households – meaning expenditure paid to other sectors and not used for direct consumption – it rose by 1.2% year-on-year (or by 0.2% in real terms), to reach €15.0 billion. The year-on-year rise in current expenditure represented 12.1%, and it was largely attributable to an increase in social security contributions and other current transfers.

The overall gross disposable income of households in 2009, after deducting current expenditure from current income, amounted to €39.8 billion, representing a year-on-year increase of 0.8% (compared to a rise of 10.0% in 2008). The

1 *Gross mixed household income includes the earnings and incomes of small entrepreneurs, including the value of agricultural products grown by households for own consumption, imputed rents, and contributions of households to the construction of their own homes; Income from property received – interest, dividends, income from rented land, etc.; Other current transfers received – insurance claims paid to households, lottery winnings, etc.*

2 *Income from property paid – loan interest payments made by households and other payments of this type; Other current transfers paid – payments for various types of non-life insurance, life and health insurance; Social security contributions – direct taxes and fees paid to the State budget, contributions paid to health insurance companies, the Social Insurance Agency, and the employment fund, etc.*

Table 9 Generation and use of income in the household sector (EUR; current prices)

	EUR billion		Same period of previous year = 100 in %		Share in %	
	2008	2009	2008/2007	2009/2008	2008	2009
Compensation of employees	25.8	25.6	107.3	99.2	47.4	46.6
of which: Gross wages and salaries	20.0	19.8	105.5	98.9	36.8	36.1
Gross mixed income	16.8	16.7	115.2	99.3	30.9	30.4
Property income – received	1.9	1.9	125.1	101.9	3.5	3.5
Social benefits	7.9	8.6	106.9	108.5	14.6	15.7
Other current transfers – received	2.0	2.1	118.7	104.8	3.6	3.8
Current income – total	54.4	54.8	110.5	100.9	100.0	100.0
Property income – paid	0.9	0.7	107.7	81.2	5.8	4.7
Current taxes on income, property, etc.	2.2	2.1	110.2	96.5	14.9	14.2
Social contributions	9.7	10.0	110.8	103.2	65.1	66.4
Other current transfers – paid	2.1	2.2	122.8	105.0	14.2	14.7
Current expenditure – total	14.8	15.0	112.1	101.2	100.0	100.0
Gross disposable income	39.5	39.8	110.0	100.8	-	-
Adjustment for changes in the net equity of households in pension funds	1.0	0.9	105.2	91.7	-	-
Household final consumption	37.6	37.7	110.9	100.3	-	-
Gross savings of households	2.9	3.1	97.8	103.8	-	-
Gross savings as a share of gross disposable income (%)	7.4	7.7	-	-	-	-

Source: SO SR.

proportion of disposable income used for final consumption was 94.7%; the rest was accounted for by gross savings, which increased by 3.8% year-on-year. The gross savings ratio rose by 0.3 of a percentage point in comparison with the previous year, to 7.7%. Amid uncertainty about labour market developments, households increased their savings despite facing a decline in remuneration (which, under current income, was largely supplemented by payments from the state in the form of social contributions). With household savings rising and household income increasing only slightly, growth in household final consumption slowed considerably.

2.1.3 Labour market

Employment

Employment as defined in the European System of Accounts 1995 (ESA 95) fell in 2009 by 2.4% year-on-year (after rising by 2.8% in 2008), as

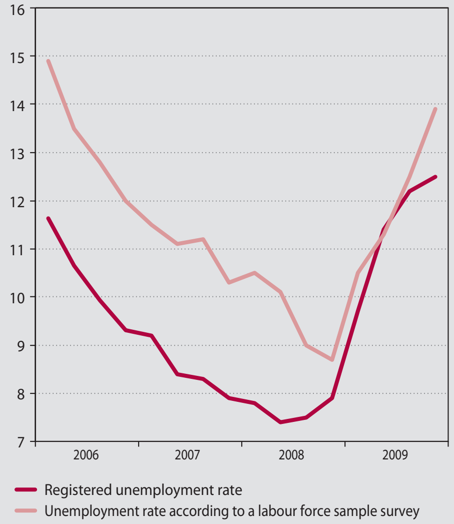
Chart 18 Propensity of households to save and to consume (%)

Source: SO SR, NBS calculations.

a consequence of the downturn in economic activity. Because of the impact of the economic crisis, firms in Slovakia began to cut production and, in an effort to protect jobs, many of them put employees on short time. This was reflected in a sharp fall in the number of hours worked in comparison with the drop in employment (by 6.5%). As the year went on, however, the decline in the number of hours worked became more moderate, and over the last three months it even increased on a quarter-on-quarter basis. Consequently, the number of employees did not fall sharply at the beginning of the year, but rather declined steadily over the course of the year.

In the breakdown of employment by sector, industry recorded the sharpest fall in employment in 2009, and in both agriculture and financial services the level of employment was lower than in the previous year. At the same time, however, employment rose in the sectors of real estate

Chart 19 Unemployment rate (%)



Source: Central Office of Labour, Social Affairs and Family and the SO SR.

Table 10 Labour market indicators

	2008	2009				
	Q1–Q4	Q1	Q2	Q3	Q4	Q1–Q4
Nominal wage (EUR)	723.0	710.5	732.5	722.5	813.2	744.5
Nominal wage (index)	108.1	104.7	102.8	102.5	102.1	103.0
Real wage (index)	103.3	101.7	100.9	101.3	101.6	101.4
Nominal compensation per employee, ESA95 (index)	108.1	106.5	106.4	104.8	102.1	104.7
Real compensation per employee, ESA95 (index)	103.5	103.0	104.9	104.9	102.0	103.5
Labour productivity of GDP (index, current prices)	106.5	95.6	96.4	100.0	102.9	98.7
Labour productivity of GDP (index, constant prices)	103.5	96.9	98.4	100.9	103.2	99.8
Labour productivity of GDP according to ESA 95 (index, current prices)	106.3	93.3	93.7	97.9	101.0	96.5
Labour productivity of GDP according to ESA 95 (index, constant prices)	103.3	94.6	95.7	98.8	101.4	97.7
Employment according to statistical records (index)	102.6	97.3	96.0	94.3	94.4	95.5
Employment based on an LFSS (index)	103.2	99.9	98.9	95.7	94.5	97.2
Employment based on the ESA95 (index)	102.8	99.6	98.7	96.3	96.0	97.6
Registered unemployment rate (%)	7.7	9.7	11.4	12.2	12.5	11.4
Unemployment rate according to an LFSS[1)] (%)	9.6	10.5	11.3	12.5	13.9	12.1
Nominal unit labour costs (ULC)[2]	102.5	112.6	111.1	106.0	100.6	107.6
Consumer prices (average index)	104.6	103.0	101.9	101.2	100.5	101.6

Source: SO SR, and NBS calculations based on data from the SO SR.
1) Labour force sample survey.
2) Ratio of growth in compensation per employee (at current prices) to growth in labour productivity as defined in ESA 95 (at constant prices).

and rental activities, construction, and public services.

The number of persons working abroad continued to fall in 2009, decreasing by 23.0% on a year-on-year basis. Across the domestic economy, the number of employees fell by 4.8% year-on-year, but the number of entrepreneurs increased by 10.7% – largely due to a rise of 12.7% in the number of entrepreneurs without employees.

Unemployment

Unemployment reflected the unfavourable situation in both the domestic and external labour market. According to a labour force sample survey (LFSS), the number of unemployed rose by 25.9% year-on-year and the unemployment rate climbed to 12.1%, an increase of 2.5 percentage points in comparison with the previous year. The rising tendency in unemployment was further confirmed by data on registered unemployment. According to the registers kept by Labour, Social Affairs and Family Offices, the average unemployment rate in 2009 was 11.4%, representing an increase of 3.7 percentage points in comparison with 2008.

Wages and labour productivity

The average nominal monthly wage in 2009 was €744.5, representing an increase of 3.0% in comparison with 2008. Its growth, however, slowed by 5.1 percentage points year-on-year as a result of the economic crisis. The sectors reporting the highest nominal wage growth were administrative services (9.0%), education (7.3%), arts, entertainment and recreation (6.4%), other activities (5.6%), health and social care (5.4%), public administration, defence and social security (5.0%). Sectors in which the average nominal wage growth was lower than in the previous year included accommodation and food service activities, real estate activities, and trade. Industry recorded the largest year-on-year slowdown in average nominal wage growth – 4.3 percentage points – since it was the sector hardest hit by the economic crisis (the average nominal wage in industry rose by 2.6% in 2009).

Real wage growth in 2009 declined by 1.9 percentage points in comparison with 2008, from 3.3% to 1.4%).

Labour productivity based on GDP per employee fell in both nominal and real terms in 2009. This decline was related to the sharp contraction of GDP in 2009. The growth dynamics of real labour productivity lagged behind those of real wage growth by 1.6 percentage points.

Unit labour costs in 2009 increased by 7.6% year-on-year against an annual HICP inflation rate of 0.9%. This represented an acceleration of 5.1 percentage points compared with 2008, the main result being a drop in real labour productivity and a relatively high rise in nominal compensation per employee.

2.1.4 Financial results of corporations

The total profit generated by financial and non-financial corporations in 2009 was €7,352.9 million, according to preliminary data from the Statistical Office of the Slovak Republic. This profit was 18% lower than the figure for 2008, largely because the profits of non-financial corporations slumped by 30.9%. But this unfavourable trend among non-financial corporations was partially offset by financial corporations, which made an

Table 11 Financial results of corporations (EUR billions; current prices)

Profit/loss before tax[1)]	2006	2007	2008	2009	Index 2009/2008
Non-financial and financial corporations – total	8.92	10.86	8.97	7.35	82.0
of which: Non-financial corporations	9.31	10.24	9.53	6.59	69.1
Financial corporations	-0.38	0.61	-0.64	0.77	-
of which: NBS	-1.50	-0.65	-1.23	0.07	-
Financial corporations excluding NBS	1.12	1.26	0.58	0.70	119.1

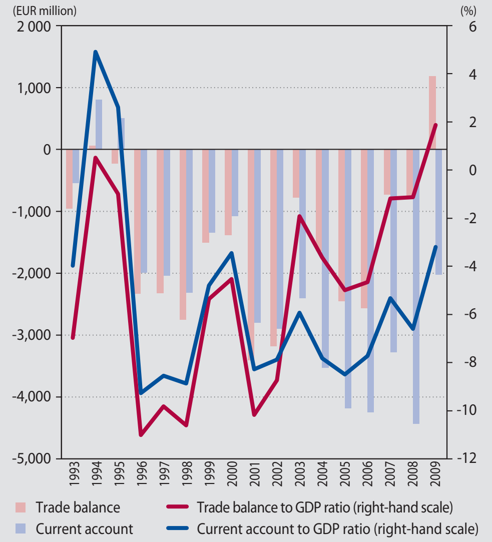
Source: SO SR and NBS.
1) Unaudited financial results.

overall profit for 2009 (compared with a loss for the previous year).

The overall drop in profits of non-financial corporations encompassed lower profits in all sectors except real estate activities, which reported an increase of 14.1% on a year-on-year basis. The sectors in which profits fell most sharply were industry (down by 29.9% year-on-year) and wholesale trade, retail trade and the repair of motor vehicles and motor cycles (41.5%). In the industry sector, the lower profits in manufacturing were to some extent offset by results in the sector of electricity, gas, steam and cold air supply, which reported a year-on-year rise in profit.

Financial corporations made an overall profit of €767.3 million in 2009, compared with a loss of €642.5 million in 2008. This improvement was driven mainly by the results of monetary financial institutions and Národná banka Slovenska. The year-on-year growth in profits of financial corporations not including NBS came to 19.1%. Profits were recorded also by insurance corporations and pension funds and by other financial intermediaries.

Chart 20 Current account and trade balance in 1993-2009 (%)



Source: NBS.

2.2 BALANCE OF PAYMENTS

2.2.1 Current account

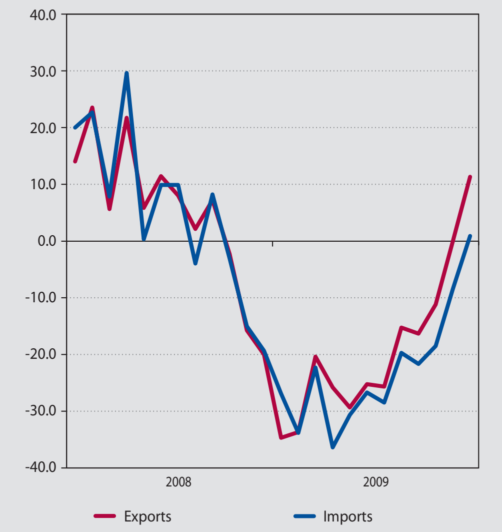
In 2009, the current account deficit of the balance of payments amounted to €2,023.4 million, down by €2,409.0 million in comparison with the previous year. That reduction in the deficit was driven mainly by improvements in the trade balance, income balance and, to a lesser extent, the current transfers balance. By contrast, the services balance performed more poorly than in 2008. The ratio of the current account deficit to GDP (at current prices) fell by 3.4 percentage points on a year-on-year basis, to stand at 3.2%. Deducting dividends and reinvested earnings from the current account, the current account to GDP ratio in 2009 represented 1.4%, compared

Table 12 Balance of payments current account (EUR millions)

	2008	2009
Balance of trade	-757.8	1,186.9
Exports	49,522.3	39,715.6
Imports	50,280.1	38,528.7
Balance of services	-488.0	-1,246.2
Balance of income	-2,293.7	-1,287.9
of which: Investment income	-3,584.9	-2,387.6
of which: Reinvested earnings	-557.7	-498.8
Current transfers	-892.9	-676.2
Current account – total	-4,432.4	-2,023.4
Ratio of current account to GDP (%)	-6.6	-3.2
Ratio of current account (less dividends and reinvested earnings) to GDP (%)	-1.5	1.4

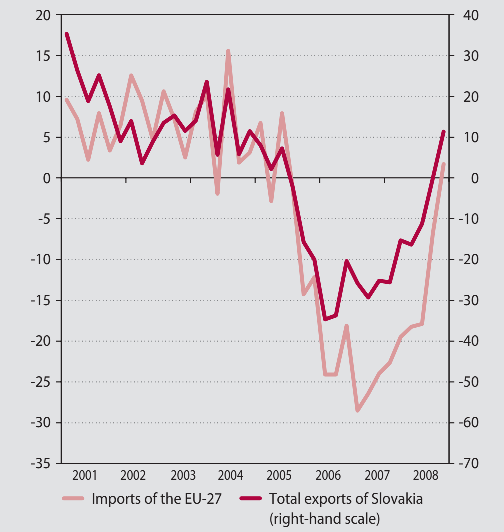
Source: NBS, SO SR (GDP).

Chart 21 Year-on-year dynamics in exports and imports (%)



Source: NBS and the SO SR.

Chart 22 Year-on-year dynamics in exports of Slovakia and imports of the EU-27 (%)



Source: NBS, the SO SR, and Eurostat.

with -1.5% in 2008. Similarly, the trade balance to GDP ratio in 2009 was 1.9%, in contrast to the figure of -1.1% recorded in the previous year. As for how the financial and economic crisis affected the current account in 2009, the volume of exports and imports of goods and services declined and the income balance improved on a year-on-year basis (dividends and reinvested earnings were lower owing to a drop in corporate profits). The adverse effect of the crisis on exports was offset on the imports side by existing import intensity and falling prices of raw materials, as well as by destocking in the economy, lower investment imports and a decline in consumption demand. The combination of these factors resulted in a trade balance surplus. The situation in external demand was the main factor behind the slump in Slovakia's exports, and it had a similar effect in neighbouring countries, which recorded a comparably sharp slowdown in export performance (despite the substantial, temporary weakening of these countries' currencies).

The trade balance recorded a surplus of €1,186.9 million in 2009. Both exports and imports plummeted in comparison with the previous year, with exports down by 19.8% and imports by 23.4%. The year-on-year changes in exports and imports did not follow an even course throughout the year, but rather began with a sharp fall, then declined at a more moderate pace, and finally, towards the end of the year, accelerated sharply into positive figures as external demand gradually began to pick up. The effect of the economic crisis on external demand was reflected in all categories of goods exports. The main factor in reducing the decline in exports towards the year-end was an increase in exports of passenger cars.

Over the twelve months of 2009, the category of exports that recorded the sharpest year-on-year fall was machinery and transport equipment. Almost half of the total decline in exports was accounted for by this category, and in particular by the sub-category of transport equipment (exports of passenger cars). In the sub-category of machinery, exports of automatic data processing machines, shafts, pumps and bearings fell on a year-on-year basis, while the overall decline in exports was partially mitigated at the beginning of the year by exports of television sets. However the positive effect of rising exports among this group of goods largely stemmed from developments in the first four months of the year. From May, exports of television sets were falling on year-on-year basis and for the whole of 2009 they were down by 3.4%. Another category in which exports decreased was chemical products and semi-finished goods. In this case, the decline was mainly due to a year-on-year slump in exports of

Table 13 Year-on-year changes in Slovak exports by segment and the contributions of these segments to the year-on-year change

	Year-on-year change in EUR millions		Contribution to the year-on-year change in p.p.	
	January – December		January – December	
	2008	2009	2008	2009
Raw materials	374.0	-839.2	0.8	-1.7
Chemicals and semi-finished goods	50.3	-3,733.6	0.1	-7.5
of which: Chemical products	-226.3	-726.1	-0.5	-1.5
Semi-finished goods	276.6	-3,007.5	0.6	-6.1
Machinery and transport equipment	1,546.4	-4,716.7	3.3	-9.5
of which: Machinery	1,861.4	-1,735.0	3.9	-3.5
Transport equipment	-314.9	-2,981.6	-0.7	-6.0
Finished products	200.5	-517.2	0.4	-1.0
Exports – total	2,171.3	-9,806.7	4.6	-19.8

Source: NBS.

Table 14 Year-on-year changes in Slovak imports by segment and the contributions of these segments to the year-on-year change

	Year-on-year change in EUR millions		Contribution to the year-on-year change in p.p.	
	January – December		January – December	
	2008	2007	2008	2007
Raw materials	1,391.2	-2,298.3	2.9	-4.6
Chemicals and semi-finished goods	260.0	-3,607.5	0.5	-7.2
of which: Chemical products	4.3	-1,025.0	0.0	-2.0
Semi-finished goods	255.7	-2,582.4	0.5	-5.1
Machinery and transport equipment	-352.4	-4,927.0	-0.7	-9.8
of which: Machinery	-119.1	-3,092.7	-0.2	-6.2
Transport equipment	-233.3	-1,834.3	-0.5	-3.6
Finished products	905.3	-918.6	1.9	-1.8
of which: Agricultural and industrial products	213.4	-171.3	0.4	-0.3
Passenger cars	454.4	-659.4	0.9	-1.3
Machines and electrical Consumer goods	237.5	-87.9	0.5	-0.2
Imports – total	2,204.1	-11,751.3	4.6	-23.4

Source: NBS.

semi-finished goods (especially iron, steel, and products thereof) and to a lesser extent because of lower exports of chemical products (mainly plastics, rubber, and products thereof), which was partially related to developments in the prices of these commodities. The most moderate decline in exports were recorded in the finished products category, in which footwear exports experienced the largest fall. The drop in exports of raw materials was largely attributable to a decrease in exports of refined petroleum oils, with a considerable part of that decline ascribable to price developments. The downturn in goods exports was most marked at the beginning of the year, while the second half of the year saw a gradual acceleration of export growth.

As with exports, the largest year-on-year decline in imports was recorded in machinery and transport equipment, which accounted for almost 42% of the total drop in imports. The downturn in imports was related to the slump in exports, particularly in regard to the fall in imports of components for the automobile industry (under the sub-category of transport equipment). In the machinery sub-category, the year-on-year decline in component imports for the electrical engineering industry was partly caused by lower import intensity in the electrical engineering industry in relation to the domestic production of screens. Another category in which imports fell sharply on a year-on-year basis was chemical products and semi-finished goods. Imports of raw materials (like exports of the same) declined largely because of oil price developments in global markets, which reflected mainly the fall in imports of crude oil. As in the case of exports, the category of imports that recorded the lowest fall was final consumption goods. But whereas the year-on-year decline under this category was more pronounced in the second half of the year, the fall in imports under other categories of goods followed the opposite course – primarily due to a gradual recovery of external demand and a slower decrease in exports.

Trade in services in 2009 produced a higher deficit compared with the previous year. Behind the rise in the services balance deficit lay lower receipts in all three of the principal categories of services. As in previous years, the category of other services (including, for example, telecommunications, construction, insurance, financial, rental, computer engineering, advertising, business, and technical services) recorded a deficit, but in 2009 the deficit increased by €396.3 million on a year-on-year basis. The main causes of this higher deficit in the other services category were a decline in receipts for intermediation services and technical services as well as a sharper fall in receipts for telecommunications services (accompanied by a rise in the respective payments). As for the tourism category of the balance of services, the year-on-year rise in its deficit was the result of receipts for tourism services falling more sharply than the expenditure of Slovak residents on tourism-related services. The downturn in receipts for tourism services was largely attributable to poor winter tourist seasons, and therefore the decline was more pronounced in the first and fourth quarters of the year. In the transport category of the services balance, the surplus decreased on a year-on-year basis mainly due to lower receipts for gas and oil transit (down by €192.6 million) and lower receipts for

Table 15 Balance of services (EUR millions)

	2008	2009
Transport	322.0	95.1
Tourism	305.3	170.4
Other services	-1,115.3	-1,511.6
Balance of services	-488.0	-1,246.2

Source: NBS.

Table 16 Income balance (EUR millions)

	2008	2009
Compensation of employees	1,291.2	1,099.7
Direct investment	-3,126.8	-2,603.1
of which: Reinvested earnings	-557.7	-498.8
Portfolio and other investments	-458.1	215.5
Income balance	-2,293.7	-1,287.9

Source: NBS.

road freight transport services and air passenger transport services, which may have been affected by falls in imports and exports stemming from weak external demand.

The income balance deficit in 2009 improved in comparison with the previous year, since the decline in receipts was far exceeded by the fall in payments – €422.8 million compared with €1,429.9 million. The main deficit-reducing factor was a decrease in dividend payments to foreign investors. In 2009, the profits of enterprises with foreign participation were negatively affected by the financial and economic crisis, and therefore estimates for reinvested earnings were lower. The effect of the crisis on the income balance was also seen in the compensation of employees category, where receipts fell in connection with a decline in the number of Slovak citizens working abroad. Therefore the lower surplus for employee compensation was partially mitigated by the positive effect of the year-on-year improvement in the balance of investment income.

The deficit in the balance of current transfers improved slightly in 2009 in comparison with the previous year. This reflected better figures in the balance of private transfers, in which ex-

Table 17 Balance of current transfers (EUR millions)

	2008	2009
Government	-172.6	-198.2
Other	-720.3	-478.0
Balance of current transfers	-892.9	-676.2

Source: NBS.

Table 18 Capital and financial account of the balance of payments (EUR millions)

	2008	2009
Capital account	806.6	463.9
Direct investment	2,237.3	-346.7
Abroad by Slovak residents	-182.6	-310.9
of which: Equity capital	-156.0	-312.7
Reinvested earnings	-39.8	29.2
In the Slovak economy	2,419.8	-35.8
of which: Equity capital	952.7	839.0
of which: FDI other than privatisation	952.7	839.0
Reinvested earnings	597.5	469.7
Portfolio investment and financial derivatives	1,550.2	-662.1
Abroad by Slovak residents	136.1	-1,494.6
In the Slovak economy	1,414.1	832.5
Other long-term investment	132.8	-846.6
Assets	-454.8	-865.1
Liabilities	587.5	18.5
Short-term investment	1,218.2	4,813.8
Assets	-86.3	-2,189.7
Liabilities	1,304.5	7,003.5
Capital and financial account in total	5,945.0	3,422.3

Source: NBS.

Table 19 Other investment – capital inflows by sector (EUR millions)

	January – December 2008	January – December 2009	Year-on-year changes
Banks	1,797.2	-10,045.2	-11,842.4
Enterprises	-491.2	-56.5	434.7
Government + NBS	45.0	14,068.9	14,023.9
Total	1,351.0	3,967.2	2,616.2

Source: NBS.

penses declined far more sharply than receipts. On the payments side, the steepest falls were in payments related to allowances, sureties and distraints of legal entities, while the largest decrease on the income side was in receipts from non-investment subsidies. The government transfers category of the current transfers balance deteriorated slightly (with payments to the EU budget rising more sharply than receipts from EU funds).

2.2.2 Capital and financial account

The capital and financial account of the balance of payments ended 2009 with a lower surplus compared with end of the previous year. There was also a change in the structure of financial flows: the categories of direct investment and portfolio investment had net outflows in 2009 in contrast to the net inflows they recorded in 2008. The cause of this turnaround was that the outflow of other capital under direct investment and the rise in residents' demand for external debt securities altogether exceeded the year-on-year increase in financial inflows under other investment.

The capital account surplus of the balance of payments declined in 2009 due to a reduced inflow of EU funds through capital transfers. Since the inflow of funds through current transfers rose slightly, capital transfer inflows as a share of total EU fund inflows fell from more than 60% in 2008 to less than 46% in 2009. The overall amount of current and capital transfers in the form of funds received from the EU came to €1,133.6 million in 2009, representing a year-on-year drop of €106.9 million.

The foreign direct investment balance recorded a net outflow of funds from January to December 2009, compared with a net inflow during 2008. This shift in the balance was largely attributable to developments in the other capital category, which, in regard to the commercial activities of enterprises with foreign participation, included an increase in claims and decrease in liabilities vis-à-vis parent undertakings. This may also have been related to the past due repayment of commercial debts to foreign parent undertakings, probably made in connection with the financial and economic crisis. On the assets side, the overall outflow of funds was amplified by the upturn in residents' demand for FDI investment abroad.

The portfolio investment category recorded a net outflow of funds in 2009, in contrast to a net inflow of funds in the previous year. That change was largely the result of rising demand for foreign debt securities among Slovak residents. On the liabilities side, the inflow of funds fell on a year-on-year basis owing to reduced demand for residents' debt securities among non-residents. This decline was only partially offset by a May issue of Eurobonds.

In the other investment category, the net inflow of funds in 2009 was higher compared with 2008. Almost the entire year-on-year change was accounted for by developments in the government and NBS sector, where the inflow of funds outweighed the outflow recorded in the banking sector. The inflow of funds in the government sector stemmed from the central bank's policy implemented after Slovakia joined the euro area. Accordingly, NBS did not use its original foreign reserves to meet liabilities to the banks sector, but instead borrowed funds from the Eurosystem through the TARGET2 system. The outflow of funds in the banks sector was reflected mainly in the year-on-year fall in residents' short-term deposits held with Slovak banks, which in turn was related to the introduction of the euro (the point of keeping accounts in euros ceased to apply) and partially also to the financial crisis. In the enterprises sector, the reduced outflow of funds was largely due to the lower net repayment of import debts.

Table 20 External debt of Slovakia

	USD million		EUR million	
	1.1.2009	31.12.2009	1.1.2009	31.12.2009
Overall external debt of Slovakia	52,815.6	65,314.2	37,491.2	45,338.2
Long-term external debt	25,388.5	27,917.9	18,022.0	19,379.3
Government and NBS[1)]	10,287.1	11,406.9	7,302.3	7,918.1
Commercial banks	3,334.6	3,983.7	2,367.0	2,765.3
Business entities	11,766.8	12,527.3	8,352.7	8,695.9
Short-term external debt	27,427.1	37,396.3	19,469.2	25,958.8
Government and NBS	315.3	21,507.0	223.8	14,929.2
Commercial banks	15,321.6	3,781.7	10,876.1	2,625.1
Business entities	11,790.2	12,107.5	8,369.3	8,404.5
Foreign assets	40,007.8	46,330.0	28,399.6	32,160.2
Net external debt	12,807.8	18,984.1	9,091.6	13,177.9

Source: NBS.
1) Including government agencies and municipalities.
Note: USD/EUR cross rate: 1.4406.

2.2.3 External debt of Slovakia

As at the end of December 2009, Slovakia had a gross external debt of USD 65.3 billion (€45.3 billion), representing a year-on-year increase of USD 12.5 billion or €7.9 billion. The overall long-term external debt rose by USD 2.5 billion year-on-year, and the overall short-term external climbed by USD 10.0 billion. The increase in Slovakia's external debt in 2009 was significantly influenced by movements in the EUR/USD cross rate.

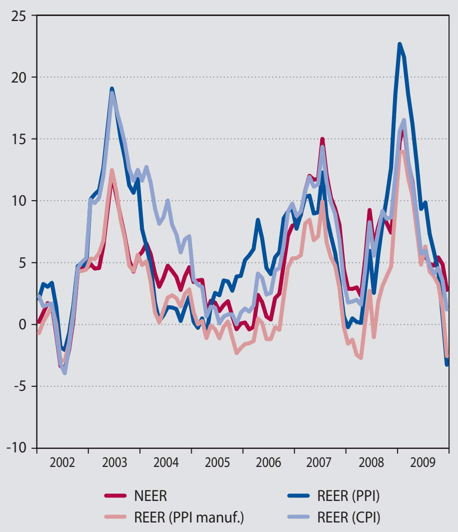
As regards the overall long-term external debt, the external liabilities of the Government and Národná banka Slovenska rose by USD 1.1 billion year-on-year. They were in part driven up by the issuance of external bonds by the Slovak Finance Ministry, at a time when demand among non-residents for Slovak government bonds was falling. The long-term external debt of the commercial sector rose by USD 1.4 billion, while the external debt of commercial banks (comprising mainly borrowings) rose by USD 0.6 billion in total. The external liabilities of business entities went up by USD 0.8 billion, with borrowings accounting for USD 0.6 billion of that rise.

As a consequence of Slovakia joining the euro area in 2009, the structure of the short-term external debt underwent a substantial change, with the component of Národná banka Slovenska's debt rising by USD 21.2 billion year-on-year. Entry into the euro area was also accompanied by a decline in the short-term external debt of commercial banks, which fell by USD 11.5 billion in total. Under the cash and deposits item, deposits fell by USD 9.6 billion as non-residents (mainly parent undertakings) withdrew funds from accounts held with Slovak commercial banks and transferred them to their own accounts abroad. Under the borrowings item, the debt fell by USD 1.9 billion on a year-on-year basis. As for the external debt of business entities, it increased by a modest USD 0.3 billion in comparison with the previous year.

At the per capita level, Slovakia's overall gross external debt amounted to USD 12,141 as at the end of December 2009, compared to USD 9,764 at the end of 2008. As a share of the overall gross external debt, the overall short-term external debt came to 57.3% at the end of December 2009, which compared with the 51.6% reported at the end of December 2008 represented a year-on-year increase of 5.7 percentage points.

The net external debt of Slovakia amounted to USD 19.0 billion (debtor position) as at the end of 2009, representing a year-on-year increase of USD 6.2 billion. That figure was calculated as the difference between, on one hand, the gross external debt of USD 65.3 billion (liabilities of NBS and the Government, commercial banks, and the corporate sector – except for equity participa-

Chart 23 The NEER and REER indices (16 trading partners; annual percentage changes)



Source: NBS.
Note: + appreciation, - depreciation of indices.

tions) and, on the other hand, external assets of USD 46.3 billion (NBS's foreign reserves, foreign assets of commercial banks and the corporate sector – except for equity participations).

According to preliminary data, Slovakia's ratio of gross external debt to GDP (at current prices) was 71.6% as at 31 December 2009, which was 16.2 percentage points higher than the figure for 2008 (55.4%).

2.2.4 Nominal and real effective exchange rate[3]

The average year-on-year appreciation of the nominal effective exchange rate (NEER) index accelerated from 6.3% in 2008 to 8.0% in 2009. Of that figure for 2009, the strengthening of the domestic currency against the euro accounted for 2.1 percentage points, and its appreciation against the Russian rouble and Czech koruna represented another 2.0 percentage points in each case. The contribution of the euro to the rise in the NEER index is a result of the substantial appreciation in 2008 that preceded the fixing of the conversion rate. This is reflected in the year-on-year changes in the effective exchange rate recorded in the first half of 2009.

Along with the faster appreciation of the NEER, the real effective exchange rate (REER) also appreciated more rapidly. The REER index defined according to consumer prices rose to 7.8%, representing an acceleration of 1.8 percentage points in comparison with the previous year. As for the REER index defined according to industrial producer prices, it increased by 4.6 percentage points year-on-year, to reach 10.2%. The REER index defined according to manufacturing output prices averaged 6.4% in 2009, representing an acceleration of 5.0 percentage points year-on-year. The REER indices based on the CPI and industrial output prices appreciated more slowly than the nominal effective exchange rate, the reason being that the inflation rate in the Slovak economy as measured by these indices was lower compared with the weighted average of the country's main foreign trading partners.

2.3 GENERAL GOVERNMENT

In 2009, the general government sector ran a budget deficit of 6.8% of GDP. Since the estimate for the macroeconomic impact of the economic crisis kept being revised, the projected budget deficit was adjusted several times.[4] The revised deficit projections took into account only the negative effect of the crisis on the income side of the general government budget, without considering any expenditure-reducing effects.

Table 21 General government deficit projection for 2009

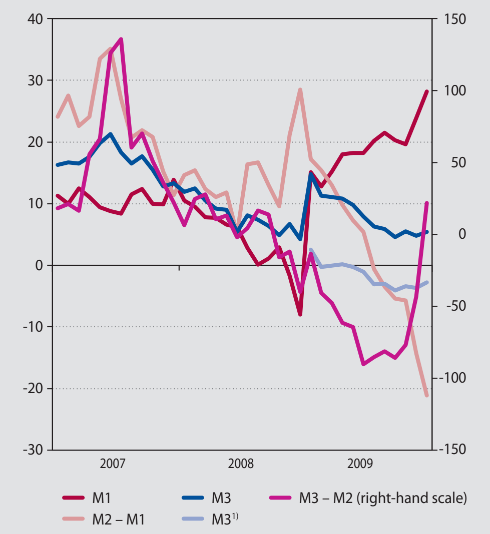
	General government budget 2009 – 2011		Revised projection (10/2009)	Actual data for 2009
	Approved (10/2008)	Revised (11/2008)		
Deficit (%GDP)	1.7	2.1	6.3	6.8
GDP growth at current prices (%; current prices)	11.3	9.2	-5.4	-5.8
GDP estimate (EUR million)	74,839	73,400	63,600	63,332

Source: Ministry of Finance of the Slovak Republic and NBS calculations.

3 *NEER and REER indices are compiled according to the IMF methodology. Monthly averages of domestic currency exchange rates against the currencies of main trading partners are used. The methodology is based on CPI, PPI, PPI-manufacturing, 1999 base year and 16 significant trading partners of the Slovak Republic representing approximately 86 to 89 % of Slovak foreign trade turnover in 1993 – 2004: Germany, Czech Republic, Italy, Austria, France, Netherlands, United States, United Kingdom, Switzerland, Poland, Hungary, Ukraine, Russia, Japan, China and Turkey.*

4 *The last projection for the general government budget assumed a deficit of 6.3% GDP.*

Chart 24 Year-on-year changes in M3 components (%)



Source: NBS.
1) M3 for analytical purposes (adjusted for the effect of currency in circulation).

All sectors of the general government ran budget deficits in 2009, but it was central government, with a budget deficit equivalent to 5.7% of GDP, that accounted for the largest share of the overall general government deficit.

Funds received from the European Union in 2009 amounted to 57.4% of the budgeted figure.

General government gross debt as a share of GDP represented 35.7% in 2009.

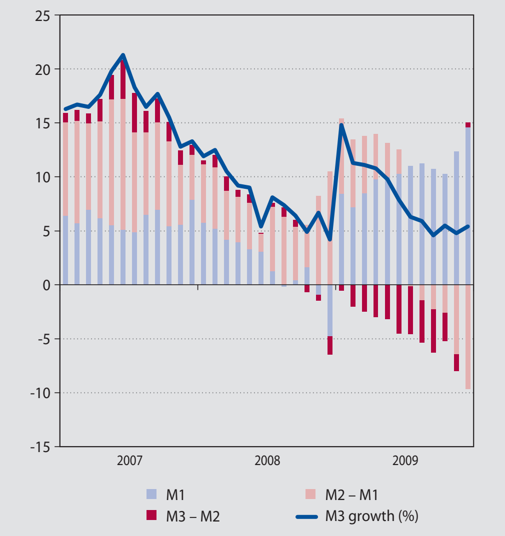
With Slovakia projecting that its general government deficit for 2009 would be above the reference value set in the EU Treaty, the European Commission adopted a report under Article 104(3) of the EU Treaty for Slovakia on 7 October 2009. On the basis of the EC's recommendation in that report, the European Council opened an excessive deficit procedure for Slovakia on 2 December 2009.

Table 22 Main components of the M3 aggregate and its counterparts in 2008 and 2009

	Annual change in EUR billions		Annual change in %		Volume (EUR billion)
	2008[1)]	2009[1)]	2008[1)]	2009[1)]	as at 31.12.2009
Currency in circulation	-3.193	5.557	-69.1	389.4	6.984
Overnight deposits	1.499	-0.175	9.5	-0.9	17.494
M1	-1.695	5.382	-8.0	28.2	24.478
Deposits and received loans with an agreed maturity of up to 2 years	3.743	-3.936	29.4	-23.7	12.676
M2	2.028	1.811	6.2	5.1	37.821
M3 monetary aggregate	1.421	1.960	4.2	5.4	38.872
M3 counterparts					
MFI claims and securities	4.442	0.185	10.7	0.4	46.134
of which: General government	0.357	-1.290	1.0	-9.9	13.793
Other residents	4.085	1.475	15.7	4.9	32.341
Net foreign assets	-3.413	4.325	-75.2	398.7	5.302
Long-term financial liabilities (excluding capital and reserves)	-0.334	-0.920	-29.2	-113.9	-0.112
Net other items (including capital and reserves)[2)]	0.058	-3.470	-0.6	37.7	-12.676

1) Data for 2008 are calculated using the ECB's methodology, with Slovakia representing a notional member of the euro area. Since monetary aggregates and counterparts of the M3 (under the ECB methodology) are not evaluated as at 1 January of the given year, the values recorded as at 31 December of the previous year are used in the table and the further text as initial values for the year.
2) Net other items include central government deposits; net other items = fixed assets + other assets – capital, reserves and provisions – other liabilities – surplus liabilities between MFIs – deposits and loans received from the general government sector. At the same time, there is balance sheet equilibrium, where M3 = claims on general government + claims on other residents + net foreign assets – long-term financial liabilities + other net items.

Chart 25 Contributions of components to M3 growth (p.p.; %)



Source: NBS.

2.4 MONETARY DEVELOPMENTS

2.4.1 Monetary aggregates

The contribution of domestic monetary financial institutions (MFIs) to the euro area's M3 monetary aggregate amounted to €38.9 billion in 2009, representing a year-on-year increase of almost €2 billion (compared with a rise of €1.7 billion in 2008). However, the year-on-year rate of M3 growth showed a falling trend during 2009 and ended the year at 5.4%. Owing to a change in the reporting methodology for currency in circulation[5], the annual changes in M3 were overestimated from January 2009. Without this change, the annual growth trend would have been the same, only at a lower level (as of December at -2.8%).

Main components of M3

Growth in the M3 monetary aggregate was driven mainly by currency in circulation, which increased in amount as a result of the euro changeover. M3 components that declined during the year included current account deposits and deposits with an agreed maturity of up to 2 years. This development stemmed from the yield curve slope, with interest rates on the shortest maturities declining to very low levels. There was thus a prevailing tendency to shift deposits from M3 to higher-yielding deposit products outside M3. Investments in money market fund shares/units recorded a slight rise in 2009. The year-on-year growth in M1 accelerated during the period under review (due to a rise in currency in circulation) and therefore contributed to the growth in the overall M3 monetary aggregate. As for the contribution of less liquid deposits (M2-M1), it was positive at the beginning of the year and turned negative towards the year-end. This was because of the sharp rise in these deposits which occurred towards the end of 2008 ahead of the introduction of the euro, and which was followed by their decline in the second half of 2009. The contribution of marketable instruments (M3-M2) was volatile during 2009. In the first six months, the negative contribution became more pronounced, but then it decelerated and, in December, broke into positive territory.

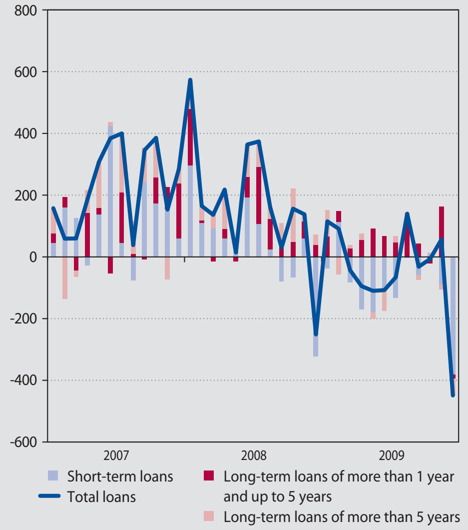
At the sectoral level, the development of deposits was very similar in the case of non-financial corporations and households. The amount of deposits taken from each sector declined during the period under review, but those taken from non-financial corporations fell the most. The slump in economic activity and the associated drop in corporate sales had the effect of reducing current account deposits and also short-term deposits with an agreed maturity. Household deposits decreased and the structure of deposits also underwent a substantial change. On the one hand, overnight deposits and deposits with an agreed maturity of up to 3 months increased, while, on the other hand, deposits with an agreed maturity of up to 2 years declined. In searching for higher yields, households invested in deposits outside M3 (deposits with an agreed maturity of more than 2 years and investment funds).

MFI loans to the private sector

In 2009, the loans of monetary financial institution to the private sector (loans and securities) amounted to €32.3 billion. That represented an increase of €1.5 billion year-on-year, which was far lower than the annual rise reported in 2008 (€4.1 billion). The breakdown of the growth in loans also differed from the previous year. In 2008, the amount of loans increased and the amount of securities fell, but in 2009 securities increased by a substantial margin while loans rose slightly. Households accounted for the largest share of the rise in loans to the private sector, with loans to households recording a rise of €1.3 billion in 2009 (compared with €2.5 billion in 2008). Loans to non-financial corporations declined by around €0.5 billion over the whole of 2009 (whereas in 2008 they

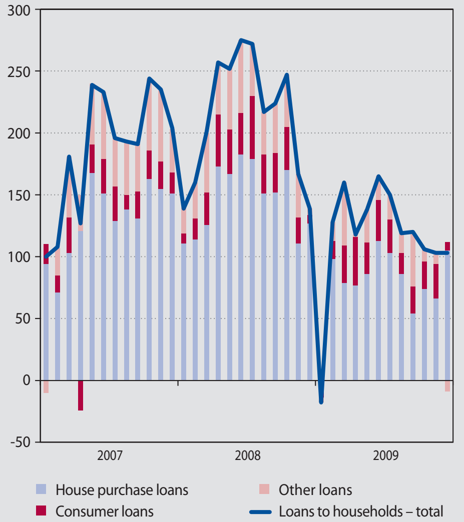
5 *„Currency in circulation" does not correspond to the actual volume of currency in circulation, but to Slovakia's banknote allocation key. This was higher than the actual volume of currency in circulation, and therefore NBS published also the M3 figures for analytical purposes.*

Chart 26 Year-on-year changes in loans to non-financial companies (EUR millions)



Source: NBS.

Chart 27 Year-on-year changes in loans to households (EUR millions)



Source: NBS.

increased by €2.0 billion). Over the whole of 2009, year-on-year growth of loans to the private decelerated, and as of end of December stood at 4.9% (or 1.1% excluding securities). The overall slower growth in loans reflected the effects of the economic crisis, which included both lower borrowing demand and a reduction in bank lending. This was confirmed by the results of the Bank Lending Survey in 2009. During the year, banks tightened credit standards by imposing higher margins, raising the requirements for collateral, and requiring borrowers to have higher amounts of own funds. The survey indicates also that due to lower economic activity, enterprises were not demanding additional funds.

Loans to non-financial corporations

For almost the whole of 2009, lending to non-financial companies had a prevailing downward trend due to the economic crisis. The slump in sales and new orders was adversely affecting the economic performance of enterprises. Banks were more cautious in providing new loans and they also cut back short-term lending through credit lines and current account overdrafts. On a month-on-month basis, the amount of such lending declined for most of the year. Thriving enterprises sought to take advantage of the relatively low interest rates (compared with 2008, they were 200 basis points lower on average) and secure cheaper funding for themselves. Thus demand among firms for longer-term loans increased in 2009, by almost €0.7 billion. The decline in the outstanding amount of loans to non-financial corporations was also reflected in the year-on-year comparison, according to which lending slowed throughout 2009 and ended in December at negative value of 3.3%. The year-on-year lending growth decelerated by almost 19 percentage points in comparison with December 2008.

Loans to households

Unlike loans to non-financial corporations, the outstanding amount of loans to households increased slightly over the whole of 2009, although the month-on-month increments were lower than in 2008. With the economic crisis bringing higher unemployment and greater uncertainty about future developments, households were less willing to borrow. Another factor was the falling trend in property prices, which is having a significant effect on lending growth. The supply of bank lending under tighter lending standards was also a drag on lending growth. Although the outstanding amount of loans increased over the year as a whole, lending growth on a year-on-year basis slowed. In December 2009, lending growth stood at 11.0% year-on-year, which was 14.3 percentage points lower than the growth reported at the end of 2008. A drop in lending growth was recorded for all types of loans.

Table 23 Cumulative net/sales of open-end investment funds in Slovakia (EUR millions)

	2008	2009
OIF shares/units in Slovakia[1)]	-975.7	110.9
Non-money market OIF shares/units	-422.1	7.7
Money market OIF shares/unit	-553.6	103.2

Source: Slovak Association of Asset Management Companies (SASS), based on data reported by its members.
1) Denominated in the domestic currency (EUR as from 2009, or SKK until the end of 2008, converted according to the conversion rate of 30.1260 SKK/EUR) and in foreign currencies in total, not including special funds for institutional investors.

Lending to households increased in nominal terms in 2009, resulting in a rise in household indebtedness as measured by the ratio of household bank loans to nominal GDP. The ratio went up substantially, from 18.8% in 2008 to 22% in 2009 (by 3.3 percentage points), the main factor being the fall in nominal GDP alongside a modest rise in the amount of lending.

Investment in open-end investment funds (OIFs)
In the first half of 2009, the global financial crisis was adversely affecting most investment fund categories (except for equity funds and real-estate special funds), which reported an outflow of funds and unfavourable results. In the second half of the year, however, the collective investment sector was already beginning to regain the confidence of investors. For 2009 as a whole, all categories of resident investment funds, whether denominated in the domestic currency or a foreign currency, achieved total positive net sales in the overall amount of €110.9 million[6], which in comparison with 2008 represented a considerable turnaround.

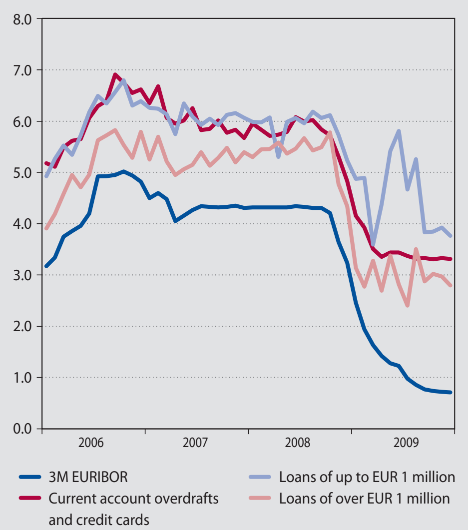
The category breakdown of 2009 net sales shows that money market funds had by far the highest positive net sales (€103.2 million), further confirming that Slovak investors remain strongly conservative. Other fund categories achieved net sales of €7.7 million in total, including, on one hand, positive net sales of equity funds (€44.0 million), mixed funds (€39.0 million), real-estate special funds (€21.4 million) and bond funds (€13.8 million), and, on the other hand, negative net sales of other/secured funds (€-57.6 million) and funds of funds (€-52.9 million).

2.4.2 Claims of leasing companies and hire-purchase companies

The overall claims of leasing, factoring, and hire purchase companies on the private sector amounted to €4,203.9 million as at the end of 2009, which represented a drop of €693.1 million in comparison with the previous year. In their year-on-year dynamics, these claims continued a declining growth trend that began in 2008, and from the second quarter until the end of 2009 they were falling year-on-year. As at the end of 2009, they were down by 14.2% compared with the end of 2008 (by contrast, the year-end figure for 2008 showed an annual rise of 18.2%). The main component of this decline was claims related to financial leasing.

Claims fell in all sectors in 2009, but the most marked decline was recorded by claims on financial corporations. These decreased by 53.8 %, driven mainly by *other claims*[7]. As at the end of 2009, claims of leasing, factoring, and hire-purchase companies on non-financial corporations were lower by 16.8% year-on-year and claims on

Chart 28 Interest rates on loans to non-financial corporations (%)

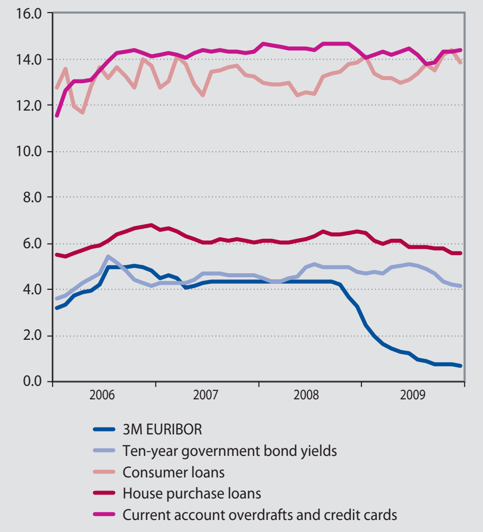


Source: NBS.

6 *The different amounts of monthly and cumulative net sales can be explained by the fact that the data of the Slovak Association of Asset Management Companies (SASS) obtained from regular weekly statistical reports and the data of individual OIFs (www.openiazoch.sk) sometimes refer to different periods (SASS releases data on Fridays, but some of its members release data on Thursdays) and the number of investment funds is recorded differently. Owing to the merging of investment funds and the redenomination of investment funds into euros at the end of 2008, the number of investment funds fell (from around 550 to 460) while number of them denominated in domestic euro currency soared and number denominated in a foreign currency decreased. The high volatility in the number of funds continued during the course of 2009, ranging from more than 570 in June to less than 500 at the year-end.*

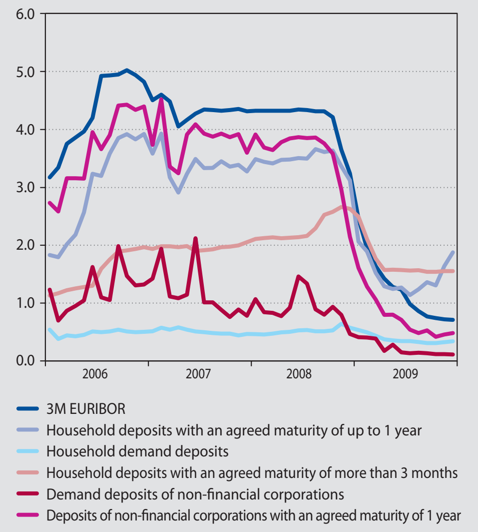
7 *In terms of their purpose, the claims of leasing, factoring, and hire-purchase companies on the private sector are divided into finance lease claims and other claims. The other claims category is further divided into hire-purchase claims and consumer credit claims.*

Chart 29 Interest rates on loans to households (%)



Source: NBS.

Chart 30 Deposit rates (%)



Source: NBS.

households were down by 6.9%. In each of these sectors, the principal determinant of developments was lease-related claims.

2.4.3 Interest rates

During 2009, the ECB cut its key rates on four occasions, by a total of 150 basis points. Together with other monetary policy measures (long-term tenders with full allotment; the covered bond purchase programme; extending the set of eligible collateral), the ECB managed to reduce market interest rates by a substantial margin in order to support the euro area economy. By the end of 2009, the shortest market rates – the overnight rate EONIA and 3-M EURIBOR – stood at 0.35% and 0.71%, respectively. This development also affected retail interest rates in Slovakia, which were mostly being cut during the year. Nevertheless, risk perception of banks increased due to negative macroeconomic situation which counteracted against more pronounced drop in retail interest rates.

Interest rates on loans to non-financial corporations

Interest rates on loans to non-financial corporations fell sharply in the first four months. This development mirrored the relatively substantial decline in market rates. In following periods, however, customer rates developed differently depending on the loan amount. A combination of the higher perception of risk and worsening economic performance, as well as the outlook for further development, were reflected in a relatively sharp increase in bank lending costs for small and medium-sized enterprises (loans of up to €1 million). In the last four months of the year, interest rates for these enterprises returned to the lowest level recorded in March 2009. Interest rates on loans to large corporations of more than €1 million fluctuated at around 3%. The most stable development was seen in interest charged on current account overdrafts, which after falling on the first quarter of 2009 remained at around 3.3% for the rest of the year.

Interest rates on loans to households

Lending rates to households remained considerably rigid throughout 2009 and they did not reflect the reduction in market rates. In the case of interest on house purchase loans, a very slight downward trend was discernible all through the year. Banks were cautious in reducing interest rates on these long-term loans, since yields of a comparable maturity (10-year government bonds) did not decline by a greater margin. As for interest rates on consumption loans, they did not react at all to the decrease in market rates. Interest rates on these types of loans remains high, at around 13% – 14% or almost twice the euro area level. One of the contributing factors to this development may have been the rising rate of unemployment. Interest rates on current account overdrafts maintained a stable course throughout 2009. Meanwhile, interest rates on loans to self-employed persons were relatively volatile, ranging from 4% – 7%.

Interest rates on deposits from non-financial corporations and households

Interest rates on deposit products for non-financial corporations and households fell sharply at the beginning of 2009 and then stabilised over the rest of the year. In the case of deposit rates for non-financial corporations, the reduction in key rates and then in market rates was passed on to them immediately and in full. Banks cut lending rates for all maturities. From the second quarter, deposit rates for non-financial corporations remained unchanged. The largest year-on-year fall in interest rates was recorded for term deposits with longer maturities. In the household sector, development was very similar to those in the non-financial corporation sector. At the beginning of the year, interest rates fell sharply, and then later they stabilised. One exception was deposits with an agreed maturity of up to 1 year, which recorded a modest rise in interest rates towards the year end, largely because of the expiration of deposits with agreed maturity of 1 year. In seeking to retain customer deposits, banks offered higher returns on them. This development was also a response to the calming of financial markets, which offer higher yields on many investment products. Banks therefore sought to maintain relatively cheap deposit funds.