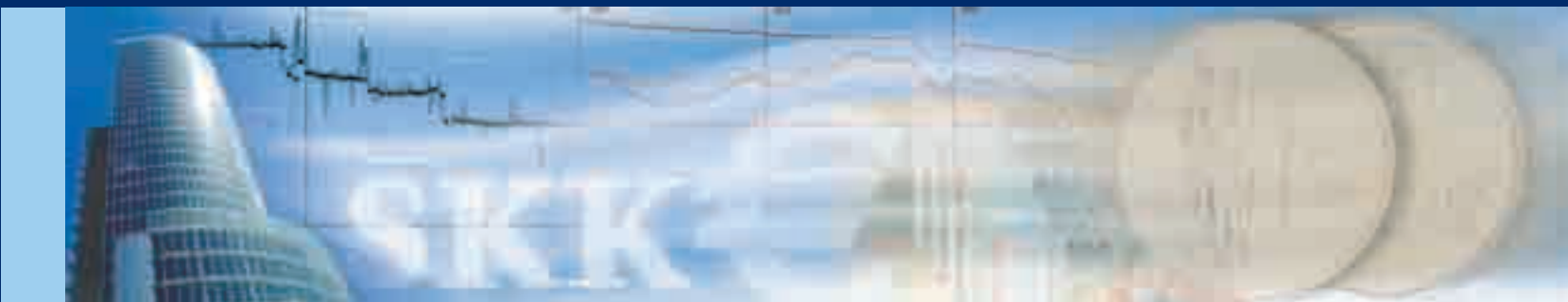




NÁRODNÁ BANKA SLOVENSKA



Annual Report

2007



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Foreword



Foreword

When assessing the previous year, it could be in a word most precisely characterized as “dynamic”. The year 2007 was dynamic not only from the point of view of the economic and monetary developments in Slovakia, but also from the point of view of activities performed within the bank. The increased activity at almost all levels was often related directly or indirectly to the forthcoming introduction of the euro.

Economic growth measured by GDP at constant prices reached record-breaking 10.4% at the year-end. The extension of production capacities and production activities, mainly in the automobile and electrotechnical industry, was reflected in the growing export performance of the economy. The overall structure of economic growth was balanced, and influenced both by foreign and domestic demand. The ongoing strong economic growth supported by the labour productivity growth was reflected in wage and employment growth, in a drop of the number of unemployed and an improvement of the financial performance of corporations.



In the first half of 2007, a gradual slowdown in the year-on-year inflation in Slovakia was observed. In the second half-year the trend changed, mainly as a result of growing prices of food products and energy commodities in the world markets. At the end of 2007, inflation measured by the harmonized index of consumer prices reached 2.5%. Despite the year-on-year drop of inflation by 1.2 percentage points, the NBS inflation target set for the end of 2007 was not met. External cost factors, which constitute exceptions from meeting the inflation target set in advance, exerted a crucial influence on price level development.

Mitigation of inflation risks in the first half-year of 2007 made it possible to gradually ease monetary policy and to reduce key interest rates. Over the course of the first half-year, NBS reduced its base interest rate in two steps (in total by 0.5 percentage points) to 4.25%.

The exchange rate policy was conducted within the ERM II mechanism. Since the entry into the ERM II, the Slovak koruna exchange rate has been gradually appreciating, influenced by the equilibrium shift in economic fundamentals. With effect from 19 March 2007, the central parity of the koruna vis-à-vis the euro was revalued to 1 euro = 35.4424 SKK. Immediately after revaluing the central parity the Slovak koruna appreciated again, this time, however, particularly in connection with market expectations regarding the euro introduction and setting the conversion rate. For this reason, in March and April, NBS intervened three times in the form of direct foreign exchange interventions against excessive volatility of the Slovak koruna's exchange rate.

Favourable economic developments supported meeting the Maastricht criteria set for the euro introduction. Estimates of developments for the following years indicate that the criteria have been met in a sustainable manner, and Slovakia is prepared to introduce the euro on 1 January 2009.

With the approaching date of expected Slovakia's joining the euro area, preparations for the euro introduction escalated gradually at all levels during 2007. An important step was the preparation and adoption of the Act on the euro introduction in the Slovak Republic and amending and supplementing certain acts (Act No. 459/2007 Coll.). This so called General Act constitutes the basic legal framework for the euro introduction in Slovakia and develops conditions for a continuous and smooth changeover from the Slovak koruna to the euro.



As follows from the report on performing the National Euro Changeover Plan for the SR for 2007, the most significant progress in completing the planned tasks was achieved mainly in the area of preparations of the information campaign, preparations for the frontloading of euro cash and preparations of public administration organizations. It is gratifying for NBS that the first two areas are under the responsibility of the working committees coordinated by Národná banka Slovenska.

Along with the tasks performed within the working committees, NBS completed a number of other tasks in 2007, specified by the Internal Euro Changeover Plan of NBS. NBS monitored and controlled the preparation of banking and financial institutions for the introduction of the euro, and, as a part of this, NBS prepared an analysis of possible effects of the euro changeover on the Slovak financial market. The euro changeover in Slovakia will influence the performance of monetary policy, administration of foreign exchange reserves, as well as reporting. NBS analysed these areas and prepared draft procedures for harmonising the procedures, statistical data and application software with the ECB. NBS hosted professional seminars on the euro changeover and organised travelling exhibitions on the Slovak sides of euro coins in several regional towns. In addition, NBS has continuously provided training for banking and other employees in relation to the euro introduction.

A significant legislative change in the financial sector was the transposition of Directive No. 2004/39/EC of the European Parliament and of the Council on markets in financial instruments (the so called MiFID Directive) into the legal framework of the Slovak Republic. Implementation of the MiFID Directive in Act No. 209/2007 Coll. led to an alteration of conditions for conducting investment services, auxiliary services and investment activities of securities dealers. It laid down requirements for the notification of transactions in financial instruments, and made the organizational rules for securities dealers and the measures for investor protection stricter.

Looking at the future, in particular tasks and challenges related to the changeover of the Slovak koruna to the euro will be of top priority: the dual display of prices, the conversion of prices, the conversion of bookkeeping, employee education and training, and informing partners and customers. This is only a brief overview of tasks the majority of entities in the business sector and public administration will have to ensure. Demanding work related to the adoption of the ECB common monetary policy awaits Národná banka Slovenska. Some of its competences will be passed to the ECB; nevertheless, in the future, the majority of them will be conducted in cooperation with NBS. However, monetary policy will no longer react to individual developments in Slovakia, for it will take into account developments in all countries of the euro area. Therefore, consistent conduct of supporting policies aimed mainly at increasing flexibility of the economy is a challenge, so that Slovakia will be able to cope with any possible shocks without the assistance of its own monetary policy.

Ivan Šramko
Governor

May 2008

External Economic Environment



1 External Economic Environment

1.1 Global trends in output and prices

The year-on-year growth of the world economy slowed down slightly to 4.9% in 2007 compared to 5.0% in 2006. Nevertheless, the global economic growth remained quite robust. A favourable development of the global economy was recorded particularly in the first half of 2007. The second half of the year was negatively affected by the financial market turmoil and by unfavourable prospects for the development of the US economy. The financial tension, which was associated with the development in the US real estate sector, resulted in a sudden shortage of liquidity in financial markets and increased risk aversion. Risk reassessment and a shift from risky assets to secure assets came to the fore. This activity was accompanied by an increased volatility on the financial markets and by fears of a more considerable pass-through of this turmoil into the global growth. The financial turbulences have primarily affected financial institutions; the effect on non-financial institutions was not significant. The crisis also did not have a strong impact on global economic growth, except for a short-term market volatility and fluctuations in the development of exchange rates. Strong economic activity in the emerging economies constituted a dampening factor hindering a more considerable

deepening of the impact of the financial turmoil on the world economy.

Another factor having dampened the world economy growth at the end of 2007 was a slowdown of the US economy and fears of its subsequent pass-through to the global economy. The impact of the economic slowdown in the United States on the global economy, however, has ultimately not been as strong as expected.

As a result of the slowdown of global economic activity, the growth rate of foreign trade decreased in 2007, with year-on-year growth reaching 6.6% as compared to 9.2% in 2006. The slowdown of foreign trade between developed economies has been compensated for by the growth of trade between the emerging economies, above all by mutual intraregional trade of South East Asia countries.

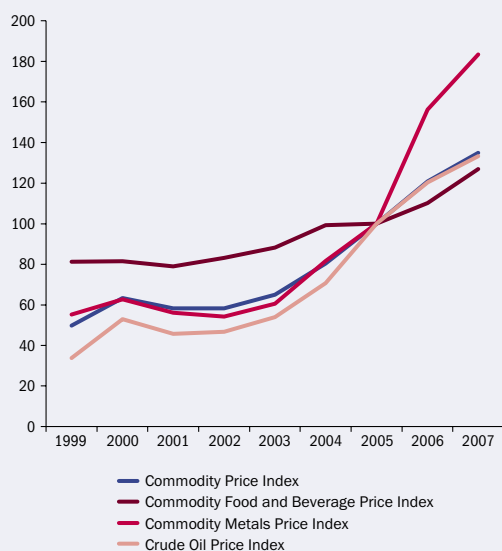
The price development in the first half of 2007 was stabilized and inflation remained at relatively low levels. In the second half of 2007, the growth rate of inflation accelerated as a result of high prices of oil and agricultural commodities. The average annual inflation for 2007 reached 3.9% against 3.4% in 2006. The year-on-year change in the price level at the end of 2007 reached 4.8% against 3.5% in 2006.

Table 1 **World output**

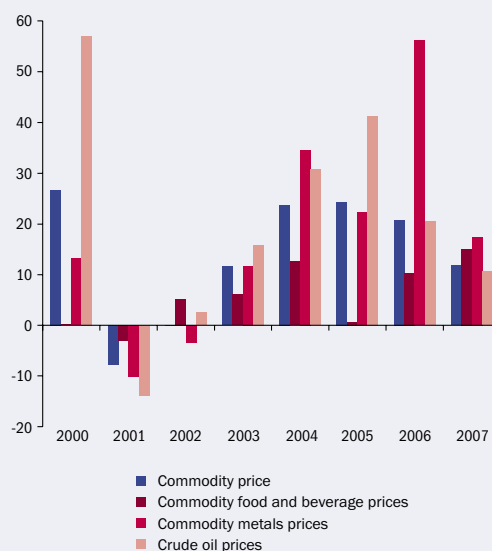
(year-on-year growth in %)

	2005	2006	2007
World	4.4	5.0	4.9
Advanced economies	2.6	3.0	2.7
United States	3.1	2.9	2.2
Japan	1.9	2.4	2.1
Euro area	1.6	2.8	2.6
Emerging Asian economies	9.0	9.6	9.7
China	10.4	11.1	11.4
India	9.1	9.7	9.2
Russia	6.4	7.4	8.1
Central and Latin America	4.6	5.5	5.6
Brazil	3.2	3.8	5.4
Middle East	5.7	5.8	5.8

Sources: World Economic Outlook, IMF, January 2008, Eurostat.

**Chart 1 Price development**
(prices in USD; index, year 2005 = 100)

Sources: World Economic Outlook, IMF, April 2008.

Chart 2 Year-on-year changes in commodity prices (%)

Sources: World Economic Outlook, IMF, April 2008.

During 2007, oil prices were permanently growing, mainly in the second half of the year, when the year-on-year oil price growth rate was accelerating. In comparison with the beginning of the year, the oil price increased by 56.9% at the end of 2007 and reached its maximum value of 95.55 USD/barrel in November. The average oil price in 2007 was 72.80 USD/barrel. Compared to the average price in 2006, when the average reached 66.30 USD/barrel, it increased by 9.8%. The demand for oil in OECD countries fell as a result of the high oil prices. This fall was compensated for by a demand growth in the emerging economies. Despite higher income of the oil countries and new investments in the oil industries, the extraction and refining capacities remain limited. This factor, as well as global tensions, the dollar depreciation, activities of speculative investors and hedge funds, continue to keep oil prices at high levels.

In the first half of 2007, the prices of metals and nonferrous metals recorded a considerable growth, primarily as a result of strong demand in the emerging Asian economies, as well as due to low processing capacities of industrial metals. In the second half of the year, however, their year-on-year growth rate decreased. Nevertheless, the prices of industrial metals showed the highest year-on-year price growth rate among commodities in 2007.

The negative price development in the second half of the year was considerably driven by the prices of agricultural and food commodities. The prices were growing as a result of strong demand on the part of Asian emerging economies. Another negative factor

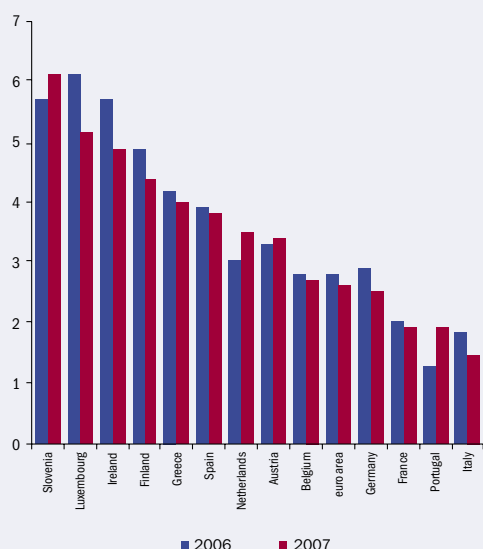
affecting the price development was an increased bio fuels production, which primarily had an impact on the growth of cereal prices. Unfavourable climatic conditions have caused crop failures of agricultural commodities and thereby also lower crops than expected, implying a pressure on price increases. The price growth of agricultural commodities was considerably promoted by historically high oil prices, which have caused the cost for agricultural producers to increase. The year-on-year change in the prices of agricultural commodities recorded a 15% growth in 2007.

The development of exchange rates in the world was characterized by a continuing euro appreciation against the US dollar, Japanese yen, pound sterling and the Swiss franc. The euro achieved the highest appreciation against the US dollar. The development of foreign exchange rates in the first half of 2007 was influenced primarily by a weak economic development in the United States and by expectations of changes in the US and euro area interest rates. The development of foreign exchange rates in the second half of 2007 was considerably influenced by the financial market turbulences.

1.2 Economic development in the euro area

In 2007 the economic growth in the euro area slightly slowed down to 2.6% from its level in 2006 (2.8%). This development was influenced by the one-off impact of the VAT increase in Germany, as well as by

Chart 3 GDP growth in euro area countries (%)



Source: Eurostat.

Chart 4 Changes in the economic growth rate in 2007 compared to 2006 (p.p.)



Source: Eurostat.

a negative impact of higher food and energy prices on the level of the disposable income of households and consumer confidence. The development of inflation, as well the money market turmoil contributed to a deterioration of consumer expectations in the second half of 2007. Despite the growing uncertainty in the second half of 2007, the euro area economy achieved relatively favourable results. In December 2007, unemployment fell considerably to 7.2% (it reached 7.8% in December 2006) and was at historically lowest levels.

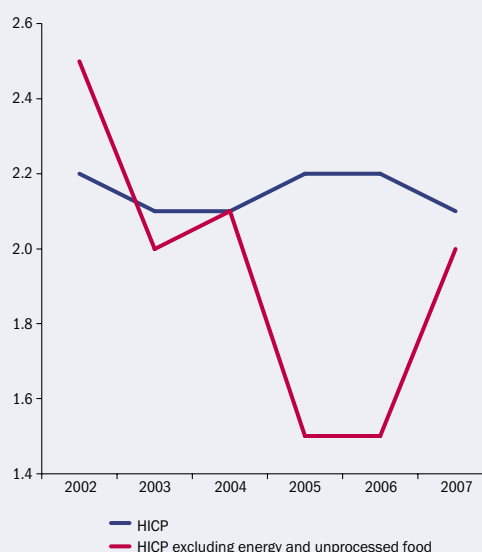
Overall average HICP inflation in 2007 reached 2.1%, i.e. 0.1 of a percentage point less than in the previous two years. The average of 2007, however, is the result of two different development trends. In general, the year-on-year rate of inflation was stable at a level below 2% till the end of the summer. Its level increased slightly in September 2007 – for the first time since August 2006 – and it kept growing up to 3.1% (in November and December 2007).

In 2007, inflation was to a great extent determined by a strong increase in the energy and food prices. The oil price increase at the beginning of 2007 and its influence on energy prices was reduced by the base effect till the end of August 2007. However, subsequently, the conjunction of the oil price increase and the unfavourable base effect caused a substantial increase in the level of the overall HICP. The contribution of prices of unprocessed food to growth of consumer prices was higher all over 2007. Prices of processed food started to rise from the late summer and they contributed to a higher inflation during the last months of the year.

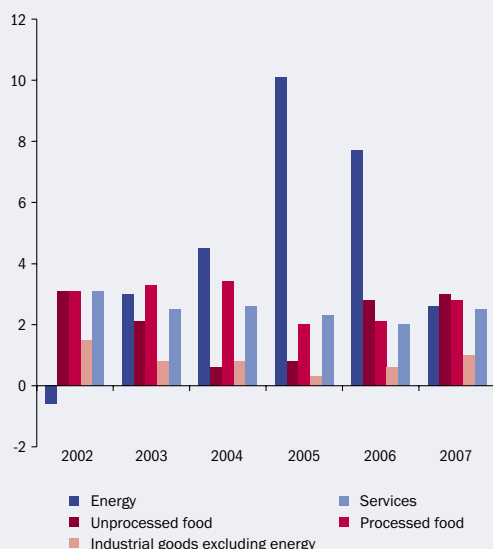
In general, food prices went up faster both at the producer and at the consumer level.

The year-on-year rate of growth in industrial producer prices reached 2.8% in 2007, which is a level considerably below that of the preceding two years (4.1% in 2005 and 5.1% in 2006). The main reason for this development was the base effect, which influenced the energy components to a considerable extent and

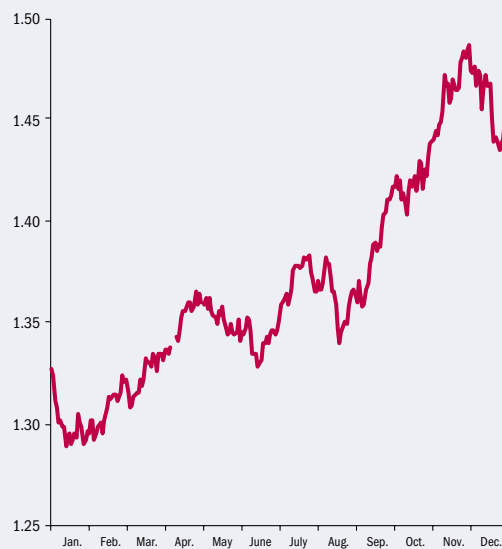
Chart 5 Development of HICP inflation in the euro area (%)



Source: Eurostat.

**Chart 6 Year-on-year changes in individual components of HICP inflation in the euro area (%)**

Source: Eurostat.

Chart 7 USD/EUR exchange rate development in 2007

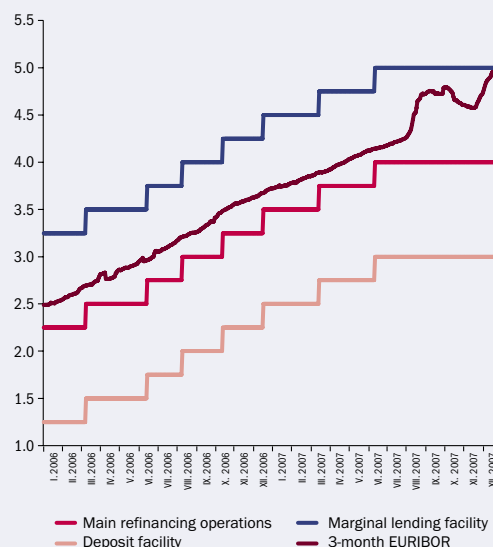
Source: ECB.

lasted till the beginning of the second half of the year. From September, the year-on-year growth rate of energy producer prices started to be pushed up by the increase in the prices of oil, agricultural commodities and by the base effect.

The euro exchange rate against US dollar appreciated by almost 11% during the year. At the beginning of 2007, the euro showed a depreciation trend against other currencies. As a result of a positive economic development in the euro area, however, the depreciation trend came to a halt and the euro started to gradually appreciate against other currencies. The financial market crisis, which resulted in an increase in risk aversion and risk reassessment, brought about considerable volatility in the development of exchange rates. Due to concerns regarding liquidity on the money market stemming from financial crisis, the euro appreciated significantly, in particular against the US dollar. Weak economic data and the continuing mortgage turmoil have contributed to the dollar depreciation. All over the year, this trend was influenced by fears of a considerable economic growth slowdown in the United States, as well as of the recent development in the US real estate market. In May and August, the euro appreciation mitigated as a result of favourable confidence indicators in the United States and a lower willingness of European banking houses to keep investments in the US real estate market. After the September cut in federal funds rates by 0.5 of a percentage point to 4.75%, the euro appreciation continued in the following months. It continued to be influenced by persistent fears that the impact of the real estate market turmoil in the

United States on the US economy could be more serious than expected.

In 2007 the ECB conducted its monetary policy in an environment of sound economic growth. Throughout the year, the ECB reacted to risks that could endanger price stability and increased the key interest rates twice, in May and June, by a total of 50 basis points. The ECB key interest rate moved up from 3.5% in De-

Chart 8 ECB interest rates and EURIBOR (%)

Source: ECB.

cember 2006 to 4.0% in June 2007. Despite growing risks associated with the development in financial markets – which could negatively affect price stability – from August 2007 onwards, the ECB Governing Council decided to keep the key interest rates unchanged in the second half of the year.

In connection with the volatility in the financial markets, the ECB decided to conduct two supplementary longer-term refinancing operations.

1.3 Development in Visegrad countries

In 2007, the economies of the Czech Republic and Poland recorded a slightly higher economic growth as compared to the previous year, driven mainly by consumption and investment. The GDP growth rate in Hungary, on the other hand, decreased, which represented a continuation of the trend towards a slowdown in the economy from the previous year. Year-on-year inflation accelerated in all Visegrad countries (V4 countries), primarily due to growing food and energy prices. As a result of positive investors' mood in the region, the Hungarian forint and Polish zloty were appreciating against the euro in the first half of the year; however, these appreciation tendencies came to a halt in the second half of the year, as a result of the turmoil in international financial markets. Compared to the zloty and forint, the Czech koruna showed conflicting trends, which were associated with the use of the Czech koruna as a funding currency in “carry trades”. Česká národní banka (ČNB) and Narodowy Bank Polski (NBP) increased their interest rates; Magyar Nemzeti Bank (MNB), on the other hand, reduced its interest rates.

The **Czech Republic** maintained its relatively high economic growth from the previous periods. In comparison with 2006, GDP growth accelerated by 0.1 of a percentage point to 6.5%. Investments and consumption – mainly household consumption – participated to an important extent in the growth of the economy. The household consumption growth was influenced by a falling rate of unemployment, growing gross disposable income and high consumer confidence. The rate of unemployment fell by 1.8 percentage points to 5.3%.

The average annual rate of HICP inflation stood at 3%, 0.9% of a percentage point above the 2006 level. Compared to the previous year, the highest price increase occurred with processed food prices, where an increase in the consumption tax on tobacco influenced the price level in the first half of the year. In the second half of the year, the food prices were primarily affected by global factors. In addition to food prices, energy prices also recorded an increase.

Chart 9 Exchange rates of V4 currencies against the euro (year-on-year changes in %)

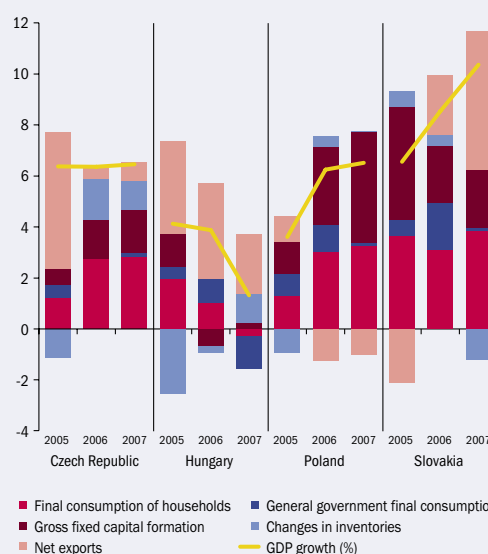


Sources: Eurostat, NBS calculations.

Note: Negative values denote appreciation.

The development of the Czech koruna exchange rate was partly different as compared to that of other currencies in the region. In the first quarter, the Czech koruna was lagging behind slightly, probably due to a negative interest rate differential against the other currencies of the V4 countries. The depreciation of the Czech koruna in the second quarter was brought about by opening of “carry trades”, in which borrowed

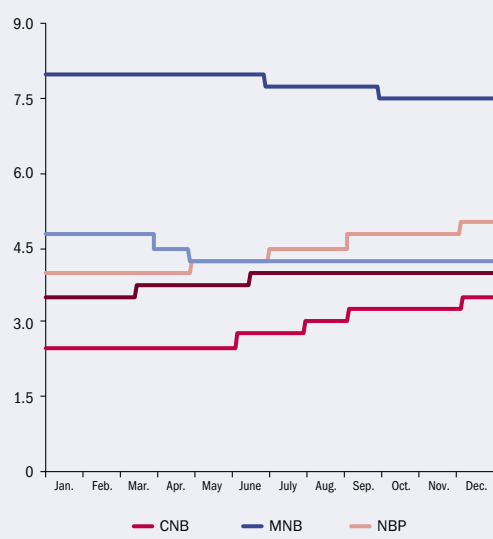
Chart 10 Contributions to GDP growth (in p. p.)



Sources: Eurostat, NBS calculations.

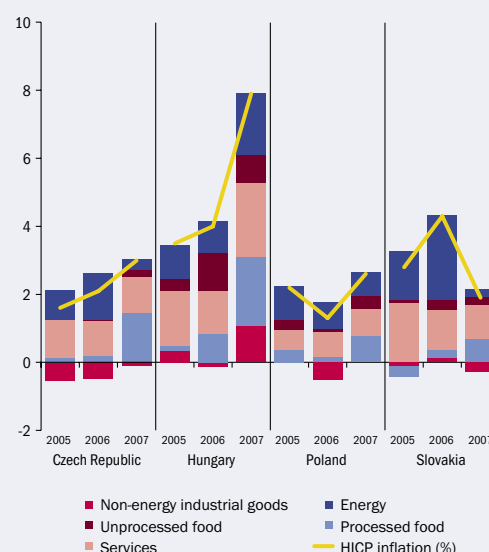


Chart 11 Key rates of national central banks
(% p.a.)



Sources: National central banks, ECB.

Chart 12 Contributions to HICP inflation
(in p.p.)



Sources: Eurostat, NBS calculations.

korunas were invested up to the level of interest-bearing foreign currency assets. In the second half of the year (as a result of growing risk aversion and subsequent closing of “carry trades”), the koruna started to appreciate again. The exchange rate appreciation was driven inter alia by CNB interest rate hikes and market expectations regarding their further increases.

Over the course of the year, Česká národní banka raised its key interest rate by a total of one percentage point to 3.5%, due to higher than expected inflation. Another reason for the increase in interest rates was an increasing production gap and its possible negative impact on the Czech economy.

In 2007, the **Hungarian** economy's slowdown continued, with GDP growth having decreased by 2.6 percentage points to 1.3%. The GDP growth decline was due to a decrease in household consumption and government spending as a result of administrative changes and fiscal measures of 2006. The growth of the economy was fuelled primarily by net exports and changes in inventories. Compared to 2006, the rate of unemployment fell slightly to 7.4%.

Inflation increased by 3.9 percentage points against the previous year, to a level of 7.9%. Services, food and changes in regulated prices in January 2007 contributed most to the acceleration of price level growth. The effect of the September 2006 VAT increase was also reflected in the prices of goods and services. At the end of the year, inflation accelerated as a result of the global growth of food and oil prices.

The Hungarian forint exchange rate appreciated from January 2007 onwards as a result of positive investors' mood and interest in currencies of the Central European region. The longer lasting appreciation trend (from August 2006) ended in the second half of the year, when the exchange rate began to be affected by the incipient liquidity tension in the United States and the related uncertainty in the financial markets. Among the V4 countries, the increase in investors' risk aversion was reflected most in the Hungarian forint exchange rate, which was subsequently depreciating until the end of 2007.

MNB reduced the interest rates twice in the course of the year. At its June meeting, it decreased the interest rate by 0.25 of a percentage point as a result of a decreasing inflation, which according to the inflation forecast had passed its peak and was supposed to decrease further. Another reduction, by 0.25 of a percentage point to 7.5%, was performed in September due to a slowdown of the economy and a persistent decline in the domestic demand.

The economic growth of **Poland** accelerated by 0.3 of a percentage point to 6.5%. Similarly to the situation in the Czech Republic, the sources of growth were investment and household consumption. Investment activity climbed in all sectors, however, primarily in the corporate sector. Consumer spending was influenced by a growth in real household income, which grew faster than labour productivity. The growth of domestic demand was also the result of improved conditions on the labour market, where the rate of

unemployment fell by 4.2 percentage points against 2006, to 9.6%.

Inflation in Poland accelerated by 1.3 percentage points and reached 2.6%. Similarly to other countries of the Visegrád group, prices of food and energy, influenced by global factors, grew most. The price level was also influenced by a growth of household income and the subsequent higher demand. The dampening effect of industrial goods prices came down at the same time.

In the first half of the year, the exchange rate of the Polish zloty was primarily influenced by domestic factors. An improved rating, a good macroeconomic situation and expectations of interest rate increases

accompanied by a decrease in risk aversion on emerging markets resulted in an exchange rate appreciation against the euro. The depreciation of the Polish zloty in the second half of the year was connected to the financial market turmoil. At the end of the year, the exchange rate appreciated again due to interest rate increases.

The NBP raised its reference interest rate four times over the course of 2007, by a total of one percentage point to a level of 5%. The main reasons for increasing the rates include a growth of the economy above its potential, faster growth of wages compared to labour productivity, as well as growing inflation towards the end of the year, which exceeded the upper limit for deviations from the NBP inflation target.

Monetary Developments



2 Monetary Developments

In 2007, NBS implemented its monetary policy in an environment of dynamic economic growth and continued pursuing an inflation-targeting strategy under ERM II in line with its Monetary Programme for the Period until 2008. In view of the commitments arising from EU membership, the task to create conditions for the adoption of the single European currency in January 2009, and the commitment of the Government to reduce the fiscal deficit, NBS set a target rate for year-on-year inflation, expressed in terms of the Harmonised Index of Consumer Prices (HICP), below 2% for December 2007 and 2008, so that the Maastricht criterion for the average 12-month inflation rate is met.

At the end of 2007, HICP inflation stood at 2.5%, representing a slowdown of 1.2 percentage points compared with the end of December 2006. Since August 2007, inflation had been below the Maastricht inflation criterion. The inflation target of NBS for end-2007 was exceeded, due to steep increases in food and oil prices in the last quarter of 2007. However, these causes represented exclusively inflation cost factors, which were defined as escape clauses.

Economic and monetary developments in 2007 were characterised by dynamic GDP growth, reaching 10.4% at constant prices. In comparison with 2006, the pace of economic growth accelerated by 1.9 percentage points. The continuing strong GDP growth in 2007 was partly reflected in an increase in wages and employment, a decrease in the number of unemployed, labour productivity growth, and an improvement in the financial results of corporations (profit growth). The deficit in the balance of payments current account decreased in comparison with the previous year, due mainly to a year-on-year improvement in the trade balance.

During 2007, NBS changed the setting of its monetary policy by lowering its key interest rates in March and April by 0.25 of a percentage point, i.e. by a total of 0.50 of a percentage point. NBS also reduced its overnight sterilisation rate by 0.75 of a percentage point in March and by 0.25 of a percentage point in April.

Due to positive developments in the basic macroeconomic indicators, the central parity of the koruna

against the euro was revalued by 8.5% with effect from 19 March 2007. The new central rate was set at SKK 35.4424 per euro (originally SKK/EUR 38.4550), the lower compulsory intervention rate at SKK/EUR 30.1260 and the upper rate at SKK/EUR 40.7588.

2.1 Economic developments

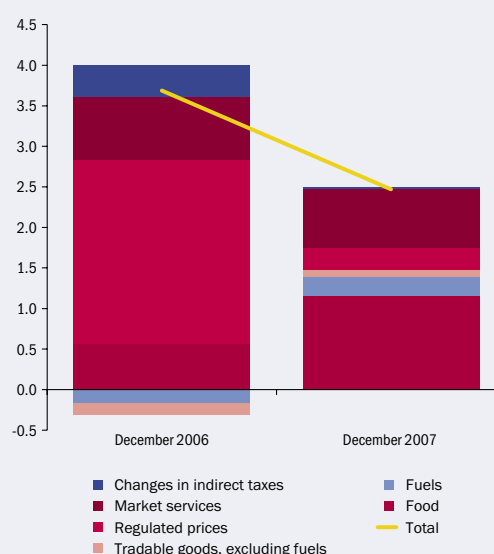
2.1.1 Price Developments

Consumer prices

Inflation as measured by the Harmonised Index of Consumer Prices

Consumer prices, expressed in terms of the Harmonised Index of Consumer Prices (HICP), had increased by 2.5% on year-on-year basis by the end of December 2007, representing a slowdown in dynamics of 1.2 percentage points in comparison with the end of 2006. The average inflation rate reached 1.9% in 2007 (compared with 4.3% in 2006), with the prices of goods and services rising by 1.4% and 2.9%,

Chart 13 **Structure of HICP inflation according the breakdown of the national index (contributions to headline inflation by component) (p.p)**



Sources: Statistical Office of the SR and NBS calculations.



respectively. The year-on-year rate of core inflation (overall inflation, excluding energy and unprocessed food prices) averaged 1.9% in 2007 and was 0.2 of a percentage point lower than in the previous year.

In its Monetary Programme for 2005–2008 of December 2004, Národná banka Slovenska defined its monetary policy as inflation targeting in the conditions of ERM II. The main anchor of such monetary policy is the setting of an inflation target. For December 2007, the year-on-year inflation rate had been set at 2%, but the actual end-year figure was 0.5 of a percentage point above the target.

The inflation target was exceeded as a result of factors outside the control of monetary policy, i.e. global increases in food and energy prices, which were also reflected in the consumer prices of food and fuels in the last months of 2007. The year-on-year dynamics of oil prices expressed in Slovak koruna reached 25.7% in December 2007, and the average oil price was USD 72.5 per barrel in 2007 (forecast in the Monetary Programme of NBS until 2008, in which the inflation target was set, predicted USD 34.6/barrel for 2007). In 2007, compared with 2006, food prices were influenced by the prices of agricultural commodities in European and global markets in the second half of 2007, as a result of poor harvests in some countries and growing demand from Asian emerging economies. Raising demand as a result of bio fuel production increase was reflected in agro-commodity prices, too. The year-on-year increase in the prices of non-energy industrial goods was nearly in line with the expectations of the Monetary Programme of NBS until 2008, while services prices showed somewhat weaker dynamics.

All the listed factors were supply shocks in character and were on the list of exemptions from inflation target achievement, which are exactly defined in the Monetary Programme of NBS for the Period until 2008 and are as such beyond the scope of NBS's monetary policy. Hence, NBS focused first and foremost on the mitigation and/or elimination of the impact of second-round factors in order to prevent price contagion spreading to other components of the consumer basket.

Goods

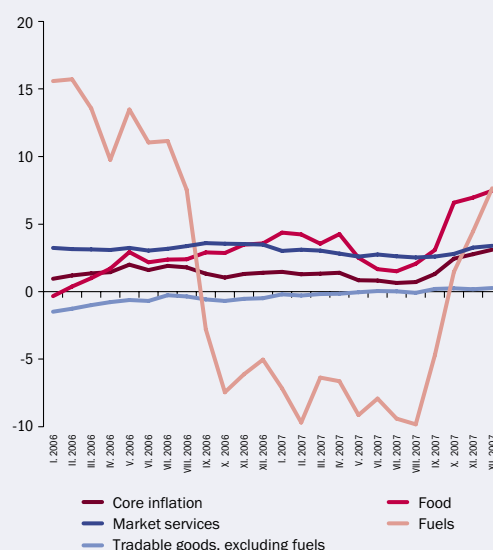
Energy prices had a dampening effect on the dynamics of goods prices in 2007, after acting as stimulants in the previous years. The average dynamics of regulated energy prices (electricity, gas, and other) weakened, from 14.9% in 2006 to 2.6% in 2007, as well as the dynamics of fuel prices, which recorded an average year-on-year fall of 4.9% in 2007 (compared with a rise of 5.5% in 2006). The prices of non-energy industrial

goods dropped by an average of 1.1 % in 2007, as a result of developments in the regulated prices of pharmaceuticals (VAT reduction from 19% to 10%, and the exclusion of an expensive medicament from production and its replacement in the consumer basket by a similar, but cheaper product). Even without this administrative measure, the average price of non-energy industrial goods would record a year-on-year fall in 2007, after a rise of 0.6% in 2006. Most exposed to the pressure of foreign competition was the sale of non-energy industrial goods, which recorded, despite the pronounced exchange rate appreciation in 2007 (by 9.3%), a much smaller year-on-year decline; this certify that the exchange rate has a weak and limited influence on consumer prices. Within the structure of this sub-aggregate, the steepest increases occurred in the prices of semi-durable industrial goods (an average of 0.7%), while the prices of durable industrial goods dropped by 5.5%. Food prices rose by an average of 4.1%, due to increases in both processed and unprocessed food prices (4.7% and 3.0% respectively).

Services

In 2007, prices for services rose annually by an average of 2.9%, representing a slowdown in dynamics compared with 2006 (3.5%). The most dynamic increases were recorded in the prices of medical, dental, and financial services. However, these increases took place mostly in the last quarter of 2007. The dynamics of transport-related prices also accelerated (from 2.6% in 2006 to 3.8% in 2007). The only category of services to record a price fall was post and

Chart 14 Developments in the prices of core inflation components (year-on-year changes in %)



Source: Statistical Office of the SR.

Table 2 Consumer price developments in terms of HICP (average for the period)
(year-on-year changes in %)

	2006		2007				
	Dec.	Year	Mar.	June	Sep.	Dec.	Year
Total	3.7	4.3	2.1	1.5	1.7	2.5	1.9
Goods	4.0	4.6	1.7	0.9	1.0	1.8	1.4
Industrial goods	3.9	6.0	0.4	-0.1	-0.1	-0.2	0.0
Non-energy industrial goods	1.1	0.6	-0.4	-1.1	-1.4	-1.2	-1.1
Energy	7.4	13.1	1.5	1.2	1.8	1.2	1.3
Food	4.1	2.3	4.1	2.8	3.0	5.8	4.1
Processed food (including alcohol and tobacco)	3.5	1.4	3.9	4.5	3.8	7.4	4.7
Unprocessed food	5.3	4.0	4.4	-0.1	1.3	2.6	3.0
Services	3.1	3.5	2.8	2.6	3.2	3.7	2.9
Core inflation (excluding energy and unprocessed food prices)	2.5	2.1	1.9	1.7	1.8	2.8	1.9
Total, excluding energy	2.8	2.3	2.2	1.5	1.7	2.8	2.0

Source: NBS calculations based on data from the Statistical Office of the SR.

telecommunications, where prices dropped during the year by an average of 0.3%.

Inflation as measured by the national Consumer Price Index

Consumer prices had increased year-on-year by 3.4% by the end of December 2007, representing a slowdown in dynamics of 0.8 of a percentage point compared with the end of 2006. As a result of a steep

rise in prices for housing-related services (house maintenance services and imputed rent increases), consumer prices expressed in terms of the CPI ended the year 2007 with a larger year-on-year increase than the HICP (by 0.9 of a percentage point). The average rate of CPI inflation in 2007 reached 2.8% (compared with 4.5% in the previous year).

In 2007, the year-on-year dynamics of consumer prices weakened in comparison with the previous year, due mainly to a slowdown in regulated prices.

Table 3 Consumer price developments (year-on-year changes)

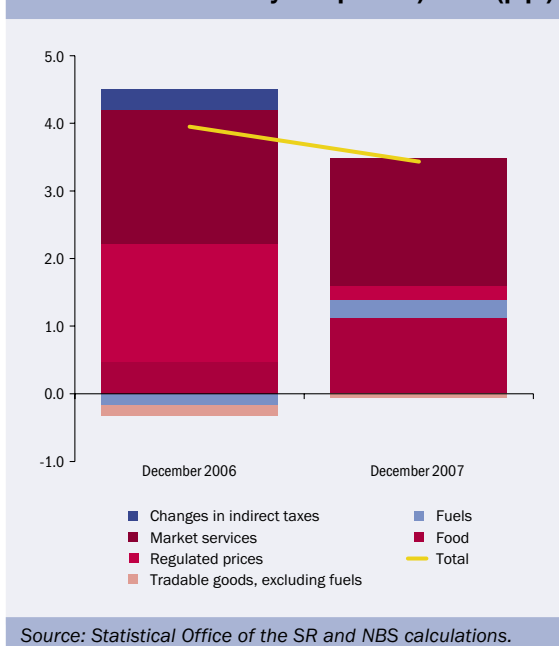
	2006		2007				
	Dec.	Year	Mar.	June	Sep.	Dec.	Year
Total in %	4.2	4.5	2.7	2.5	2.8	3.4	4.5
Regulated prices in %	7.5	10.5	2.3	1.5	2.1	0.9	1.7
Impact of changes in indirect taxes on non-regulated prices – share of total in percentage points	0.31	0.13	0.23	0.23	0.05	0.00	0.15
Core inflation in %	2.7	2.5	2.5	2.5	3.0	4.2	2.9
of which:							
Food prices in %	3.0	1.5	2.9	2.0	3.8	8.0	4.0
Tradable goods in % ¹⁾	-1.0	-0.1	-0.8	-1.0	-0.6	0.6	-0.7
Tradable goods, excluding fuels in % ¹⁾	-0.5	-0.8	-0.2	-0.2	-0.1	-0.2	-0.2
Fuels in %	-5.1	6.0	-6.4	-7.9	-4.7	7.6	-4.8
Market services in % ¹⁾	7.3	6.5	6.6	7.1	7.0	6.8	6.8
Net inflation (excluding the impact of changes in indirect taxes)	2.7	2.8	2.4	2.6	2.8	3.4	2.6
Net inflation, excluding fuels (excluding the impact of changes in indirect taxes)	3.2	2.6	3.0	3.3	3.3	3.1	3.1

Source: Statistical Office of the SR.

1) NBS calculations based on data from the Statistical Office of the SR.



Chart 15 Structure of CPI inflation (contributions to headline inflation by component) (p.p.)



Price levels in 2007 were determined mostly by external factors. Price developments were influenced by the global trends in commodity, oil, and energy prices, which, in turn, were reflected in regulated price changes and in fuel and food prices development. The rise in price level was mainly caused by increases in prices for market services (especially house maintenance services and imputed rents). The prices of tradable goods recorded an acceleration in the year-on-year rate of decline. This resulted from a marked year-on-year drop in fuel prices, despite a slowdown in the year-on-year decline in the prices of tradable goods, excluding fuels, at a time when the exchange rate strengthened to a significant extent.

Regulated prices

One of the determining factors in consumer price developments was, as in previous years, the adoption of administrative measures in the area of regulated prices. The year-on-year dynamics of regulated prices reached an average of 1.7% in 2007 (compared with 10.5% in 2006). Slowdown took place mainly in energy prices (heating, gas, electricity). Regulated prices reflected the impact of a VAT reduction for pharmaceuticals, from 19% to 10%, with effect from January 2007.

Changes in indirect taxes

In 2007, non-regulated prices were not affected by any changes in indirect taxes. In the first half of

2007, their year-on-year dynamics were influenced by the increase in excise taxes on tobacco and tobacco products from 2006 (0.15 of a percentage point of the year-on-year average CPI inflation rate).

Core inflation

In 2007, core inflation reached an average of 2.9%, representing a rise of 0.4 of a percentage point in comparison with the previous year. In December 2007, the year-on-year rate of core inflation stood at 4.2% (compared with 2.7% in December 2006).

Within the basic structure of core inflation, the determining factor in the accelerating price increase was food prices (their steep rise at the end of 2007, caused by the rising prices of agricultural commodities in world markets, affected food prices in all EU Member States differently in terms of intensity). Prices for market services recorded a modest increase in their average year-on-year dynamics (due to increases in house-maintenance prices and bank fees at the end of 2007). The year-on-year decline in tradable goods prices (excluding fuel prices) slowed in 2007, compared with 2006, and thus contributed to the higher average year-on-year rate of core inflation (steeper increases in the prices of non-alcoholic and alcoholic beverages).

Core inflation was dampened by fuel prices, which rose in 2006 by an average of 6.0% and dropped in 2007 by an average of 4.8% on a year-on-year basis. Their level reacted to changes in oil prices and the exchange rate of the Slovak koruna against the US dollar.

Developments in services prices showed no signs of excessive demand-based pressures. The steepest year-on-year increase during the year was recorded in the prices of housing-related services.

Producer prices

Producer price developments in 2007 were influenced by various factors, the most important being the price of oil, which caused a much slower year-on-year increase in refined oil products prices (falling under the category of manufacturing products) in the first nine months of 2007, compared with the previous year. This was connected with the slower rise in energy prices. In the final quarter, however, oil prices began to accelerate in the world markets and the prices of basic food commodities increased as well. As a result of these factors, the dynamics of industrial producer prices weakened considerably in 2007, compared with 2006.

Table 4 Year-on-year developments in producer prices (average for the period, %)

	2006	2007				
		Q1	Q2	Q3	Q4	Q1-Q4
Industrial producer prices	8.4	3.4	1.6	1.1	2.2	2.0
Raw materials prices	38.4	-0.5	-3.4	-5.2	-3.8	-3.3
Manufacturing products prices	2.1	0.9	-0.3	-0.7	1.4	0.3
Prices of electricity, gas, steam, and hot water	14.5	7.0	4.2	3.8	3.6	4.6
Construction prices	3.9	4.1	4.1	3.7	4.0	4.0
Building materials prices	3.0	5.2	5.4	6.7	5.1	5.6
Agricultural products prices	-0.2	0.8	-2.1	8.3	10.6	5.4
Prices of plant products	1.1	21.9	15.9	23.9	25.8	24.0
Prices of animal products	-0.7	-2.8	-3.9	-1.6	0.3	-2.0

Source: Statistical Office of the SR.

The combination of the effects of various, mostly external factors (drought in Australia, growing demand for food in China and India, increased use of cereals for bio fuel production), also caused a rise in agricultural products prices in Slovakia.

In 2007, construction prices continued to rise virtually at the same rate as in 2006, but the prices of building materials increased more rapidly than a year earlier.

In 2007, industrial producer prices recorded a substantially slower year-on-year increase than in the past year, mainly as a result of a marked year-on-year slowdown in electricity, gas, steam, and hot water prices (by an average of 10 percentage points, to 4.6%). The slowdown in energy prices took place in virtually all the basic components. The only prices that rose at the same rate as a year earlier (9.0%) were prices for electricity production and distribution. Prices for gas production and the distribution of gaseous fuels by pipeline dropped by an average of 3.6% in 2007, after rising in 2006 by an average of 22.7%. The year-on-year dynamics of prices for steam and hot water production and supply weakened in comparison with the previous year by 11.1 percentage points, to 7.3% in 2007, and prices for water treatment and supply slowed by 8.9 percentage points, to 0.7 %.

The year-on-year slowdown in manufacturing products prices in 2007 (by 1.8 percentage points, to 0.3%) was mainly the result of a fall in the prices of refined oil products (7.5%, compared with a rise of 13.1% a year earlier), though they began to increase again in the final quarter. Year-on-year drops in 2007 were also recorded in the prices of transport vehicles (3.3%, after stagnation a year earlier), electrical and optical equipment (0.5%, compared with a rise of 1.7% in 2006). The prices of base metals and finished metal

products increased at a slower rate than in 2006 (by 0.5 of a percentage point, to 2.5%). On the other hand, the prices of food products increased more rapidly than a year earlier (by 3.5%, after falling a year earlier by 0.4%), other non-metal mineral products (by 3.1 percentage points, to 4.9%), and wood products (by 3.9 percentage points, to 5.9%).

2.1.2 Gross domestic product

In 2007, gross domestic product (GDP) increased year-on-year by 10.4% at constant prices (according to a revised estimate of the Statistical Office of the SR). Compared with 2006, the pace of economic growth accelerated by 1.9 percentage points, due mainly to increased net exports and, in part, to the effect of stocking-up on cigarettes and tobacco products.

In terms of use, economic growth in 2007 was influenced by both domestic and foreign demand. In terms of production, real economic development was mostly influenced by value added growth in manufacturing and in public administration, education, health care, and other services. The nominal volume of GDP created in the period under review amounted to SKK 1,851.8 billion, which was 11.6% more than a year earlier.

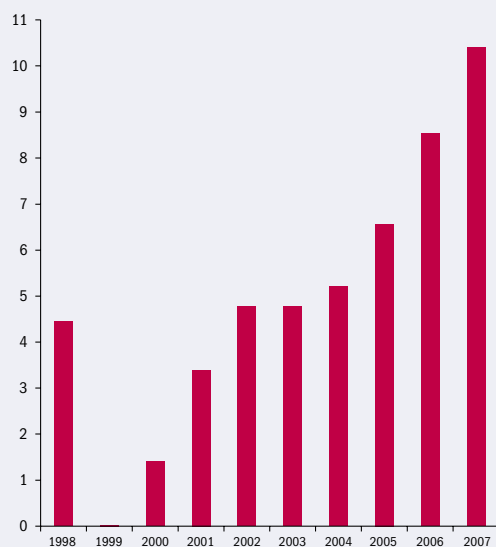
Broken down by quarter, real economic growth accelerated during 2007 from 8.3% in the first quarter to 14.3% in the fourth quarter.

Supply side of GDP

GDP generation in 2007 was influenced by value added creation, which grew year-on-year by 10.2% at constant prices (compared with 10.2% in 2006), as well as by net taxes (value added tax, excise duty,

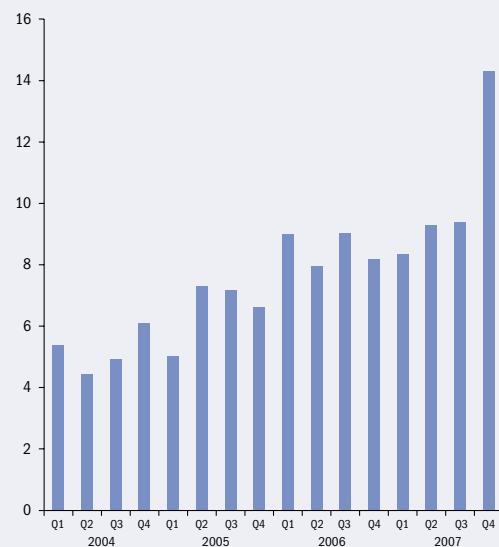


Chart 16 Annual real GDP growth
(year-on-year growth in %)



Source: Statistical Office of the SR.

Chart 17 Quarterly real GDP growth
(year-on-year growth in %)



Source: Statistical Office of the SR.

Table 5 GDP creation by component

(index, same period a year earlier = 100, constant prices 2000)

	2006	2007				
		Q1	Q2	Q3	Q4	Q1-Q4
Gross output	112.0	112.9	109.4	105.8	113.2	110.4
Intermediate consumption	113.2	114.7	108.9	102.5	115.3	110.4
Value added	110.2	110.1	110.2	110.7	109.9	110.2
Net taxes on products ¹⁾	95.4	92.6	101.8	97.8	160.9	111.8
Gross domestic product (GDP)	108.5	108.3	109.3	109.4	114.3	110.4

Source: Statistical Office of the SR.

1) Including value added tax, excise tax, and import tax, minus subsidies.

Table 6 GDP growth by sector

(index, same period a year earlier = 100, constant prices 2000)

	2006 2005	Q1 07 Q1 06	Q2 07 Q2 06	Q3 07 Q3 06	Q4 07 Q4 06	2007 2006
Gross domestic product (GDP)	108.5	108.3	109.3	109.4	114.3	110.4
of which:						
Agriculture, hunting, forestry, and fishing	112.6	84.9	80.6	81.3	72.6	79.8
Industry	110.2	117.2	122.0	118.1	121.2	119.7
Construction	115.2	111.6	107.8	101.4	98.3	104.0
Trade, hotels and restaurants, transport	112.4	119.0	110.8	104.1	105.5	109.4
Financial intermediation, real estate business	111.6	89.2	93.6	119.1	108.4	101.5
Public administration, education, health care, other community, social, and personal services	102.0	117.4	116.0	116.3	111.9	115.2
Other ¹⁾	95.4	92.6	101.8	97.8	160.9	111.8

Source: Statistical Office of the SR.

1) Value added tax, excise tax, import tax, minus subsidies and imputed production of banking services (FISIM).

Table 7 GDP development by use

(index, same period a year earlier = 100, constant prices 2000)

	2006	2007				
		Q1	Q2	Q3	Q4	Q1-Q4
Gross domestic product (GDP)	108.5	108.3	109.3	109.4	114.3	110.4
Domestic demand	106.6	103.3	105.2	105.0	109.7	105.9
Final consumption	106.7	105.7	105.0	106.9	104.5	105.5
households	105.9	106.3	107.8	108.3	105.9	107.1
general government	110.1	103.5	96.5	102.2	100.8	100.7
non-profit institutions serving households	89.6	102.2	107.2	108.7	109.5	106.8
Gross capital formation	106.6	96.9	105.6	101.1	125.6	107.1
Gross fixed capital formation	108.4	111.0	105.9	106.5	108.9	107.9
Exports of goods and services	121.0	122.7	118.1	108.5	116.0	116.0
Imports of goods and services	117.7	114.5	113.2	103.0	111.6	110.4

Source: Statistical Office of the SR.

import tax, minus subsidies), which increased by a total of 11.8% (after decreasing by 4.6% in 2006).

In 2007, value added growth was recorded in all sectors, except in agriculture; stronger real growth than in 2006 was achieved in industry (19.7%) and in public administration, education, health care, and other community, social and personal services (15.2%).

Demand side of GDP

Economic growth in 2007 was influenced by both domestic and foreign demand. Foreign demand grew

in real terms by 16.0%, and thus increased the export performance of the economy. Economic growth was also stimulated by domestic demand, but its pace lagged behind the figure recorded a year earlier.

Turning to domestic demand, the most rapid growth in 2007 was recorded in investment demand (7.1% in real terms), which was 0.5 of a percentage point faster than in the previous year. The growth in the 'consumption' component of demand was 1.2 percentage points slower than a year earlier, which was mainly the result of a sharp slowdown in the growth of general government final consumption (0.7% in real terms, compared with 10.1% a year earlier). The dy-

Table 8 Structure of gross fixed capital formation in 2007

	Gross fixed capital formation (SKK million)	Proportion (%)	Index 2007/2006	Index 2006/2005
Economy of the SR in total	476,285	100.0	109.2	110.6
of which (by sector):				
Non-financial corporations	335,733	70.5	110.5	110.3
Financial corporations	6,825	1.4	140.8	83.1
General government	37,596	7.9	103.5	117.0
Households	95,097	20.0	105.4	111.2
Non-profit institutions	1,034	0.2	105.4	107.8
of which (by production):				
Machinery	201,067	42.2	109.1	95.0
of which: metal products and machines	148,494	31.2	107.3	87.1
transport equipment	52,573	11.0	114.2	130.7
Buildings and structures	247,943	52.1	107.5	133.6
of which: residential buildings	43,881	9.2	113.3	88.8
other structures	204,062	42.8	106.3	148.7

Source: NBS calculations based on data from the Statistical Office of the SR.



Table 9 Investments and savings

(% , current prices)

	2006	2007
Savings ratio ¹⁾	24.2	26.5
Gross investment ratio ²⁾	28.0	27.2
Fixed investment ratio ³⁾	26.3	25.7
Coverage of investments by savings ⁴⁾	86.3	97.3

Source: NBS calculations based on data from the Statistical Office of the SR.

1) Ratio of gross savings (GDP less final consumption in total) 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.

namics of household final consumption strengthened year-on-year by 1.2 percentage points.

Domestic investment demand

Gross capital formation increased by 7.1% (at constant prices), due to growth in fixed investments (by 7.9% year-on-year) and growth in inventories (by SKK 16.6 billion at constant prices). Within the structure of inventories, all components increased in 2007, with the most rapid increases recorded in goods and materials inventories.

Gross fixed capital formation was mostly affected by the purchase of new fixed assets (a growth of 4.4% at constant prices). Looking at the breakdown of fixed assets by national accounts sector, their increases were most significantly influenced by the investment activities of non-financial corporations, which comprised both foreign and domestic investments.

Most investments were made by entrepreneurial entities in manufacturing. The growth in gross fixed capital formation in real terms was also supported by the investment activities of households (a growth of 4.2% at constant prices) and the general government sector (a growth of 2.3% at constant prices).

According to revised data from the Statistical Office of the SR, investments increased in both machines and construction, but the most rapid growth took place in investment in transport equipment. In construction, investment grew most dynamically in residential buildings.

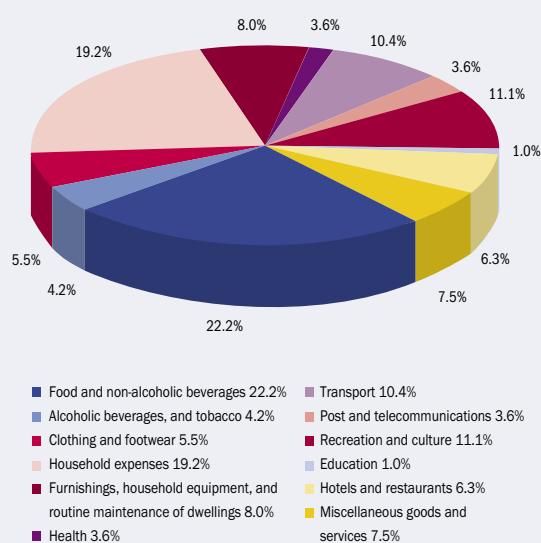
The share of domestic savings in the financing of investment demand increased in 2007. There were almost 86 haliers worth of gross savings in the national economy for one koruna worth of gross investments in 2006; this ratio increased to 97 haliers in 2007. This increase was a consequence of accelerated year-on-year growth in savings, accompanied by slower growth in gross investments.

Domestic consumer demand

In 2007, final consumption expenditure increased year-on-year by 5.5%, due to growth in all sectors. Within the structure of final consumption, the dynamics of general government final consumption weakened in 2007 (compared with the previous year), whereas the dynamics of household final consumption strengthened.

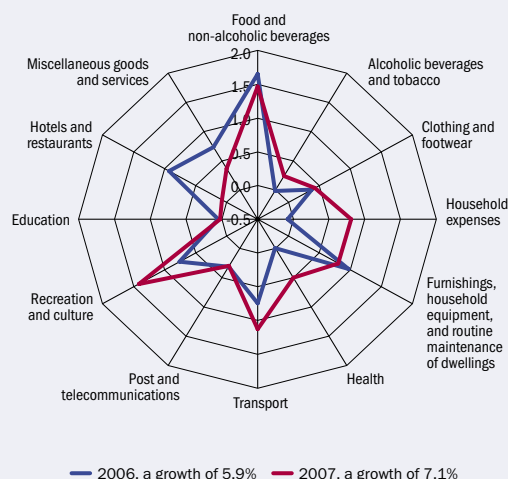
Final consumption by households increased in real terms by 7.1% year-on-year in 2007, and its share of total GDP reached 52.0% (compared with 53.6% in 2006). Private household consumption growth was connected with the growth of wages, employment, gross mixed income (remuneration for work and profits earned by sole traders), and with the utilisation of credit resources. The total receivables of monetary financial institutions from households as a share of

Chart 18 Structure of household final consumption



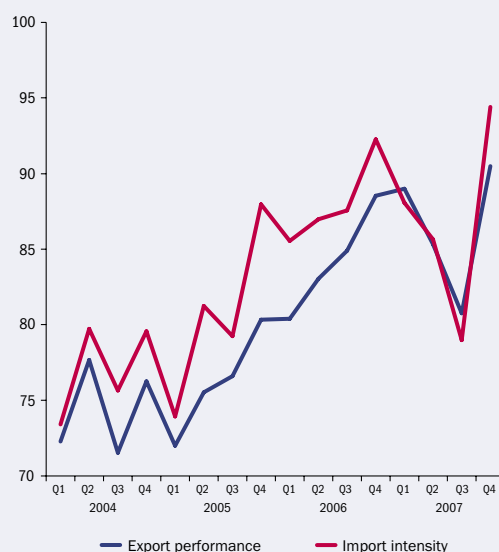
Source: Statistical Office of the SR.

Chart 19 Contributions of individual consumer expenses to growth in household final consumption (p.p.)



Source: NBS calculations based on data from the Statistical Office of the SR.

Chart 20 Export performance and import intensity (%)



Source: Statistical Office of the SR.

their final consumption continued to increase during 2007, by 4.1 percentage points, to 29.3% (compared with 25.2% at the end of 2006).

An analysis of household final consumption in 2007 shows that the most significant year-on-year increases occurred in the expenditures of households on health care (23.8% at constant prices), recreation and culture (13.4% at constant prices), and transport (11.3% at constant prices). In percentage terms, the largest consumption component (22%, as in 2006) was spending on food and non-alcoholic beverages. The second largest component was expenditure related to housing (19%), whose proportion to household consumption decreased by 0.6 of a percentage point in comparison with 2006.

The year-on-year growth in household final consumption was based primarily on consumer expenditures on food and non-alcoholic beverages, recreation and culture, and transport.

Exports and imports of goods and services showed weaker dynamics in 2007 than a year earlier. Exports grew by 14.2% and imports by 9.8% at current prices.

In nominal terms, net exports resulted in a deficit of SKK 8.7 billion (SKK 63.5 billion in 2006).

The export performance of the Slovak economy improved year-on-year by 2 percentage points in 2007, when the exports of goods and services as a share of GDP at current prices reached 86.4%. Import intensity weakened on a year-on-year basis, to 86.8% (from 88.2% in 2006). The openness of the Slovak economy, expressed in terms of the ratio of exports and imports of goods and services to nominal GDP, reached 173.2%, representing a year-on-year increase of 0.6 of a percentage point.

Income and expenditure of households¹

According to preliminary data from the Statistical Office of the SR, the current income of households reached SKK 1,458.5 billion in 2007, representing a year-on-year increase of 10.4% in nominal terms (7.4% in real terms). Compared with 2006, the rate of growth slowed in nominal terms by 0.2 of a percentage point. Within the scope of current income, the most rapid growth occurred in property income received (21.4 %) and gross mixed income² (11.2%). In current income,

1 Income from property received (interest, dividends, income from rented land, and other), other current transfers received (insurance compensation paid to households, lottery winnings, etc.), income from property paid (interest paid to households for loans 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.).

2 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 the contribution of households to individual housing construction.



Table 10 **Generation and use of income in the household sector** (current prices)

	Volume in SKK billions		Index ¹⁾		Share in %	
	2006	2007	2006 2005	2007 2006	2006	2007
Compensation of employees (all sectors)	656.4	720.7	109.9	109.8	49.7	49.4
of which: gross wages and salaries	512.5	566.2	109.3	110.5	38.8	38.8
Gross mixed income	384.5	427.6	112.9	111.2	29.1	29.3
Property income – received	31.8	38.6	106.7	121.4	2.4	2.6
Social benefits	206.2	226.6	107.2	109.9	15.6	15.5
Other current transfers – received	41.7	45.0	121.2	107.9	3.2	3.1
Current income in total	1,320.6	1,458.5	110.6	110.4	100.0	100.0
Property income – paid	20.9	23.3	244.1	111.6	6.0	6.1
Current taxes on income, property, etc.	50.6	55.7	110.2	110.2	14.4	14.5
Social contributions	244.7	267.8	113.5	109.4	69.7	69.9
Other current transfers – paid	34.9	36.3	104.6	104.0	9.9	9.5
Current expenditure in total	351.1	383.2	115.7	109.1	100.0	100.0
Gross disposable income	969.5	1,075.3	108.8	110.9	-	-
Adjustment for changes in the net equity of households in pension funds	30.4	28.4	250.0	93.4	-	-
Final consumption of households	928.5	1,020.1	111.0	109.9	-	-
Gross savings of households	71.4	83.6	106.9	117.0	-	-
Gross savings as a share of gross disposable income (%)	7.4	7.8	-	-	-	-

Source: Statistical Office of the SR.

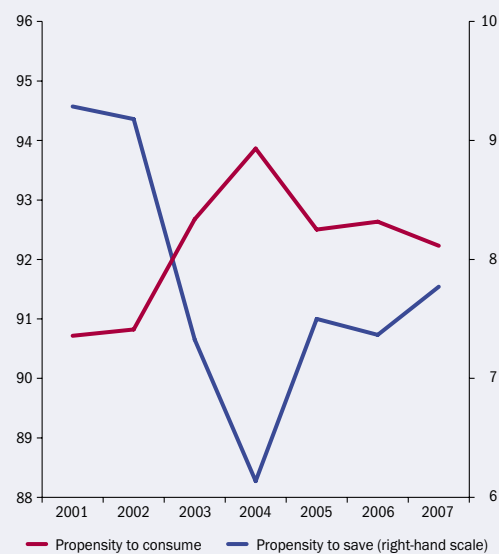
1) Indices calculated from values expressed in millions of SKK.

the largest component was the compensation of employees, which increased year-on-year by 9.8%.

The current expenditure of households (paid to other sectors and not used for direct consumption) increased year-on-year by 9.1% (in real terms by 6.1%), to SKK 383.2 billion. In 2006, current expenditure increased by 15.7%. The year-on-year growth in current expenditure was mainly connected with increases in expenses related to property income and current taxes on income. The smallest year-on-year increase was recorded in other current transfers.

With current expenditure being deducted from current income, the gross disposable income of households amounted to SKK 1,075.3 billion, representing a year-on-year increase of 10.9% (compared with 8.8% a year earlier). Of the disposable income, 94.9% was used for final consumption; the remainder went to gross savings, which increased year-on-year by 17%. The total increase in the dynamics of gross savings, which exceeded the dynamics of gross disposable income, was reflected in the ratio of gross household savings (7.8%), which was 0.4 of a percentage point higher than a year earlier (7.4%).

Chart 21 **Propensity of households to save and to consume** (%)



Sources: Statistical Office of the SR, NBS calculations.

2.1.3 Labour market

Employment

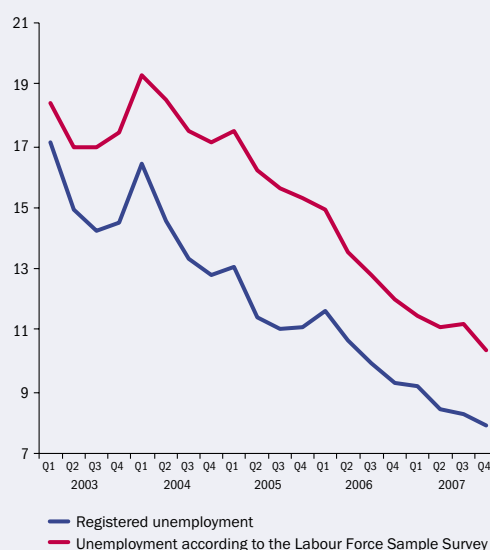
The favourable economic development in 2007 was also reflected in the level of employment. Employment according the methodology of national accounts (ESA 95) grew year-on-year by 2.1% (in 2006 by 2.3%). Looking at the breakdown of employment by sector, the year 2007 witnessed growing demand for labour in services, which led to dynamic growth in employment, mainly in real state, renting, and business activities; health and social services. On the other hand, employment remained below the previous year's level in education, other community services, public administration and defence, and in financial intermediation. In production sectors, employment grew dynamically in construction, while employment in agriculture, forestry, and fishing declined.

Unemployment

The persistent demand for labour was also reflected in the level of unemployment. On the basis of the Labour Force Sample Survey, the number of people out of work decreased year-on-year by 17.4% in 2007. This decrease was also mirrored in the annual unemploy-

Chart 22 Unemployment rate

(%)



Sources: Centre for Labour, Social Affairs and Family and the Statistical Office of the SR.

ment rate, which reached 11.0% in 2007, representing a drop of 2.3 percentage points compared with 2006. The falling trend in unemployment was also confirmed by data on registered unemployment. Ac-

Table 11 Labour market indicators

	2006	2007				
		Q1	Q2	Q3	Q4	Q1-Q4
Nominal wage (SKK)	18,761	18,511	19,598	19,514	22,925	20,146
Nominal wage (index)	108.0	107.1	106.7	106.8	108.0	107.2
Real wage (index)	103.3	104.2	104.1	104.2	104.5	104.3
Compensation per employee in nominal terms, ESA 95 (index)	107.9	108.7	106.8	107.6	109.9	108.2
Compensation per employee in real terms, ESA 95 (index)	103.5	106.4	105.1	106.1	107.4	106.2
Labour productivity of GDP (index, current prices)	109.3	109.2	108.1	109.1	109.1	108.9
Labour productivity of GDP (index, constant prices)	106.2	105.6	106.6	106.6	111.8	107.7
Labour productivity of GDP, ESA 95 (index, current prices)	109.2	109.7	108.6	109.8	109.0	109.3
Labour productivity of GDP, ESA 95 (index, constant prices)	106.1	106.0	107.2	107.2	111.7	108.1
Employment according to statistical records (index)	102.2	102.6	102.5	102.6	102.2	102.5
Employment according to ESA 95 (index)	102.3	102.2	102.0	102.0	102.3	102.1
Registered unemployment rate (%)	10.4	9.2	8.4	8.3	7.9	8.4
Unemployment rate according to LFSS ¹⁾ (%)	13.3	11.5	11.1	11.2	10.3	11.0
Unit labour costs in nominal terms ²⁾ (ULC)	101.7	102.5	99.6	100.3	98.4	100.2
Consumer prices (average index)	104.5	102.8	102.5	102.5	103.3	102.8

Sources: Statistical Office of the SR and NBS calculations based on data from the Statistical Office.

1) Labour Force Sample Survey (LFSS).

2) Ratio of growth in compensation per employee at current prices to growth in labour productivity according to ESA95 (at constant prices).



cording to the registers of Offices for Labour, Social Affairs and Family, the average unemployment rate in 2007 stood at 8.4%, representing a fall of 2 percentage points compared with 2006.

The continuing year-on-year growth in labour supply (i.e. persons at productive and post-productive age) was mostly reflected in the increased number of economically inactive persons (i.e. persons outside the labour market) in 2007. As a result of this development, the rate of economic activity reached 58.8%, representing a year-on-year fall of 0.3 of a percentage point. Among the economically active population, the increasing share of persons in employment led to a rise in the employment rate, by 1.1 percentage points year-on-year, to 60.7% in 2007.

Wages and labour productivity

In 2007³, the average monthly nominal wage in the Slovak economy increased year-on-year by 7.2%, to SKK 20,146. Compared with 2006, the rate of wage growth slowed by 0.8 of a percentage point. The strongest nominal wage growth in 2007 occurred in health and social care (15.6%); mining and quarrying (10.6%); and agriculture, forestry, and fishing (10.3%). The smallest increases in nominal wages were recorded in hotels and restaurants (6.2%), real estate and renting (5.7%).

Compared with 2006, real wage dynamics increased in 2007 by 1 percentage point (from 3.3% to 4.3%), which was the result of lower average inflation than a year earlier. Real wages increased in all sectors of the economy in 2007.

Labour productivity (GDP per employee) increased more dynamically than in 2006, in nominal terms by

8.9% and in real terms by 7.7%. Labour productivity followed a positive trend in relation to wages, when the dynamics of real labour productivity exceeded the rate of real wage growth by 3.4 percentage points.

Unit labour costs increased year-on-year by 0.2% in 2007, while the annual HICP inflation rate stood at 1.9%. This represented a considerable slowdown in comparison with 2006.

2.1.4 Financial results of corporations

According to preliminary data from the Statistical Office of the SR, financial and non-financial corporations generated a total profit of SKK 328 billion in 2007. The profit achieved was 22.2% higher than in 2006, which was attributable to increased earnings reported by financial/non-financial corporations and to the reduced negative financial result of NBS.

The increased profits of non-financial corporations were due largely to year-on-year increases in earnings in wholesale as well as retail trade; transport, storage, post and telecommunications; and in real estate, renting, and business activities. The year-on-year growth in earnings in manufacturing production (4.4%) lagged behind the overall year-on-year growth in the profits of non-financial corporations (a year-on-year increase of 10.1%). In 2007, the year-on-year growth in the profits of non-financial corporations was slower than in the previous year (profits in 2006 grew year-on-year by 25.8%), due mainly to a slowdown in the year-on-year growth of profits in the production and supply of electricity, gas, and water; metal and metal products; chemicals and chemical products; rubber and plastic goods.

Table 12 **Financial results of corporations** (SKK million, current prices)

	2006	2007	Index 2005/2004	Index 2006/2005	Index 2007/2006
Financial result (before taxation)					
Non-financial and financial corporations in total	268,380	327,980	141.3	106.7	122.2
Non-financial corporations	280,350	308,606	117.4	125.8	110.1
Financial corporations	-11,970	19,374	-	-	-
of which: NBS	-45,128	-19,464	-	-	-
Financial corporations, excluding NBS	33,158	38,838	149.3	113.0	117.3

Sources: Statistical Office of the SR and NBS.

³ With effect from 2007, a methodological change was made in the reporting of average monthly wages; on the basis of this change, the incomes of professional soldiers are now also included in the wages and the year-on-year indices are calculated from comparable data.

2.2 Balance of payments

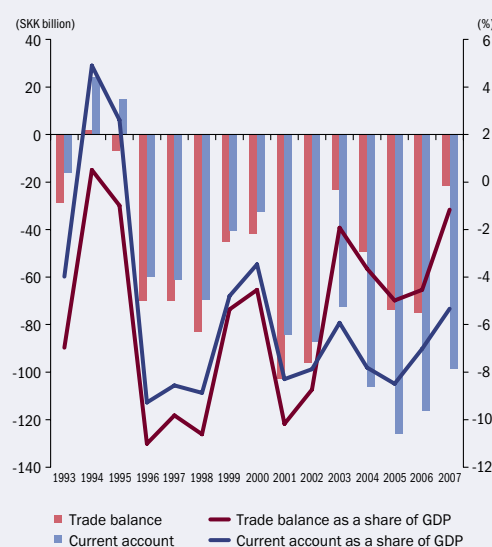
2.2.1 Current account

In 2007, the balance of payments on current account resulted in a deficit of SKK 98.7 billion, which was SKK 17.8 billion less than in the previous year. The main factor behind the year-on-year reduction in the current account deficit was an improvement in the trade balance. On the other hand, year-on-year deterioration occurred in the income balance and, to a lesser extent, in the balances of current transfers and services. The current account deficit as a share of GDP at current prices reached 5.3%, representing a year-on-year decrease of 1.7 percentage points (the share of the current account balance, excluding dividends and reinvested earnings, was positive (0.3%), while 2006 saw a deficit of 1.8%). The trade balance deficit as a share of GDP dropped to 1.2% in 2007 (the value of this ratio stood at 4.5% in 2006).

The trade balance resulted in a deficit of SKK 21.4 billion, representing a year-on-year improvement of SKK 53.9 billion. The improvement in foreign trade can be ascribed to the stronger dynamics of exports compared with imports, while the growth of imports, as well as exports, slowed in comparison with the previous year, as a result of developments in the koruna exchange rate, since exports and imports in euro showed approximately twofold dynamics (in US dollars almost threefold dynamics).

The year-on-year improvement in the trade balance resulted from the fact that exports recorded a larger year-on-year increase (SKK 187.9 billion) than imports (SKK 134.0 billion). The most significant increase in exports took place in 'machinery and transport equipment', in virtually the same amount as in

Chart 23 Trade balance and current account developments



Sources: NBS and the Statistical Office of the SR.

2006. Within the scope of this category, transport equipment recorded a larger year-on-year increase in exports, which was offset by a smaller increase in machinery exports. In imports, a smaller year-on-year increase was recorded in 'machinery and transport equipment' (reduced import of investment goods); the smaller increase in imports compared with 2006 was attributable to a year-on-year change in the growth of raw materials imports (owing to the exchange rate and lower oil prices).

According to preliminary data from the Statistical Office of the SR, goods were exported during 2007 in the total amount of SKK 1,420.7 billion, which

Table 13 Balance of payments on current account

(SKK billion)

	2007	2006
Balance of trade	-21.4	-75.3
Exports	1,420.7	1,232.9
Imports	1,442.1	1,308.2
Balance of services	13.1	22.5
Balance of income	-79.3	-62.1
of which: investment income	-114.0	-92.9
of which: reinvested earnings	-23.3	-23.8
Current transfers	-11.1	-1.6
Current account in total	-98.7	-116.5
Current account as a share of GDP in %	-5.3	-7.0
Current account (excluding dividends and reinvested earnings) as a share of GDP in %	0.3	-1.8

Sources: NBS, Statistical Office of the SR.

Table 14 **Exports from January to December**

	Year-on-year changes in billions of SKK		Contribution to the year-on-year change in percentage points	
	2007	2006	2007	2006
Raw materials	-5.2	10.7	-0.4	1.1
Chemicals and semi-finished goods	15.4	58.7	1.3	5.9
of which: Chemical products	1.7	16.5	0.1	1.7
Semi-finished goods	13.7	42.2	1.1	4.3
Machinery and transport equipment	168.0	169.5	13.6	17.1
of which: Machinery	72.5	98.7	5.9	10.0
Transport equipment	95.5	70.8	7.7	7.2
Finished products	9.7	4.0	0.8	0.4
Exports in total	187.9	242.8	15.2	24.5

Source: NBS calculation based on data from the Statistical Office of the SR.

Table 15 **Imports from January to December**

	Year on-year changes in billions of SKK		Contribution to the year-on-year change in percentage points	
	2007	2006	2007	2006
Raw materials	-14.5	38.8	-1.1	3.6
Chemicals and semi-finished goods	32.7	51.9	2.5	4.9
of which: Chemical products	7.5	19.8	0.6	1.9
Semi-finished goods	25.2	32.1	1.9	3.0
Machinery and transport equipment	91.1	123.7	7.0	11.6
of which: Machinery	56.0	93.7	4.3	8.8
Transport equipment	35.1	30.0	2.7	2.8
Finished products	24.7	29.7	1.9	2.8
of which: Agricultural and industrial products	20.6	12.0	1.6	1.1
Passenger cars	7.1	5.6	0.5	0.5
Machines and electrical consumer goods	-3.0	12.0	-0.2	1.1
Imports in total	134.0	244.1	10.2	22.9

Source: NBS calculation based on data from the Statistical Office of the SR.

was 15.2% more than in 2006 (38.6% in USD and 27.1% in EUR).

The increase in the volume of exports in 2007 was mostly influenced by the exports of machinery and transport equipment (accounting for almost 90% of the total increase in exports). In contrast with 2006, when machinery exports accounted for more than half of the increase in the 'machinery and transport equipment' category, almost 57% of the year-on-year increase in 2007 took place in the exports of transport equipment, as a result of growth in the exports of automobiles and components.

The volume of goods imported in 2007 amounted to SKK 1,442.1 billion, representing a year-on-year increase of 10.2% (in USD 32.6% and in EUR 21.5%).

In goods imports, 2007 saw the strongest growth in the imports of machinery and transport equipment. In this category of goods, accelerated growth was recorded in the imports of transport equipment (motor vehicle parts and components), in connection with the expansion of production in the automotive industry. On the other hand, the strong year-on-year growth in machine imports from 2006 slowed gradually over the course of 2007. In the 'machinery' sub-category, the most rapid growth took place in the

imports of components for the electrical industry. The year-on-year increase in imports in 'chemicals and semi-finished goods' also contributed significantly to the year-on-year growth in total imports, despite a certain slowdown in comparison with 2006. The imports of raw materials, whose year-on-year decline significantly reduced the total year-on-year increase in imports, were affected by a year-on-year fall in oil prices, which was mainly reflected in the lower imports of oil and natural gas.

Trade in services during 2007 resulted in a surplus of SKK 13.1 billion, which was SKK 9.4 billion less than in the previous year. The fall in the balance of services surplus was mainly the result of developments in transport services and, to a lesser extent, services related to tourism, while the balance of 'other services in total' improved on a year-on-year basis. The surplus in transport services diminished significantly on a year-on-year basis, mainly as a result of lower receipts from the transit of oil and natural gas (the fall in transit receipts was caused in part by the non-standard settlement of retained payments for 2004 – 2006 last year and in part by the appreciation of the Slovak koruna against the US dollar) and increased trade costs of importing goods, whose growth was associated with the expansion of foreign trade. At the same time, the balance of transport services was positively influenced by passenger air transport services, the receipts for which grew at a faster pace than the expenses of Slovak residents on services rendered by non-residents, owing to the development of air transport in the SR. Positive effects on the overall balance were also produced by insurance, legal, and advisory services, where the growth in receipts was accompanied by a fall in expenses.

Table 16 Balance of services (SKK billion)		
	2007	2006
Transport	10.2	21.3
Tourism	12.0	13.6
Other services	-9.1	-12.4
Balance of services	13.1	22.5

Source: NBS.

In 2007, the income balance resulted in a deficit of SKK 79.3 billion, representing a deterioration of SKK 17.2 billion compared with the previous year, when a modest year-on-year decrease in receipts (SKK 0.5 billion) was accompanied by a marked increase in payments (SKK 16.7 billion). The increase in the deficit was caused mainly by increased dividend payments to foreign investors (by SKK 16.8 billion) in 2007, when foreign investors received dividends in the total amount of SKK 81.1 billion. Within the overall income

balance, the increased deficit was moderated to some extent by an increase in the incomes of Slovak residents from abroad, coupled with an increased surplus in the compensation of employees.

Table 17 Income balance (SKK billion)		
	2007	2006
Compensation of employees	34.7	30.8
Direct investment	-109.2	-90.9
of which: reinvested earnings	-23.3	-23.8
Portfolio and other investments	-4.8	-2.0
Income balance	-79.3	-62.1

Source: NBS.

The balance of current transfers produced a deficit of SKK 11.1 billion in 2007. This represented a year-on-year deterioration of SKK 9.5 billion and was mainly the result of a methodological change concerning

Table 18 Balance of current transfers (SKK billion)		
	2007	2006
Government	0.5	8.3
Other	-11.6	-9.9
Balance of current transfers	-11.1	-1.6

Source: NBS.

Box 1 **Reclassification of part of the receipts from EU funds, from current to capital transfers**

In 2007, a methodological change was introduced in respect of the recording of receipts from the EU budget. Originally, all receipts were recorded within the balance of current transfers, since receipts from EU funds could not be identified and classified as current or capital transfers. According to an analysis of the structure of receipts from EU funds, based on partner data supplied to Eurostat by the European institutions concerned, the individual receipts from EU funds could be divided into current and capital transfers. The new classification takes into account the character of the individual funds through which money is drawn from the EU budget, i.e. distinguishes between funds set up for common and/or investment purposes. This led to the shift of part of the receipts (intended for investment purposes) from the balance of current transfers to the balance of capital transfers, with a consequent negative impact on the current account balance. The methodological change had no effect on the external equilibrium, since the lower current account receipts were fully offset by the higher inflow into the capital and financial account.

Table 19 **Balance of payments capital and financial account****(SKK billion)**

	2007	2006
Capital account	11.4	-1.2
Direct investment	71.2	112.9
SR abroad	-9.5	-10.9
of which: equity capital abroad	-6.0	-9.5
reinvested earnings	-1.2	-1.2
In the SR	80.7	123.8
of which: equity capital in the SR	27.4	56.0
of which: FDI other than privatisation ¹⁾	27.4	25.0
Reinvested earnings	24.5	25.0
Portfolio investment and financial derivatives	-16.2	43.4
SR abroad	-19.7	-18.1
In the SR	3.5	61.5
Other long-term investment	18.9	18.6
Assets	-6.4	5.3
Liabilities	25.4	13.3
Short-term investment	100.4	-141.3
Assets	-29.3	-38.4
Liabilities	129.7	-102.9
Capital and financial account in total	185.7	32.4

Source: NBS.

1) Foreign direct investment.

the reclassification of part of the funds drawn from the EU budget, from current to capital transfers (the balance of current transfers was negatively affected, by SKK 16.2 billion).

2.2.2 Capital and financial account

The b.o.p. capital and financial account resulted in a surplus of SKK 185.7 billion, which was SKK 153.3 billion more than in the previous year. The structure of financial flows also changed during the year. In 2006, capital inflows were dominated by direct and portfolio investments, which were partly offset by an outflow of short-term capital. In 2007, the dominant inflow took place in short-term capital for the banking sector. Thus, the structure of the b.o.p. capital

and financial account changed in comparison with the previous year, but, with regard to the marked improvement in the current account balance, only a small part of the deficit was covered by an inflow of short-term funds.

The balance of payments on capital account resulted in a surplus of SKK 11.4 billion in 2007, while the previous year saw a deficit of SKK 1.2 billion, which was influenced by the aforementioned methodological change.

From January to December 2007, foreign direct investment (FDI) recorded an inflow of SKK 71.2 billion, representing a decline of SKK 41.7 billion compared with 2006. The year-on-year change in the balance of direct investments was mainly caused by privatisation

Table 20 **Capital inflows in other investment by sector****(SKK billion)**

	2007	2006	Year-on-year changes
Banks	88.4	-150.6	239.0
Enterprises	36.1	26.5	9.6
Government + NBS	-5.2	1.4	-6.6
Total	119.3	-122.7	242.0

Source: NBS.

tion receipts from 2006, since 2007 witnessed no privatisation. While the total equity capital of foreign investors invested in Slovakia decreased by SKK 28.6 billion in 2007 (compared with the previous year), the equity capital of foreign investors in Slovakia, adjusted for privatisation receipts, increased by SKK 2.4 billion. The lower inflow of capital in form of FDI compared with 2006 was also supported by developments in 'other capital', where there was a decrease in export claims exceeding the increase in import liabilities.

Portfolio investment resulted in a net outflow of SKK 16.2 billion, compared with a net inflow of SKK 43.4 billion in the previous year. The year-on-year change from an inflow to an outflow of SKK 59.6 billion was influenced on the assets side by an increase in demand for long-term foreign bonds among Slovak residents. On the liabilities side, there was a smaller inflow than a year earlier, as a result of lower demand for long-term government debt securities among investors and a new issue of government eurobonds with a lower koruna equivalent. In the corporate sector, there was a larger outflow than in the previous year, resulting from an increase in the repayment of liabilities in respect of bond issues.

In 'other investment', 2007 saw an inflow of funds in an amount of SKK 119.3 billion, compared with an outflow of SKK 122.7 billion in the same period a year earlier. Virtually the entire year-on-year change (SKK 239.0 billion) was associated with developments in the banking sector, while the main factor was again (after an outflow in 2006) an inflow of short-term capital into Slovak banks (bank deposits) in 2007.

This capital inflow was, to a large extent, the result of interbank foreign exchange market developments in March and April, which led to the appreciation of the Slovak koruna and subsequent NBS interventions.

2.2.3 Foreign reserves

At the end of December 2007, the foreign reserves of Národná banka Slovenska reached USD 18.98 billion (EUR 12.91 billion), representing an increase of USD 5.61 million since the beginning of the year. The total foreign reserves of NBS were influenced by several factors during the year. The key factor positively affecting revenues was income arising from NBS interventions in the foreign exchange market in the first half of the year. Expenditures were mainly determined by debt service payments made on behalf of the Government. The Bank's foreign reserves were also affected during the year by movements in the exchange rates of fully convertible currencies in global financial markets. The surplus in the balance of revenues and expenditures (USD 3.77 billion) was accompanied by positive exchange rate differentials (USD 1.84 million), which resulted from movements in the euro exchange rate against the US dollar in international financial markets.

At the end of 2007, the foreign reserves of NBS were 3.5 times greater than the volume of average monthly imports of goods and services to Slovakia during 2007. The ratio of foreign reserves to the amount of payments for goods and services, recorded in banking statistics, reached 4.6 times the volume of average monthly imports of goods and services in 2007.

Table 21 **External debt of the SR**

	In millions of USD		In millions of EUR	
	1.1.2007	31.12.2007	1.1.2007	31.12.2007
Total external debt of the SR	32,205.9	44,308.7	24,448.9	30,156.2
Long-term external debt	16,649.7	20,709.7	12,639.5	14,094.9
Government and NBS ¹⁾	7,702.1	9,502.4	5,847.0	6,467.3
Commercial banks	1,559.2	2,150.8	1,183.6	1,463.8
Entrepreneurial entities	7,388.4	9,056.5	5,608.9	6,163.8
Short-term external debt	15,556.2	23,599.0	11,809.4	16,061.3
Government and NBS	0.0	0.0	0.0	0.0
Commercial banks	6,148.8	12,095.6	4,667.8	8,232.2
Entrepreneurial entities	9,407.4	11,503.4	7,141.6	7,829.1
Foreign assets	26,718.4	37,017.4	20,283.2	25,193.8
Net external debt	5,487.5	7,291.3	4,165.7	4,962.4
SKK/USD and SKK/EUR rates	26.246	22.870	34.573	33.603
EUR/USD cross exchange rate	-	-	1.317	1.469

Source: NBS.

1) Including government agencies and municipalities.



The foreign reserves of commercial banks reached USD 3.0 million (EUR 2.0 billion) at the end of 2007. The volume of foreign reserves in the banking sector, including NBS, stood at USD 21.9 billion (EUR 14.9 billion) at the end of the year.

2.2.4 External debt of the SR

At the end of December 2007, Slovakia's total gross external debt reached USD 44.3 billion (EUR 30.2 billion). Total per-capita gross external debt was at the level of USD 8,237 in the period under review. The share of short-term debt in the country's total gross external debt reached 53.3% at the end of December 2007.

In 2007, the total gross external debt of Slovakia increased by USD 12.1 billion, of which long-term foreign debt accounted for USD 4.1 billion and short-term foreign debt for USD 8.0 billion. The most significant increase was recorded in the short-term foreign liabilities of commercial banks (USD 6.0 billion). This increase was partly due to interbank market developments. Total per-capita gross external debt increased during the year by USD 2,250; the proportion of short-term foreign debt to the country's total gross external debt increased year-on-year by 5 percentage points.

The net external debt of Slovakia, expressed as the difference between gross foreign debt, i.e. USD 44.3 billion (liabilities of NBS and the Government, commercial banks, and the corporate sector – except for equity participation), and foreign assets, i.e. USD 37.0 billion (foreign reserves of NBS, foreign assets of commercial banks and the corporate sector – except for equity participation), increased over the course of 2007 by USD 1.8 billion, to USD 7.3 billion (debtor position) at the end of December 2007.

According to preliminary data, Slovakia's total gross external debt as a share of GDP at current prices reached 54.7% in 2007, representing an increase of 3.8 percentage points compared with 2006.

2.2.5 Nominal and real effective exchange rates of the Slovak koruna

The average year-on-year appreciation of the nominal effective exchange rate (NEER) of the Slovak koruna accelerated in 2007 to 10.2%, from 2.4% in the previous year. To the accelerated appreciation of the NEER index contributed mostly the strengthening of the koruna against the euro (5.6 percentage points), followed by the contribution of an appreciation in relation to the Czech koruna (1.6 percentage points).

The faster appreciation of the Slovak koruna in 2007 (in nominal terms) led to an accelerated appreciation in the real effective exchange rate (REER). The average year-on-year appreciation of the REER index, defined on the basis of consumer prices, accelerated in comparison with the previous year by 5.6 percentage points, to 9.8%. In the case of the REER index, defined on the basis of industrial producer prices, the rate of appreciation accelerated by 1.2 percentage points, to 7.8%. The appreciation of the REER index, defined on the basis of manufacturing products prices, accelerated by 5.5 percentage points, to 5.9%. The slower appreciation of the individual real effective exchange rate indices in comparison with the nominal effective exchange rate resulted from the ongoing disinflation process in the Slovak economy, mainly in the first half of 2007. The main factors in this process were a slower rise in regulated prices and raw materials and energy prices, but also an economic growth not exceeding markedly the dynamics of potential output and exerting no excessive demand-based inflationary pressures.

2.3 General government sector

Budgetary performance in the general government sector during 2007 resulted in a deficit corresponding to 2.2% of GDP. Compared with the approved deficit (2.9% of GDP), the actual outcome was much more favourable. This result is mainly attributable to the central government budget performance. Though the reduction in the central government budget deficit can partly be ascribed to saving on the expenditure side, the determining factor was the higher than expected tax revenues. In addition to better than expected macroeconomic developments, tax revenues were significantly influenced by the effect of pre-stocking-up on tobacco products, as a result of an excise tax increase with effect from 1 January 2008.

Apart from the State budget, the overall result was also influenced favourably by the budgetary performance of the Social Insurance Agency and public universities. On the other hand, budgetary performance at the level of local governments was unfavourable in comparison with the central government budget. A negative contribution also came from the higher than projected payments under Pillar II of the pension insurance system. The budgetary performance of health insurance companies also showed a slightly unfavourable tendency in comparison with the budget. The additional inclusion of the Slovak Television and Slovak Radio in the general government sector (upon the recommendation of Eurostat) had a neutral effect on the sector's overall budget deficit.

Funds drawn from the EU budget reached 88% of the figure planned for 2007.

In 2007, the gross debt of the general government sector reached 29.4% of GDP, which was less than the budgeted figure (31.8% of GDP).

The parameters of the sector's deficit and debt in 2007 reached the values required for meeting the Maastricht criteria and the conditions of the Stability and Growth Pact.

2.4 Monetary developments

2.4.1 Monetary aggregates

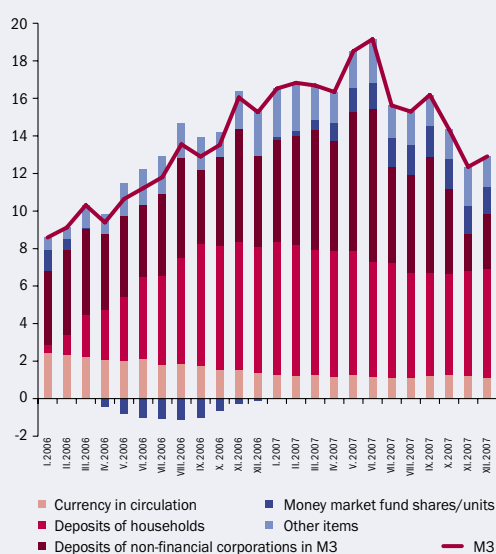
The M3 monetary aggregate followed different trends in the two halves of 2007. Its year-on-year dynamics showed a slightly increasing tendency over the first six months (the strongest dynamics were recorded in June: 19.2%). The second half of the year saw a gradual slowdown, to 12.8% in December 2007. The volume of M3 reached SKK 1,082.7 billion at the end of 2007. Among the money supply components, the largest contributions to M3 growth were made during the year by the less liquid components, mainly household deposits and received loans with an agreed maturity of up to 2 years, though their contributions diminished in the second half of the year. The opposite trend was recorded in deposits and received loans repayable on demand. Their growth accelerated in the second half of the year, due to developments in household deposits, while the deposits of non-financial corporations grew at a slightly slackening pace throughout the year. Among the counterparts of M3, the growing trend continued in the monetary financial institutions (MFIs) loans to the private sector, mainly to non-financial corporations.

Main components of M3

After diminishing in the first half of the year, the contribution of deposits and received loans repayable on demand was growing steadily over the second half. The contribution was, however, positive throughout the period under review. Contributions from the most liquid types of deposits to M3 growth reflected developments in household deposits and received loans repayable on demand. The deposits of non-financial corporations recorded a slowdown in dynamics throughout 2007. This trend was also supported by increased dividend payments abroad by the corporate sector. After decelerating in the previous year, the year-on-year rate of growth in currency in circulation was stagnant (at 8.5% on average), which was also reflected in its stagnating contribution to the money supply growth.

Developments in the less liquid money supply components (M2 minus M1), mainly in fixed-term house-

Chart 24 Contributions of individual M3 components to its year-on-year dynamics (p.p.)



Source: NBS.

hold deposits, were also connected with the trend in deposits repayable on demand, which represented their main substitutes. During the first half of the year, they followed the trends from the previous year and their contributions reached a relatively high level. This trend came to a halt in the second half of the year, when the contributions of household deposits with an agreed maturity of up to 2 years began to diminish. The deposits and received loans of non-financial corporations repayable within 2 years recorded stable growth virtually throughout the year, which, however, slowed in the final quarter. Deposits redeemable at notice of up to 3 months continued to decrease and thus made a negative contribution to the money supply growth.

The smallest increase in the money supply was generated by marketable instruments (M3 minus M2). They represent the least liquid components and are formed mostly by money market fund shares/units. In 2007, households' interest in investment in money market fund shares/units recovered, at the expense of a slight fall in the volume of fixed-term household deposits and, towards the end of the year, a similar recovery was recorded with regard to the shares/units of investment funds other than money market funds. As a result of this growth, they made a positive contribution to the year-on-year dynamics of M3 throughout the year. Other marketable instruments were repo operations and debt securities issued with a maturity of up to 2 years, whose share in the money market stagnated around the level of 0.7%. Consequently, their contributions to M3 growth remained virtually unchanged during the year.

Table 22 **Developments in the main M3 components and counterparts**

	Changes since the beginning of the year (SKK billion)		Changes since the beginning of the year (%)		Volume as at 31.12.2007 (SKK billion)
	2006 ¹⁾	2007 ¹⁾	2006 ¹⁾	2007 ¹⁾	
Currency in circulation	11,3	10,5	9,5	8,0	141,7
Deposits and received loans repayable on demand	53,6	61,3	14,6	14,4	480,9
M1	64,9	71,9	13,4	12,9	622,6
M2	123,2	106,9	15,7	11,7	1 015,0
M3 monetary aggregate	127,0	124,4	15,3	12,9	1 082,7
Main counterparts of M3					
Loans and securities of MFIs	100,5	151,2	13,4	17,8	1 046,9
of which: general government	-18,7	6,8	-6,3	3,1	261,6
other residents (private sector)	119,2	144,3	23,6	23,6	785,3
Net foreign assets	-5,5	6,2	-2,8	-0,7	262,2
Long-term financial liabilities (excluding capital and reserves)	19,7	19,3	19,0	15,7	141,9
Other items net (including capital and reserves) ²⁾	51,6	-13,8	-54,8	-11,5	-84,5

Source: NBS.

1) Since the components and counterparts of the M3 monetary aggregate are not compiled for 1 January of the given year (in line with ECB methodology), the initial values for these years as stated in the table and the text below are values for 31 December of the previous years.

2) Other items net, including the deposits of the central government. The values are calculated as follows: M3 = loans to the general government + loans to other residents + net foreign assets – long-term financial liabilities + other items net.

Main counterparts of M3

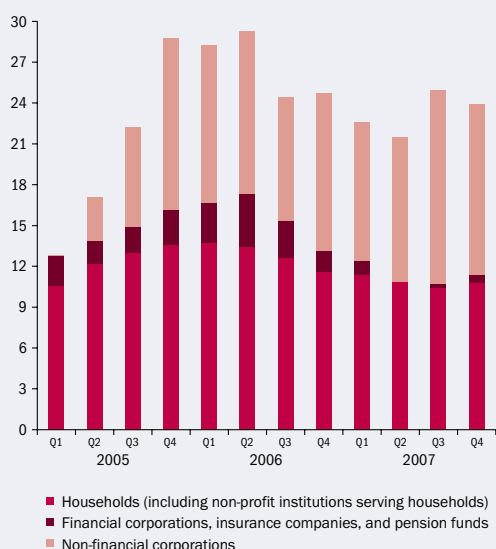
Among the main M3 counterparts, the decisive factor was loans to the resident private sector, which consisted of loans to enterprises and households (both being virtually equal). The annual increase in long-term financial liabilities (excluding capital, reserves, and provisions) diminished somewhat in 2007, due mainly to a smaller increase in deposits and received loans with an agreed maturity of over 2 years. Developments in 'other items net' were substantially influenced by a fall in capital, reserves, and provisions, which was much smaller than in 2006.

The volume of MFI loans to residents (including securities issued by clients and held by MFIs) increased during 2007 by SKK 151.2 billion, which was 50% (SKK 50.7 billion) more than in the previous year. The growth in MFI loans took place mostly in the private sector (SKK 144.3 billion), but its year-on-year dynamics remained unchanged, at the level of 2006. The increase in MFI loans to the general government sector was positive (unlike in 2006). Their contribution to the total growth in MFI loans was roughly the same as that of MFI loans to the private sector.

MFI loans to the private sector

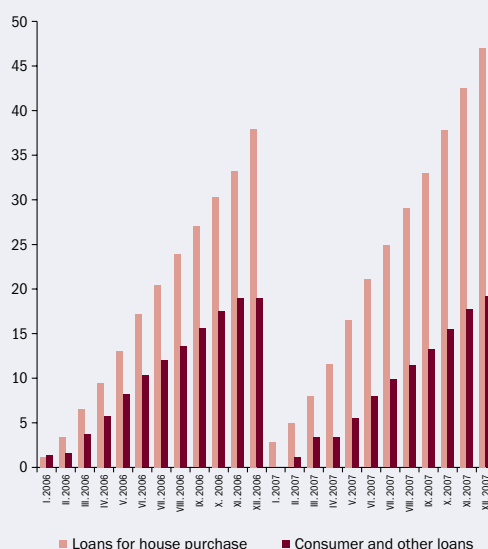
The MFI loans to the private sector (excluding securities) reached SKK 770.0 billion at the end of December 2007, representing an increase of SKK 142.7 billion since the end of 2006 (compared with SKK 119.8 billion in the previous year). Broken down by sector, the most significant contribution to credit growth came from non-financial corporations, with slightly increasing dynamics, mainly in the second half of 2007. Loans to households recorded a slowdown in the rate of growth over the first three quarters, which were followed by a period of stagnation. This development took place partly in loans denominated in Slovak koruna (an increase of SKK 104.9 billion) and partly in euro-denominated loans (an increase of SKK 34.9 billion) and loans in other foreign currencies (SKK 2.8 billion). The structure of loans by currency had remained virtually unchanged until the end of 2007. The share of koruna loans in the total volume decreased somewhat, to 78.8%, while the share of euro loans increased to 19.8%, and loans in other currencies accounted for 1.4%. At the end of 2006, koruna loans accounted for 80.0%, euro loans for 18.8%, and loans in other foreign currencies for 1.2% of the total volume of loans. Most loans in foreign currencies were concentrated in the non-financial

Chart 25 Contributions to the year-on-year growth in MFI loans to the private sector (p.p.)



Source: NBS.

Chart 26 Increases in loans to households (cumulative data since the beginning of the year) (SKK billion)



Source: NBS.

corporations sector (an average 34.8% of the total corporate loans), while households tended to borrow funds in Slovak koruna (foreign-currency loans accounted for only 2.6 %).

MFI loans to households

During 2007, the MFI loans to households followed the growing trend from the previous year, and closed the year with an absolute year-on-year increase of SKK 66.2 billion; they reached a year-on-year growth rate of 28.5%. The dynamics of bank lending to households were weakening slightly until September, when this trend came to a halt; the final quarter of 2007 was marked by stagnation. Compared with December 2006, the rate of growth slowed by 4.0 percentage points.

In 2007, as in the previous year, households used credit resources mostly for long-term investment. Within the structure of loans by purpose, the steepest year-on-year increase was recorded in loans for house purchase⁴ (SKK 47.0 billion, compared with SKK 37.9 billion in 2006), which contributed 19.9 percentage points to the year-on-year growth in loans to households. Consumer and other loans recorded an absolute year-on-year increase of SKK 19.2 billion, which was similar to the figure for 2006 (SKK 18.9 billion). Their contribution to the growth dynamics of loans to households diminished gradually during the year,

to 8.6 percentage points in December. Consumer and other loans represented one of the sources of growth in household final consumption. Their share in household final consumption slightly increased in 2007, by 1.1 percentage points compared with the previous year, to 9.7% (2006 saw an increase of 1.3 percentage points, to 8.6%). It was, however, lower than in the euro area and the other V4 countries.

The growth in monetary financial institutions loans to households was accompanied by a rise in the level of indebtedness (expressed in terms of the ratio of loans to households to GDP), which increased year-on-year by 2.1 percentage points and reached 16.4% at the end of 2007. Similar developments in connection with the process of real convergence were also recorded in the other new EU Member States, while household indebtedness in these countries was much lower than in the euro area (54.4% in 2007).

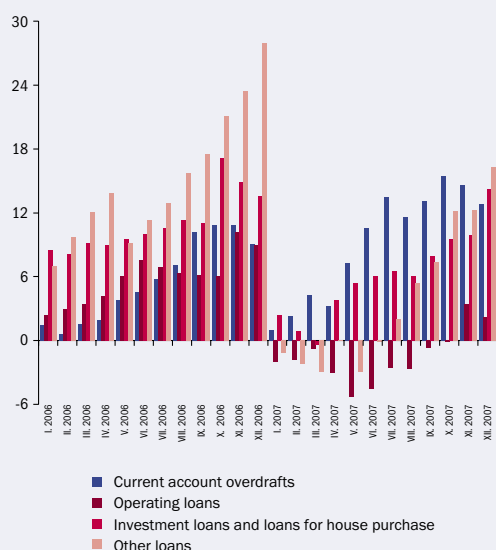
MFI loans to non-financial corporations

Loans to the non-financial corporations sector showed less dynamic development than those to the household sector. After moderating over the first half of the year, the year-on-year rate of growth accelerated again and reached an average of 22.4% in 2007. In terms of purpose, the increase in loans to non-financial corporations was concentrated in investment loans and loans for house purchase throughout the year,

⁴ Loans to households (including non-profit institutions serving households) broken down by purpose comprise house purchase loans, consumer loans, and other loans.

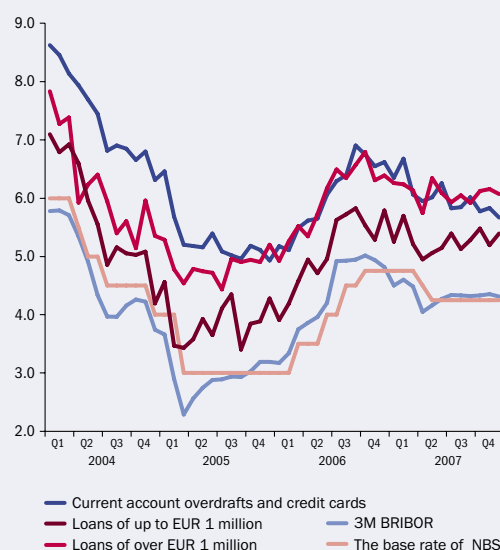


Chart 27 Increases in loans to non-financial corporations (year-on-year growth) (SKK billion)



Source: NBS.

Chart 28 Interest rates on loans to non-financial corporations, 3-M BRIBOR, and the NBS base rate (%)



Source: NBS.

even if these increases were much smaller than in the previous year. Current account overdrafts grew significantly almost throughout the year. Regarding the time structure of loans, the growth in MFI loans to non-financial corporations took place mostly in short-term loans (up to 1 year), which recorded a gradual increase in dynamics. Concerning long-term loans, the contributions of loans from 1 to 5 years and those over 5 years were virtually equal, while their dynamics were stagnant during the year. The dynamics of loans with the longest maturities weakened somewhat at the end of the year.

2.4.2 Factoring, leasing and consumer credit companies loans

In 2007, NBS began to collect data from financial corporations granting loans (leasing companies, factoring companies, and consumer credit companies, personal or business finance companies) that according to ESA95 methodology form the S.123 sector "Other financial intermediaries, except for insurance corporations and pension funds". By definition, this sector is formed also by investment funds, except for money market funds, financial corporations providing credit and loans (leasing, factoring, instalment financing, personal or business financing), dealers in securities and derivatives, financial holding companies, and financial vehicle corporations. These statistics provide a more comprehensive picture of developments in the Slovak financial market, on the basis of balance-sheet data reflecting the activities

of financial intermediaries outside the sector of monetary financial institutions.

The factoring, leasing and consumer credit companies (FLCC) loans to the private sector reached SKK 124.1 billion at the end of 2007. About 71% of these loans were loans to non-financial corporations, and 28.5% were loans to households.

The volume of loans to non-financial corporations increased throughout the year and reached SKK 88.4 billion at the end of December. Broken down by purpose, loans to enterprises were dominated by financial leasing (SKK 65.8 billion). The share of FLCC loans in total loans to corporations (MFI and FLCC loans) reached an average of 18.1% in 2007.

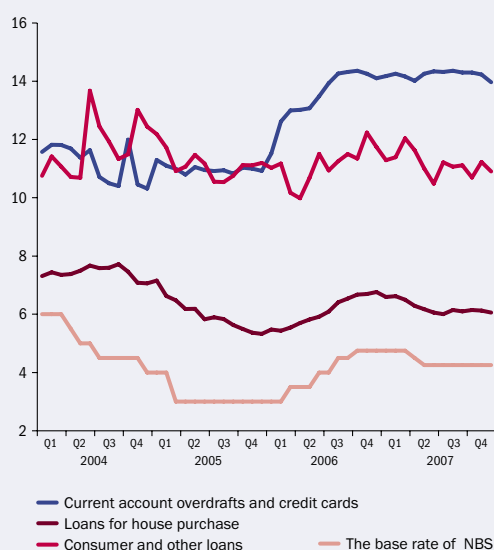
2007 also saw a gradual increase in the volume of loans in the household sector (totalling SKK 35.3 billion at the end of the year). The main components were instalment loans and consumer loans; they accounted for two thirds of the total FLCC loans to households. The growth in their volume was accompanied by an increase in their share in household final consumption, which reached 3.4% at the end of the year. This form of household financing accounted for 10.3% of the total loans to households (MFI and FLCC loans).

2.4.3 Customer interest rates

Customer interest rates were influenced in 2007 by reductions in the key NBS rates at the end of March

Chart 29 Interest rates on loans to households by type

(%)



Source: NBS.

and April (by 0.50 of a percentage point in total) and by developments in interbank market rates. Banks reacted to changes in the key interest rates of NBS relatively flexibly in the case of loans to non-financial corporations and households, and less flexibly in the case of deposits from non-financial corporations and households. In the case of certain types of loans and deposits, the effects of interbank market developments prevailed. Customer interest rates fell mostly in the first few months of 2007, later in the year they were relatively stable.

Interest rates on loans to non-financial corporations

Developments in interest rates on loans to non-financial corporations were dominated at the beginning of the year by a slightly falling trend, resulting from a cut in the base interest rate of NBS coupled with low interbank market rates attributable to a liquidity surplus. In the following period, interest rates were relatively stable, showing only small fluctuations. The changes in the base interest rate of NBS and the low interbank market rates were mostly reflected in short-term customer interest rates; long-term rates reacted very mildly. Most loans to non-financial corporations were provided with a short fixation period or without initial rate fixation, hence their interest rates reacted relatively sensitively to changes in the key rates. Interest rates on loans for small and medium-sized enterprises (up to EUR 1 million) and loans for large enterprises (over EUR 1 million) behaved in the same way. They

fell somewhat in the first few months, and followed a slightly rising trend in the following period. The falling trend in rates for current account overdrafts for non-financial corporations persisted throughout 2007, which was partly the result of developments in interbank market rates.

Interest rates on loans to households

Developments in interest rates on loans to households were characterised, as in the case of non-financial corporations, by a slightly falling trend in 2007, which reflected the cuts in the key NBS rates in the first months of the year.

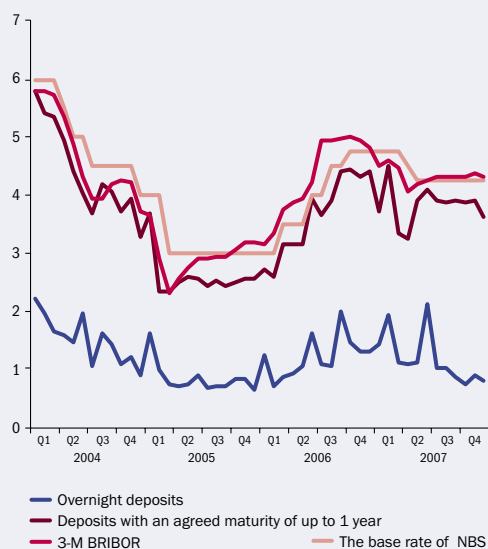
Interest rates on current account overdrafts and credit cards were stable throughout the year, and showed no reactions to the cuts in the key NBS rates.

The rising trend in interest rates on loans for house purchase, which persisted throughout 2006, came to a halt at the beginning of 2007. After NBS had lowered its key rates, customer interest rates on loans for house purchase began to fall slightly. This trend continued until July, when the decline came to a halt. From that time, interest rates on loans for house purchase were more or less stable, at the level of approximately 6.1%. This represented a fall of 0.70 of a percentage point compared with December 2006. Within the scope of loans for house purchase, interest rates dropped considerably on mortgage loans and other loans for house purchase. Interest rates on home savings bank loans showed different tendencies. Interest rates on intermediate loans dropped somewhat, while the rate for building loans rose slightly. Interest rates on home savings bank loans reacted to changes in the key NBS rates and market rates in a minimum extent, which can be explained by the different character of these products (compared with bank loans).

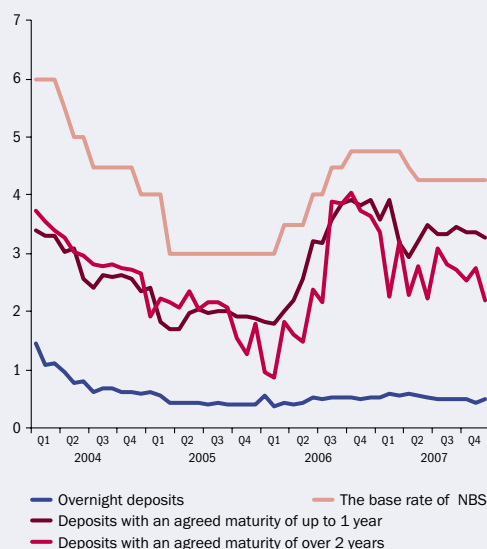
Interest rates on loans for consumption (consumer and other loans) were relatively volatile during the year, and showed a slightly falling tendency. This development was mostly influenced by drops in rates for non-specific loans and other loans. On the other hand, the opposite trend was recorded in rates for consumer loans granted for specific purposes, which increased.

Interest rates on deposits from non-financial corporations

Interest rates on deposits from non-financial corporations followed a slightly falling trend in 2007. The most significant drops were recorded in interest rates on deposits with agreed maturity. Among these rates,

**Chart 30 Interest rates on deposits from non-financial corporations (%)**

Source: NBS.

Chart 31 Interest rates on household deposits (%)

Source: NBS.

the sharpest drop occurred in the rate for short-term deposits (deposits with an agreed maturity of up to 7 days and up to 3 months). A fall was also recorded in the price of overnight deposits, which reacted to changes in interbank rates relatively sensitively. Interest rates on long-term deposits were rather volatile, owing to the small share of these deposits.

Interest rates on household deposits

Interest rates on household deposits were characterised by a slight fall in 2007 (except for overnight deposits). Rates for overnight deposits remained unchanged throughout the year, though a significant drop was recorded within this category in the price of one day deposits. A slight fall was also recorded in rates for deposits with an agreed maturity of up to 1

year (mainly for deposits fixed for up to 7 days). This occurred in the first half of the year as a result of a reduction in the key NBS rates. The sharpest drops were recorded in rates for long-term deposits (fixed for over 2 years), which fell by as much as 1.4 percentage points. Interest rates on deposits redeemable at notice dropped only slightly in 2007.

Real interest rates, calculated by deflating the average interest rate on new one-year household deposits by HICP inflation, showed a slightly rising tendency until August 2007, mainly as a result of a slowdown in inflation coupled with a slight fall in interest rates on household deposits. In the following months, the inflation rate accelerated somewhat, while deposit rates were at a standstill, which led to a modest fall in real interest rates.

NBS Operations



3 NBS Monetary Policy Operations, Foreign Exchange Operations and Investment Activities in Foreign Reserve Management

3.1 Monetary policy operations

In 2007, NBS continued in monetary policy implementation using the same instruments. Goal-directed decision-making took place within the dates set out in the schedule of NBS Bank Board's meetings. The essential parameter of the monetary policy in the medium term was to set the target value for inflation, defined as inflation targeting in the ERM II conditions. The main instruments of NBS in relation to this medium-term target were the key interest rates. The Central Bank conducted its monetary policy using the basic set of instruments, which comprised operations with banks and foreign bank branches, in particular open market operations including the issuance of short-term securities and O/N operations. As in the previous year, NBS was interested in correcting increased volatility in the exchange rate of the Slovak koruna in the foreign exchange market.

Liquidity of the banking sector

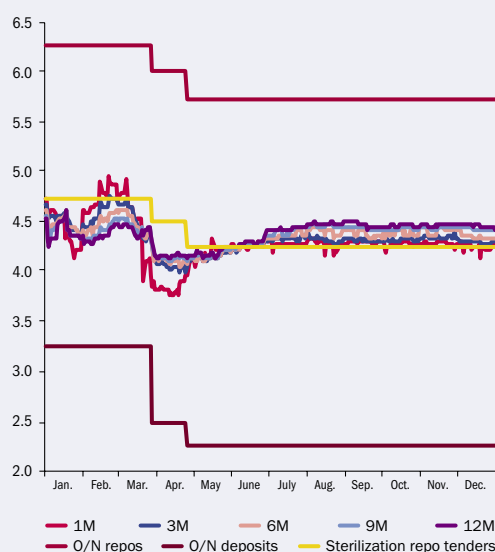
The banking sector had a liquidity surplus at its disposal in the recent nine years. The average daily amount placed by banks in sterilization operations with NBS was SKK 360.3 billion in 2007; in comparison with 2006 it increased by SKK 14.2 billion. In comparison with the sterilization amount of SKK 273.2 billion at the beginning of 2007, the highest sterilization position was recorded in June, in an amount of SKK 400.9 billion. The reason for this increase in the total sterilization amount was an inflow of funds from foreign exchange interventions.

Main monetary policy operations

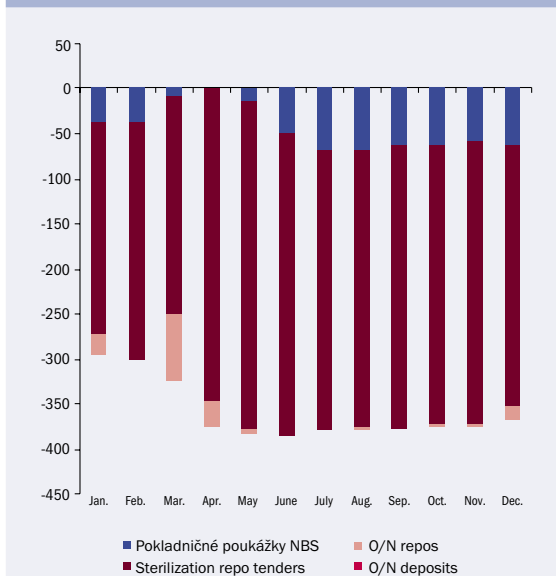
Standard sterilization repo tenders continued to dominate the open market operations. This instrument's share in the total sterilization position was changing during the year, depending on the Central Bank's

activity in the domestic foreign exchange market. 84% of liquidity surplus was absorbed on average through this instrument (sterilization repo tenders). Nevertheless, its share fell to 74% in March. Likewise in the previous period, sterilization repo tenders were held on a regular weekly basis and their 14-day maturity period remained also unchanged. A total of 52 sterilization repo tenders were held during the year, and NBS accepted the full demand in 39 cases. In 34 cases, the average interest rate matched NBS current interest rate limit for two-week repo tenders. This key interest rate was reduced by the NBS Bank Board several times during the year. After starting at 4.75%, it underwent two adjustments to stand at 4.25%. The first adjustment extended the spread for O/N refinancing and sterilization operations with NBS from the original 3% to 3.5%. The banking sector

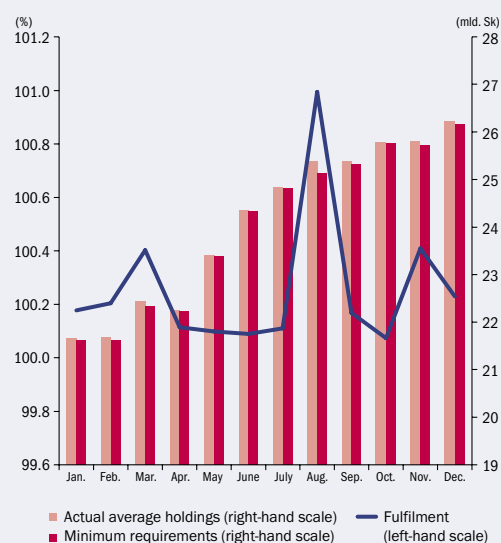
Chart 32 **BRIBOR interest rates in 2007**
(% p. a.)



Source: NBS.

**Chart 33 Open market operations by type (monthly average) (SKK billion)**

Source: NBS.

Chart 34 Required minimum reserves in 2007

Source: NBS.

reflected the key interest rate cut in money market interest rates. Under the effect of interest rate movements as well as persisting expectations for further rate cuts, the money market yield curve acquired an inverse shape during the first three months of the year. The emergence of a standard shaped curve approximately in April reflected the market expectations of stable NBS interest rates until the end of 2007.

Longer-term monetary policy operations

Regular auctions of NBS bills represented a supplementary monetary instrument that NBS also used in 2007. In total, 11 auctions with a standard 84-day maturity were held. An interest in this form of sterilization in the first half-year was mainly related to the expectation of the banking sector for a reduction in the NBS key interest rates. In the first two months of 2007, the share of funds absorbed through this three-month instrument reached 12% of the total NBS sterilization position on average. In March and April, banks held no NBS bills in their portfolios; thus, their share was zero. With the return of the Central Bank to standard monetary policy operations, the sterilization through this instrument started to grow. In the second half of 2007, the share of NBS bills in the overall sterilization was 16.3%.

Standing facilities

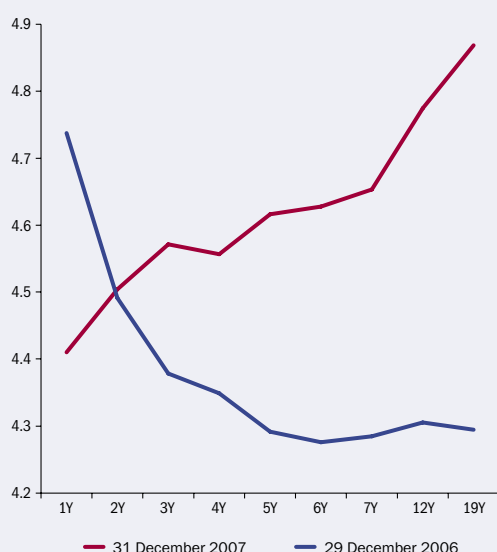
O/N standing facilities, which take the form of deposits with NBS, if there is liquidity excess, or repo transactions, if liquidity is insufficient, were used by

banks to adjust their current liquidity positions. Both forms were applied in a standard way with a one-day maturity. They were typically used at times when banks incorrectly estimated their liquidity needs for meeting the minimum reserve requirements. Towards the ends of months, especially on the last days, bank's recourse to these facilities accelerated. In the second half of March, the share of O/N deposits in the overall sterilization reached as much as 50%. Sterilization operations were a dominating factor of entire monetary policy; they also dominated standing facilities. Nevertheless, banks made also use of overnight credit from time to time. Another line of financing consisted of drawing intra-day credit. In comparison with standing facilities, this method was used only to ensure smooth operation of the payment system and did not have any monetary effects.

Minimum reserve system

NBS applies the requirement to create and maintain minimum reserves to banks, branches of foreign banks, building societies and electronic money institutions. A total of 25 financial institutions maintained minimum reserves in 2007, and two of them started to hold the reserves only over the course of the year. The minimum reserve rate was 2% and was applied to the set basis valid since 2004. By using this direct monetary instrument NBS affects the level of banking sector's liquidity and also maintains the minimum liquidity in financial institutions to which the minimum reserve system applies, with regard to the needs of non cash payment system. The minimum reserves basis consisting of financial institutions' primary de-

Chart 35 Benchmark yield curve of government bonds (% p. a.)



Source: NBS.

posits in the entire term spectrum except mortgage bond issues, increased 19.3% compared to 2006. As a result, the value of minimum reserve requirements followed a growing trend during the previous year. The initial amount of minimum reserves (SKK 21.6 billion) increased to 26.2 billion as at the end of the year.

Risk management

In 2007 NBS continued to apply the risk management system introduced in 2005. The assessment of counterparties, financial assets eligible for monetary policy operations and the valuation of financial assets including the application of haircuts follow the rules set in advance. However, NBS procedures applicable to assets were significantly simplified in 2007, for monetary policy operations were conducted using exclusively NBS securities. As of 2007, NBS started to implement an integrated information system for monetary policy operations, including communication with external participants, such as Burza cenných papierov v Bratislave, a. s. (Bratislava Stock Exchange), Centrálny depozitár cenných papierov SR, a. s. (Central Securities Depository), and, in selected parts, also with NBS's counterparties or with the Target2 payment system being in preparation. NBS plans to complete this integrated information system by the end of 2008.

Benchmark bond yield curve

NBS monitored the benchmark portfolio structure on a continuous basis and updated it in cooperation with

the banks. The benchmark portfolio of securities was last updated in May 2007, with the aim to broaden the term structure of quoted government bonds. As at the end of 2007, the portfolio consisted of bonds with maturity from 1 to 7 years and 10, 12 and 19 years. The prices were set by processing of quotations by seven banks active in the market on a daily basis, and they were published on the Reuters system. NBS and banks use indicative benchmark curve prices for the theoretical valuation of financial assets.

Government bond yields were affected mainly by expectations for a cut in NBS key interest rates in the first months of 2007. Based on this fact, the entire benchmark curve shifted downwards, with yields on shorter maturities dropping most significantly. In May and June 2007, a marked rise of bond yields towards the European level was a typical feature. In the second half of 2007, the Slovak bond yield curve was affected mainly by the European benchmark. Moreover, the exchange rate of the Slovak koruna influenced this trend to a certain extent. This period of time was rather calm and the bond yields did not record significant changes.

3.2 Foreign exchange operations

Foreign exchange market operations

During 2007, the exchange rate of the Slovak koruna against the euro appreciated by 2.8% (from SKK/EUR 34.573 at 31 December 2006 to SKK/EUR 33.603 at 31 December 2007). The average exchange rate was SKK/EUR 33.378, representing an appreciation of 9.3% in comparison with 2006. Over the course of 2007, the exchange rate of the Slovak koruna against the US dollar strengthened by 12.9% (from SKK/USD 26.246 SKK/USD at 31 December 2006 to SKK/USD 22.870 at 31 December 2007). The average exchange rate was SKK/USD 24.713, representing an appreciation by 16.9% compared to the previous year. The exchange rate of the Slovak koruna against the Czech koruna weakened by 0.6%.

At the beginning of the year, the intervention made in the last days of 2006 faded out in the Slovak foreign exchange market, influencing the consideration and investment intentions of market players. However, the exchange rate of the Slovak koruna continued to move, and, on 8 March, the Slovak koruna approached the level of SKK/EUR 33.800. In this situation NBS intervened, and started to purchase the euro in the foreign exchange market. During the intervention, EUR 530 million was purchased. By this intervention NBS stabilized the exchange rate of the Slovak koruna only for a short period of time. On Friday 16 March a change was made to the central

**Chart 36 Exchange rates of the Slovak koruna against the euro and dollar in 2007**

Source: NBS.

Chart 37 Foreign reserve assets managed by the NBS (USD billion)

Source: NBS.

parity, from which the exchange rate of the Slovak koruna can deviate in the ERM II system. The original rate of SKK/EUR 38.455 was reduced by 8.5% to SKK/EUR 35.4424. During the following weekend, the exchange rate of the Slovak koruna changed by more than 100 haliers, to as little as SKK/EUR 32.710. On Tuesday 20 March, NBS entered the foreign exchange market again and purchased EUR 1,400 million, thus moving the exchange rate of the Slovak koruna to as much as SKK/EUR 33.650. At its meeting at the end of March, the Bank Board of NBS reduced the base rate by 25 basis points to 4.50%. In the following days, transactions with the Slovak koruna approached the level of SKK/EUR 33.100, and NBS reacted to this situation with the third and last intervention in 2007. On 4 April, NBS purchased EUR 700 million, and the exchange rate of the Slovak koruna moved to a level above SKK/EUR 33.600. Later on, at the end of April, the Bank Board of NBS reduced the base rate to 4.25%. The exchange rate of the Slovak koruna stabilized, and in the following months it was influenced mainly by regional or global market factors. The exchange rate of the Slovak koruna correlated markedly with the exchange rates of the comparable surrounding countries, except with the Czech koruna, and the movement of the exchange rate of the Slovak koruna was subject rather to a risk appetite or aversion of the world markets. Till the end of the year, the Slo-

vak koruna copied developments in the region and hovered at around SKK/EUR 33.500.

Investment activities in foreign reserve management

In 2007, as in previous years, NBS followed, in foreign reserve management, investment policy in accordance with the rules set out in the long-term investment strategy approved in 2004. Since the trend of the exchange rate of the Slovak koruna against the euro had a markedly high volatility over the course of 2007, the subsequent interventions to correct it influenced the amount of total foreign exchange reserves. Over the course of 2007, NBS purchased a total of EUR 2,630 million in interventions. The value of foreign reserve assets at the respective exchange rates and market prices increased from USD 13.36 billion at the end of 2006 to USD 18.98 billion at the end of 2007. The increase in foreign reserve assets was mainly due to interventions. The amount of foreign assets denominated in US dollars was also affected by the strengthening of the euro against the dollar. The return on foreign reserve assets was 3.7% for the euro investment portfolio and 7% for the dollar investment portfolio. The total income from foreign reserve assets based on both portfolios reached approximately SKK 17.7 billion in 2007.

Supervision of the Financial Market



4 Supervision of the Financial Market⁵

4.1 Financial market regulation in Slovakia

In exercising supervision of the financial market – in banking, the capital market, the insurance industry and pension saving – the Národná banka Slovenska follows general procedural rules laid down in Act No. 747/2004 Coll. on financial market supervision and on amendments to certain acts as amended. This Act entered into force on 1 January 2006, the date when Národná banka Slovenska assumed the competences of an integrated financial market regulator. Until 31 December 2005, the said powers with respect to the insurance sector, capital market and pension saving had been exercised by the Financial Market Authority.

The aim of financial market supervision (responsibility for which lies with a Vice-Governor of Národná banka Slovenska) is to support both the stability of the financial market as a whole and its secure and smooth operation. Based on this fact, the financial market supervision unit conducts financial market regulation, involving mainly the following activities:

- rulemaking activities (it produces draft generally binding legal regulations of Národná banka Slovenska in the financial market field, in particular, draft prudential regulation, operational security rules and other requirements for the conduct of business by supervised entities, it participates in the preparation of generally binding legal regulations issued by central government bodies),
- licensing activities (it conducts proceedings, takes first-instance decisions, issues authorizations, approvals and prior approvals, and imposes sanctions and corrective measures),
- supervision activities (it supervises financial market entities through on-site and off-site supervision),
- analytical activities (it produces analyses of the financial market as a whole, as well as of individual financial entities).

A new area, falling within the competence of the financial market supervision unit from February 2007, is consumer protection by virtue of Art. 3(1) of Act of

the National Council of Slovakia No. 566/1992 Coll. on NBS as amended.

The financial market comprises four sectors – the banking sector (principally represented by banks and branches of foreign banks), the capital market (principally represented by investment firms, management companies, the stock exchange, the central securities depository, issuers and intermediaries of investment services), insurance sector (principally represented by insurance companies and branches of foreign insurance companies) and the pension savings market (principally represented by pension fund management companies and supplementary pension companies).

Slovakia's membership of the European Union means that foreign regulated entities may operate in the country without an authorization from Národná banka Slovenska, provided that they are authorized to conduct such activities in another EU Member State (the single passport principle).

4.2 Rulemaking activities of the supervision unit

In the field of financial market regulation, several acts, regulations, methodological instructions and recommendations governing the legal environment of regulated entities were adopted in 2007. The purpose of this part is not to enumerate these measures, but rather to draw attention to those which have had the greatest effect on the activities of regulated entities in individual financial market sectors in Slovakia.

The main tasks of acts and regulations adopted in the banking sector in 2007 were an improvement of the criteria for prudential behaviour for banks and investment firms, as well as the criteria for the conduct of business and for keeping records of the conduct of business in the single market in the European Union. The most important legal regulation for the banking sector and the investment services sector was the adoption of Act No. 209/2007 Coll. amending Act No. 566/2001 Coll. on securities and investment

⁵ A detailed report for 2007 is published on the NBS website [www.nbs.sk/Financial Market Supervision/Banking Sector and Securities Dealers Supervision/Statistical Data and Analyses/Analysis of the Slovak Banking Sector](http://www.nbs.sk/Financial%20Market%20Supervision/Banking%20Sector%20and%20Securities%20Dealers%20Supervision/Statistical%20Data%20and%20Analyses/Analysis%20of%20the%20Slovak%20Banking%20Sector).



Table 23 Number of supervised entities as at 31 December 2007

	Number of institutions as at 31 December 2007	Number of institutions as at 31 December 2006	Change
Number of banks in Slovakia	16	17	-1
Home savings banks	3	3	0
Mortgage-lending banks	8	9	-1
Other banks	5	5	0
Number of branches of foreign banks in Slovakia	10	7	3
of which: authorized by NBS	1	1	0
on the single European passport principle	9	6	3
of which: branches of foreign mortgage-lending banks	1	1	0
Number of foreign banks branches' contributing to the Deposit Protection Fund	2	2	0
Number of foreign banks' representative offices in Slovakia	9	10	-1
Number of branches (organizational units) of banks in Slovakia	738	715	23
Number of lower organizational units in Slovakia	431	460	-29
Number of branches of Slovak banks in other countries	1	1	0
Number of representative offices of Slovak banks in other countries	1	1	0
Number of foreign entities freely providing cross-border banking services	190	131	59
of which: Banks	178	123	55
Electronic money institutions	6	3	3
Foreign financial institutions	4	3	1
Credit cooperatives	2	2	0
Slovak banks providing free cross-border banking services abroad	1	1	0
of which: Electronic money institutions	0	0	0
Number of staff of banks and branches of foreign banks	19,779	19,525	274
Number of insurance companies in Slovakia	23	24	-1
of which: Insurance companies providing only life insurance	5	5	0
Insurance companies providing only non-life insurance	5	6	-1
Insurance companies providing life or non-life insurance	13	13	0
Insurance companies providing services on a freedom to provide services basis	370	296	74
of which: without establishing a branch	360	289	71
of which: through branches	10	7	3
Number of insurance companies in Slovakia providing compulsory contractual third-party liability insurance for motor vehicles	9	9	0
Number of pension fund management companies	6	6	0
Number of supplementary pension companies	5	3	2
Number of supplementary pension insurance companies	0	1	-1
Number of domestic management companies in Slovakia	10	10	0
of which: management companies with an extended licence under Article 3(3) of the Collective Investment Act	6	7	-1
Number of domestic mutual funds	118	109	9
of which: Open-end mutual funds	72	62	10
Closed-end mutual funds	41	44	-3
Special mutual funds	5	3	2
Number of foreign management companies and foreign collective investment undertakings operating in Slovakia on the basis of an authorisation issued under Article 75 of the Collective Investment Act	2	3	-1

Table 23 Number of supervised entities as at 31 December 2007 (continuation)

	Number of institutions as at 31 December 2007	Number of institutions as at 31 December 2006	Change
of which: through a branch in Slovakia	0	2	-2
without establishing a branch	2	1	1
Number of foreign management companies and foreign collective investment undertakings operating in Slovakia on the basis of a single European passport	43	21	22
of which: With a branch of foreign management companies under Art. 28 of the Act	2	0	2
Foreign management companies without a branch under Art. 29 of the Act on collective investment	10	5	5
European Funds under Art. 61			
– foreign management companies	11	7	4
– foreign investment companies	19	14	5
within which: Number of foreign mutual funds and sub-funds of foreign investment companies	617	360	257
Number of foreign management companies performing activities under Article 3(3) of the Act on Collective Investment	11	5	6
Number of investment firms	32	33	-1
of which: Banks and branches of foreign banks – investment firms with a NBS licence	13	14	-1
Branches of foreign banks – investment firms with a licence of the home authority	6	4	2
Number of foreign entities operating in Slovakia as investment firm	582	304	278
of which: through a branch in Slovakia	3	2	1
without establishing a branch	579	302	277
Number of Slovak investment firms providing services abroad	7	7	0
Number of investment services intermediaries in Slovakia	937	888	49
of which: Legal persons	61	55	6
Natural persons	876	833	43

Source: NBS.

services and on amendments to certain acts (the Securities Act) as amended and on amendments to certain acts. This act has implemented the directive No. 2004/109/EC on the harmonization of transparency requirements (the Transparency Directive) and directive No. 2004/39/EC on markets in financial instruments (the MiFID directive). The most important regulation is NBS Decree No. 4/2007 on own funds for the financing of banks and capital requirements for the financing of banks and investment firms and on capital requirements for the financing of investment firms. The decree's purpose is to make the capital requirements match true risks, to which banks and investment firms are exposed, and to prevent that groups providing financial services in more than one country are subject to an excessive burden resulting from several levels of legal regulation and supervision. The newly regulated prudential rules, which, in this case, are represented by provisions on capital require-

ments and rules for the restriction of exposures, are also aimed at reinforcing the risk sensitivity, take into account the risk reduction resulting from the context, in which the individual exposures have arisen, and take into account the considerable progress in the measuring procedures and risk management procedures, which will enable reactions to market innovations and will contribute to the creation of a situation where the financial services of the EU continue to be effective and competitive. For the same reasons, provisions regulating the keeping of the trading book have been rendered more precisely and provisions on the treatment of credit derivatives and other financial instruments have been introduced.

Within legislation regulating the capital market, several EU directives were transposed to the legal system of the Slovak Republic, e.g. directive No. 2004/25/EC on takeover bids, the MiFID directive



and the Transparency Directive. The result of the implementation of the directive on takeover bids (by Act No. 644/2006 Coll.) has been the regulation of the conditions and procedures for performing a takeover bid, an extension of the definition of the term “concerted action”, the regulation of duties of the bodies of the target company after the announcement of the takeover bid and cooperation between the supervisory bodies regarding takeover bids, when the securities are accepted for the regulated market in one or more Member States. The MiFID directive has been implemented in the Securities Act and in Act No. 429/2002 Coll. on the Stock Exchange as amended. The amendment regulates above all the legal framework of financial market regulation, the conditions for performing investment services, ancillary services and for performing investment activities of investment firms in connection with the development of the financial markets of the European Union, it adds further types of financial instruments, it introduces the new concept of tied agents, abrogates restrictions related to the access to regulated markets and sets a regime for the organization of markets in financial instruments on a multilateral trading facility. The implementation of the MiFID directive relates primarily to investment firms and markets; however, it also has an impact on management companies performing further activities (the so-called trader activities) under Art. 3(3) of Act No. 594/2003 Coll. on collective investment and on amendments to certain acts as amended (the Act on Collective Investment). In connection with the Transparency Directive, the amendment sets above all the basic principles of harmonization of transparency requirements in connection with the ownership of shares, debt securities or voting rights, sets the minimum requirements for information dissemination, extends the content of published annual and semi-annual financial reports on issuers, introduces a central register of regulated information at Národná banka Slovenska, or a person authorized thereby, and between supervisory bodies of the Member States. The Act on Collective Investment has also been amended by Act No. 209/2007 Coll. The main purpose of that amendment has been to eliminate some legislative barriers in the part regulating real-estate special funds, as well as some provisions related to a single passport. In 2007, in the area of regulations, the NBS Bank Board discussed and approved NBS Decree No. 3/2007 on the submission of statements by entities ensuring the distribution of securities issued by foreign management companies and foreign investment companies based on a public offer to investors in the territory of the Slovak Republic for statistical purposes, NBS Decree No. 16/2007 on the submission of statements by the Stock Exchange and the Central Securities Depository for the purposes of financial market supervision, and NBS Decree No. 17/2007 on the submission of statements by management companies and mutual

funds depositories for the purposes of financial market supervision.

In the insurance sector, fundamental changes to the legislation regulating the activities of insurance companies, branches of foreign insurance companies, reinsurance companies and branches of foreign reinsurance companies in the Slovak Republic have been carried out in 2007 by the adoption of Act No. 8/2008 Coll. of 28 November 2007 on insurance and on amendments to certain acts. This act has changed the definition of insurance and reinsurance activity, the possibility to outsource some activities to another person and the definition, status and responsibilities of the internal audit unit within the organizational structure of an insurance company, reinsurance company, branch of a foreign insurance company and branch of a foreign reinsurance company. In the area of technical provisions, the provision for unexpired risks, as a part of the technical provision for unearned premium, and the equalisation reserve have been defined. The new legal regulation enables an insurance company, provided it has fulfilled the set conditions, to conduct insurance and reinsurance activity simultaneously without demanding a higher registered capital. The act has also introduced an exception from the compliance with the maximum level of the technical interest rate in the case of life insurance products with a single premium with a maximum period of insurance of 5 years, added a requirement on the quality of assets covering the guarantee fund or the possibility to have more than one responsible actuary in the case of an insurance company or a branch of a foreign insurance company that simultaneously carries on life and non-life insurance, or of a reinsurance company or branch of a foreign reinsurance company that simultaneously carries on reinsurance of life and non-life insurance. In December 2007, the Bank Board of NBS approved NBS Decree No. 15/2007 on the submission of statements, notifications, reports and other information by the Slovak Bureau of Insurers (Slovenská kancelária poisťovateľov) for the purposes of financial market supervision and for statistical purposes, which will enable to collect data needed for the purposes of off-site supervision and for statistical purposes by means of the STATUS DFT application program system.

As for changes of generally binding legal regulations in the area of pension savings, the most important step has been the adoption of Act No. 555/2007 Coll. amending Act No. 461/2003 Coll. on social insurance as amended and on amendments to certain acts. The act has amended Act No. 43/2004 Coll. on retirement pension saving and on amendments to certain acts as amended, as well as Act No. 650/2004 Coll. on supplementary pension saving and on amendments to certain acts as amended. The NBS has proposed several changes to increase system security, which are implementation of risk management aspects to

the regulation, more stringent conflict of interest rules, extension and strengthening of the internal control and a definition of the right of NBS to intervene in the selection of external auditors for companies and pension funds. The purpose of the changes has been to strengthen the core corporate governance of companies so as to enable, later on, a better implementation of new regulatory principles in the investment of individual pension fund management companies and supplementary pension companies.

4.3 Licensing activities of the supervision unit

Within its licensing activities regarding financial market entities, the financial market supervision unit of NBS issued a total of 905 decisions in 2007, which can be subdivided as follows.

Table 24 Number of decisions issued by the financial market supervision unit of Národná banka Slovenska in 2007

Financial sector	Number
Banking sector and investment firms	181
Capital market	329
Insurance sector	228
Pension saving	120
Foreign exchange licences	47
Total	905

Source: NBS.

The most important activities of Národná banka Slovenska related to the licensing activity of entities of the Slovak financial market in 2007 included the following decisions:

- Under the Decision of Národná banka Slovenska of 12 January 2007, Všeobecná úverová banka, a.s. received prior approval to use an internal model for the calculation of market risk.
- Granting of a prior approval for a merger to UniBanka, a.s., and HVB Bank Slovakia, a.s. of 15 January 2007.
- Granting of a prior approval of 5 June 2007 to PENTA INVESTMENTS LIMITED, Cyprus to exceed the limit of a 66% share of the registered capital and voting rights in Privatbanka, a.s.
- Granting of a prior approval of 18 September 2007 to the company ISTROKAPITAL SE, Cyprus to exceed the limit of a 66% share of the registered capital and voting rights in Poštová banka, a.s.
- Granting of a prior approval to Tatra banka, a.s. to become a subsidiary of the company Cembra Beteiligungs GmbH, Republic of Austria, of 2 October 2007.
- Granting of a banking licence to Československá obchodná banka, a.s. of 19 November 2007.
- Under its decision of 21 December 2007, Národná banka Slovenska granted to the investment firm AMSLICO AIG Securities o.c.p., a.s., a prior approval to return of its licence for the provision of investment services.
- On 22 May 2007, Allianz Asset Management, správ. spol., a.s. was granted a licence for the incorporation and activities of a management company.
- In 2007, OTP Asset Management, správ. spol., a.s. decided to terminate its activities; as a first step, the company transferred the management of its two open-end mutual funds to Investičná a Dôchodková, správ. spol., a.s. (decision of 27 April 2007) and, later on, it ceased to exist by a merger with the Investičná a Dôchodková, správ. spol., a.s. (decision of 23 May 2007).
- In 2007, the following companies received 19 licences for the creation of an open-end mutual fund:
 - Asset Management Slovenskej sporiteľne, správ. spol., a.s. (7 open-end mutual funds)
 - Allianz Asset Management, správ. spol., a.s. (4 open-end mutual funds)
 - Tatra Asset Management, správ. spol., a.s. (4 open-end mutual funds)
 - Investičná a Dôchodková, správ. spol., a.s. (2 open-end mutual fund)
 - VÚB Asset Management, správ. spol., a.s. (1 open-end mutual funds)
 - AIG Funds Central Europe správ. spol., a.s. (1 open-end mutual fund)
- A prior approval to a merger of closed-end mutual funds and subsequently a prior approval to a conversion of the closed-mutual fund to an open-end mutual fund have been granted to PRVÁ PENZIJNÁ správ. spol., a.s.
- A prior approval to entrust the performance of activities specified in Art. 3(2a) of the Act on Collective Investment has been granted to ISTRO ASSET MANAGEMENT, správ. spol. a.s. In this prior approval, the performance of activities was entrusted to BAWAG P.S.K. INVEST GmbH, with reference to the open-end mutual fund ISTRO ASSET MANAGEMENT, správ. spol., a.s., and equity open-end growth fund EUROPA).
- On 13 December 2007, VERITAS SG INVESTMENT TRUST GmbH was granted a prior approval for a return of the licence under Art. 75 of the Act on Collective Investment.
- A prior approval for the acquisition of a 6.69% share of voting rights associated with shares of BCPB, a.s., Patria Finance, a.s. pursuant to Article 6(a) of Act No. 429/2002 Coll. on the Stock Exchange (in the wording valid until 31 October 2007). Národná banka Slovenska decided to grant the prior approval on 12 October 2007.



- On 5 March 2007, based on a request, QBE poisťovňa, a.s. was extended its licence for the conduct of insurance activities to include the following classes of non-life insurance: class B5 – Aircraft insurance and B11 – Insurance of the liability arising out of the ownership and use of aircraft including carrier's liability.
- On 14 May 2007, based on a request, Poisťovňa AIG Slovakia, a.s. was granted a prior approval for the sale of the enterprise to AIG EUROPE S. A. acting by its organizational component AIG Europe S.A. (branch for the Slovak Republic).
- On 31 July 2007, based on a request, HDI Hannover Versicherung Aktiengesellschaft was granted a prior approval to acquire a share of the registered capital of POISŤOVŇA HDI-GERLING Slovensko, a.s., to such an extent that it will, for the first time, exceed the 66% share of the registered capital of the insurance company.
- KOMUNÁLNA poisťovňa, a.s., Vienna Insurance Group was granted a prior approval to conduct intermediary activities for a financial institution.
- On 22 October 2007, ING Životná poisťovňa, a.s. was granted a prior approval to a merger with ING Management Services Slovensko spol. s r.o.
- On 14 November 2007, based on a request, Assicurazioni Generali S.p.A. was granted a prior approval to the acquisition of a 100% share of the registered capital of Generali Poisťovňa, a.s.
- Under its decision of 6 March 2007, NBS granted ČSOB d.s.s., a.s. a prior approval to UniBanka a.s. becoming the depository of the company.
- Under its decision of 7 March 2007, NBS granted AXA, d.s.s., a.s. a prior approval to UniBanka a.s. becoming the depository of the company.
- Under its decision of 9 March 2007, NBS granted VÚB Generali dôchodková správcovská spoločnosť, a. s. a prior approval to ING Bank N. V., pobočka zahraničnej banky becoming the depository of the company.
- Under its decision of 8 January 2007, NBS granted Tatra banka, a.s. a prior approval to DDS Tatra banka, a.s. becoming a subsidiary of Tatra banka, a.s.
- Under its decision of 30 March 2007, NBS granted AXA, d.d.s., a.s., a prior approval to UniBanka a.s. becoming the depository of the company.
- Under its decision of 7 May 2007, a licence for incorporation and activities of the supplementary pension company was granted to AEGON, d. d. s., a.s.
- Under its decision of 13 December 2007, NBS granted prior approval to Winterthur Life Switzerland to AXA, d.d.s., a.s. to become a subsidiary of Winterthur Life by a merger of AXA, d.d.s., a.s. with AXA Slovensko, a. s.
- NBS granted a prior approval to Slovenské investičné družstvo to exceed the share of registered capital and voting rights in Stabilita, d.d.s., a.s. in the amount of 10%.
- Národná banka Slovenska has granted a prior approval to LOREA INVESTMENTS LIMITED Republic of Cyprus to exceed the share of registered capital and voting rights in Stabilita, d.d.s., a.s. in the amount of 20%.
- In 2007, based on a legal and factual assessment of requests and attached documents, Národná banka Slovenska granted a total of 45 foreign exchange licences for money exchange activities, namely for buying and selling funds in a foreign currency for the Slovak currency in cash to natural and legal persons.
- In 2007, 2 foreign exchange licences for non-cash funds transactions, which authorise the holder of those licences to conduct non-cash foreign currency transactions consisting in buying and selling foreign currency conducted for own account or for account of another by means of a non-cash transfer.

4.4 Consumer protection

The responsibilities of NBS in the field of consumer protection result from Art. 3(1) of Act of the National Council of the Slovak Republic No. 566/1992 Coll. on Národná banka Slovenska as amended. 380 petitions, the content of which is discontent of natural and legal persons with the procedure of financial services providers, were submitted to the department from the creation of the client's protection section in the financial market supervision unit in February 2007. 357 files could be completed and closed out of that number, which corresponds to a 93.95% success in processing petitions. Out of the total number of 380 petitions, 107 concerned the banking sector, 154 the insurance sector and 119 other areas of the financial market (e.g. investment firms, retirement pension saving, etc.). In the field of insurance, the clients of insurance companies seek mainly a new reassessment of the attitude of an insurance company regarding the provision of insurance benefits after the event insured. A considerable number of petitions were petitions, the content of which was the clients' discontent in the area of payment transactions. For other fields of the financial market, it is not possible to say in general terms, which type of petitions prevailed, because the activity of the client protection department in this field focused on a great number of financial market entities and a part of the activities of the client protection department was also devoted to entities that are not supervised by NBS.

4.5 Supervision activities of the supervision unit

In conducting supervision of the supervised entities, Národná banka Slovenska ascertains important facts on the supervised entities and their activity,

Table 25 Number of on-site supervisions conducted in supervised entities of the financial market in 2007

On-site supervision	Comprehensive	Thematic	Follow-up	Total
Banks	-	10	4	14
Investment firms which are not banks	3	1	1	5
Management companies	4	2	-	6
Pension fund management companies and supplementary pension companies	1	-	-	1
Insurance companies	5	1	-	6
Insurance, reinsurance and investment services intermediaries	9	-	-	9
Entities subject to foreign exchange supervision	8	-	-	8
Supervisions total	30	14	5	49

Source: NBS.

especially deficiencies in their activity, the reasons of the detected deficiencies, the consequences of the detected deficiencies and the persons responsible for the detected deficiencies.

Supervision of the supervised entities is performed as supervision on an individual basis for the supervision of individual supervised entities, as supervision on a consolidated basis for the supervision of groups of persons and special-purpose asset pools, part of which are also the supervised entities, and as supplementary supervision for the supervision of financial conglomerates.

In 2007, 49 on-site supervisions were conducted in the supervised financial market entities and they can be subdivided as follows:

19 on-site supervisions were conducted in the banking sector and at investment firms in 2007. The comprehensive on-site supervisions at investment firms were primarily focused on the organization, management, the way of entering into transactions, professional care of clients and reporting, on the fulfilment of provisions of the Securities Act and on the fulfilment of special acts to the extent resulting from them, and of generally binding regulations issued to implement them, and on the fulfilment of the conditions set by the licence for the provision of investment services. In banks, thematic supervisions, focused on selected activities of the supervised institutions or on evaluation of a selected risk, and follow-up supervisions, focused on the assessment of the fulfilment of measures adopted by the supervised institution on the basis of comprehensive and thematic supervision, were conducted. The subject of thematic supervisions was the evaluation of the use of the IRB model or a pre-validation evaluation of the bank's rating system due to an intention to apply for an approval of the IRB model, the evaluation of credit risk, the credit risk

management system, the operational risk management system and of the information systems used and their security, and the evaluation of the activity of a investment firm and depository; the supervisions having also focused on the verification of selected statistical statements and prudential reports and on the verification of the provision of investment services to the clients. In addition to the said supervisions, pre-validation meetings focusing on the evaluation of the internal models of credit and operational risk took place in some banks. Within off-site supervision, an analysis of the credit portfolio in selected entities, in which no on-site supervision was conducted within the supervision plan, was drawn up in 2007.

On-site supervision in regulated capital market entities in 2007 concentrated on companies, in which no on-site supervision had been conducted yet, as well as on the importance of the companies in the sector. In some cases, an informative visit in the companies took place. The specific focus of the supervisions conducted was: the assessment of the activity of the management company in performing the management of mutual funds managed by the company, of the organization and management of the company, of its internal rules, system of entering into transactions, system of portfolio management, risk management in mutual funds and internal audit system in the company; the assessment of the process of issuing shares of the management company, the fulfilment of the conditions of capital adequacy of a management company, operational risk management, selected accounting and reporting procedures, the process of issuing and paying out unit certificates and of the valuation of the assets of a management company and of mutual funds managed by the management company; the verification of the fulfilment of the statutes of mutual funds and of by-laws of the management company, as well as the fulfilment of the conditions, under which the company was granted licences. In



2007, supervision over the activities of the Bratislava Stock Exchange Plc. (BCPB) consisted mainly in the conduct of ongoing monitoring of the concluded securities transactions accepted for the individual BCPB markets within the modules of the stock exchange's trading system. Until the end of April 2007, Národná banka Slovenska also performed off-site supervision over the fulfilment of the reporting duty of issuers of securities issued based on a public offer, or issuers whose securities have been accepted for trading on the stock exchange market and over the reporting duty of announcers of a public offer of assets who have raised funds from the public based on a public offer under Article 130 of the Securities Act.

In the insurance sector, 5 comprehensive supervisions and 1 thematic on-site supervision were conducted over the course of 2007. The supervisions focused on the verification of the settlement of claims by an insurance company, requirements of file documentation to events insured and adequacy of technical provision for outstanding claims, verification of the handling of client complaints within time periods prescribed by law and of reporting of those complaints, as well as verification of whether the insurance company carries on its activities in line with its licence for the performance of insurance activities, or whether the insurance company was granted the necessary prior approvals, on the organization and management of an insurance company, the legal framework of the functioning of the insurance company, its internal rules and regulations, information system, its trading activities, accounting and reporting, insurance management, technical provisions checks and the placement of these provisions. In the field of off-site supervision, standard statements and reports of insurance companies for late 2006 (audited) and for all quarters of 2007 (ongoing), as well as reports of insurance companies sent ad-hoc via the application program system STATUS DFT, were verified. On-site supervision at insurance and reinsurance intermediaries concentrated on the fulfilment of the provisions of generally binding legal regulations; in 2007, informative talks with commercial insurance companies aimed at the verification of the way the commercial insurance companies conduct one of the insurance activities – the conclusion of contracts with an exclusive insurance intermediary, insurance agent and insurance broker, the content of which is insurance mediation, the conduct of activities associated with the registration of an exclusive insurance intermediary, special training of insurance intermediaries, as well activities to prevent damages.

In the area of pension saving, one comprehensive on-site supervision was carried out in 2007. It focused on

the organization and management of a pension fund management company, internal regulations, the system of doing deals, the portfolio management system, risk management in pension funds and the company's internal audit system. Off-site supervision in 2007 concentrated primarily on retirement pension saving. The operation of the application program software STATUS DFT was launched in 2007, and the supervised entities started to send reports to Národná banka Slovenska by means of this software. From 1 January 2007, the pension fund management companies and pension fund depositories have the additional duty to inform Národná banka Slovenska not only on each transaction conducted with the assets in a pension fund, but also on the level of assets in the pension fund on a daily basis. Thus, as a first step, off-site supervision involved checks of the fulfilment of reporting duties of pension fund management companies and pension fund depositories under Decree of Národná banka Slovenska No. 567/2006 Coll. and, based on information obtained in this way, the riskiness of the individual transactions and their impact on the riskiness of pension fund portfolios was evaluated.

Foreign exchange supervision focused on the fulfilment of the reporting obligation, above all based on an inducement by the statistics department of NBS. In all cases of the conducted foreign exchange supervision focusing on the fulfilment of the reporting obligation, it was established that the obligation is not fulfilled. Foreign exchange supervision focusing on money exchange activities verified primarily the keeping of prescribed, special records (the issuing of purchase or sale statements, foreign exchange bookkeeping, etc.).

4.6 Analytical activities of the supervision unit

A part of the work of the NBS financial market supervision unit is dedicated to analytical activities. The supervision unit prepares the Analysis of the Slovak Financial Sector on a semi-annual basis. The report is submitted to the Bank Board of NBS and is published in a shortened form⁶. Another regular analysis with semi-annual periodicity is the Report on the State and Development of the Slovak Financial Market, submitted for meetings of the government and of the National Council of the Slovak Republic under the Act on financial market supervision. The main content of the said reports is a description of the most important trends and an evaluation of risks resulting from them. Within market risks, this evaluation, including stress testing, has been extended to also include insurance companies, pension funds of pillar II and III and mu-

⁶ The 2007 Analysis of the Slovak Financial Sector has been published on the NBS website [www.nbs.sk/Financial Market Supervision/Banking Sector and Securities Dealers Supervision/Statistical Data and Analyses/Analysis of the Slovak Banking Sector](http://www.nbs.sk/Financial%20Market%20Supervision/Banking%20Sector%20and%20Securities%20Dealers%20Supervision/Statistical%20Data%20and%20Analyses/Analysis%20of%20the%20Slovak%20Banking%20Sector).

tual funds. In addition, a macro-stress testing model has been created, by means of which it is possible to estimate the impact of a possible slowdown of the growth of the Slovak economy on the financial sector by means of credit risk, foreign exchange risk and interest rate risk channels.

In 2007, within its analytical activities, the supervision unit also dealt with the impact of the adoption of the euro on the financial sector. The analysis has been also published on the website of NBS in a shortened form⁷.

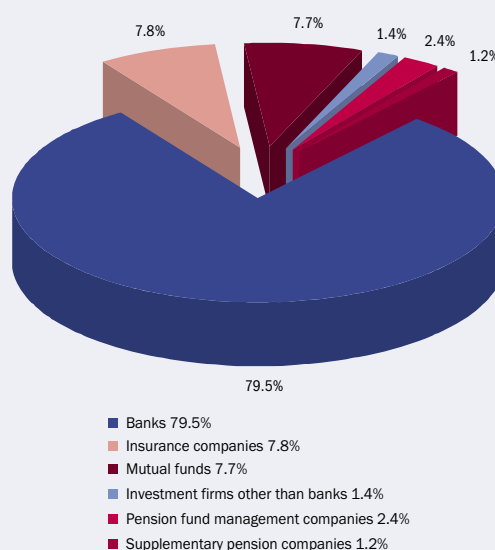
Special attention has been given to the fast growth of loans provided by banks, and to an analysis of the risks and performance of pillar II and III pension funds. Extensive analytical activities have been carried out in examining the impacts of amendments of specific legal regulations on the financial market. It primarily related to amendments to the Act on voluntary auctions, Act on consumer credits (introduction of an interest rate cap), Income Tax Act, Act on pension saving and the Home Savings Act.

4.7 Financial market developments in 2007

In 2007, the total value of the assets and managed assets of financial institutions regulated by Národná banka Slovenska increased by SKK 342.5 billion (19.5%) to SKK 2.088 billion at the end of the year. The increase in assets slowed down slightly in several segments of the financial market in the second half of the year, which, in some cases, might be associated with a lower performance of the world financial markets.

Pillar II pension funds reached the highest asset growth. Over 2007, their assets rose 83.5% and reached the value of SKK 51.3 billion. Their importance grew not only in the context of the pension scheme, but also in terms of important accumulation of resources in the economy at a time where the overall economic boom and interest environment motivates Slovak households rather to create debts than to save. The growth of the assets of supplementary pension funds by 18.7% to a level of SKK 25.3 billion is a positive trend in this context. Mutual funds recorded the second fastest growth (24.5%), constituting a revival after stagnation in 2006. As opposed to 2006, investments of households in such funds grew faster than the volumes on bank accounts in 2007. This development was reflected in an increase in deposits by mutual funds in banks.

Chart 38 The structure of assets and managed assets of the financial market¹⁾ (%)



Source: NBS

1) Entities supervised by NBS.

The asset growth in the banking sector was more moderate than that of pension and mutual funds, as a result of which its share of the assets of the entire financial market fell slightly against 2006. At the end of 2007, the banking sector assets reached a value of SKK 1,660 billion. The dominant trend in the banking sector in 2007 was a continuing growth of loans to customers. Banks financed mainly the household and business sector, above all small and medium sized enterprises. The volume of corporate loans for real estate financing also continued to go up. Loans to households maintained their high growth rate, the household demand for loans having been influenced mainly by the growth of real estate prices. Banks decreased their investment in securities comparing to the previous year. Holdings of domestic government bonds were the main group to decrease; investment in foreign securities, on the other hand, rose.

In 2007, the growth of loans to customers was predominantly financed from the resources of clients or by issuing debt securities. The Slovak banking sector is thus one of the few banking sectors in EU countries not to be dependent on short-term interbank resources in financing loans to customers. Deposits of the retail continued to go up despite a reduction of interest rates; deposits in the domestic currency having grown the most. Deposits of businesses and financial companies except banks also continued to grow.

⁷ The Analysis of the Impact of the Euro Introduction on the Slovak Financial Market has been published on the NBS website [www.nbs.sk/Financial Market Supervision/Banking Sector and Securities Dealers Supervision/Statistical Data and Analyses /Analysis of the Slovak Banking Sector](http://www.nbs.sk/Financial%20Market%20Supervision/Banking%20Sector%20and%20Securities%20Dealers%20Supervision/Statistical%20Data%20and%20Analyses/Analysis%20of%20the%20Slovak%20Banking%20Sector).



In 2007, the banking sector maintained its high profit generation level, the number of banks with a year-on-year profit growth increased, although the net profit of the banking sector fell by 1% against the previous year in 2007 to a level of SKK 17.6 billion as at 31 December 2007. Interest income made up the greatest share of bank income in 2007. Their share of gross income moved up from 63% in 2006 to 70% in 2007. Interest income grew mainly in large banks, because the banks have taken advantage of their market position and increased the interest income by means of a higher volume of loans; the growth of interest income was more moderate in other banks. Non-interest income fell off against the previous year. Income from trading, above all income from debt securities trading, decreased in several banks. The ROE⁸ of the banking sector declined from 22% in 2006 to 20% in 2007. In addition to profitability, the development of this indicator was negatively affected by an increase of own funds in several banks.

In 2007, capital adequacy in all banks was above the set level of 8%. The trend towards a gradual decline of the average capital adequacy value (an average weighted by the volume of risk-weighted assets) abated in 2007. This value decreased from 13.0% to 12.8% against 2006; in some banks, however, it fell below 9%. Several banks have increased the volume of their own funds by drawing a subordinated debt or from the profit generated in 2006.

In 2007, the written premium reached a value of SKK 54.1 billion. This amount consisted of SKK 25.3 billion in life insurance and SKK 28.8 billion in non-life insurance. The technical premium, which includes investment contracts reported according to the IFRS, reached SKK 28.5 billion in life insurance. In 2007, the difference between the technical premium in life and non-life insurance was the lowest in the history of Slovakia. If the faster growth of technical premium in life insurance comparing to the non-life insurance continues, the technical premium in life insurance can be expected to reach a higher value than the technical premium in non-life insurance. The expenses for claims increased by 13% to a level of SKK 24 billion against 2006. The profit of insurance companies grew by 25% to SKK 5.6 billion as a result of a higher growth of technical revenues as compared to technical expenses. The return on assets and return on equity also grew slightly. No substantial changes occurred in the investment of the technical provisions, they continue to be invested in low-risk assets.

The amount of customer securities transactions carried out by investment firms virtually did not

change, changes occurred only in the structure of traded instruments. The amount of bond transactions decreased by more than 50%, derivative instrument transactions, on the other hand, increased. The amount of customer assets managed by these entities rose 7% against 2006 to a level of SKK 30 billion. The capital adequacy of Slovak investment firms fulfilled the prescribed minimum level with a sufficient tolerance.

The net asset value managed in open-end mutual funds grew by 25% in 2007 after moderate stagnation in 2006. Both investments of resident entities in foreign mutual funds, and the net asset value managed by domestic management companies, went up. Capital shifts from equity and bond funds to money market, mixed and other funds, especially to the so-called guaranteed funds, occurred. Stagnation of the world financial markets caused a lower average performance of share funds and similar funds. Higher yields compared to 2006 were achieved by funds investing predominantly in debt securities.

For pillar II of pension saving, the year 2007 was the first comprehensive calendar year, in which the system was closed for voluntary entries and new savers entered the system only on the basis of fixed age-related rules (automatic enrolment). The amount of assets in the funds of pension fund management companies almost doubled in a year. Pillar III of pension saving also grew in a relatively dynamic way in terms of net asset value growth. In both pillars, the structure of the aggregated portfolio was changing over 2007. In the funds of pillar II, the structure developed towards slightly less risky assets and in the supplementary pension system in the opposite direction. Compared to previous years, the balanced and growth funds recorded a decline of annual performance to a level of 3.8% and 3.6%, respectively, which brought them below the performance level of conservative funds, whose performance was 4.1% in 2007⁹.

The riskiness of the financial sector was partly influenced by the negative developments on the global financial markets. Direct exposure of the financial sector to subprime loans by means of securities holdings or generally structured products was only minimal. In the case of financial institutions holding such instruments, the credit quality, liquidity and valuation of such instruments remain an issue.

The total increase in volatility and uncertainty in the capital markets enhanced the equity risk. The equity risk went up mainly in some funds of pension fund management companies, supplementary pension

⁸ Capital weighted.

⁹ Weighted average of performance as at 31 December 2007 weighted by the NAV of funds in the given group. This is no average performance (moving average) pursuant to Act on retirement pension saving and on amendments to certain acts No. 43/2004 Coll.



companies and in mutual funds. The global decrease in liquidity, accompanying the current development in financial markets, has not affected the domestic financial sector considerably. The banking sector – in general the sector being most sensitive to the level of liquidity – showed a sufficient level of domestic primary resources.

In the banking sector, the high growth of loans to households continued, which also increased the exposure of banks to credit risk resulting from those loans in 2007. However, the amount of debt of the household sector at the macro level reached a low level in 2007. The interest rate risk of the banking sector did not change considerably in 2007. In terms of liquidity risk, the situation in 2007 was character-

ized by a high proportion of funds sterilized in NBS, as well as of other liquid assets.

The most important type of risks, to which insurance companies are exposed, are insurance risks. In addition, insurance companies are exposed to market risks, which can cause an unexpected decrease in the value of assets covering the technical provisions. The most important market risk is interest rate risk. The insurance market as a whole was exposed to a relatively low equity risk.

Funds of pension fund management companies and supplementary pension companies are exposed primarily to market risks. Balanced and growth funds are exposed mainly to equity risk.

Issuing Activity and Currency in Circulation



5 Issuing Activity and Currency in Circulation

5.1 Slovak currency issuance

In 2007, in accordance with the needs of currency circulation, Národná banka Slovenska arranged for the reprint of 16.5 millions of banknotes in the denomination of SKK 1000. The banknotes were printed by the British printing house De La Rue in its Malta plant at Žejtun.

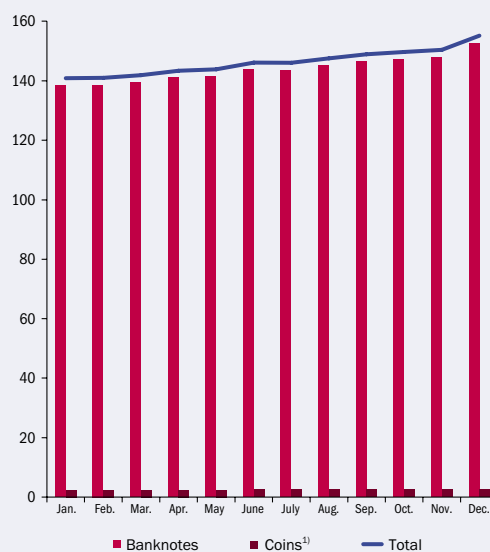
Besides banknotes, 44.0 million coins in the denomination of 50 halier, 5.54 million coins in the denomination of SKK 1, 13.2 million coins in the denomination of SKK 2 and 5.320 million coins in the denomination of SKK 5 were produced for the needs of cash circulation. In addition to coins issued for circulation, 18 thousand coins in the denominations of SKK 10, SKK 5, SKK 2, SKK 1 and 50 halier were produced as collector items; those coins were used in three types of annual collector sets of circulation coinage of the Slovak Republic.

In 2007, Národná banka Slovenska issued two commemorative coins as collector items to commemorate important events and anniversaries. A silver coin in the denomination of SKK 200 on the occasion of the 200th birth anniversary of Jozef Maximilián Petzval was issued on 9 January 2007 and a commemorative silver coin in the denomination of SKK 500 for the 450th anniversary of the completion of the construction of the Old Fortress in Komárno was issued on 15 May 2007. The production of all circulation coinage and commemorative coins was ensured by Mincovňa Kremnica, š. p., which was also charged with the sale of annual collector sets.

5.1.1 Currency in circulation and net annual issuance¹⁰ in the SR

The value of currency in circulation in the Slovak Republic as at 31 December 2007 represented SKK 155.15 billion (including commemorative coins). The year-on-year increase in the value of currency in circulation was SKK 11.6 billion, which represented

Chart 39 The monthly development of currency in circulation in 2007 (SKK billion)



Source: NBS.

1) Including commemorative coins.

Table 26 Commemorative silver coins issued by NBS in 2007

Denomination	Event commemorated by the coin	Number of coins issued		NBS Decree
		total	proof	
SKK 200 ¹⁾	200th birth anniversary of Jozef Maximilián Petzval	7,200	2,500	617/2006 Coll.
SKK 500 ¹⁾	450th anniversary of the completion of the construction of the Old Fortress in Komárno	7,200	2,600	183/2007 Coll.

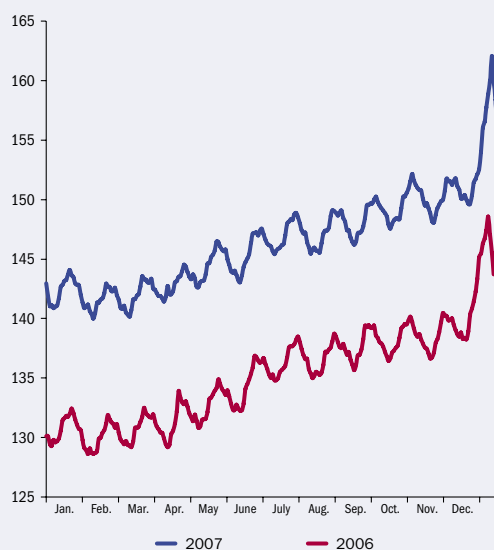
Source: NBS.

1) Commemorative silver coin.

¹⁰ The net issuance is the difference between the amount of money put into and received from circulation over a specified period of time. The terminology used is identical with that of the European Central Bank.



Chart 40 The daily development of currency in circulation (SKK billion)



Source: NBS.

a year-on-year increase of 8.1%. The total net issuance decreased by SKK 1.8 billion (13.2%) against 2006.

The development of the value of currency in circulation (measured at the end of the individual months) showed a typically seasonal pattern: falling in the first quarter and rising at the end of the year. The monthly values of net issuance ranged from SKK -2.6 billion in January 2007 to SKK 4.8 billion in December 2007. The development of currency in circulation in 2007 is shown in chart 39.

The daily value of currency in circulation in 2007 ranged from SKK 139.98 billion (7 February 2007) to SKK 162.08 billion (21 December 2007). The development of the daily value of currency in circulation in 2007 and in the previous year is shown in chart 40.

5.1.2 Structure of currency in circulation and net issuance

As at 31 December 2007, 186.7 million banknotes with a value of SKK 152.6 billion, 1,163.2 million

Table 27 Value of currency in circulation in SKK

	Value in SKK		Share in %	
	31 December 2007	31 December 2006	31 December 2007	31 December 2006
Banknotes				
5000 Sk	74,381,077,500	68,029,362,500	47.94	47.40
1000 Sk	65,888,564,500	61,320,830,500	42.47	42.73
500 Sk	5,693,748,375	5,361,164,875	3.67	3.74
200 Sk	2,459,868,650	2,292,431,250	1.59	1.60
100 Sk	2,553,773,150	2,512,164,150	1.65	1.75
50 Sk	903,850,100	867,629,800	0.58	0.60
20 Sk	773,488,305	720,110,265	0.50	0.50
Total	152,654,370,580	141,103,693,340	98.39	98.32
Circulation coins				
10 Sk	895,795,870	881,149,330	0.58	0.61
5 Sk	359,567,040	333,777,320	0.23	0.23
2 Sk	251,880,460	232,742,040	0.16	0.16
1 Sk	164,910,186	152,756,209	0.11	0.11
50 hal.	26,082,860	25,042,035	0.02	0.02
50 hal. II	83,835,690	74,212,418	0.05	0.05
20 hal.	44,275,412	44,304,304	0.03	0.03
10 hal.	26,967,812	26,980,004	0.02	0.02
Total	1,853,315,331	1,770,963,661	1.19	1.23
Commemorative coins	646,400,190	643,389,180	0.42	0.45
Banknotes and coins in total	155,154,086,101	143,518,046,181	100.00	100.00

Source: NBS.

circulation coins with a value of SKK 1.85 billion and 889.6 thousand commemorative coins with a value of SKK 646.4 million were in circulation. Banknotes represented 98.4% of the total value of currency in circulation, circulation coins 1.2% and commemorative coins 0.4%. The share of banknotes in the total number of banknotes and coins in circulation was 13.8% and that of circulation and commemorative coins 86.2%.

Banknotes made up SKK 11.55 billion, circulation coins SKK 82.35 million and commemorative coins SKK 3.0 million of the net issuance in 2007 (SKK 11.6 billion).

Banknotes in the denomination of SKK 5000 (SKK 6.35 billion, 1.27 million pieces) and banknotes in the value of SKK 1000 (SKK 4.56 billion, 4.56 million pieces) had the highest net issuance value. These two denominations together represented 93.8% of the value of net issuance in 2007.

The structure of banknotes in circulation remained unchanged against 2006. The most frequent banknotes

in circulation were banknotes in the denominations of SKK 1000 (65.9 million pieces), SKK 20 (38.7 million pieces) and SKK 100 (25.5 million pieces). In terms of value, banknotes in the denominations of SKK 5000 and SKK 1000 made up together SKK 140.3 billion, 90.4% of the total value of currency in circulation, which was a slightly higher share than in the previous year (90.1%).

The net issuance of circulation coins reached the value of SKK 82.4 million (49.4 million pieces) in 2007. The net issuance reached positive values for all valid circulation coins. From among circulation coins, the coin of SKK 5 reached the highest net issuance value (SKK 25.8 million), and the amount of 50 halier coins recorded the highest increase (by 21.3 million pieces). In 2007, 144.5 thousand pieces of invalid 20 halier coins and 121.9 thousand pieces of invalid 10 halier coins were returned from circulation. More than 491 million pieces of these coins have remained in circulation, i.e. more than 83% of the total amount of 10 and 20 halier coins issued from 1993 till the end of 2003. The deadline

Table 28 Number of currency in circulation in pieces

	Number in pieces		Share in %	
	31 December 2007	31 December 2006	31 December 2007	31 December 2006
Banknotes				
5000 Sk	14,876,216	13,605,873	1.10	1.05
1000 Sk	65,888,565	61,320,831	4.88	4.75
500 Sk	11,387,497	10,722,330	0.84	0.83
200 Sk	12,299,343	11,462,156	0.91	0.89
100 Sk	25,537,732	25,121,642	1.89	1.95
50 Sk	18,077,002	17,352,596	1.34	1.34
20 Sk	38,674,415	36,005,513	2.86	2.79
Total	186,740,769	175,590,940	13.82	13.61
Circulation coins				
10 Sk	89,579,587	88,114,933	6.63	6.83
5 Sk	71,913,408	66,755,464	5.32	5.17
2 Sk	125,940,230	116,371,020	9.32	9.02
1 Sk	164,910,186	152,756,209	12.21	11.84
50 hal.	52,165,721	50,084,071	3.86	3.88
50 hal. II	167,671,380	148,424,836	12.41	11.50
20 hal.	221,377,062	221,521,521	16.39	17.17
10 hal.	269,678,123	269,800,042	19.96	20.91
Total	1,163,235,697	1,113,828,096	86.11	86.32
Commemorative coins	889,584	866,959	0.07	0.07
Banknotes and coins in total	1,350,866,050	1,290,285,995	100.00	100.00

Source: NBS.



for the exchange of these two coins is 31 December 2008.

In 2007, the total number of commemorative coins in circulation increased by more than 22 thousands pieces and their value increased by SKK 3.0 million.

5.1.3 Average values of currency in circulation

The value of currency in circulation per capita¹¹ as at December 31, 2007, including commemorative coins, totalled SKK 28,767. This consisted of SKK 28,303 in banknotes, SKK 344 in circulation coins and SKK 119 in commemorative coins. As compared to 2006, the total value of currency in circulation per capita increased by SKK 2,135, of which banknotes accounted for SKK 2,120 and circulation coins SKK 15. Compared to the previous year, the value of commemorative coins per capita remained virtually unchanged.

The average number of banknotes per inhabitant was 35, two banknotes more than in 2006. The most numerous banknotes were in the denomination of 1000 SKK (12 per capita) and 20 SKK (almost 7 per capita). In 2007, the number of circulation coins per capita was 216, compared to 207 in 2006. Coins in the lowest denominations, i.e. 50 halier coins (almost

41 pieces per capita; 37 pieces in 2006) and SKK 1 coins (31 pieces, 28 in 2006) made up the largest share of valid coins in circulation.

The average value of the currency mark¹² increased in 2007 by SKK 3.7 to SKK 114.9. The development of the currency mark corresponds to the quantity and value of currency in circulation. Table 29 shows a comparison of the development of the average value of the currency mark by individual types of money since 1993.

In recent years, the development of the average value of the currency mark has been characterized by a faster growth of the value of currency in circulation as compared to its quantity.

5.1.4 Currency in circulation and selected macroeconomic variables

In connection with the growth of the total value of currency in circulation, the amount of currency held by the public increased from SKK 131.2 billion to SKK 141.7 billion (by 8.0%) and that held by the banks from SKK 12.3 billion to SKK 13.4 billion (by 8.9%) in 2007.

The share of the M0 in the M1 aggregate¹³ decreased by 1.1 percentage points to 22.8% as compared to the

Table 29 **Development of the average value of the currency mark** (SKK)

Year	Banknotes	Circulation coins	Currency including commemorative coins
1993	289.3	3.2	90.2
1994	384.1	2.0	76.4
1995	455.6	1.8	76.7
1996	537.3	1.7	81.8
1997	566.3	1.6	80.5
1998	552.3	1.5	72.2
1999	594.1	1.5	76.1
2000	631.4	1.4	77.1
2001	693.6	1.4	84.4
2002	697.8	1.4	80.3
2003	729.2	1.4	85.0
2004	738.8	1.6	94.0
2005	788.9	1.6	106.0
2006	803.6	1.6	111.2
2007	817.5	1.6	114.9

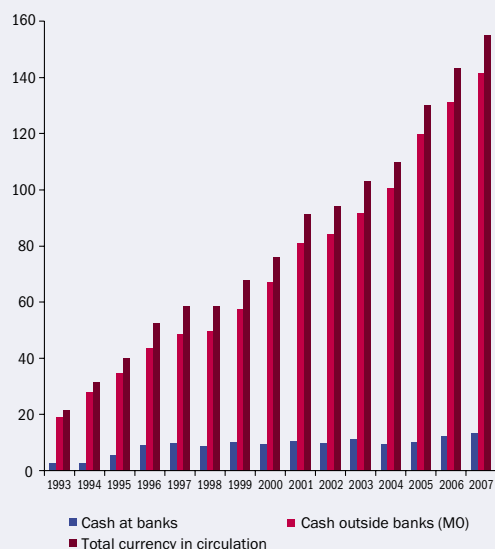
Source: NBS.

11 As at 31 December 2006, the population numbered 5,393,637, according to the Statistical Office of the Slovak Republic.

12 Average value of the currency mark = total value of currency in circulation / total amount of currency in circulation.

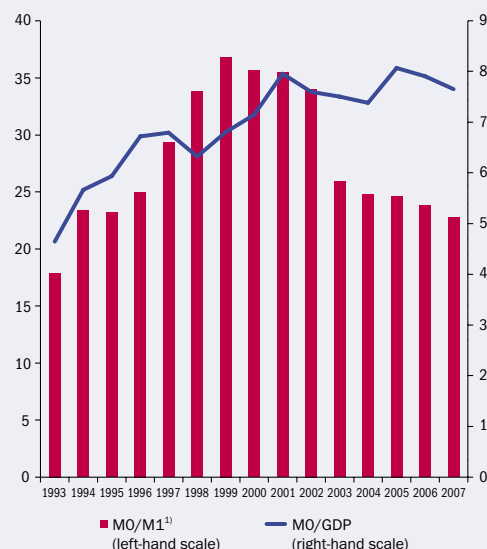
13 The monetary aggregates M0 and M1 had been calculated using NBS methodology until 2002. From 2003 onwards, the calculation is based on ECB methodology.

Chart 41 Currency in circulation held by banks and outside banks (SKK billion)



Source: NBS.

Chart 42 The share of M0 in M1 and GDP (at current prices) (%)



Source: NBS.

1) Since 2003, according to ECB methodology.

previous year. This indicator had shown a declining trend since 2003, pointing to the fact that the utilization of cashless payment system in Slovakia is moderately improving.

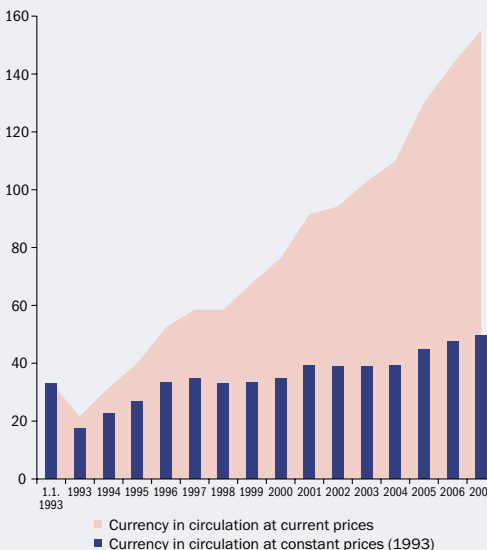
The share of M0 in GDP¹⁴ decreased year-on-year by 0.3 percentage points to 7.7% in 2007, which is comparable to the levels in euro area countries (ranging from 3% to 10%).

As at 31 December 2007, the value of currency in circulation at constant prices¹⁵ stood at SKK 49.62 billion, which represents an increase of SKK 2.16 billion compared to 2006. The year-on-year increase in currency in circulation at constant prices was, just like in the previous year, considerably influenced by a faster growth of currency in circulation (by 8.1%) than the growth of the annual rate of inflation (by 3.4%).

5.2 Counterfeit money seized in the territory of the Slovak Republic

A total of 1,066 pieces of counterfeits of Slovak and foreign currencies were seized in the territory of the Slovak Republic in 2007. Compared to 2006, this represents a decrease in the total number of counterfeits seized by 167 pieces, i.e. by more than 13%. 92% of

Chart 43 Effect of inflation on the value of currency in circulation (SKK billion)



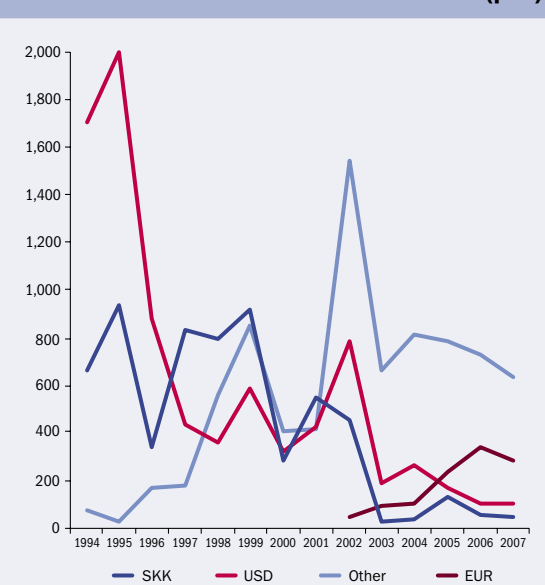
Sources: Statistical Office of the Slovak Republic and NBS.

the said number of counterfeits was seized directly from the circulation by banks, branches of foreign banks, non-banking entities and security services.

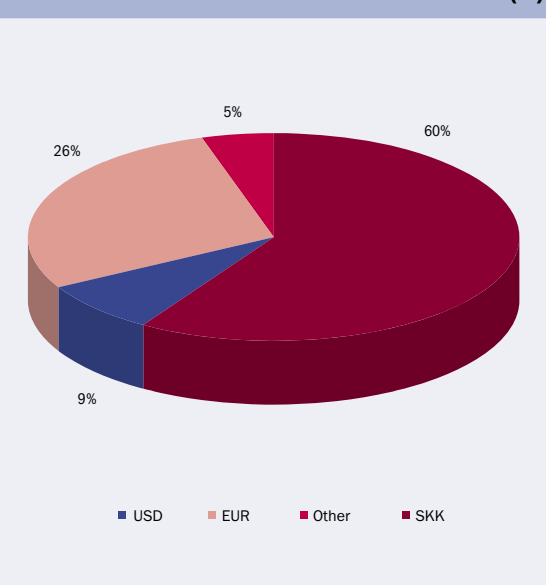
The proportions of Slovak koruna (60%) and euro (26%) made up the largest share in the structure of

¹⁴ GDP at current prices; source: Statistical Office of the Slovak Republic.

¹⁵ In terms of consumer price index (CPI), the price level has increased by 212.7% since 1993; source: Statistical Office of the Slovak Republic.

**Chart 44 Development of the number of seized counterfeit (pcs)**

Source: NBS.

Chart 45 Structure of counterfeit in 2007 (%)

Source: NBS.

counterfeits. The proportion of US dollars reached 9% and that of other foreign currencies 5%.

5.2.1 Slovak koruna counterfeits

A total of 639 Slovak koruna counterfeits were seized in 2007, including five pieces of adapted banknotes. The greatest number of counterfeits was registered in the Nitra region (161 pieces) and Žilina region (115 pieces). Like in the previous period, the most frequently counterfeited banknotes were SKK 1000 and SKK 500, they accounted for more than two thirds of Slovak koruna counterfeits.

5.2.2 Counterfeits of foreign currencies

In 2007, a total of 287 euro counterfeits, 97 US dollar counterfeits and 52 counterfeits of other foreign currencies were seized in the territory of the Slovak Republic. The largest incidence was recorded in the Bratislava region.

Euro counterfeits

A decrease in the number of seized euro counterfeits became apparent in 2007, but due to the fact that almost all of them were seized from circulation, they presented the same danger as the counterfeits seized in 2006, when almost one third of them was seized

before they had been put into circulation. In comparison with euro area countries, in which counterfeits of the lower denominations of EUR 50 and EUR 20 occur most frequently, in the territory of the Slovak Republic the most numerous counterfeits were 100 EUR and 200 EUR banknotes, accounting for more than two thirds of euro counterfeits.

Counterfeit US dollars

Only a slight decrease in the number of seized US dollar counterfeits against the previous year was recorded in 2007, while the US dollar's share in the total number of seized counterfeits remained approximately at the level of 2006. The highest occurrence was recorded in Bratislava region, where 50 counterfeits were seized in 43 cases. The most frequently counterfeited denomination was, again, the 100 USD banknotes, which made up approximately 95% of the total number of US dollar counterfeits.

Counterfeits of other foreign currencies

A development similar to that of US dollars was also recorded for the number of seized counterfeits of other foreign currencies, where six pieces of counterfeits less than in 2006 were seized in 2007. As in the previous period, the British pounds formed the highest share of counterfeits.

Table 30 Number of seized Slovak koruna counterfeits (pcs)

Year	Denomination									Total
	5000	1000	500	200	100	50	20	10	P ¹⁾	
2003	14	396	131	58	31	27	8	0	1	666
2004	45	419	203	36	68	36	11	1	1	820
2005	23	337	151	103	87	48	28	0	7	784
2006	28	344	138	95	55	22	6	0	38	726
2007	32	302	150	65	31	22	7	25	5	639

Source: NBS.

1) Forgeries, adapted and composed banknotes and coins, coin plate.

Table 31 Number of seized euro counterfeits (pcs)

Year	Denomination										Total
	1	2	5	10	20	50	100	200	500	P ¹⁾	
2003	0	0	0	2	18	41	9	13	4	1	88
2004	0	3	1	0	1	48	26	17	2	5	103
2005	0	8	0	0	13	114	26	37	34	2	234
2006	0	3	1	4	6	69	217	38	10	0	348
2007	4	8	0	2	10	59	99	90	6	0	278

Source: NBS.

1) Manipulated banknotes, forgeries, adapted and composed banknotes.

Table 32 Number of seized US dollar counterfeits (pcs)

Year	Denomination								Total
	1	5	10	20	50	100	1000	P ¹⁾	
2003	0	0	0	3	3	176	0	5	187
2004	3	0	1	1	5	252	0	2	264
2005	0	0	1	1	3	163	0	3	171
2006	2	1	0	0	3	94	1	0	101
2007	0	0	0	2	3	92	0	0	97

Source: NBS.

1) Manipulated banknotes, forgeries, adapted banknotes.

Table 33 Number of seized counterfeits of other foreign currencies (pcs)

Year	Currency							Total
	GBP	CZK	CAD	PLN	CHF	HUF	Others ¹⁾	
2003	20	3	6	2	1	0	0	32
2004	14	12	4	2	1	3	0	36
2005	82	21	3	1	1	18	1	127
2006	39	9	0	2	0	7	1	58
2007	34	6	0	2	0	3	7	52

Source: NBS.

1) German mark, Australian dollar and Czechoslovak koruna.

Payment System



6 Payment System

6.1 Legal and institutional aspects

The payment system in the Slovak Republic is governed primarily by Act No. 510/2002 Coll. on the Payment System and on amending and supplementing certain acts as amended (the Act on the Payment System).

The Act on the Payment System was amended by Act No. 659/2007 Coll. on the introduction of euro in the Slovak Republic and on amending and supplementing certain acts, as amended, in 2007. Within this indirect amendment to the Act on the Payment System, among other things, the constant symbol will be cancelled as a compulsory element of transfer orders for domestic transfers, from the date of introduction of euro in the Slovak Republic.

In the course of 2007, work on a direct amendment to the Act on the Payment System began. This amendment to the Act is based on the National Euro Changeover Plan in the Slovak Republic and is related to changes in the SIPS domestic payment system and to connecting to the TARGET2 payment system as of the date of introduction of euro in the Slovak Republic.

With effect from 1 January 2007, also Regulation 1781/2006 of the European Parliament and of the Council of 15 November 2006 on information on the payer accompanying transfers of funds became a part of Slovak legislation.

In the course of 2007, Directive 2007/64/EC of the European Parliament and of the Council of 13 November 2007 on payment services on the internal market (Directive on payment services) was adopted, amending and supplementing Directives 97/7/EC, 2002/65/EC, 2005/60/EC and 2006/48/EC and repealing Directive 97/5/EC.

The aim of this Directive on payment services is to create a single payment market within the Community by introducing a harmonised legal framework; the intention is to eliminate borders in the internal market when providing payment services.

The scope of the Directive on payment services is limited to payments in euro or in national currencies

of the Member States executed on the territory of the Community. This Directive regulates, inter alia, also the transparency of conditions for the provision of payment services, the rights and obligations relating to the provision and use of payment services, as well as the out-of-court settlement of disputes.

By reason of increased economic competition in the payment services market, the Directive defines the conditions for the origination and business of a new category of payment services providers – so called payment institutions, which, in addition to the banks and branch offices of foreign banks, will be allowed to provide payment services (i.e. they will be allowed to execute payment transactions and settlement).

The Directive on payment services will be transposed into the Slovak legal code by adopting a new generally binding legal Act with the expected effect from 1 November 2009.

The Permanent Court of Arbitration of the Slovak Banking Association was established with effect from 1 July 2003 and has its registered office in Bratislava; at present, it has two chambers:

- a) the chamber for deciding disputes on payments,
- b) the chamber for deciding disputes arising from other commercial or civil relations, which commenced operation on 1 January 2004.

In 2007, Národná banka Slovenska approved the Slovak Banking Association's proposal not to pay any contribution in 2007 for the activity of the Permanent Court of Arbitration of the Slovak Banking Association with regard to the economic results of this court and the sufficient funds for the activity of the chamber for deciding disputes on payments. At the same time, Národná banka Slovenska approved Addendum 3 to the Rules of Procedure of the Permanent Court of Arbitration.

Strategic work on dealing with the change in the payment infrastructure of the Slovak Republic in relation to the integration into the euro area

In the course of 2007, the work on defining a new form of payment infrastructure in the SR after accession to the euro area intensified.



The basis of this infrastructure will be operation of the TARGET2-SK payment system, through which all payments will be processed at the real time, and the holding of funds by participants on their current accounts maintained in this system will be deemed to be the fulfilment of the compulsory minimum reserves.

Another important element of the new infrastructure will be a new retail payment system, EUROSIPS, which will be established by transformation from the current SIPS system. It will be a domestic multilateral clearing system with the final settlement on RTGS accounts in the TARGET2 system. EUROSIPS will be a so called ancillary system to the TARGET2.

TARGET2 is a real-time gross settlement system provided by the central banks of the Eurosystem. The use of this system is mandatory for all central banks of the countries that have adopted euro as their currency. The basis of TARGET2 is a single shared technical platform ensuring a harmonised access to this system for all participants within the Eurosystem. From the legal point of view, however, TARGET2 is structured as a multiplicity of payment systems. The TARGET2 component system operated by Národná banka Slovenska will be named as TARGET2-SK.

In February, the basic features of the future TARGET2-SK payment system were presented, and also of the EUROSIPS retail payment system. In April, participants in the interbank payment system confirmed to Národná banka Slovenska in writing that they would become direct participants in the TARGET2-SK system and also that they would use the services of the EUROSIPS system.

At the beginning of the year, the specification of requirements was prepared for the functions of the new EUROSIPS system, and in May 2007, Národná banka Slovenska opened an internal project for the implementation of the EUROSIPS system. In addition to the development of this system itself, the aim of this project is also testing of the functions so that within the testing of connection of the participants to the TARGET2-SK also the functions of the EUROSIPS system are tested as of an ancillary system of TARGET2-SK.

6.2 The payment system of the Slovak Republic

As at the end of 2007, Národná banka Slovenska operated the SIPS interbank payment system for 32 participants, of which 30 were direct participants and 2 third parties. Over the course of 2007 the number of direct participants increased through the addition of two branches of foreign banks operating in the Slovak Republic on the basis of a single banking passport.

In 2007, the SIPS interbank payment system did not undergo any changes to its basic functions.

6.2.1 Concept of the payment system in the SR in relation to the introduction of euro

In connection with the preparation of introduction of the TARGET2 system, Národná banka Slovenska began preparing the transformation of the present SIPS system to the new retail payment system, EUROSIPS. Within the accession to the euro area, this system will be implemented as a domestic multilateral system of net settlement for retail payments. The system will not require immediate finality, since it will process customer payments of a low value and with low priority (interbank payments of a high value will be directed to the TARGET2 system). Received payments will be processed during the clearing day on technical accounts continuously, and the final settlement of payments will occur twice a day on RTGS accounts in the TARGET2 system. The transfer of data between the EUROSIPS and TARGET2 systems will be executed by transfer of information in the defined structure via the SWIFT-Net network. The operator of the EUROSIPS payment system will be Národná banka Slovenska.

In the course of 2007, the new conception of the payment system in the SR had been presented several times to SIPS interbank payment system participants, being the result of consensus reached between Národná banka Slovenska and banks represented by the Slovak Banking Association as well as other participants of the SIPS interbank payment system.

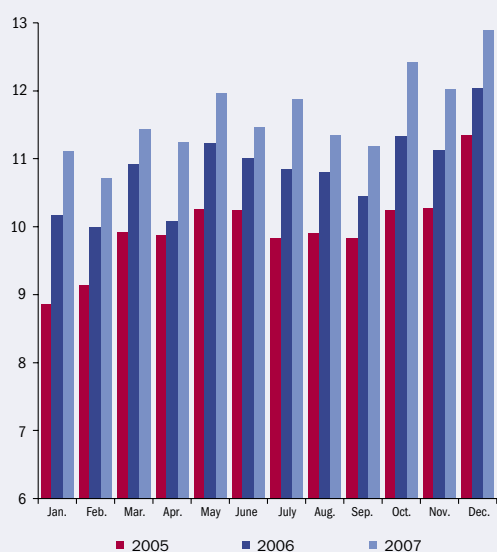
Table 34 Number of transactions made in SIPS

(million)

	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sep.	Oct.	Nov.	Dec.
2004	8.12	8.09	8.94	8.57	9.11	9.46	8.81	9.06	8.94	9.27	9.42	10.93
2005	8.86	9.14	9.91	9.88	10.25	10.24	9.84	9.91	9.83	10.24	10.28	11.34
2006	10.18	9.99	10.92	10.09	11.23	11.01	10.85	10.80	10.45	11.34	11.13	12.04
2007	11.12	10.72	11.45	11.26	11.97	11.46	11.87	11.35	11.19	12.42	12.02	12.89

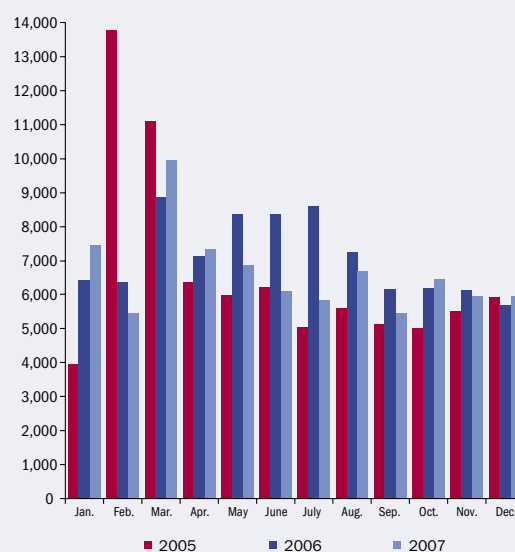
Source: NBS.

Chart 46 Number of transactions made in SIPS (million)



Source: NBS.

Chart 47 Value of transactions made in SIPS (SKK billion)



Source: NBS.

6.2.2 Payments realised via SIPS

During 2007 a total of almost 140 million transactions were processed in the SIPS payment system. Against 2006 the number of transactions rose by 7.47% for the same period, confirming the stable growing trend of previous years.

Chart 46 and Table 34 show data on transactions made in the individual months of 2007 in comparison with the previous years.

Unlike the previous years, in 2007, in comparison with 2006, the total volume of transactions processed decreased by 7.1 percentage points. Thus the growing trend from the previous years, which in the total value of transactions processed represented an annual increase of 40–50% on average, turned around. In 2007, SIPS processed transactions only in the value of almost SKK 79 545 billion. After analyses of the average value of the transfers of client and interbank payments we may conclude that the stabilisation of the national currency could have a significant impact on the decrease in the

value of payments. A significant growth of the value of payments in February 2005 indicated its direct connection with the occurrence of sterilisation operations (Chart 47). Growth rate of the value of payments in year-to-year indicators (in particular, dynamics of growth of the value of priority payments) was considerable until 2007, when a stabilisation occurred (the value of priority payments dropped by 3% in comparison with 2006).

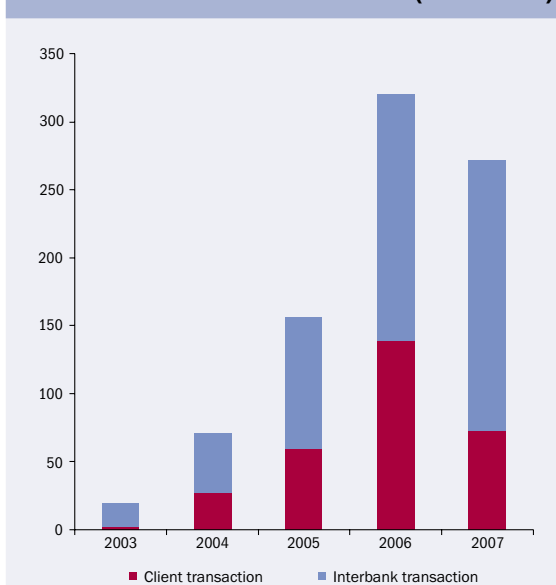
Chart 47 and Table 35 show data on the values of transactions made in the individual months of 2007 in comparison with the previous years.

Since the beginning of 2003, when NBS commenced operation of SIPS system, the number of priority payments reached a significant growth, year-to-year by almost 100%, whereas in 2007, a drop of the number of priority payments was recorded by more than 20%. The fastest growth from among all types of transactions was recorded in customer and interbank priority payment orders. Whereas the total number of priority payments processed and settled stood at 275,000, the figure in the previous year

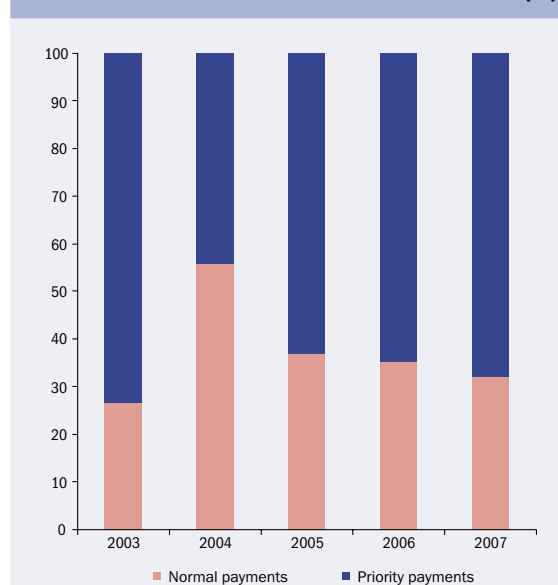
Table 35 Value of transactions made in SIPS (SKK billion)

	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sep.	Oct.	Nov.	Dec.
2004	2.77	2.62	3.05	2.86	3.30	3.95	3.84	3.70	3.46	3.43	3.25	4.46
2005	3.95	13.78	11.12	6.35	5.98	6.22	5.04	5.60	5.14	5.00	5.53	5.93
2006	6.43	6.36	8.88	7.15	8.37	8.38	8.61	7.25	6.17	6.21	6.13	5.69
2007	7.46	5.45	9.97	7.34	6.87	6.10	5.85	6.69	5.44	6.47	5.95	5.95

Source: NBS.

**Chart 48 Number of priority payments (thousands)**

Source: NBS.

Chart 49 Shares of payments in the value of transactions (%)

Source: NBS.

was more than 320,000. However, their share in the total number of transactions made did not change considerably – it represents almost 0.2%, while in 2006, the figure was 0.25%, which is actually related to a minimum representation in the total number of payments. The development of the number of priority payments processed in SIPS is shown in Chart 48.

A decreasing value was recorded also in the value of priority payments, though only by almost three per cent (to SKK 53,959 billion). In comparison with the previous year, however, this is a significant change, as in the years 2004-2006 also the value of priority payments recorded almost a triple growth. Chart 49 shows the shares of normal and priority payments from the total value of transactions processed in 2003-2007, and their ratio has not changed markedly in 2007 compared to the previous year.

Information on the number and volume of transactions processed in the SIPS is published on Národná banka Slovenska¹⁶ website and is updated daily at 15:50 hours.

On bank holidays and weekends the payment system is closed and system maintenance is carried out. In 2007 there were 250 working days. On a daily basis, SIPS processed and settled an average of 532,000 payments in a total amount of almost SKK 318.18

billion, with an average value per transaction of approximately SKK 598,000.

To better understand this data, it can be said that over the course of roughly 5.82 working days, SIPS processed and settled payments with a cumulative value equivalent to Slovakia's gross domestic product for 2007¹⁷.

Národná banka Slovenska provides intraday credit to those participants of the interbank payment system who are required to hold minimum reserves. Intraday credit is offered as an overdraft facility on financial reserve accounts, with a maximum overdraft limit. The intraday credit is payable within one operating day and must be fully collateralized, i.e. by the relevant amount of securities listed in the central register of short-term securities maintained by NBS.

In 2007, SIPS participants who applied for intraday credit were provided with this credit in the total amount of more than SKK 3,442 billion. The amount of intraday credit provided to participants is monitored on a weekly basis. Per week, Národná banka Slovenska provided intraday credit¹⁸ in an average amount of SKK 66.092 billion.

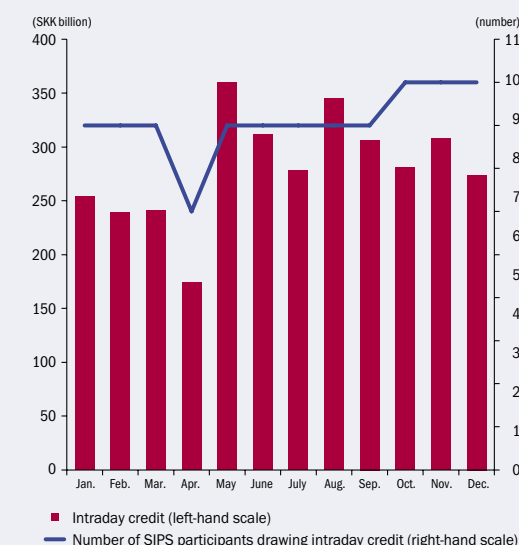
Chart 50 shows the amount of intraday credit provided in the individual months of 2007 and the number of SIPS participants who applied for this credit.

¹⁶ www.nbs.sk – Payment systems / Statistical data.

¹⁷ GDP for 2007 amounted to SKK 1,851.8 billion (Source: Statistical Office of the SR).

¹⁸ The amount of provided intraday credit is deemed to be the value of the securities (decreased by the haircut) that NBS accepted from participants as collateral for the intraday credit. This is the maximum limit up to which participants may draw down intraday credit. At present, actual drawing of credit is not subject to statistical tracking.

Chart 50 Intraday credit in 2007
(SKK billion)



Source: NBS.

6.2.3 Payment cards

In 2007, the number of payments cards issued increased by 6% almost to 4.75 million. Of the total, debit payment cards represent almost 76% and credit payment cards 24%.

As of 31 December 2007, bank clients on the territory of the Slovak Republic could utilize the network of 2,166 ATMs and 25,826 EFT POS payment terminals.

In 2007, the domestic payment card holders made almost 115 million transactions in the total amount of more than SKK 334 billion, and of this figure almost 121 million transactions were made on the territory of the Slovak Republic in the total amount of SKK 322 billion, and more than 4 million in the total amount of SKK 12 billion were made outside the SR. Card holders from abroad made 13 million transactions in the total amount of more than SKK 29, billion on the territory of the Slovak Republic.

6.3 Cooperation with the international financial institutions in the field of payment systems

European Payments Council – SEPA

The Single Euro Payments Area (SEPA) will be area where the consumers, companies and other economic entities will be able to send and receive

payments in euro – whether within one country or between individual countries – on the same conditions, rights and obligations regardless of where they are located. The governing and coordinating body of SEPA on the European level is the European Payments Council, in which the Slovak Banking Association is a member. The SEPA project covers two basic payment instruments – credit transfer and direct debit, and also defines the common framework for card payments.

In 2007 the SEPA project entered the implementation phase in the euro area countries. This phase dealt mainly with preparation for the introduction of new payment instruments, standards and infrastructures of SEPA. Over the course of the year, 28 January 2008 was set as the date of commencement for the use of SEPA credit transfer, and 1 November 2009 was defined as the launch of SEPA direct debit. SEPA direct debit will be introduced later due to technical and legal reasons. Emphasis on the implementation of SEPA payment instruments is laid at the beginning of the project on the euro area countries, and then the SEPA project will be implemented in the entire SEPA area, which will finally consist of 27 EU Member States and Island, Norway, Liechtenstein and Switzerland.

In June, the European Payments Council adopted version 2.3 of Scheme Rulebook for SEPA Credit Transfer, and the same version for SEPA direct debit. The said versions create a basis for the implementation of SEPA credit transfer and direct debit. At the same time, for the versions 2.3, the relevant implementation guidelines were approved, for both payment instruments.

The SEPA project is supported by the European Commission, the European Central Bank, the national central banks, as well as by the European banks. One of the main reasons of general supporting the SEPA is the fact that it will bring new benefits for both the consumers and companies making payments in euro.

The Slovak banking sector is likewise preparing for compatibility with SEPA. In March, the General Plan for Implementation of SEPA – Implementation of SEPA in the SR was approved by the Bank Board of National Bank of Slovakia and then by the Ministry of Finance of the SR. The objective of this Plan is, on one hand, to confirm the obligation of the banking sector to implement SEPA in Slovakia, and to express and point out the main aspects of the changeover to SEPA, on the other hand. The first version of the Plan will be updated and supplemented with a time schedule, including the deadlines and responsibilities, and with a communication strategy depending on the current status of operations and the information and documents available in the course of the SEPA development. In 2007 the Committee for SEPA was



established by the Slovak Banking Association, which is the governing body for the SEPA implementation in the Slovak Republic. It is composed of the representatives of Národná banka Slovenska, the Ministry of Finance of the SR, the Slovak Banking Association, commercial banks, the State Treasury, Slovenská pošta, and of the representatives of employers and consumers.

The Eurosystem, ESCB and the preparation of a new generation of the TARGET2 payment system

Also in 2007, the representatives of NBS participated in the working groups and committees established within the ESCB system and working at the European Central Bank. In 2007 cooperation continued between representatives of central banks of the Eurosystem, the European System of Central Banks and also of future users in the development of a new generation of the TARGET2 payment system. The result of cooperation of the said entities was also continued development of the TARGET2 payment system. On its protected website intended for future TARGET2 users, the ECB continued in publishing materials on the development of the TARGET2 system. In June 2007, the fourth report was released on the development of TARGET2 intended for the public, which contained information concerning remaining pricing and financing issues, interaction with the securities settlement systems and the final version of the General functional specifications of the SSP Single Shared Platform. Moreover, it contained information on the process of testing and migration activities of banking communities of individual countries of the ESCB system. Shortly before launching the TARGET2 operation, in October 2007 the ECB published the fifth report on the development of the TARGET2 system. The purpose of this document was to update the information on the process of development of TARGET2 and to confirm the readiness of the ESCB system for the launch of the first migration phase to the new payment system, TARGET2, which was successfully launched on 19 November 2007. At the same time, it confirmed the readiness of the two remaining migration phases, which are to be performed in 2008.

TARGET2-SK – component of the TARGET2 payment system

In relation to connection to the TARGET2 system, Národná banka Slovenska is obliged to perform several tasks such as e.g. active participation in the operation of the TARGET2-SK system – the national component of the TARGET2 system, coordination of the access process to the TARGET2 system, active participation in the legislative process, and the provision of services relative to the connection to the TARGET2-SK system.

Following a decision of the Bank Board of NBS of December 2006, in January 2007 NBS announced by letter of the Governor to the ECB President the scope of the use of the SSP Single Shared Platform services, which is the basic infrastructure of the TARGET2 (i.e. which optional modules of the platform NBS undertakes to use).

In August, a meeting of representatives of the Payment Systems Department and of representatives of the European Central Bank was held in Národná banka Slovenska, the aim of which were consultations regarding the coordination of the access process of Národná banka Slovenska and of the banking community to the TARGET2 system. Possible methods for implementation of the ECB Guideline on TARGET2 were discussed on the meeting, the “migration” profile of Slovakia and of the EUROSIPS ancillary system to the TARGET2 system, a general schedule for registration and testing of participants of the banking sector of the SR, and other issues.

In September, Národná banka Slovenska presented, to participants of the interbank payment system, a schedule of steps related to the preparation of connection, registration of participants into the SWIFT services, registration of participants in the testing environment of the Single Shared Platform and the performance of the testing itself. These registrations and also the four testing phases should be performed in the next year with an expected duration of 9 months.

In October, the migration profile of NBS and of the Slovak banking community was published on the protected website of ECB intended for future TARGET2 users, for the first time, and also the migration profiles of the subsidiary systems of EUROSIPS and of the Central Securities Depository of the Slovak Republic.

In connection with the preparation of legal regulations, Národná banka Slovenska participated in the correction of a translation of the Slovak version of ECB Guideline on TARGET2, which was published in the Official Journal of the European Union on 8 September 2007.

6.4 Preparation for the introduction of euro

The highest directing and coordinating authority for the preparation of euro changeover in Slovakia is the National Coordination Committee. Expert opinions on individual issues concerning the Slovak economy's transition to euro are being prepared in working committees for euro changeover. The banking sector falls within the remit of the Working Committee for Banks and the Financial Sector, the activity of which is co-

ordinated by a representative of Národná banka Slovenska, and its members consists of representatives of Národná banka Slovenska, the Ministry of Finance of the SR, Slovenská pošta, the State Treasury, the Slovak Banking Association and individual associations of the financial sector. The Working Committee officially began its activity at the end of 2005.

In 2007, negotiations of the Working Committee for Banks and the Financial Sector focused primarily on solving tasks resulting from the National Euro Changeover Plan for the field of payment systems. In addition to this, the Committee participated in updating of the National Plan.

In the field of cashless payment systems this concerned in particular the preparation of an amendment to the Act on the Payment System, the so called Euro Amendment, which is related directly to the process of euro introduction, changes in the SIPS system and connection to the TARGET2 payment system.

In the field of cash payment systems this concerned in particular a more exact identification of the need

of cash and its procurement from NBS, as well as the provision of euro cash in the form of so called starter kits to inhabitants.

At the meeting of the Working Committee for Banks and the Financial Sector also the Regulation of Národná banka Slovenska was the subject of discussion, which lays down certain rules of the dual display and other rules for the conversion of certain prices, payments and other values for the sphere of the financial market and for the services of financial institutions in the sphere of the banking sector, the capital market, the insurance sector and pension saving.

Within the Working Committee for Banks and the Financial Sector a Subcommittee for Banks and a Subcommittee for Insurance Companies was established. Within the Working Subcommittee for Banks, a strategy for the introduction of euro for cash circulation in the SR was adopted. Moreover, the Subcommittee for SEPA was cancelled, since a separate Committee for SEPA was established within the remit of the Slovak Banking Association.

Statistics



7 Statistics

Národná banka Slovenska collects, compiles and publishes various types of statistics in order to support the implementation of monetary policy and financial stability. In 2007, the process of harmonizing individual fields of statistics in accordance with the requirements of the ECB, other Community institutions as well as other international institutions continued. In addition, an extensive change of the presentation of data in the main menu of the NBS website for the statistics area was introduced, and tasks connected with the introduction of the single European currency were ensured in line with the medium-term strategy.

Monetary and banking statistics

Activities carried out in 2007 focused mainly on fulfilling the ECB requirements for monetary statistics and statistics on financial institutions and markets. In 2007, the following statistics were compiled and published: harmonized statistics of monetary aggregates and counterparts to the M3 monetary aggregate, stocks and flow data in financial statements for the monetary financial institutions sector, mutual funds and other financial intermediaries, and interest rates on deposits received and loans granted. In addition, statistics on long-term interest rates for representative government bonds were provided for the purposes of monitoring the fulfilment of one of the convergence criteria.

In statistical reporting for 2007 for credit institutions, the structure of required data was improved through inclusion of conceptual changes made in the previous years. New requirements for the reporting of interest rate statistics for new loans and deposits in euro were introduced. Apart from this, the technological environment for the automation of data file compilation for financial statement statistics and interest rate statistics was completed.

In connection with the preparation of new ECB directives for this part of monetary and banking statistics, NBS focused on ascertaining the availability and significance of new data and costs of their acquiring, as required. NBS cooperated on a variety of methodological questionnaires of the ECB monitoring the

national environment. Work on setting up historical time series continued in line with the strategy of euro area expansion to include Slovakia as well.

New ECB requirements for the reporting of transactions/non-transactions and securities reporting on a security-by-security basis were incorporated to the existing statistical reporting of mutual funds (outstanding amounts of assets and liabilities) in 2007.

From the beginning of the year, the first data for the other financial intermediaries sector, submitted by companies engaged in financial leasing, consumer credits and factoring started to be processed and compiled.

In addition to cooperation with the IMF, more intensive communication with the BIS regarding the statistics on issued debt securities began.

The interrelation between monetary and banking statistics and other types of statistics and the utilization of these statistics in other activities ensured by NBS is clearly proved by the fact that the data provided are employed not only for the conduct of monetary policy, but also as underlying data for compiling quarterly financial account statistics, calculation of credit institutions' required reserves, compilation of balance of payments statistics and bank development statistics, financial stability (prudential) analyses, calculating structural statistical indicators, as well as for payment system statistics within the ESCB.

In 2007, an extensive change of the presentation and availability of harmonized national data for the monetary and financial statistics area was completed on the website of NBS.

Quarterly financial account statistics

In terms of ECB requirements, Národná banka Slovenska also contributes to the compilation of quarterly financial accounts (QFAs) of the monetary union. The main purpose for compiling QFAs is to create a supporting analytical tool for the purpose of monitoring the monetary policy transmission mechanism and for financial stability analyses.



The matrix of QFAs contains data on the structure of financial flows for individual financial instruments (currency in circulation, deposits, loans, debt and equity securities, financial derivatives, mutual funds and insurance technical reserves) between individual institutional sectors in the economy, classified according to the European System of Accounts (ESA 95). In compiling QFAs, Národná banka Slovenska cooperates closely with the Statistical Office of the SR, which is responsible for the general government sector and for the annual financial accounts for the whole economy.

In 2007, in cooperation with the Statistical Office of the SR, methodological differences in the financial flow data in the general government sector were focused on, due to existing significant compilation differences between the underlying data of NBS and that of the Ministry of Finance of the SR. In connection with the overall structure of QFAs, it was also necessary to automate the interconnection of input data from the individual financial market entities with the output matrices of QFAs within the application programme systems for STATUS and STATUS DFT statistics. Over the course of the year, consultations with representatives of insurance companies and pension saving companies took place in connection with a prepared update of the NBS decree for data collection for the needs of QFAs. The process of statistical balancing of all underlying data of QFAs started in the second half of 2007. This process will lead to methodologically and statistically consistent time series of QFAs for the whole national economy of Slovakia.

Statistics on insurance companies and the capital market

In connection with the integrated supervision of the entire financial market conducted by NBS, the need to ensure – in addition to rendering the supervisory and regulatory activities more effective – a simplified communication with the supervised entities emerged. Emphasis was placed on ensuring the collection, processing and storage of data of financial market entities, which are of utmost importance not only for supervision performance, but also for statistical purposes, both for national and supranational institutions.

The year 2007 was the first year of operation of APS STATUS DFT, which, to a maximum extent, exploits the

possibilities of APS STATUS, which has been used by banks and branches of foreign banks for many years, and, at the same time, makes it possible to cover a considerably higher number of reporting entities, their various categorization, and provides the option to report by means of a representative.

The beginning of the year was typical of the provision of methodological instructions to entities for the use of this certified data transfer and subsequent rendering mutual communication between NBS and the reporting entities more effective, above all by completing the design of possible logical relations between individual data. Changes resulting from the gradual implementation of the European Union directives regulating the activities of financial market entities were made to the statement forms.

At the end of the year, NBS also started to focus on work related to the changeover to the single European currency and the associated requirements for conversion of statistical databases.

Statistics of non-banking entities

The field of statistics of non-banking entities involves the acquisition and processing of statistical reports from entities other than banks and branches of foreign banks, for the purposes of compiling the balance of payments and international investment position.

Concerning activities performed in the statistical area of non-banking entities, the year 2007 saw a harmonization of statistics in accordance with the recommendations of international institutions, primarily the ECB, which concern the methodology for the compilation of balance of payments and international investment position statistics.

Upon Slovakia's entry to the euro area, the scope of reported data will also undergo changes, so as to allow the compilation of the balance of payments and international investment position statistics. In the second half of 2007, work in connection with Slovakia's euro area entry and the related requirements on the conversion of statistical data began.

In 2007 information on foreign direct investment continued to be published on NBS website, in its Monetary Survey monthly bulletin.

Foreign Activities



8 Foreign Activities

8.1 The European Union

Active cooperation of Národná banka Slovenska with the EU institutions and its Member States continued also in 2007.

Národná banka Slovenska participated in the preparation of an updated Convergence Programme of the Slovak Republic for 2007-2010, and the NBS Governor was a member of the delegation which presented this Programme in Brussels to the Chairman of the European Commission, José Barroso, and to the Commissioner for Economic and Monetary Affairs, Joaquín Almunia.

The highest representatives of NBS took part in regular informal meetings of the Economic and Financial Affairs Council (ECOFIN), which took place in Berlin in April and in Porto, Portugal, in September. The discussed topics involved social relations, the quality of public finance, financial markets, the economic condition and financial stability of the EU, tax-related issues and securities settlement in the EU.

NBS participates in the decision-making process of the EU bodies via its representatives in selected committees and working groups of the EU Council and the European Commission. NBS plays an important role in the Economic and Financial Committee (EFC) of the EU Council, and NBS experts also participate in the activities of several sub-committees. Within the European Commission committees, experts of Národná banka Slovenska take part in sessions of the committees and sub-committees for supervision (CEBS, CEIOPS, CESR), in meetings of the committee and working groups for the monetary and financial statistics and payment balance statistics, as well as in meetings of the working group of mint directors.

In coordination of Slovakia's participation in the decision-making process on EU issues, the Commission for EU Affairs, established at the Ministry of Foreign Affairs of the SR, has a significant position. In 2007, NBS continued to participate in the said process by the preparation of background papers for drafting instructions, and in the form of participation of its representatives at regular meetings of this Commission.

NBS participates in the process of preparation of EU legal acts in the form of comments. In 2007, NBS expressed its opinion on draft directives on process rules and prudential assessment criteria for the acquisition of and increase in shares in the financial sector, payment services in the internal market, consumer credit contracts, and the commencement and conduct of direct insurance and reinsurance (Solvency II).

The European System of Central Banks (ESCB) and the European Central Bank (ECB)

Národná banka Slovenska cooperates with the ECB at several levels. The NBS Governor is a member of the General Council of the ECB, which convened four times in 2007. These meetings are attended by the governors of all national central banks of the EU and the highest representatives of the ECB. Other negotiations of the General Council of the ECB were held in the form of a teleconference in relation to a request by the Ministry of Finance of the SR and NBS for a change to the central rate of the Slovak koruna in the ERM II (March 2007) and on the occasion of adoption of the ECB Convergence Reports for Malta and Cyprus (May 2007). During the year, NBS representatives participated in the activity of committees and working groups of the ESCB by performing specific tasks, including the preparation of documents for negotiations of the General Council.

In 2007, the area of consultations on draft legal regulations of the ESCB member countries, which fall under the remit of the ECB, was characterized by adopting opinions on the legal regulations related to the introduction of a common currency in Cyprus and Malta. However, from the point of view of NBS, the most significant consultation in 2007 referred to the Act on the euro introduction in the Slovak Republic. Before adopting the Act by the National Council of the Slovak Republic it was necessary, in compliance with applicable procedures, to consult the ECB on this general act, which were successfully concluded. In 2007, NBS commented on a high number of ECB opinions related to draft legal regulations of the other EU Member States.



8.2 NBS cooperation with international institutions

International Monetary Fund (IMF)

In connection with the fact that, as of 2006, the Slovak Republic belongs to the donor countries participating in the Financial Transaction Plan (FTP), it was invited in 2007 by the IMF to provide, for the first time, a part of foreign exchange reserves to other member states experiencing balance of payments difficulties. In 2007, the Slovak Republic granted from its foreign exchange reserves SDR 3 million.

The cooperation of Slovakia and the IMF evolved in 2007 as well, mainly through the IMF missions. In February to March, regular consultations were held with the Slovak Republic under Article IV, conducted with each member state. An IMF delegation visited Slovakia again in November 2007 (the so called Staff Mission). The main topics of the discussions at both meetings were inflation forecasts, participation in ERM II, adoption of the euro, the balance of payments and banking supervision.

In accordance with the Article VIII of the Articles of Agreement of the IMF, NBS updated for the IMF its Annual Report on Exchange Arrangements and Exchange Restrictions, and forwarded to the IMF Executive Board for notification, the list of foreign exchange restrictions that Slovakia applies in order to preserve national and international security, and to protect the financial system against financial terrorism.

In April 2007, the representatives of Národná banka Slovenska attended the Spring Meetings of the International Monetary Fund and the World Bank, held in Washington, and their Annual Meetings, held in Washington, too, in October. The meetings focused on outlooks for the world economy and financial markets, and the IMF medium-term financing strategy. The highest attention was paid, however, to the revision of the quotas of member states and member votes of the countries.

The meeting of representatives of the Belgian Constituency of the IMF and the World Bank on the level of representatives of central bank governors and Ministers of Finance, in Ljubljana, Slovenia, in June 2007, was focused mainly on the revision of IMF quotas.

In 2007, NBS represented the Slovak Republic in operations resulting from the participation of the Slovak Republic in dealing with the remission of Liberia's debt against the IMF.

The World Bank (WB)

Also in 2007, the position of the Slovak Republic in the group of the World Bank developed depending on the transformation process of the Slovak economy and with a promising aim of Slovakia to graduate in this institution from the position of a subsidy recipient to a provider.

On 15 August 2007, the Slovak Government appointed NBS Vice-Governor Ing. Viliam Ostrožlík, MBA, to the position of an Alternate Governor in the group of the World Bank for the SR.

In cooperation with the International Bank for Reconstruction and Development (IBRD), the Slovak Republic drew a financial and technical subsidy in 2007. Over the course of 2007, projects in the field of health service and social affairs, carried out through the government departments concerned, were successfully completed.

As the donor country, the Slovak Republic in the International Development Association (IDA) attended negotiations about the 15th replenishment of IDA funds. Over the course of 2007, the SR paid the second instalment of its contribution under the 14th replenishment of IDA funds, which should reach the total amount of EUR 2.07 million.

In July 2007, the World Bank issued a report on the Financial Sector Assessment Program (FSAP), which assessed the standards applied in the banking and insurance sectors.

Bank for International Settlements (BIS)

On 23-25 June 2007, the 77th annual meeting of the member central banks of the BIS was held, where the distribution of profit was approved in the form of dividends among the BIS shareholders.

Over the course of 2007, five ordinary meetings of the Governors were held at the BIS. The meetings addressed the roles of central banks, development in the financial markets, activities of the Basel Committee, and the central bank policy in the field of statistics.

Národná banka Slovenska joined central bank surveys, which were organised by the Central Bank Governance Group within the BIS on such issues as the method of decision-making and communication on monetary policy, salary issues, perception of central banks by the public, participation of central banks in the environmental protection and the use of agreements in managing the central bank's assets.

Organisation for Economic Cooperation and Development (OECD)

In 2007, the NBS representatives contributed to the activities of relevant working bodies of the OECD. In particular, they contributed to the work of the Economic Policy Committee (EPC), the Economic and Development Review Committee (EDRC), the Committee on Financial Markets (CFM) and the Insurance and Private Pensions Committee. Economies of the OECD member countries were assessed by the EDRC in 2007, including the economy of Slovakia and of some non-member countries.

In April 2007, Angel Gurría, the Secretary-General of the OECD, presented the publication *Economic Survey of the Slovak Republic* in Bratislava. This is a regular report of the OECD about the condition of the Slovak economy, which is prepared by the EDRC in cooperation with NBS and other Slovak institutions. The OECD report evaluated the economic development in Slovakia positively.

European Bank for Reconstruction and Development (EBRD)

In 2007, the European Bank for Reconstruction and Development adopted, for the first time in its history, a resolution on the allocation of net income for 2006 in the amount of EUR 1.374 billion, since the amount of general reserves exceeded, for the first time, 10% of the registered capital (i.e. EUR 2 billion). At the annual meeting of the EBRD in Kazan, the Russian Federation, the allocation of net income to the reserves was approved by the EBRD Board of Governors.

In general, activities of the EBRD in the SR focus in a selective manner on operative objectives defined in the EBRD Strategy for the SR of 2006. In 2007, the EBRD approved a credit line for the SR for energy saving projects and renewable resources projects.

International Investment Bank (IIB) and International Bank for Economic Cooperation (IBEC)

The Slovak Republic has been a member state of the IIB and IBEC headquartered in Moscow since their foundation. Upon the split in the common assets held together with the Czech Republic, on the agreed double to one principle, the Slovak Republic as one of the succession states of the Czech and Slovak Federative Republic of 1993 has a member's share in the paid-up capital of the IIB of 4.8% (EUR 10.4 million) and that of the IBEC of 6.0% (EUR 8.6 million).

International Investment Bank (IIB)

A significant impulse for IIB development are procedures of the new management of the bank approved on the 85th and 86th meeting of the IIB Bank Board in 2007. The IIB implements systematically individual parts of the adopted development plan, the aim of which is to reach the status of a fully recognised international banking institution. A part of this programme is a medium-term development agenda involving the preparation of a bank strategy for streamlining banking activities in individual member states. Over the course of 2007, the IIB completed the changeover to international accounting standards, which was confirmed also by an international audit conducted by KPMG.

An important practical result of the effort made by the bank, compared to 2006, is the growth of total income by 60% and the corresponding increase in profit, which reached EUR 6.4 million. The credit/investment activity of the bank has been gradually developing, which was positively reflected in the structure and qualitative parameters of its credit portfolio.

One of the main objectives focused on for the upcoming period is to obtain an investment grade rating, which would support further qualitative development of the bank.

International Bank for Economic Cooperation (IBEC)

The settlement of claims of the bank against the former Soviet Union had a significant impact on activity of the IBEC. In addition to this, the bank continued to solve problems related to its financial relations with another very important partner – the Republic of Cuba. Over the course of the year, business contacts became more intensive with Bulgaria and Mongolia.

An important moment for the IBEC in 2007 related to personnel and organization. After a prolonged vacancy, the Chairman of the Board of Directors was appointed, and the IBEC proceeded to the optimisation of the organisational structure and to development of organisational preconditions for improved performance of banking operations.

8.3 NBS foreign training and development activities

Národná banka Slovenska contributes to the common strategy of the European System of Central Banks (ESCB) in the area of training and development by active participation of its representative in the ESCB Task Force on Training and Development.



The aims are to approach or build a common basis for the training and development of employees of the ESCB central banks, as well as to create a common corporate culture. The results of cooperation are common training activities focused mainly on the development of management skills and professional development of ESCB employees, coordination of training activities of individual ESCB central banks, as well as new initiatives and projects, and adjustment of the existing activities according to the current and prospective needs.

In 2007, NBS was again the organiser and the host of the first part of the seminar "Heading for Leadership", which belongs to the ESCB common training activities. Held on 21-25 May 2007 at the premises of NBS in Bratislava, the event was attended by 14 representatives of 12 ESCB central banks. In addition, the following four open seminars were organised for employees of the ESCB central banks:

1. Banking and Financial English, 14-17 May 2007,
2. Risk Management – Hedging by Derivatives, 30-31 May 2007,
3. Financial English for Corporate Lawyers and Non-Financial Managers, 15-18 October 2007, and
4. IAS/IFRS Workshop for Financial Analysts and Risk Managers, 19-21 November 2007, focused on the issues of International Accounting Standards and International Financial Reporting Standards.

All the events met stated objectives and foreign participants evaluated them positively. In total, 29 employees of the ESCB central banks participated in these trainings.

In 2007, Národná banka Slovenska organised several trainings within the foreign technical cooperation, which is coordinated by the group of coordinators working under the supervision of the Bank for International Settlements (BIS). The lecturing and consultation activities were performed by experts from the relevant specialised departments of NBS and the costs of the preparation of training were borne by NBS.

For the specialists from the supervision departments/authorities of the neighbouring countries and for other experts that deal with the issue of financial stability, for the fourth time, a workshop was organised on current topics. The three-day workshop was held in an interactive manner and representatives of all participating central banks (from the Czech Republic, Hungary and Poland) were engaged in its programme.

In 2007, the recipient of foreign technical assistance provided by NBS in a form of training was mainly the National Bank of Ukraine, in harmony with the EU common foreign policy (the so called Neighbourhood Policy). Realised activities were based on a bilateral agreement. During 2007, NBS prepared seven trainings for employees of the National Bank of Ukraine: four consultations/study visits and two specialised seminars in Bratislava, and one round table in Kiev. In terms of expertise, the events were led by 30 NBS experts and were attended by 84 employees of the National Bank of Ukraine.

Technical assistance was also provided to the National Bank of Serbia and to the Bosnia-Herzegovina financial market supervisory bodies.

Preparation for the Euro Introduction



9 Preparation for the Euro Introduction

With the oncoming accession of Slovakia into the euro area, preparations for this event escalated on all levels. At the beginning of 2007, the National Euro Changeover Plan was updated. As early as during preparations and approval of the so called General Act secondary legal regulations started to be elaborated. All tasks resulting from the National Euro Changeover Plan and the NBS Internal Plan were performed on schedule or were being performed continuously. It results from surveys made at the end of 2007 that the majority of entities of the public and corporate sectors has already started their preparations for the euro introduction. A favourable economic development has supported successful fulfilment of the Maastricht Criteria. Estimates of development for the following years indicate that the Criteria were fulfilled in a sustainable manner, and Slovakia is ready to introduce the euro as of 1 January 2009.

9.1 The National Euro Changeover Plan and organizational preparations

In 2007 activities became markedly more intensive in all sectors with the aim to prepare citizens and the public and private sectors for the administrative, technical and organizational aspects of a smooth introduction of the euro as of 1 January 2009.

A significant step was the update of the National Euro Changeover Plan in the Slovak Republic, which led to its specification and extension by additionally identified tasks. In the interest of reaching better mutual understanding with the EU institutions before the readiness of the SR to enter the euro area was

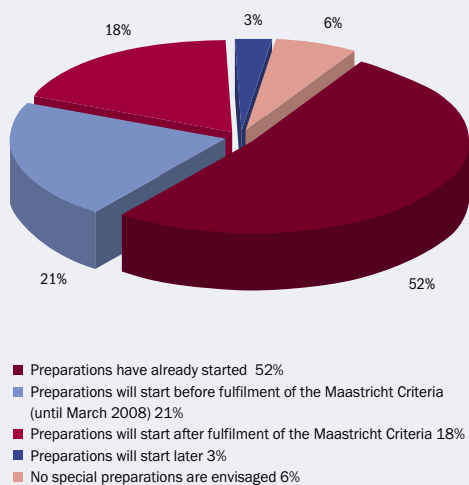
assessed, an action plan for the intensification of consultations with the EU institutions and with selected EU Member States in order to introduce the euro in the SR as of 1 January 2009 was prepared and approved. A Euro Committee was established, and the highest representatives of NBS and the MF SR were appointed its members. The Committee dealt mainly with tasks linked with the fulfilment of the Maastricht Criteria, related preparation of essential documents, and coordination of technical discussions with the European Commission representatives. For the needs of communication with the public in the event of serious problems, the Crisis Communication Staff was established.

Over the course of the year, several joint meetings of the working committees for the euro changeover were held. The Plenipotentiary of the Slovak Government for adopting euro in cooperation with the Minister of Finance prepared and summoned three meetings of the National Coordination Committee for the euro changeover. The Working Committee for Legislation coordinated and controlled preparation work on Slovak legislation regulating an organized, smooth and transparent introduction of the euro in Slovakia and the compliance with the approved schedule of legislative steps leading to the euro introduction in Slovakia. The key legislative act is Act No. 659/2007 Coll. on the introduction of the euro in the Slovak Republic and on amendments to certain acts, (the so called General Act), drafted by NBS and MF SR, which constitutes the basic legal framework for the euro introduction in Slovakia. In the second half of 2007, attention was focused on preparations of secondary legal regulations, i.e. regulations which, depending on their contents, will become effective either in 2008 (so as to allow necessary preparations for the euro

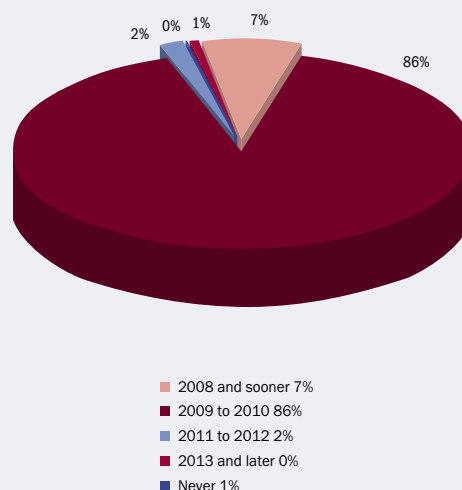
Table 36 **Time table for the euro adoption in the SR**

Fulfilment of the Maastricht Criteria	March 2008
ECB and EC Convergence Reports	May 2008
EC proposal to the Council of the EU for abrogation of the derogation	May 2008
Consultation with the European Parliament	June 2008
Council of the EU abrogates the derogation and sets the conversion rate	July 2008
Euro area entry – „€ Day“	1 January 2009

Source: NBS.

**Chart 51 Preparedness of entities for the euro introducing in the SR**

Source: The Business Alliance of Slovakia, 2007.

Chart 52 Expectations of Slovak citizens for the date of the euro changeover in Slovakia

Source: Eurobarometer, 2007.

introduction to be performed), or, at the date of euro introduction at the latest. The most important were ministerial decrees which laid down details about procedures and methods of the dual display, special rules for the dual display and for introducing and rounding prices, unit prices and payments at the euro changeover, and of the display of prices, unit prices and payments exempted from the dual display obligation. Preparation of the decree on rules for reporting and conversion of monetary data in relation to the euro changeover for accounting purposes, taxes, fees and customs purposes was also important.

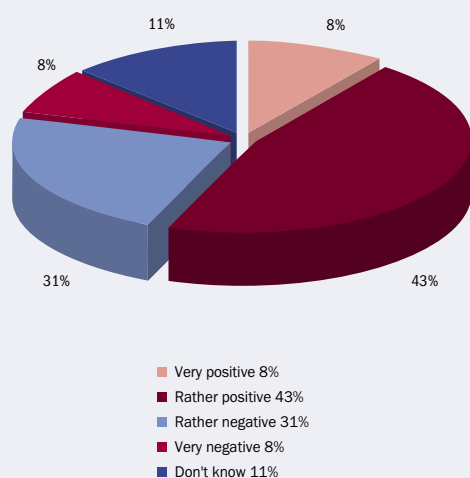
A report on the fulfilment of the National Euro Changeover Plan in the SR for 2007 stated that in the period under review the most considerable progress had mainly been achieved in the performance of tasks related to preparations of an information campaign, preparations for the euro cash frontloading, and preparations of general government bodies. The former two areas are within the responsibility of working committees under the remit of NBS.

All tasks assigned to the Working Committee for Communication for 2007 were completed. In cooperation with the Government Plenipotentiary, the Communication Strategy on the Introduction of the Euro in the Slovak Republic was prepared and adopted. It summarizes the current knowledge and plans for communication activities on the euro introduction. Along with the Strategy the competitive bidding process to select a communication agency was successfully completed. The agency will perform the main campaign aimed at increasing public awareness of

the euro introduction process. A company for the preparation and operation of the national Internet website on the euro adoption, www.euromena.sk, was also selected. At the end of 2007, the website was officially launched. The public perceived very positively informal discussions entitled “Summer Fridays about the Euro”, where preparations for the euro introduction were presented. At the initiative of the Working Committee for Communication, operators of a toll-free info line were trained, as well as lecturers for selected target groups, namely for small and medium-sized enterprises. In cooperation with the ECB, NBS prepared a partnership programme for institutions from both the private and the public sector. The partnership programme allows companies and institutions to use ECB publications, the Euro Campaign logo “Our currency”, and to use source materials prepared by the ECB in their own publications. In cooperation with the Ministry of Education of the SR and the Plenipotentiary of the Slovak Government for adopting euro, preparatory work on the project “Euro to Schools” was completed. Specialized training of teachers on the issue of euro introduction and the production of special educational aids was launched.

In 2007, tasks of the Working Committee for Banks and Financial Sector were focused mainly on the area of connection to the European payment system Target2, preparations of the ATM and POS terminal conversion to the euro, changes of payment cards and the issue of electronic banking. Tasks in the area of cash circulation also belong to its competence, namely the frontloading and sub-frontloading with

Chart 53 Expectations of Slovak citizens for the effect of the euro changeover in Slovakia



Source: Eurobarometer, 2007.

Chart 54 The koruna's exchange rate following entry into ERM II



Source: NBS.

cash and the overall strategy of the euro introduction into circulation in the SR. These tasks are being performed continuously. The Committee discussed the tasks related to the settlement of financial market transactions, the issue of conversion and replacement of market indices, revaluation of securities, preparation of dual statements and exchange rate list adjustments after introducing the euro.

In 2007, in addition to tasks performed within the working committees, NBS completed several other tasks defined by the NBS Internal Plan for the euro introduction. A draft decree was elaborated, under which certain rules were laid down for the dual display and other rules for the conversion of certain prices, payments and other values in the areas of financial market and services provided to financial institutions in the areas of banking, capital market, and insurance and retirement pension saving. NBS monitored and controlled the preparation of banking and financial institutions for the euro introduction, and prepared an analysis of the effects of the euro changeover on the Slovak financial market. Even before the end of the year, preparations started for the frontloading with euro cash. NBS elaborated draft contracts with banks regulating conditions for the frontloading, and prepared a plan for financial backing and adaptation of facilities for placing and processing of euro cash in NBS. Preliminary discussions were held with selected business entities in relation to destruction of Slovak banknotes and coins. The introduction of the euro in Slovakia will affect the performance of monetary policy, administration of foreign reserves and reporting. NBS analysed these areas, prepared proposals for

the harmonization of related activities, statistical data and application software with the ECB. NBS prepared and held specialized seminars on the euro introduction, as well as touring exhibitions on Slovak sides of the euro coins in several regional towns. Training of bank and other employees in relation to the euro introduction continued.

Between May and July 2008, crucial discussions will be made and respective decisions pertaining to the euro introduction will be taken. Experiences of countries that have already introduced the euro imply that ECB and EC Convergence Reports will be prepared at the beginning of May 2008. Positive assessment of the fulfilment of the Maastricht Criteria will be the key step to abrogation of the derogation, setting of a conversion rate, and introduction of the euro as at the planned date, i.e. on 1 January 2009.

The euro adoption process implies several tasks, which will have to be ensured by general government bodies and financial and non-financial companies. The most important tasks involve the dual display of prices, conversion of prices and cash circulation. Among the most demanding tasks is the technical support, in particular the modification of software and hardware of information systems. It will also be necessary to convert accounting items; in many cases it will be required to convert and modify the registered capital. Companies and public institutions should adequately train and inform their partners, clients and employees. Surveys conducted at the end of 2007 indicate that the majority of entities had already started preparations for the euro adoption.

Table 37 **Fulfilment of the Maastricht Criteria in 2007**

Criterion	Figure for 2007	Reference value
Inflation (average HICP, in %)	1.9	2.8
Long-term interest rates (%)	4.5	6.4
Government debt (% HDP)	29.4	60.0
General government deficit (% of GDP)	2.2	3.0
Exchange rate stability	Participation in ERM II since November 2005	Participation in ERM II for more than 2 years without severe tensions

Sources: Eurostat, NBS, MF SR.

At that time, preparations were mainly at the early stage. Most steps were executed in companies from the banking sector, insurance industry and financial services, to which most tasks apply resulting from the euro adoption. About one third of addressed entities adopted a decision to start preparations. One fifth of companies appointed responsible persons and prepared an audit plan. Several companies had already passed an audit of activities related to the euro introduction and conducted legislation monitoring. Certain companies had prepared an action programme for the euro changeover and a marketing strategy.

An opinion poll on the euro changeover which the European Commission conducted in the new EU Member States in September 2007 confirmed rising confidence in the euro introduction as at 1 January 2009. More than 86% of Slovak citizens expect the Slovak Republic to introduce the euro in SR 2009-2010. The same survey shows that the majority of Slovak citizens expect the introduction of the euro in Slovakia to have a positive effect, compared to 39% who forecast a negative effect.

9.2 Economic policies and the Maastricht Criteria for euro adoption

In 2007, Slovakia experienced a record growth, based in particular on foreign demand, accompanied by a decrease in current account deficit and deceleration of the inflation. This favourable economic development improved conditions for meeting a key precondition for the euro introduction, which is the fulfilment of the Maastricht Criteria.

From the point of view of Národná banka Slovenska, the primary objective is to meet the Inflation Maastricht Criterion. The average inflation rate for 2007 was 1.9%, which is significantly lower than the reference value as at December 2007 (2.8%). For introducing the euro, fulfilment of the Inflation Maastricht Criterion in March 2008 will be most important.

Another criterion for which NBS is co-responsible is the exchange rate stability in ERM II. NBS is responsible mainly for preventing short-term fluctuations of the exchange rate, and, together with the Government, seeks to keep the medium-term development of the exchange rate close to the equilibrium level and prevent creation of imbalances that could affect exchange rate developments. In November 2007 the condition of two-year membership in ERM II was met. During 2007 the koruna stood on the appreciation side of the set fluctuation band $\pm 15\%$ around a central parity. NBS exercised the option and intervened in the interest of exchange rate stabilization, and, in total made three interventions in response to unreasonable volatility of the exchange rate in the period before and after the revaluation of the central parity on 16 March 2007. Despite the interventions, the exchange rate's stability was maintained in a natural way, and an attempt for exchange rate stabilization did not have to be sought at the expense of the stability of the rest of the economy. The new central parity of the koruna against the euro was set at 1 euro = 35.4424 SKK. The lower compulsory intervention rate was reduced to 30.1260 SKK/EUR and the upper compulsory intervention rate to 40.7588 SKK/EUR. The need for revaluation of the central rate resulted from significant structural changes in the Slovak Republic. With regard to a high differential in productivity growth in comparison with the euro area, the real equilibrium exchange rate strengthened substantially in the period from joining ERM II, and the central parity ceased to be in line with current state of the economy. At the end of 2007, the value of the koruna stood at the level of 5% above the central parity.

At the same time, administrative pressures to strengthen the exchange rate were not present, and the exchange rate was developing in accordance with the fundamentals. Appreciation of the nominal exchange rate resulted from a high differential in labour productivity and a low inflation differential in comparison with the euro area. The development of the exchange rate did not threaten the business sector; both exports and the profitability of companies were growing.

The fulfilment of the Maastricht criterion in the field of long-term interest rates is closely related to meeting the other criteria. Given the decline in inflation and the high credibility of economic policies, Slovak long-term interest rates are substantially lower than the reference value. If all the other Maastricht Criteria are met, the fulfilment of the interest rate criterion should not be at risk.

The general government deficit including the effect of introducing the pension pillar II declined in 2007 to 2.2% of GDP. The government debt in proportion to GDP was 29.4% of GDP. Thus, Slovakia met also the fiscal criterion.

The Slovak Government committed itself to continue in gradual reducing of the general government deficit in the following years. In 2011, the general govern-

ment budget should be balanced. A lower general government deficit will enable to ensure the long-term sustainability of public finance.

Reducing the deficit and meeting the fiscal criterion will help to curb demand and inflation pressures. In a period after the euro adoption a responsible and credible fiscal policy will also work as a stabilizing factor for the development of the exchange rate. From a current estimate of the development of inflation for the next years follows that the inflation criterion will be met not only in 2008, but also in 2009. Several factors work in support of the sustainability of the fulfilment of the inflation criterion: the core inflation has historically been relatively low, and the Slovak Government refuses to decrease indirect taxes. The regulated prices have not been artificially reduced and the prices of energies are at the level of an EU average or higher.

Legislation



10 Legislation

In 2007, Národná banka Slovenska continued to exercise its legislative and approximation competences in the monetary area and in the areas of currency in circulation, foreign exchange management and banking, capital market, insurance and retirement pension saving.

Legislative amendments prepared and implemented in 2007 to laws on matters within the competence of Národná banka Slovenska:

Act No. 659/2007 Coll. on the introduction of the euro in the Slovak Republic and on amendments to certain acts, as amended (the so called General Act). This Act provided for basic legal prerequisites in the Slovak Republic for smooth and successful introduction of the euro in Slovakia and integration of the Slovak Republic into the euro area.

In 2007, Slovak National Council Act No. 566/1992 Coll. on Národná banka Slovenska, as amended, was amended by Act No. 659/2007 Coll. in its Section II. This Act modified in particular the provisions related to monetary policy, monetary policy instruments and issuance of banknotes and coins, and also to the regulations of provisions on transactions, financial management, accounting and other activities of NBS in a manner ensuring the compliance of the Act on NBS with the European Commission legislation on the legal framework for the single European currency and for central banks in the euro area.

Act No. 483/2001 Coll. on banks and on amendments to certain acts, as amended, was amended in 2007 by Act No. 209/2007 Coll. and by Act No. 659/2007 Coll. An alteration made by Act No. 209/2007 Coll. followed the amendment to the Securities Act, which, in a new manner, defined investment services, and also investment activities and auxiliary services in the area of financial instruments. The most important changes, however, were made under Act No. 659/2007 Coll., in particular concerning regulations related to the preparation for the euro introduction in the SR and for the changeover from the present Slovak currency to the euro currency.

Act No. 566/2001 Coll. on securities and investment services and on amendments to certain acts (the

Securities Act), as amended, was amended in 2007 by Act No. 209/2007 Coll. and Act No. 659/2007 Coll. Act No. 209/2007 Coll. made an alteration of the Securities Act in particular in relation to new regulations on organizational requirements and conditions for the performance of activities of investment companies within the single financial market in the European Union. For securities dealers and for branches of foreign securities dealers also the rules of activities in relation to clients were modified. Act No. 659/2007 Coll. made alterations relative to the preparation for the euro introduction in the SR and for the changeover from the present Slovak currency to the euro currency.

Act No. 510/2002 Coll. on the payment system and on amendments to certain acts, as amended, was amended in 2007 by Act No. 659/2007 Coll. This amendment contains regulations relative to the preparation for the euro introduction in the SR and for the changeover from the present Slovak currency to the euro. By virtue of this amendment, mandatory use of constant symbols was abolished in the payment system as well, and from the introduction of the euro on, it will be possible to use constant symbols in the payment system.

Act No. 747/2004 Coll. on financial market supervision and on amendments to certain acts, as amended, was amended in 2007 by Act No. 659/2007 Coll. Under this Act modifications were made to the Act on financial market supervision related in particular to the preparation for the euro introduction in the SR and for the changeover from the present Slovak currency to the euro.

Slovak National Council Act No. 202/1995 Coll., the Foreign Exchange Act, and act under which the Slovak National Council Act No. 372/1990 Coll. on misdemeanours, as amended, was amended and supplemented in 2007 by Act No. 209/2007 Coll. and Act No. 659/2007 Coll. Under Act No. 209/2007 Coll. financial derivatives were exempted from the term "foreign assets". Under Act No. 659/2007 Coll. modifications were made related in particular to the preparation for the euro introduction in the SR and for the changeover from the present Slovak currency to the euro currency.



Act No. 95/2002 Coll. on the insurance and on amendments to certain acts, as amended, was amended in 2007 by Act No. 110/2007 Coll. Under Act No. 110/2007 Coll. modifications were made following the adjustment of technical provision for the payment of liabilities against the Slovak Insurers' Bureau resulting from activities under Act No. 381/2001 Coll. on compulsory contractual third-party liability insurance for motor vehicles, as amended.

Act No. 594/2003 Coll. on collective investment and on amendments to certain acts, as amended, was amended in 2007 by Act No. 209/2007 Coll. and Act No. 659/2007 Coll. Under Act No. 209/2007 Coll. EU requirements were modified for the harmonization of requirements for transparency in relation to information on issuers whose securities were accepted for trading in the regulated market, and also organizational requirements and conditions of the performance of management companies' activity. Under Act No. 659/2007 Coll. modifications were made in relation to the preparation for the euro introduction in the SR and for the changeover from the present Slovak currency to the euro currency.

Act No. 43/2004 Coll. on retirement pension saving and on amendments to certain acts, as amended, was amended in 2007 by Act No. 209/2007 Coll., Act No. 555/2007 Coll. and Act No. 659/2007 Coll. A notable change was made by Act No. 555/2007 Coll., which introduced material changes regulating pillar I and II of old-age pension scheme. Act No. 659/2007 Coll. introduced changes relative to the preparation for the euro introduction in the SR and for the changeover from the present Slovak currency to the euro currency.

Act No. 650/2004 Coll. on supplementary pension saving and on amendments to certain acts, as amended, was amended in 2007 by Act No. 555/2007 Coll. and Act No. 659/2007 Coll. Under Act No. 555/2007 Coll., certain accounting rules and rules for the performance of transactions by a supplementary pension company were modified. Act No. 659/2007 Coll. modified in particular changes relative to the preparation for the euro introduction in the SR and for the changeover from the present Slovak currency to the euro currency.

Act No. 340/2005 on insurance mediation and re-insurance mediation and on amendments to certain acts was amended in 2007 by Act No. 330/2007 Coll. Under this Act, certain competences of the Ministry of Finance of the SR were transferred to Národná banka Slovenska.

Act No. 381/2001 Coll. on compulsory contractual third-party liability insurance for motor vehicles and on amendments to certain acts, as amended, was amended in 2007 by Act No. 110/2007 Coll. Under

this Act, for instance, a limit of insurance benefit from an insured event was introduced; an obligation was modified for the Slovak Insurers' Bureau to create technical provisions, and provisions on supervision of the Bureau's activity were modified.

Slovak National Council Act No. 310/1992 Coll., the Home Savings Act, as amended, was amended in 2007 by Act No. 658/2007 Coll. and Act No. 659/2007 Coll. Under Act No. 658/2007 Coll. in particular provisions on activity a building society may perform were modified, and provisions on purpose for which a building credit can be used, and provisions on certain rules of home savings were introduced. Under Act No. 659/2007 Coll. in particular modifications were made related to the preparation for the euro introduction in the SR and for the changeover from the present Slovak currency to the euro.

Slovak National Council Act No. 118/1996 Coll. on deposits protection and on amendments to certain acts, as amended, was amended in 2007 by Act No. 659/2007 Coll. Under this Act, modifications were made in the Deposits Protection Act related to the preparation for the euro introduction in the SR and for the changeover from the present Slovak currency to the euro.

Act No. 530/1990 Coll. on bonds, as amended, was amended in 2007 by Act No. 209/2007 Coll. and Act No. 659/2007 Coll. A notable change was made by Act No. 659/2007 Coll. following the preparation for the euro introduction in the SR and for the changeover from the present Slovak currency to the euro.

Act No. 429/2002 Coll. on the Stock Exchange, as amended was amended in 2007 by Act No. 209/2007 Coll. This amendment modified in particular provisions on the position and activity of the securities exchange in relation to alterations made by Act No. 209/2007 Coll. in the Securities Act.

Decrees and provisions issued by Národná banka Slovenska in 2007 under its legislative competences to issue implementing, generally binding legal regulations

Decree No. 100/2007 Coll. laying down the details on entries into the Register of Supplementary Pension Saving Mediators.

NBS Decree No. 183/2007 Coll. on the issue of silver commemorative coins of a nominal value of 500 SKK at the 450th anniversary of the completion of the Old Fortress in Komarno.

NBS Decree No. 271/2007 Coll. on the second issue of 1 000 SKK banknotes model 1999 into circulation.

NBS Decree No. 285/2007 Coll. executing certain provisions of Act No. 340/2005 Coll. on insurance mediation and reinsurance mediation and on amendments to certain acts.

NBS Decree No. 425/2007 Coll. amending Decree of the Ministry of Finance of the Slovak Republic No. 166/2005 Coll. on the own funds of a financial conglomerate and on how to calculate the adequacy of the own funds of a financial conglomerate and on amendments to certain decrees as amended by Decree of Národná banka Slovenska No. 657/2006 Coll.

NBS Decree No. 498/2007 Coll. on the issue of silver commemorative coins of a nominal value of 200 SKK at the 100th anniversary of the death of Andrej Kmeť.

NBS Provision No. 1/2007 on information provided by banks and branches of foreign banks (Notification No. 41/2007 Coll.).

NBS Provision No. 2/2007 on the submission of reports, statements and other notices by banks, branches of foreign banks, securities dealers and branches of foreign securities dealers for supervision and statistical purposes (Notification No. 42/2007 Coll.).

NBS Provision No. 3/2007 on the submission of reports by entities ensuring the distribution of securities issued by foreign management companies and foreign investment companies on the basis of a public offer by an investor on the territory of the Slovak Republic for statistical purposes (Notification No. 61/2007 Coll.).

NBS Provision No. 4/2007 on the own funds of financing of banks and requirements for own funds of financing of banks and on the own funds of financing of securities dealers and requirements for own funds of financing of securities dealers (Notification No. 121/2007 Coll.) as amended by NBS Provision No. 10/2007 (Notification No. 420/2007 Coll.).

NBS Provision No. 5/2007 amending and supplementing Provision of Národná banka Slovenska No. 15/2004 on the own funds of a financial conglomerate and on the proprietary involvement of a financial conglomerate as amended by Provision of Národná banka Slovenska No. 13/2006 (Notification No. 352/2007 Coll.).

NBS Provision No. 6/2007 on the record of assets and liabilities of banks and branches of foreign banks (Notification No. 385/2007 Coll.).

NBS Provision No. 7/2007 on reporting on a consolidated unit (Notification No. 379/2007 Coll.).

NBS Provision No. 8/2007 on the own funds of a financial conglomerate and on how to calculate the adequacy of the own funds of a financial conglomerate in accordance with the Securities Act (Notification No. 386/2007 Coll.).

Provision No. 9/2006 on information provided by securities dealers and branches of foreign securities dealers and on amendment to Provision of Národná banka Slovenska No. 1/2007 on information provided by banks and branches of foreign banks (Notification No. 421/2007 Coll.).

NBS Provision No. 10/2007 amending and supplementing Provision of Národná banka Slovenska No. 4/2007 on the own funds of financing of banks and requirements for own funds of financing of banks and on the own funds of financing of securities dealers and requirements for own funds of financing of securities dealers (Notification No. 420/2007 Coll.).

NBS Provision No. 11/2007 on the submission of reports, statements and other notices by banks, branches of foreign banks, securities dealers and branches of foreign securities dealers for supervision and statistical purposes (Notification No. 496/2007 Coll.).

NBS Provision No. 12/2006 on the submission of reports by banks and branches of foreign banks for statistical purposes (Notification No. 505/2007 Coll.).

NBS Provision No. 13/2007 on reporting by management companies in respect of mutual funds for statistical purposes (Notification No. 506/2007 Coll.).

NBS Provision No. 14/2007 on reporting by factoring companies, instalment credit companies and leasing companies for statistical purposes (Notification No. 507/2007 Coll.).

NBS Provision No. 15/2007 on the submission of reports, statements, notices and other information by the Slovak Insurers' Bureau (Notification No. 650/2007 Coll.).

NBS Provision No. 16/2007 on reporting by the Stock Exchange and the Central Securities Depository for the purposes of financial market supervision (Notification No. 651/2007 Coll.).

NBS Provision No. 17/2007 on reporting by management companies and depositories of mutual funds for the purposes of financial market supervision (Notification No. 652/2007 Coll.).

Institutional Developments



11 Institutional Developments

The Audit of Management Processes and Activities conducted in Národná banka Slovenska during 2006 produced a comprehensive report and a recommendation proposal for organizational structure optimization. Its gradual implementation over the course of 2007 initiated the process of organizational structure optimization aimed at achieving maximum effectiveness of internal management system. This process also entailed necessary staff reductions.

11.1 Organization and management

In line with the conclusions of the Audit, the new Bank's Organizational Rules were approved. They came into effect on 1 February 2007, and brought about major changes to the management of Národná banka Slovenska, which are as follows:

- Introduction of a new system of management of Bank's divisions and units with 9 management areas headed by the members of the Bank Board,
- Streamlined management processes by elimination of one management level (division chief executive directors) and by a reduction of the number of managers from 132 to 109,
- Streamlined position plan of NBS.

Three amendments to the Organizational Rules adopted in 2007 brought about certain improvements in the organizational structure and regrouped activities performed in the individual management areas, primarily as a result of the appointment of a new Vice Governor.

Bank Board of Národná banka Slovenska

The Bank Board of Národná banka Slovenska is the supreme management body of Národná banka Slovenska; pursuant to NBS Act it consists of 11 members. The scope of its powers is laid down by the NBS Act, other generally binding regulations, and the NBS Organizational Rules.

With effect from 10 January 2007, RNDr. Karol Mrva, whose previous tenure ended on 30 November 2006, was reappointed as a Bank Board member. Ing. Viliam Ostrožlík, MBA, became a new member

of the NBS Bank Board on 1 March 2007; he was appointed a Vice Governor of NBS on 11 July 2007. With effect from 1 June 2007, Ing. Gabriela Sedláková was appointed an external member of the NBS Bank Board.

As at 31 December 2007, members of the NBS Bank Board were:

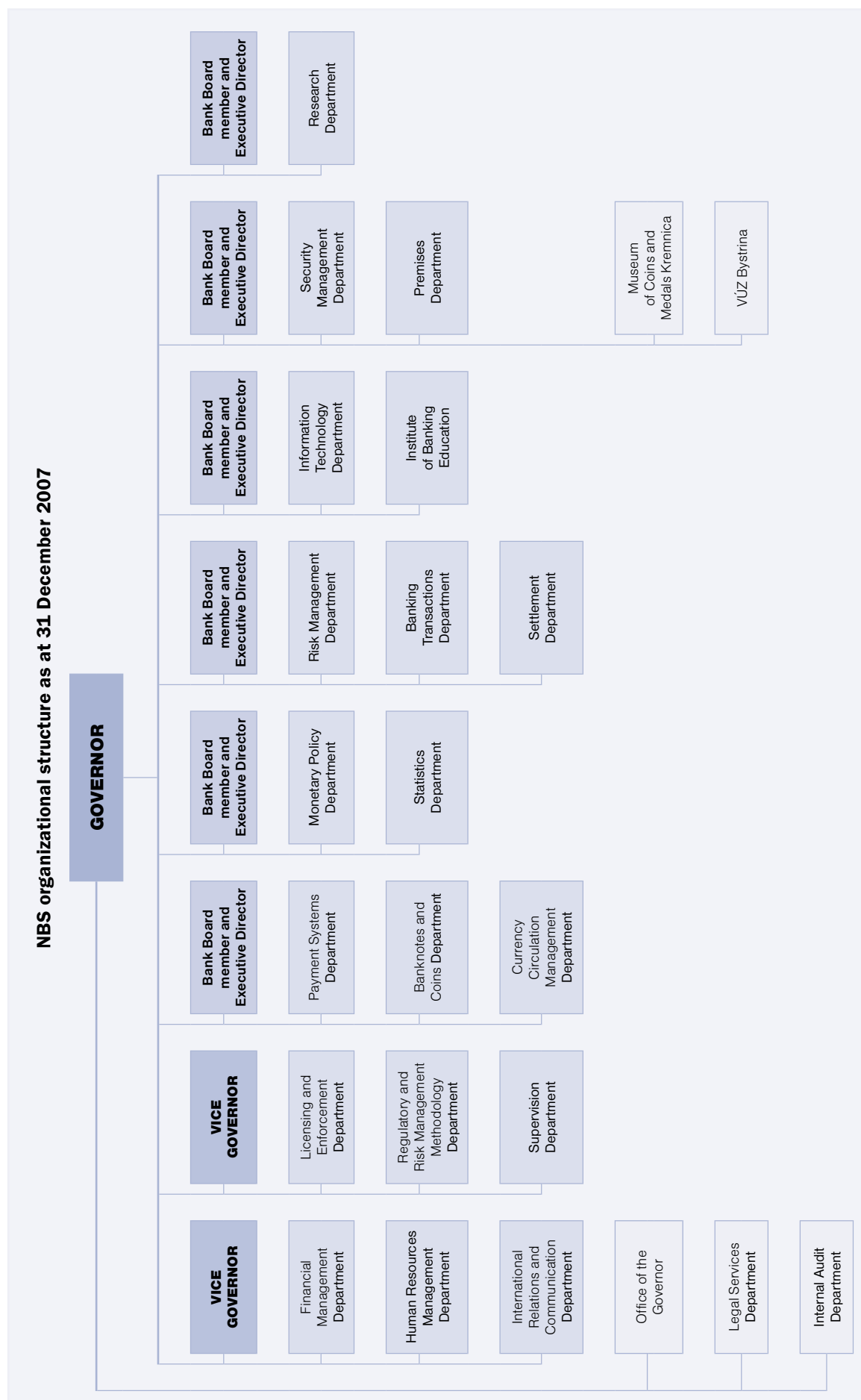
- Ing. Ivan Šramko, Governor
- Ing. Viliam Ostrožlík, MBA, Vice Governor, responsible for the coordination of the euro introduction policy and for the Financial Management Department, Human Resources Management Department and International Relations and Communication Department
- Ing. Martin Barto, CSc., Vice Governor, responsible for integrated financial market supervision
- Ing. Milena Koreňová, responsible for the management of payment systems and currency circulation
- Ing. Peter Ševčovič, responsible for the management of the monetary policy area
- RNDr. Karol Mrva, responsible for the management of financial markets operations
- Ing. Slavomír Šťastný, responsible for the management of financial education and information technology
- doc. Ing. Jozef Makúch, PhD., responsible for the management of security and premises areas
- Mgr. Ľudovít Ódor, responsible for the management of research
- Ing. Gabriela Sedláková, external member of the NBS Bank Board

11.2 Human resources

11.2.1 Personnel

During the course of 2007, the number of planned positions and thereby the number of employees was substantially reduced as a result of an organizational change effective from 1 February 2007.

The number of planned positions in NBS fell by 75 as at 1 February 2007, from 1,221 to 1,146, by further 16 as at 1 July, and by 12 as at 31 December, to a total of 1,118. In 2007, the number of planned positions decreased in total by 103 positions, i.e. by almost 8.5% against 2006.





NBS Bank Board¹⁹

Front row: Viliam Ostrožlík – Vice Governor

(left to right) Ivan Šramko – Governor

Martin Barto – Vice Governor

Back row: Peter Ševčovic – Member of the NBS Bank Board, Executive Director, Monetary Area

(left to right) Ľudovít Ódor – Member of the NBS Bank Board, Executive Director, Research

Milena Koreňová – Member of the NBS Bank Board, Executive Director, Payments System and Currency Circulation

Slavomír Šťastný – Member of the NBS Bank Board, Executive Director, Banking Education and Information Technology

Karol Mrva – Member of the NBS Bank Board, Executive Director, Financial Market Operations

Gabriela Sedláková – Member of the NBS Bank Board

Jozef Makúch – Member of the NBS Bank Board, Executive Director, Security and Premises

As at 31 December 2007, NBS had 1,075 employees (99 employees less than in 2006), which represents a reduction of some 8.5%, similar to the fall in the number of planned positions.

A total of 167 employees ceased to be employed by NBS in 2007. Out of these employees, 106 were made redundant due to the organizational change.

Since NBS underwent restructuring, new employment contracts were concluded, and 69 employees were recruited. Employees from outside NBS were taken on only if no NBS employee showed interest in the position within one of 68 internal recruitment campaigns organized over the course of the year.

11.2.2 Personnel development

The organizational change and associated personnel changes in 2007 did not influence the employee structure to a significant extent.

The age structure of employees is almost identical with that of 2006. The share of employees up to 30 years fell by 1% and that of employees in the age group from 31 to 40 grew by 1%. The largest group consisted of employees aged 31-40, numbering 344 (32%) as at 31 December 2007.

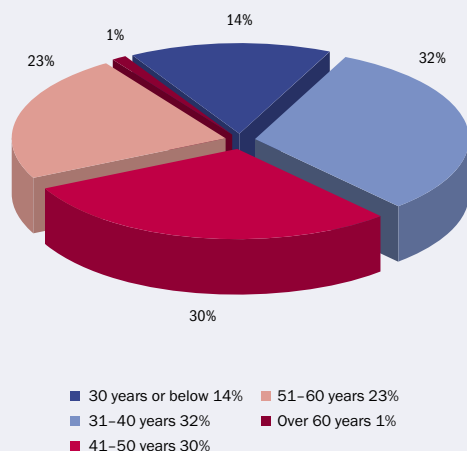
The balanced and almost unchanged age structure of the staff corresponds with the structure of staff in terms of length of service at NBS, where no changes occurred as compared to 2006. The largest group (610) includes employees with a length of service between 11 and 20 years, and the second largest group is represented by employees with a length of service of less than 5 years (240 employees).

The structure of employees according to the educational background is also comparable to that of 2006. The number of employees with elementary and vocational education decreased by 0.5%. The shares of employees with secondary-school education (school leaving certificate) and with university education are

¹⁹ As at 31 December 2007.

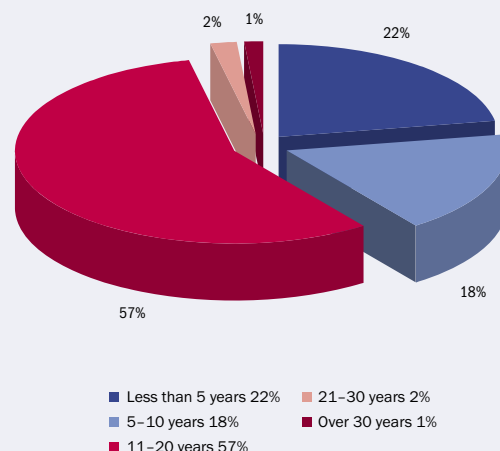


Chart 55 NBS staff by age



Source: NBS.

Chart 56 NBS staff by length of service at the Bank



Source: NBS.

the same as in 2006, 30% and 50%, respectively. A positive trend is the increase in the number of employees with a degree in sciences, which constituted about 2% of the total staff in 2007.

As a result of the organizational changes in 2007, the total number of employees decreased by 8.5% in 2007, with the number of managers falling by as much as 18%.

The percentage shares of male and female employees did not change in 2007 against 2006 and stood at 47% and 53%, respectively.

11.2.3 Employee remuneration

The principles and rules of remuneration at NBS are regulated by NBS internal regulation No. 20/2002 on remuneration of NBS employees as amended. An amendment to that regulation was adopted in 2007 as a result of an amendment to the Labour Code in force from 1 September 2007.

The average wage at the Bank in 2007 was SKK 43,420 with an index of 107.8 in comparison with 2006. Statutory premium contributions for 2007 amounted to SKK 174,147,000.

11.2.4 Social expenses

Social expenses in 2007 included severance payments (and compensatory provision) of 70,558,000 SKK in connection with termination of employment

due to organizational changes. Social expenses also included payments made on the termination of employment contracts (including compensations) due to retirement, disability and early retirement of 66 employees, in the total amount of SKK 7,238,000. NBS social expenses in 2007 included contributions to supplementary pension saving and pension insurance, totalling SKK 21,875,000.

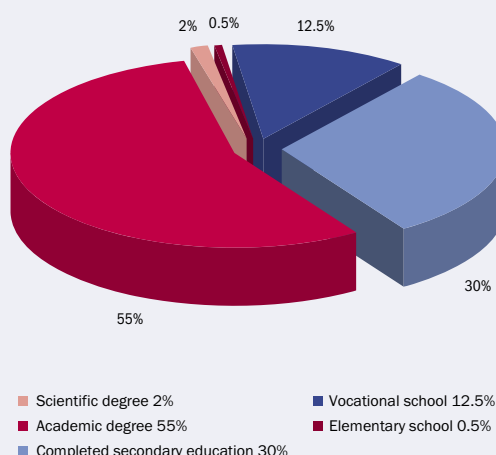
11.3 Training and Education

By joining the European Union and adopting the Lisbon Strategy, Slovakia has set out on the road towards a competitive knowledge-based society and economy. In harmony with this strategy NBS considers training and education one of the most important aspects of furthering the professional and personal development of its employees and thus of improving the quality of their work. NBS training and educational activities are organized by the Institute of Banking Education (IBE) and they are provided not only for NBS staff, but also for the banking sector and other financial institutions employees. The quality management system implemented in the IBE complies with the International Standard of Quality Management System ISO 90012000, which the Institute is certified for.

The prevailing training form is classroom training which is supplemented, to a lesser extent, by distance learning programmes. One of the most interesting distance learning projects is "The Preparatory Course for the European Foundation Certificate in Banking (EFCB)". In the capacity of the only provider of the course in Slovakia accredited by the European Bank-

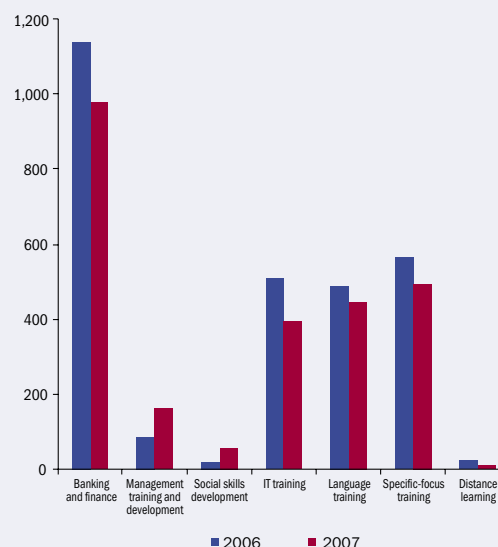
Chart 57 NBS staff by education

(%)



Source: NBS.

Chart 58 Number of NBS participants



Source: NBS.

ing & Financial Services Training Association (EBTN) to hold the exams and to award internationally valid and recognized EFCB certificates, the IBE has been running this course since 2005.

11.3.1 Training and education of NBS employees

In 2007 NBS employees attended 553 training and educational events at which they spent 49,312 hours. The total number of NBS employees who took part at the events was 2,543. In comparison with 2006 both the number of training and educational events and participants decreased slightly which was due to extensive organizational changes and a reduction of the total number of employees of NBS. The ratio of training and education related expenses to wage costs rose slightly year-on-year, reaching 4.33%. Altogether NBS staff spent 2.27% of their total usable working time in training and education.

As in the previous years, the main focus of NBS staff training and education in 2007 was on technical issues of professional training in banking and finance. Other significant areas included specific-focus training, language training, and IT training. The total NBS employee participation by training category, as compared to 2006, is shown in Chart 58.

Professional training in the area of banking and finance centred on the issues directly relating to the performance of the tasks emerging from NBS membership in the European System of Central Banks (ESCB), from the planned entry into the Eurosystem

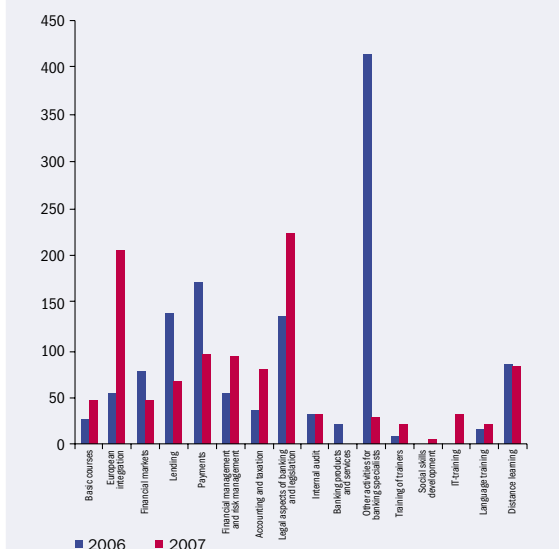
and from the introduction of the euro in Slovakia, as well as on enhancing the European dimension of NBS activities and, to a considerable extent, on financial market regulation and supervision issues, including risk management. To carry out specialized professional training activities organised within the framework of the foreign technical cooperation which are provided free-of-charge, for years NBS has been predominantly utilizing the offers of such institutions as the International Monetary Fund, the BIS Financial Stability Institute in Basel, as well as the national central banks of the EU and other countries (the United States, Switzerland). In 2007 such foreign training and educational events (numbering 141) were attended by 174 NBS employees.

NBS staff also took part in common training activities organized within the ESCB and in so-called Open Seminars offered by the ESCB central banks. For the first time NBS experts were involved as speakers in some of the ESCB common training activities.

In 2007 the IBE continued training new NBS employees by running a special course "Orientation Fundamentals for an NBS Employee", as well as so-called European integration education, mainly in the form of short, half-day and one-day seminars on current issues. In comparison with 2006, considerable growth was registered in the number of events and participants in the management training and development, above all in connection with instructing managers about creation of the cards of working positions. A quite considerable fall occurred in language training and a slighter decline in IT training.



Chart 59 Training and education for employees of financial institutions
(in numbers of participants)



Source: NBS.

NBS supports also the employees who raise or enhance their qualifications for work purposes through external university study or certified educational programmes. Besides taking care of training and education of its own staff, NBS provided 8 students of secondary vocational schools with the opportunity to perform their practical training in NBS. Seven university students were given the opportunity to perform their diploma practical training or to take part in consultations on their diploma thesis topics in NBS. Moreover, NBS received 15 university students from the Instituto Tecnológico de Monterrey of Mexico for a one-day study visit.

11.3.2 Training and education for commercial banks and other financial institutions employees

In 2007, the Institute of Banking Education prepared and held 93 training and educational events attended

by a total of 1,076 employees of banks and other financial institutions. The structure and contents of these events emerged from the needs of target groups, in particular banks.

The core of the IBE programme comprised expert-oriented training and educational events on topical technical issues of banking and finance. Participation by training category, as compared to 2006, is shown in Chart 59.

The numbers reflect the current relevance of the issues dealt with to practical needs. The categories of training and educational events which attracted the most interest in 2007 were “European Integration” and „Legal Aspects of Banking and Legislation“. The interest in other categories remained relatively stable.

The training events were usually held in the form of interactive and practical seminars during which trainers used primarily participative teaching methods which facilitated active involvement of participants in the training process and the acquisition or development of practical knowledge and skills.

11.3.3 Internal trainers

Despite their demanding work duties, internal trainers – members of NBS staff – were able to make time to take active part in preparation and realization of training and educational events and to share their expertise and experience with their colleagues from NBS and with the employees of commercial banks and other financial institutions.

NBS experts also participate in teaching activities within the context of providing foreign technical co-operation and assistance and their presentations are performed at a highly professional level.

In 2007 altogether 60 NBS experts were involved in teaching activities and made a total of 131 training presentations.

Communication



12 Communication

In ensuring its principal aims and statutory tasks, Národná banka Slovenska is an independent institution. Through open communication and transparency in information provision, it demonstrates an effort to be accountable for its activities, not only to parliament but also to the general public.

Národná banka Slovenska is required by law to inform on monetary developments at least once every calendar quarter. In providing an assessment of monetary developments on a monthly basis, and (since 2005) a quarterly forecast of economic and monetary developments, Národná banka Slovenska does more than is required.

Národná banka Slovenska considers communication to be an integral part of its activity and one of the implementation tools of monetary policy. The rules and principles applicable to the communication of monetary policy are elaborated in the "Communication Strategy of NBS until 2009".

By providing information on meetings of the NBS Bank Board in 2007, Národná banka Slovenska observed the principle of openness and transparency. This included publishing the schedule of meetings, holding telephone and press conferences immediately after the Bank Board met to discuss the situation report on monetary developments and to assess the level of key interest rates, and the convening of press conferences by the Governor for announcements on monetary developments and on the breakdown of votes on any interest rate changes.

One of NBS's most important communication channels is its website. Over the years it has developed into a comprehensive information base for professionals, but more recently it has become a means of communicating with all target groups without exception. As part of the information campaign on the euro adoption, at the end of the year, Národná banka Slovenska in cooperation with the Ministry of Finance of the Slovak Republic launched the official Internet website on the euro adoption, www.euromena.sk, and made a separate e-mail address euoinfo@nbs.sk available.

Again in 2007, Národná banka Slovenska prepared a full range of expert publications and information

materials published in print and electronic form. The main sources of core analytical and evaluative information were the Annual Report, Financial Stability Report, Report on the Results of an Analysis of the Financial Sector in the SR, and the Monetary Survey monthly bulletin. Additional analyses and research works concerning monetary developments, the financial market, convergence of the Slovak economy and the effect of the euro introduction were published in electronic form.

Národná banka Slovenska is a member of the European System of Central Banks (ESCB) and its communication activities are linked to the communication activities of the European Central Bank (ECB). NBS representatives participate in meetings and activities of the EUROSYSTEM/ESCB Communications Committee (ECCO) and its working groups, established for the preparation of national language versions of official ECB publications, as well as for the euro changeover information campaign and for communications concerning issues related to the new euro banknotes. In the context of communication about the euro introduction, Národná banka Slovenska also cooperates with partner units of the European Commission and, as part of a twinning programme, with the Oesterreichische Nationalbank.

In line with the principles of ESCB's multilingual communication, Národná banka Slovenska ensures the translation of official ECB publications. In 2007 this applied to the quarterly issues of the ECB monthly bulletin, the ECB Annual Report and the Convergence Report.

The BIATEC journal also plays an important role in the area of public communication, being a respected platform for the presentation of specialist knowledge in banking, finance and economics. Its authors and readers represent a balanced link between Národná banka Slovenska, the banking and financial sector, and the academic and educational sphere. The journal has become not only a communication tool of the central bank, but also its contribution to the fulfilment of the Lisbon Strategy objectives and the creation of a knowledge-based economy.

NBS's communication activities in 2007 were in large part focused on preparations for the euro introduction



in Slovakia. Národná banka Slovenska is the coordinator of two of the six working committees which, under the National Euro Changeover Plan for the Slovak Republic, coordinate the entire process of euro adoption in Slovakia. One of these two committees is the Working Committee for Communication.

During the course of the year, the Governor and other members of the NBS Bank Board had several meetings with representatives of the economic sphere at which they presented the results of analyses of the Slovak economy's convergence and issues concerning the effect of the euro introduction on the corporate sector.

Národná banka Slovenska presented the designs chosen for the national sides of Slovakia's euro coins at an exhibition called "Slovak Euro Coins". Held in Trnava, Prešov, Žilina, Poprad, in the Slovak Institute in Warsaw, in Zvolen and Nitra, it attracted a total of almost 40,000 visitors in 2007. The exhibition, which is due to be taken to more Slovak cities and towns in 2008, includes some of the other designs entered in the competition and selected designs of children who could also send in their ideas of what should be on the Slovak sides of the euro coins.

In the area of internal communication Národná banka Slovenska provides information from the external environment towards the bank, in particular by obtaining, processing, sorting and providing selectively information from the domestic and foreign press to the top management of the bank, as well as to all its employees. This activity includes in particular the monitoring of press and electronic media and publishing of the basic press monitoring (Express Information, Dailies Overview).

One of the aims of NBS's communication policy is to provide the general public with appropriate information on its activity. To this end, NBS also organizes visits for students which include topical lectures given by NBS experts. For those interested, technical information on the NBS headquarters building is provided and a video of its construction is available to watch. In 2007 Národná banka Slovenska was visited by more than 1,037 secondary schoolchildren and university students, including students from foreign universities.

The NBS building houses a permanent exhibition entitled "Past and Present of Slovak Currency", which is open every working day from 10:00 to 15:00.

Národná banka Slovenska also offers library and information services to the public from a specialised collection focused on monetary policy, the banking sector, financial markets and the law and legislation, computer technology and statistics. In 2007, the online library catalogue processed 4,500 books, research reports, periodicals and articles. The central NBS library provides an access to the domestic and foreign electronic information resources, from which it executes search services and other information output in particular to NBS staff. Members of the public may access any of the reference, bibliographical and search services by writing to centralna.kniznica@nbs.sk. The high standard of services rendered has a favourable response with the public, which was reflected in 2007 by increased visits and lending on the spot. In 2007 the central library processed 1,500 searches for the public to information requests on various disciplines of economics.

During 2007 Národná banka Slovenska answered more than 2,100 queries sent and requests for information pursuant to Act No. 211/2000 Coll. on freedom of access to information.

The Museum of Coins and Medals at Kremnica is a part of Národná banka Slovenska. In 2007 it inaugurated a new long-term exhibition entitled "The Routes of Collecting 15th-18th Century Art", subtitled "Public and Private Collecting in Kremnica". The exhibition presents for the first time to the public almost a complete collection of the art of that period, which underwent a restoration process in the previous decade. In addition to the permanent exhibitions, it opened 14 temporary exhibitions, among others also an international medals exhibition of the Visegrad countries. In 2007, the 9th International Medal Symposium was held, which was attended by 5 prominent European medal makers. Culmination of the Symposium was the opening of an exhibition which presented a collection of coined and cast medals created during the Symposium. The museum centres a substantial part of its activities on the organization of cultural and educational events designed for secondary schoolchildren and university students and to the general public. For the second time, the museum took part in the international event "Museums' Night" held on International Museum Day. In 2007 permanent and temporary exhibitions of the Museum of Coins and Medals at Kremnica attracted more than 40,000 visitors from Slovakia and abroad.

Independent Auditors' Report and Financial Statements of NBS for the Year Ended 31 December 2007





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Independent Auditors' Report

To the Bank Board of Národná banka Slovenska:

We have audited the accompanying financial statements of Národná banka Slovenska ('the NBS'), which comprise the balance sheet as at 31 December 2007, the income statement and notes.

NBS Bank Board's Responsibility for the Financial Statements

The Bank Board of the NBS is responsible for the preparation and fair presentation of these financial statements in accordance with the Slovak Act on Accounting and with the European Central Bank accounting rules ('the ECB rules'). This responsibility includes: designing, implementing and maintaining internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

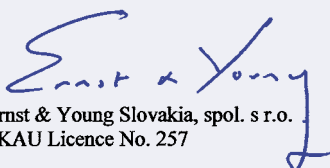
An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate for the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Bank Board of the NBS, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.


Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Národná banka Slovenska as of 31 December 2007, and its financial performance for the year then ended in accordance with the Slovak Act on Accounting and the ECB rules.

18 March 2008
 Bratislava, Slovak Republic



Ernst & Young Slovakia, spol. s r.o.
 SKAU Licence No. 257



Ing. Dalimil Draganovský
 SKAU Licence No. 893



NÁRODNÁ BANKA SLOVENSKA
Financial statements as at 31 December 2007 – Balance sheet
(in millions of SKK)

The Ministry of Finance of the Slovak Republic
Decree No. MF/8338/2005-74

BALANCE SHEET
of Národná banka Slovenska
in millions of SKK

Assets		Notes	As at	As at
			31.12.2007	31.12.2006
1.	Gold	1	21,538	18,788
2.	Debt securities denominated in foreign currency	2	387,289	312,364
3.	Derivatives	3	318	226
4.	Receivables from banks and central banks	4	33,844	25,154
4.1	Current accounts, deposits and loans denominated in foreign currency		31,102	21,872
4.2	Loans related to monetary policy operations in SKK			
4.3	Receivables not related to monetary policy operations in SKK		2,742	3,282
5.	Receivables from the International Monetary Fund	5	13,454	15,870
6.	Receivables from clients	6	316	245
7.	Equity shares in subsidiary and affiliated accounting units and other shares and participating interests	7	413	437
8.	Non-current assets	8	5,712	6,053
8.1	depreciable		5,318	5,711
8.2	non-depreciable		394	342
9.	Other assets	9	242	260
TOTAL ASSETS			463,126	379,397



NÁRODNÁ BANKA SLOVENSKA
Financial statements as at 31 December 2007 – Balance sheet
(in millions of SKK)

Liabilities

	Notes	As at 31.12.2007	As at 31.12.2006
1. Currency in circulation	10	155,154	143,518
2. Liabilities to banks and central banks	11	332,547	272,238
2.1. Current accounts denominated in SKK		2,536	2,560
2.2. Overnight deposits, loans and deposits denominated in SKK and minimum reserves		325,590	261,603
2.3. Current accounts, deposits and loans denominated in foreign currency		4,421	8,075
3. Liabilities from debt securities	12	67,712	37,435
3.1. Denominated in SKK		67,712	37,435
3.2. Denominated in foreign currency			
4. Derivatives	3	2,442	1,382
5. Liabilities to the International Monetary Fund	5	13,311	15,833
6. Liabilities to other international financial institutions	13	772	2,462
7. Liabilities to clients	14	1,163	863
8. Provisions and other liabilities	15	276	305
9. Statutory fund	16	483	483
10. Funds from profit appropriations and capital funds	16	10,312	10,312
11. Valuation differences from revaluation of	16	20,783	16,931
11.1. Gold		19,208	16,456
11.2. Derivatives		190	418
11.3. Securities		1,385	57
11.4. Foreign currencies			
12. Retained profit / (outstanding loss) from previous years	16	(122,365)	(77,237)
13. Profit / (loss) for the current accounting period	16	(19,464)	(45,128)

Translation of the financial statements originally issued in the Slovak language.

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NÁRODNÁ BANKA SLOVENSKA
Financial statements as at 31 December 2007 – Income statement
(in millions of SKK)

The Ministry of Finance of the Slovak Republic
Decree No. MF/8338/2005-74

INCOME STATEMENT

of Národná banka Slovenska

in millions of SKK

	Notes	As at 31.12.2007	As at 31.12.2006
1. Interest income and similar revenues		16,943	14,450
1.1. on SKK - denominated loans related to monetary policy operations		24	144
1.2. on SKK - denominated receivables not related to monetary policy operations		92	93
1.3. on receivables and securities denominated in foreign currency		16,827	14,213
a. Interest expense and similar expenses		(15,947)	(14,186)
a.1. on SKK - denominated liabilities related to monetary policy operations and from securities		(15,585)	(13,797)
a.2. on SKK - denominated liabilities not related to monetary policy operations		(65)	(49)
a.3. on liabilities and securities denominated in foreign currency		(297)	(340)
I. Net interest income	17	996	264
2. Revenues from fees and commissions		237	169
b. Expenses on fees and commissions		(16)	(23)
II. Net profit / (loss) from fees and commissions	18	221	146
3./c. Net profit / (loss) from operations in, and derivatives involving, securities denominated in foreign currency	19	(296)	(3,984)
4./d. Net profit / (loss) from operations in, and derivatives involving, foreign exchange and gold	20	(18,529)	(39,862)
5. Revenues from dividends and other profit distributions		28	31
6. Revenues from currency in circulation		5	208
e. Expenses on currency in circulation		(129)	(156)
III. Net profit / (loss) from currency in circulation		(124)	52
7. Revenues from dissolution of provisions and written-off receivables and securities			
f. Expenses on provisioning and the write-off of receivables and securities			
8. Other operating revenues		125	118
g. Other operating expenses	21	(1,885)	(1,893)
g.1. Staff expenses		(867)	(899)
g.2. Depreciation of tangible & intangible assets		(481)	(519)
g.3. Other operating costs		(537)	(475)
A. Profit / (loss) before appropriations		(19,464)	(45,128)
h. Profit appropriations			
B. Profit / (loss) after appropriations		(19,464)	(45,128)

NÁRODNÁ BANKA SLOVENSKA
Financial statements as at 31 December 2007 – Statement of changes in equity
(in millions of SKK)

The Ministry of Finance of the Slovak Republic
Decree No. MF/8338/2005-74

STATEMENT OF CHANGES IN EQUITY
of Národná banka Slovenska
in millions of SKK

	Statutory fund	Capital fund	Reserve fund	Revaluation funds	Outstanding loss	Equity
1. Balance as at 31 December 2006	483	43	10,269	16,931	(122,365)	(94,639)
2. Settlement of loss from previous accounting periods						
3. Appropriation to statutory fund						
4. Appropriation to outstanding loss						
5. Appropriation to reserve funds						
6. Revaluation of securities				1,328		1,328
7. Revaluation of derivatives				(227)		(227)
8. Change in gold revaluation fund				2,751		2,751
9. Revaluation of foreign currencies						
10. (Loss) / profit for the current accounting period					(19,464)	(19,464)
11. Profit appropriations						
12. Appropriation to social fund						
13. Change over the accounting period				3,852	(19,464)	(15,612)
14. Balance as at 31 December 2007	483	43	10,269	20,783	(141,829)	(110,251)

Translation of the financial statements originally issued in the Slovak language.

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NÁRODNÁ BANKA SLOVENSKA
Financial statements as at 31 December 2007 – Statement of changes in equity
(in millions of SKK)

The Ministry of Finance of the Slovak Republic
Decree No. MF/8338/2005-74

STATEMENT OF CHANGES IN EQUITY
of Národná banka Slovenska
in millions of SKK

	Statutory fund	Capital fund	Reserve fund	Revaluation funds	Outstanding loss	Equity
1. Balance as at 31 December 2005	467	43	10,165	16,260	(77,300)	(50,365)
2. Integration of ÚFT to NBS as at 1 January 2006	16		104		63	183
3. Adjusted balance as at 1 January 2006	483	43	10,269	16,260	(77,237)	(50,182)
4. Settlement of loss from previous accounting periods						
5. Appropriation to statutory fund						
6. Appropriation to outstanding loss						
7. Appropriation to reserve funds						
8. Revaluation of securities				57		57
9. Revaluation of derivatives				418		418
10. Change in gold revaluation fund				196		196
11. Revaluation of foreign currencies						
12. (Loss) / profit for the current accounting period					(45,128)	(45,128)
13. Profit appropriations						
14. Appropriation to social fund						
15. Change over the accounting period				671	(45,128)	(44,457)
16. Balance as at 31 December 2006	483	43	10,269	16,931	(122,365)	(94,639)



NÁRODNÁ BANKA SLOVENSKA
The notes to the financial statements as at 31 December 2007
(in SKK millions)

NOTES

to the financial statements for the year ended 31 December 2007

Bratislava, 18 March 2008

These Notes are an integral part of the financial statements of Národná banka Slovenska.
Translation of the financial statements originally issued in the Slovak language.

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NÁRODNÁ BANKA SLOVENSKA
Notes to the financial statements as at 31 December 2007
(in SKK millions)

A. General information on Národná banka Slovenska

Národná banka Slovenska (The National Bank of Slovakia – ‘the NBS’ or ‘the Bank’) is the independent central bank of the Slovak Republic. The NBS was established in accordance with Act N° 566/1992 Coll. on the National Bank of Slovakia as amended (‘the NBS Act’). It commenced its activities on 1 January 1993 as the bank of issue of the Slovak Republic. The NBS is a legal entity (Corporate ID: 30 844 789) seated at Imricha Karvaša 1, Bratislava. In respect of its own assets, the NBS acts as a business entity. The NBS has its head office in Bratislava, nine branches in the Slovak Republic and special-purpose organizational units.

The Bank’s primary objective is to maintain price stability. Therefore, the NBS:

- determines the monetary policy;
- issues banknotes and coins;
- manages, co-ordinates and ensures money circulation, payment transactions, the clearing of payment transaction data and ensures their fluency and efficiency;
- effects the activities, tasks, rights and obligations resulting from the participation of Národná banka Slovenska in the European System of Central Banks;
- contributes to the stability of the financial system as a whole and to the safe and sound functioning of the financial market in the interest of maintaining credibility of the financial market, protection of clients and respecting of the rules of economic competition; the Bank also supervises the financial market and other financial market activities;
- represents the Slovak Republic in international financial institutions and ensures the fulfillment of tasks resulting from such representations; and
- represents the Slovak Republic in international financial market operations related to the implementation of the monetary policy.

The NBS’s supreme executive body is the NBS Bank Board (‘the Bank Board’). The Bank Board has eleven members: the Governor, two Deputy Governors, and eight other members, three of whom may be persons not employed by the NBS. Membership in the Bank Board is limited to a maximum of two consecutive terms of office. The NBS is represented by the Governor.

In 2007, the Bank Board consisted of the following members:

	Term of office in the Bank Board		Current position	Date of appointment
	from	to		
Ing. Ivan Šramko	11 Jan. 2002	1 Jan. 2010	Governor	1 Jan. 2005
Ing. Martin Barto, CSc.	1 Dec. 2004	31 Jan. 2010	Deputy Governor	31 Jan. 2005
Ing. Viliam Ostrožlík, MBA	1 Mar. 2007	11 July 2012	Deputy Governor	11 July 2007
Ing. Peter Ševčovic	1 Oct. 2004	1 Oct. 2009	Member	1 Oct. 2004
Ing. Milena Koreňová	1 Jan. 2005	1 Jan. 2010	Member	1 Jan. 2005
Doc. Ing. Jozef Makúch, PhD.	1 Jan. 2006	1 Jan. 2011	Member	1 Jan. 2006
Mgr. Ľudovít Ódor	1 Jan. 2006	1 Jan. 2011	Member	1 Jan. 2006
Ing. Slavomír Šťastný, PhD., MBA	1 Jan. 2006	1 Jan. 2011	Member	1 Jan. 2006
RNDr. Karol Mrva	10 Jan. 2007	10 Jan. 2012	Member	10 Jan. 2007
Ing. Gabriela Sedláková	1 June 2007	1 June 2012	Member	1 June 2007

In accordance with the NBS Act, the Bank Board determines the monetary policy, the instruments for its implementation and decides on NBS’s monetary policy operations. The Bank ensures the implementation of the monetary policy mainly by using the following

NÁRODNÁ BANKA SLOVENSKA
Notes to the financial statements as at 31 December 2007
(in SKK millions)

instruments – base interest rate, open market operations (repo tenders, issues of treasury bills, direct purchase or direct sale of state securities and NBS treasury bills, foreign exchange operations), overnight refinancing and overnight money withdrawing operations, minimum reserves requirements, exchange rate regime after the entry of the Slovak Republic into the Exchange Rate Mechanism ERM II from 28 November 2005.

The Bank ensures the administration of foreign exchange reserves especially by means of financial operations related to securities denominated in foreign currencies, acceptance of loans from foreign entities, purchase of foreign currency from banks and branches of foreign banks, and financial transactions with foreign currencies and gold with the purpose of their appreciation.

All the costs necessary for the Bank's activities are covered from its revenues. According to Article 38 of the NBS Act, over the accounting period the Bank generates either a profit or a loss. Profit generated by the Bank is allocated to the reserve fund and to other profit reserves, or used to settle losses from previous years. The remaining profit is transferred to the State budget or, based on the Slovak Government's decision, to state financial assets under a separate regulation. The NBS may settle the loss for the current period from the reserve fund or from other reserves; alternatively, the Bank Board may decide to transfer the outstanding loss to the next accounting period (refer to Note 16).

The Bank submits an annual report on its financial results to the National Council of the Slovak Republic, within three months of the end of the calendar year; in addition to the NBS financial statements data and the auditor's opinion on these financial statements, the report specifically states information about the NBS operating costs. Should the National Council of the Slovak Republic request so, the NBS is obliged to amend the report within six weeks to bring it into compliance with the request or, as appropriate, provide explanations to the data stated in the report.

B. Accounting principles and accounting methods applied

(a) Basic principles of preparation of the financial statements

The NBS financial statements have been prepared in accordance with Act N° 431/2002 Coll. on Accounting as amended ('Accounting Act'). Pursuant to Section 17b of the above Act, the NBS maintains its accounting in accordance with the Guideline of the European Central Bank of 10 November 2006 on the legal framework for accounting and financial reporting in the European System of Central Banks N° ECB/2006/16 ('ECB Guideline').

When accounting for transactions not regulated by the ECB Guideline, the Bank proceeds in line with the International Financial Reporting Standards ('IFRS') issued by the International Accounting Standards Board ('IASB') and in line with the interpretations issued by the International Financial Reporting Interpretations Committee ('IFRIC') as adopted by the European Commission pursuant to the Directive of the European Parliament and the Council of the European Union. Other cases are subject to the Accounting Act.

When disclosing items of its financial statements, the Bank proceeds in line with the Decree of the Ministry of Finance of the Slovak Republic N° MF/8338/2005-74 of 14



December 2005 setting out details on the arrangement, description of items in individual financial statements, contents of these items, and the extent of data from financial statements designated for publishing for the National Bank of Slovakia ('Decree of MF SR').

(b) Changes in accounting methods and reporting

In accordance with Guideline ECB/2006/16 effective from 1 January 2007, the Bank applied new procedures for accounting of options and interest rate futures.

Based on the new rules, option premiums and changes in the fair value of options, recognized in SKK in 2006, are accounted for in foreign currency with the effect from 1 January 2007. The unrealized foreign exchange difference (SKK 97 million) resulting from the change in the accounting method is recognized as revaluation differences in the equity.

Starting from 1 January 2007, any changes in the fair values of interest rate futures are accounted for on a daily basis as realized foreign exchange gains and losses in the income statement. In 2006, the changes in fair values of futures were posted in the equity, and it was only the losses which entered the income statement at the end of the accounting period. As at 31 December 2006, gains from revaluation (SKK 12 million) were posted as revaluation differences in the equity.

In addition to the changes in accounting for interest rate futures with effect from 1 January 2007, the Bank also changed the method of reporting gains and losses from these financial instruments. To maintain year-on-year comparatives, the following 2006 item data were accordingly adjusted in the income statement (SKK 30 million): 'Net profit/(loss) from operations in, and derivatives involving, foreign exchange and gold', 'Interest income and similar revenues on receivables and securities denominated in foreign currency' and 'Interest expense and similar expenses on liabilities and securities denominated in foreign currency'. The Bank also changed the method of reporting 'Staff expenses' in 'Other operating expenses' (SKK 8 million).

(c) Recognition rules

The Bank records an accounting entry on the day the respective accounting event occurred, i.e. on the day when cash was paid or received; in the case of a direct debit, on the payment day; in the case of securities and gold, on the settlement date; in the case of derivatives and spot transactions, on the trade date; in the case of cash in foreign currency, on the day it was credited according to the deal message received; in the case of property relations, on the day when the property title was acquired or terminated; and in the case of a shortage, deficit or surplus, on the day the difference was identified.

(d) Methods of foreign currency valuation and settlement of valuation differences

During the year, assets (including gold and derivatives) and liabilities denominated in foreign currencies are valued using the average currency exchange rate. Differences between the exchange rate announced by the NBS and the average currency exchange rate represent unrealized foreign currency gains or losses. As at the financial statements date, unrealized foreign exchange gains exceeding unrealized foreign exchange losses are

NÁRODNÁ BANKA SLOVENSKA
Notes to the financial statements as at 31 December 2007
(in SKK millions)

recognized in the Bank's equity on revaluation accounts. Unrealized foreign exchange losses are recognized in the income statement. Foreign exchange losses of one currency cannot be offset by foreign exchange gains of other currencies or gold.

Realized foreign exchange gains and losses from the sale of assets and settlement of liabilities are recognized in the income statement.

The exchange rates of principal foreign currencies used for the valuation of assets and liabilities as at 31 December 2007 were as follows:

Currency	Amount	31 December 2007	31 December 2006
EUR	1	33.603	34.573
USD	1	22.870	26.246
JPY	100	20.218	22.081
XDR	1	36.068	39.484

(e) Gold

Gold is stated at the market price of London's commodity market morning fix of gold in USD/oz. (troy ounce) as at the financial statements date. Gains from gold revaluation to fair value are included in equity, while losses from gold revaluation to fair value have impact on the Bank's financial results. The sale of gold is reflected in the income statement.

Swap transactions with gold are recorded as repurchase transactions with gold, i.e. gold used in these transactions as collateral is part of the balance sheet amount under the caption 'Gold'.

(f) Debt securities

Debt securities are initially recognised at acquisition cost. As of the day after the purchase up to and including the security's sale or maturity date the Bank amortises the premium or the discount on a daily basis (the difference between the security's acquisition cost and nominal value). The amortization of the premium/discount is recognized under Interest income and similar revenues in the income statement.

In the financial statements, the Bank recognizes debt securities at fair value. The difference between the security's fair value and the average acquisition cost adjusted for the amortized discount or premium represents a valuation difference. Valuation differences constituting gains are recognized in the Bank's equity. Valuation differences constituting losses are included in the Bank's income statement.

The fair value of debt securities, for which there is an active market and whose market value can be reliably measured, is determined on the basis of the market value on such a market. If the market value is not available, fair value is determined as the sum of future cash flows discounted using market interest rates of the relevant currency, maturity rates and the risk rating of the security's issuer.



Upon the sale of a security, the difference between the average acquisition cost adjusted for the amortized discount or premium and the sales price represents a realized gain or loss that has an effect on the Bank's income statement.

(g) Derivatives

The derivative financial instruments include options and interest rate futures. Options entered into with respect to swap transactions with gold are recorded as derivatives embedded to other financial instruments. Embedded derivatives are treated as separate derivatives from the host financial instrument provided that they are not closely related to the economic characteristics and risks of the host financial instrument.

As at the trade date, derivatives are posted in the off-balance sheet in the amount of the underlying instrument. Options are individually measured at fair value on the balance sheet, where gains from revaluation are reported as 'Equity' on the balance sheet and revaluation loss is recognized in the income statement. As at 31 December 2007, options are stated at fair value based on market prices, discounted cash flows and Merton option pricing formula. Futures contracts are valued to fair value on a daily basis and the revaluation difference is recognized in the income statement.

All interest rate futures and option contracts are recorded separately. Offsetting of gains or losses from different contracts is not permitted.

Major risks influencing derivatives include the price volatility of gold and changes in interest rates and foreign currency rates.

(h) Receivables

Receivables are recognized on the balance sheet in their nominal value increased by accumulated interest ("amortized cost"). Receivables are decreased by impairment losses. Creation and release of impairment losses has an impact on the income statement.

Following the prudence principle, the Bank evaluates the risk rate of receivables, categorizes them and creates impairment losses for them.

Bad debts are written off to costs based on a court decision and upon the Bank Board's decision and the release of the related impairment losses is credited to costs.

(i) Repurchase and reverse repurchase transactions

Transactions, in which the Bank accepted securities in exchange for cash, along with the commitment to return these securities at a certain date in exchange for the transferred cash amount plus interest (reverse repurchase transaction), are recorded as loans provided. The collateral accepted in a reverse repurchase transaction is recognized in market value on off-balance sheet accounts.

Transactions in which the Bank provided securities or gold in exchange for cash, along with the commitment to accept back these securities or gold at a certain date in

NÁRODNÁ BANKA SLOVENSKA
Notes to the financial statements as at 31 December 2007
(in SKK millions)

exchange for the original cash amount plus interest (repurchase transaction), are recorded as received loans with a transfer of collateral. The collateral provided in a repurchase transaction remains in the balance sheet and in the financial statements it is fair valued.

Tri-Party reverse repurchase transactions are transactions with a third party entering the relationship between the NBS and a partner bank. The partner bank is an entity with whom the NBS performs financial transactions relating to the administration of foreign exchange assets.

In addition to repurchase and reverse repurchase transactions performed directly by the Bank, the Bank issued a mandate to perform transactions with securities held by the NBS to selected banks based on contracts for provision of services, the so-called 'Securities Lending'. Reverse repurchase transactions including lending of securities carried out under the program of lending and receiving of securities, are recognized on off-balance sheet accounts. For these transactions, the NBS receives a portion of the income, which is recognized in the income statement.

The Bank's market and credit risks in these transactions are minimised through the specification of products in which the cash received can be invested, as well as the counterparties with whom deals may be performed.

(j) Receivables from and liabilities to the International Monetary Fund

Receivables from and liabilities to the International Monetary Fund ('IMF') as at 31 December 2007 are stated using the gross method, i.e. receivables and liabilities are not offset.

(k) Equity shares in subsidiary and affiliated accounting units and other shares and participating interests

The Bank has an ownership interest with a majority control over RVS, a.s. Bratislava. The equity shares of RVS, a.s. Bratislava are stated at cost.

The Bank has an equity stake in the Bank for International Settlements, Basel, Switzerland ('BIS'). Shares in BIS are stated at cost. The equity interest in BIS is disclosed in the amount of the paid-up share (25%). The unpaid part (75%) is due upon request. Dividends are paid out in EUR from the NBS total share in BIS maintained in XDR.

As part of other participating interests, the Bank accounts for a contribution in the European Central Bank ('ECB'). On 1 May 2004, the NBS became a member of the European System of Central Banks ('ESCB'). In accordance with the Statute of the ESCB and ECB, the NBS has paid the initial minimum contribution to the ECB's capital. The amount of the total capital share of individual national central banks depends on the capital key determined on the basis of the following statistical categories: GDP and population. In accordance with the Protocol on the Statute of the ESCB and the ECB, the capital key is adjusted every five years or when new members enter the ESCB. Last time, the capital key was adjusted as at 1 January 2007 (refer to Note 7).



NÁRODNÁ BANKA SLOVENSKA
Notes to the financial statements as at 31 December 2007
(in SKK millions)

(l) Non-current assets

Non-current assets include tangible assets, the acquisition cost of which is higher than SKK 30,000 and whose term of operational and technical capabilities exceeds one year, and intangible assets, the acquisition cost of which is higher than SKK 50,000 and whose term of operational and technical capabilities exceeds one year. On the balance sheet, they are stated at acquisition cost, including the costs related to their acquisition. The carrying value of depreciated non-current assets is shown net of accumulated depreciation. Land, works of art, collections and tangible and intangible fixed assets in progress are not subject to depreciation.

The NBS's tangible and intangible fixed assets were classified into individual depreciation groups as follows:

Depreciation group	Depreciation period in years
1. Buildings and halls	30
	8 - 30 ¹⁾
2. Engineering structures	8 - 30
3. Machines and equipment	4 - 20
4. Transportation means	4 - 6
5. Fixtures and fittings	4 - 20
6. Software	3 - 5
7. Other non-current intangible assets	4
8. Technical improvement of intangible cultural landmarks	30

¹⁾ components of assets

(m) Non-current assets held for sale

Non-current assets held for sale comprise buildings and land, which are classified for sale in their present condition and their sale is considered to be highly probable.

Assets classified as non-current assets held for sale are included in 'Other assets' at the lower of acquisition cost less accumulated depreciation and impairment losses and fair value less costs to sell.

(n) Currency in circulation

NBS administers the issue of bank notes and coins and their withdrawal from circulation. Currency in circulation represents the Bank's liability arising from issued bank notes and coins. The liability is decreased by the bank notes and coins in the NBS's cash desk. The liability due to currency in circulation is stated at the nominal value.

(o) Liabilities arising from debt securities

The Bank issues short-term securities falling due within one year (NBS bills). The issues are made in order to create a sufficient stock of securities for the performance of

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money withdrawing repurchase transactions. Money withdrawing repurchase transactions relate to the implementation of monetary policy in open market operations.

From the settlement date of the issue to the due date, the value of issued and sold NBS bills is gradually increased by the accrued interest (the so-called amortized cost). On the balance sheet, issued NBS bills are shown netted off by any bills repurchased to the NBS portfolio, including the accrued interest.

(p) Provisions

The Bank recognizes provisions if it has a present obligation as a result of a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

(q) Interest income and interest expense

Interest income and interest expense are recognized in the income statement based on the accrued amount using the straight-line method. The effective interest method ('IRR') is applied to interest income which is accrued from discounted securities with the residual maturity exceeding 1 year at the time of their acquisition.

The interest includes amortized discounts or premiums from purchased and issued securities.

(r) Cost of employee benefits

The NBS pays regular contributions on behalf of its employees to health insurance agencies for health insurance and to the Social Insurance Agency for sickness, retirement, accident, guarantee, and unemployment insurance, and a contribution to the Guarantee Fund. Contributions are paid in the amounts required by law in the respective year. The Bank also pays a contribution for not employing the obligatory percentage of persons with disability, as set out in the Employment Act.

In co-operation with agencies offering supplementary retirement insurance, the NBS has created an additional pension scheme for its employees.

(s) Taxation

The NBS is liable to corporate income tax arising from the application of withholding tax in accordance with Section 12 of Act N° 595/2003 Coll. on Income Taxes as amended ('Income Taxes Act').

The NBS is registered as a VAT payer.



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C. Related party transactions

According to the Decree of MF SR, parties related to Národná banka Slovenska are mainly the members of the Bank Board. In 2007, their remuneration and other employee benefits amounted to SKK 36 million (SKK 31 million for 2006).

The Bank recognizes receivables from the Bank Board members for loans provided in the total amount of SKK 11 million as at 31 December 2007 (SKK 9 million as at 31 December 2006).

D. Notes to balance sheet items and income statement items

1. Gold

The gold consists of the following items:

	2007	2006
Bullion in standard form	21,510	18,760
Gold in other form	28	28
	<u>21,538</u>	<u>18,788</u>

As at 31 December 2007, 'Gold' comprised a total of 1,126 thousand ounces of gold (1,126 thousand ounces of gold as at 31 December 2006), of which 724 thousand ounces were deposited in correspondent banks, 400 thousand ounces were used in repurchase transactions, and 2 thousand ounces were held by the Bank.

The market value of gold as at 31 December 2007 was USD 836.50 /oz. (USD 635.70 /oz. as at 31 December 2006). Despite the strengthening of the SKK/USD exchange rate (refer to Note E), the growth in the market price of gold positively affected the amount reported under 'Gold' at fair value and under 'Valuation differences from revaluation of gold'. As at 31 December 2007, the balance on Gold revaluation funds was SKK 19,208 million (SKK 16,456 million as at 31 December 2006).

In January and March 2007, two long-term repurchase transactions totalling 400 thousand ounces of gold were closed (refer to Note 11).

The value of gold provided as collateral in gold repurchase transactions as at 31 December 2007 (refer to Note 11) amounted to SKK 7,656 million (SKK 13,354 million as at 31 December 2006).

From the beginning of the year through to 31 December 2007, the Bank sold 251 ounces of gold in the form of golden coins.

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2. Debt securities

As at 31 December 2007, the Bank's portfolio of securities comprised the following items (at fair value):

	2007	2006
State zero-coupon bonds	123,098	66,863
State coupon bonds	76,689	76,650
Coupons	1,650	1,681
Securities of state bodies - total	201,437	145,194
Other zero-coupon bonds	20,074	21,398
Other coupon bonds	162,822	143,230
Coupons	2,956	2,542
Securities of other entities - total	185,852	167,170
Total securities	387,289	312,364

According to the issuer of securities the sector breakdown of the Bank's portfolio of securities is as follows:

	2007	2006
Public sector	201,437	195,543
Financial institutions	159,905	84,867
Financial auxiliaries	23,775	31,954
Non-financial institutions	2,172	
Total securities	387,289	312,364

According to the issuer of securities, as at 31 December 2007 the Bank registered securities from EMU countries in the amount of SKK 300,473 million (SKK 197,160 million as at 31 December 2006) and securities from other countries, including international institutions, in the amount of SKK 86,816 million (SKK 115,204 million as at 31 December 2006). The Bank trades with securities on foreign financial markets, mainly in New York, London, Basel, and in the Euro zone countries. These trades mostly involve transactions outside the stock exchanges.

3. Derivatives

The fair value of derivatives is as follows:

	2007		2006	
	Assets	Liabilities	Assets	Liabilities
Put options purchased	271		217	
Call options sold		2,442		1,382
Interest rate futures	47		9	
	<u>318</u>	<u>2,442</u>	<u>226</u>	<u>1,382</u>

The Bank concluded four long-term repurchase transactions in gold ('gold repos') in 2005 and 2006. To eliminate the risk of a decrease in the market value of gold, the Bank purchased four European put options and sold four European call options for the same amount of gold. Option premiums for the purchased and sold options were not paid, but were

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incorporated in the rate of interest (lower than the market rate) for the long-term loan accepted by the Bank. The options are embedded derivatives which meet the criteria of separating the derivative from the host financial instrument. Therefore, the options were separated from the accepted loan and are recorded separately.

The difference between the market value of purchased put options and sold call options in closing the transaction had an effect on the amount of the accepted loan. Using the IRR method, it is accrued into expenses on a daily basis.

As at 31 December 2007, the Bank recorded futures contracts entered into with respect to debt securities. Initial margins are provided as deposits. All contracts are measured at fair value on a daily basis and changes in the fair value are recognized in the income statement as 'Net profit/ (loss) from operations in, and derivatives involving, foreign exchange and gold'.

4. Receivables from banks and central banks

Current accounts, deposits and loans in foreign currency

	2007	2006
Loans granted in repurchase transactions in foreign currency	25,646	16,252
Deposits	4,326	4,910
Receivables from banks in the European System of Central Banks	387	384
Loans granted to commercial banks for the support of business in foreign currency	13	33
Other	730	293
	31,102	21,872

Loans provided in repurchase transactions with foreign entities total SKK 25,646 million (SKK 16,252 million as at 31 December 2006); all loans were granted in EUR. The value of securities accepted as collateral in a Tri-party Reverse Repo transaction as at 31 December 2007 was SKK 25,636 million (SKK 16,249 million as at 31 December 2006). The collateral accepted was composed of long-term securities denominated in EUR.

At 31 December 2007, the Bank had receivables from repurchase transactions based on Securities Lending Agreements, recognized only on off-balance sheet accounts (refer to Note i). The value of securities accepted as collateral under the Securities Lending Agreements as at 31 December 2007 totalled SKK 217,314 million (SKK 141,931 million as at 31 December 2006), of which SKK 198,952 million in EUR (SKK 107,126 million as at 31 December 2006) and SKK 18,362 million denominated in USD (SKK 34,805 million as at 31 December 2006).

The item 'Other' covers mainly the Bank's current accounts abroad, in countries outside the European System of Central Banks.

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Receivables in SKK not related to monetary policy operations

	2007	2006
Loans granted to domestic banks for the support of business activities by JBIC (Japan Bank for International Cooperation) and EIB in SKK	230	378
Redistribution loans	2,491	2,882
Other	21	22
	2,742	3,282

The aim of loans accepted from foreign banks (JBIC and EIB) is to support small and medium-sized enterprises and specific industries of the Slovak economy.

The redistribution loan was provided for a complex construction of apartment buildings. By virtue of decisions of the NBS Bank Board, the redistribution loan interest rate was adjusted in the course of 2007 to 2.75% (3.25% as at 31 December 2006). As at 31 December 2007, the NBS recorded a state guarantee accepted for the redistribution loan provided in the amount of SKK 3,193 million (SKK 3,821 million as at 31 December 2006). The state guarantee is provided for the amount of principal, plus interest to maturity of the loan.

5. Receivables from and liabilities to the International Monetary Fund

	2007		2006	
	XDR equivalent	SKK	XDR equivalent	SKK
Membership quota in the IMF	357	13,419	357	15,833
XDR holdings	1	35	1	37
Investments and receivables in foreign currency	358	13,454	358	15,870
Account No. 1, 2	15	555	15	668
Securities	340	12,756	343	15,165
Liabilities to non-residents in domestic currency	355	13,311	358	15,833

The membership quota of the Slovak Republic in the IMF is denominated in special drawing rights (XDR). It is converted to SKK using the representative XDR exchange rate set by the IMF. The Bank thus records a receivable of XDR 358 million which as at 31 December 2007 translated into SKK 13,454 million (SKK 15,870 million as at 31 December 2006). Part of the membership quota is a receivable from the granted loan which based on the IMF call was provided by the Slovak Republic in the amount of XDR 3 million, i.e. SKK 114 million.

The Bank records a liability of the Government of the Slovak Republic to the IMF of SKK 13,311 million (SKK 15,833 million as at 31 December 2006), representing mainly a non-transferable and non-interest-bearing promissory note payable on demand in the amount of SKK 12,756 million (15,165 million as at 31 December 2006).

**6. Receivables from clients**

As at 31 December 2007, the NBS recorded receivables from clients of SKK 316 million (SKK 245 million as at 31 December 2006). The major part of the receivables from clients consists of consumer and investment loans provided to employees totalling SKK 302 million (SKK 231 million as at 31 December 2006) and debit balances on current accounts of employees totalling SKK 9 million (SKK 8 million as at 31 December 2006).

7. Equity shares in subsidiary and affiliated accounting units and other shares and participating interests**Equity shares in subsidiary accounting units**

The Bank holds shares in RVS, a.s. Bratislava, a company active in the area of relaxation and educational activities. As at 31 December 2007, similarly to 31 December 2006, the Bank held 1,080 certified shares in the amount of SKK 108 million, which represented a 51.58% share in the company's share capital.

Even though the Bank is the majority shareholder in RVS, a.s. Bratislava, the NBS does not prepare consolidated financial statements according to Section 22 of the Accounting Act.

Other participating interests

The Bank holds ownership interests in BIS. As at 31 December 2007, the Bank held 2,858 shares of BIS valued at SKK 599 million (SKK 656 million as at 31 December 2006), which represented a 0.52% share in the BIS share capital. The share in BIS is disclosed on the balance sheet in the amount of the 25% paid-up share, i.e. at SKK 213 million (SKK 233 million as at 31 December 2006). The liability from the unpaid share at 75% of the nominal value of each share amounts to SKK 386 million (SKK 423 million as at 31 December 2006). The unpaid part of the share is due upon request. In July 2007, the NBS received dividends from BIS shares in the amount of SKK 28 million.

As at 31 December 2007, the amount of paid-up initial contribution of the Bank to ECB's subscribed capital was SKK 92 million (SKK 96 million as at 31 December 2006), which represents 7% of the NBS total share in the ECB subscribed capital.

As a result of the entry of new members into the European Monetary Union, as at 1 January 2007, the Slovak Republic was prescribed a new percentage share in the ECB's subscribed capital amounting to 0.6765%, which totalled EUR 39 million. Compared to the initially specified share of 1 May 2004 (0.7147%), the new share represents a drop of 0.0382 percentage point, which is less by EUR 56 thousand in financial terms. This amount was transferred to the NBS account in January 2007.

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8. Non-current assets

Movements in non-current tangible and intangible assets in 2007 were as follows:

	Land	Other non-depreciable tangible assets	Buildings and constructions	Technological equipment and machines	Other depreciable tangible assets	Software and other intangible assets	Advances on tangible and intangible assets	Total
Acquisition cost as at 31 December 2006	232	56	6,450	1,457	251	516	92	9,054
Additions			7	26	1	61	147	242
Disposals				109	3	8	95	215
Acquisition cost as at 31 December 2007	232	56	6,457	1,374	249	569	144	9,081
Acc. depreciation as at 31 December 2006			1,384	1,183	202	194	38	3,001
Additions			230	142	23	93		488
Disposals				109	3	8		120
Acc. depreciation and provisions as at 31 December 2007			1,614	1,216	222	279	38	3,369
Book value of tangible and intangible assets as at 31 December 2006	232	56	5,066	274	49	322	54	6,053
Book value of tangible and intangible assets as at 31 December 2007	232	56	4,843	158	27	290	106	5,712

As at 31 December 2007, the Bank recognized a provision for advances paid in the amount of SKK 38 million (SKK 38 million as at 31 December 2006).

9. Other assets

	2007	2006
Assets held for sale	156	158
Receivables from supplier-consumer relations	46	45
Cash in foreign currency	15	23
Other	25	34
	242	260

As at 31 December 2007, the Bank posted provisions for receivables from fines of financial market entities in the amount of SKK 20 million (SKK 20 million as at 31 December 2006), provisions for receivables from contributions of financial market entities in the amount of SKK 2 million (SKK 2 million as at 31 December 2006) and provisions for operating receivables of SKK 15 million (SKK 47 million as at 31 December 2006).

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As at 31 December 2007, the Bank recorded inventories of SKK 7 million (SKK 10 million as at 31 December 2006). Inventories are stated at cost, i.e. inclusive of costs related to their acquisition.

10. Currency in circulation

The issue of banknotes and coins represents the valid national bank notes and coins in circulation:

	2007	2006
Issued coins	2,500	2,414
Issued bank notes	152,654	141,104
	<u>155,154</u>	<u>143,518</u>

11. Liabilities to banks and central banks

Current accounts in SKK

	2007	2006
Current accounts of banks for transfers and replenishments	2,521	2,544
LORO accounts of central banks	15	16
	<u>2,536</u>	<u>2,560</u>

As at 31 December 2007, the NBS had liabilities to banks and central banks in SKK worth SKK 2,536 million (SKK 2,560 million as at 31 December 2006), a major portion of which consisted of current accounts of banks used for transfers and replenishments.

Overnight deposits, deposits and loans in SKK and minimum reserves

	2007	2006
Loans received in repurchase transactions in SKK	260,834	225,898
Minimum reserves in the NBS	17,826	26,199
Overnight deposits from banks	45,034	8,738
Interbank settlement in SKK	1,896	768
	<u>325,590</u>	<u>261,603</u>

Within the money withdrawing repurchase transactions in the Slovak inter-bank market, the NBS had liabilities from repurchase transactions in the total amount of SKK 260,834 million as at 31 December 2007 (SKK 225,898 million as at 31 December 2006) - (refer to Note 12).

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Current accounts, deposits and loans in foreign currency

	Loan maturity in year	FC code	2007		2006	
			FC	SKK	FC	SKK
Gold repo	2007	USD			116	3,046
Gold repo	2015	USD	81	1,861	80	2,108
Gold repo	2016	USD	110	2,530	109	2,854
AGL II	2009	EUR	1	30	2	67
			<u>x</u>	<u>4,421</u>	<u>x</u>	<u>8,075</u>

As at 31 December 2007, the Bank had liabilities from gold repurchase transactions in the amount of SKK 4,391 million (SKK 8,008 million as at 31 December 2006). In January and March 2007, two long-term gold repurchase transactions were terminated (refer to Note 1).

12. Liabilities from debt securities

As at 31 December 2007, the NBS issued bills of SKK 1,067,712 million (SKK 537,435 million as at 31 December 2006) and repurchased bills in the amount of SKK 1,000,000 million (SKK 500,000 million as at 31 December 2006).

As at 31 December 2007, NBS bills of SKK 329,893 million were used for money withdrawing operations (SKK 264,095 million as at 31 December 2006), of which SKK 262,181 million (SKK 226,660 million as at 31 December 2006) were in the form of money withdrawing repurchase transactions and SKK 67,712 million (SKK 37,435 million as at 31 December 2006) remained in the portfolios of domestic banks.

13. Liabilities to other international financial institutions

	2007	2006
Current accounts - Euro Account European Commission	169	1,769
Loro accounts - World Bank, Bank for International Settlements	602	693
Deposits - PHARE	1	
	<u>772</u>	<u>2,462</u>

As at 31 December 2007, the NBS recorded liabilities to other international financial institutions in the amount of SKK 772 million (SKK 2,462 million as at 31 December 2006).



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14. Liabilities to clients

	2007	2006
Term deposits of employees	650	497
Current accounts of employees	289	207
Accounts of government	147	17
Term deposits of financial auxiliaries	48	18
Current accounts of financial auxiliaries	28	45
Other	1	79
	<u>1,163</u>	<u>863</u>

'Term deposits of financial auxiliaries' include term deposits of the Investment Guarantee Fund. Major portion of 'Current accounts of financial auxiliaries' is represented by current accounts of the Deposit Protection Fund. 'Other' mainly includes current accounts of other clients and liabilities from terminated bank accounts and term deposits.

15. Provisions and other liabilities

	2007	2006
Provisions	125	169
Liabilities to suppliers	61	70
Other	90	66
	<u>276</u>	<u>305</u>

As at 31 December 2007, the Bank recorded provisions for liabilities to employees of SKK 95 million (SKK 150 million as at 31 December 2006), provisions for uninvoiced supplies, lawsuits, audit of the financial statements and the annual report of SKK 30 million (SKK 19 million as at 31 December 2006).

'Other' includes settlements with employees, with entities entitled to the salaries settlement and other liabilities.

16. Equity

As at 31 December 2007, the NBS generated a loss of SKK 19,464 million (SKK 45,128 million as at 31 December 2006) and posted a negative equity of SKK 110,251 million (SKK 94,639 million as at 31 December 2006). Funds generated from the revaluation differences of securities, derivatives, gold and foreign currency represented SKK 20,783 million (SKK 16,931 million as at 31 December 2006).

The Bank Board decided that the losses of the NBS would be covered from the Bank's future income and own resources.

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Valuation differences

	2007	2006
Revaluation of gold	19,208	16,456
Revaluation of derivatives	190	418
Revaluation of securities	1,385	57
	20,783	16,931

17. Net interest income

	2007	2006
Interest received on loans related to monetary policy operations, in SKK	24	144
Interest received on receivables not related to monetary policy operations, in SKK	92	93
Interest received on receivables and securities in foreign currency	16,827	14,213
Interest income and similar revenues	16,943	14,450
Interest paid on liabilities related to monetary policy operations and securities, in SKK	(15,585)	(13,797)
Interest paid on liabilities not related to monetary policy operations, in SKK	(65)	(49)
Interest paid on liabilities and securities in foreign currency	(297)	(340)
Interest expense and similar expenses	(15,947)	(14,186)
Net interest income	996	264

18. Net profit from fees and commissions

As at 31 December 2007, fee income from transactions concluded based on contracts for provision of services in the area of securities, the so-called 'Securities Lending', amounted to SKK 174 million (SKK 107 million as at 31 December 2006).

	2007	2006
Revenues from fees and commissions	237	169
Expenses on fees and commissions	(16)	(23)
Net profit from fees and commissions	221	146

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19. Net loss from operations in, and derivatives involving, securities denominated in foreign currency

	2007	2006
Revenues from debt securities	228	148
Losses from debt securities and revaluations	(524)	(4,132)
Net loss from operations in, and derivatives involving, securities denominated in foreign currency	(296)	(3,984)

20. Net loss from operations in, and derivatives involving, foreign exchange and gold

	2007	2006
Revenues from operations in, and derivatives involving, FX and gold	5 497	11 535
Losses from operations in, and derivatives involving, FX and gold	(24 026)	(51 397)
Net loss from operations in, and derivatives involving, FX and gold	(18 529)	(39 862)

The total net loss from operations in, and derivatives involving, foreign exchange and gold was most significantly affected by decrease of the value of assets denominated in foreign currency of SKK 16,429 million (SKK 39,825 million as at 31 December 2006) as a result of a significant strengthening of SKK against EUR and USD.

21. Other operating expenses

	2007	2006
Salaries and bonuses	(566)	(558)
Social costs	(174)	(168)
Other personnel costs	(127)	(173)
Staff expenses	(867)	(899)
Depreciation of tangible and intangible assets	(481)	(519)
Other operating costs	(537)	(475)
Other operating expenses	(1,885)	(1,893)

As at 31 December 2007, the average number of staff employed was 1,081 (1,204 as at 31 December 2006), of whom 107 held managerial positions (136 as at 31 December 2006). As at 31 December 2007, the average number of staff in banking supervision over the capital market, insurance market, pension savings, banks and securities brokers was 177 (162 as at 31 December 2006).

As at 31 December 2007, costs of audit and advisory amounted to SKK 4 million (SKK 2 million as at 31 December 2006).

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E. Foreign exchange structure of assets and liabilities

Line No.	SKK	Foreign currencies converted to SKK - total		of which		Not defined	
				EUR	USD	Other	
1. Gold			21,538		21,538		
2. Debt securities denominated in foreign currency			387,289	313,075	74,214		
3. Derivatives			318	24	294		
4. Receivables from banks and central banks	2,742		31,102	26,715	4,351	36	
5. Receivables from the International Monetary Fund	13,424		30			30	
6. Receivables from clients	316						
7. Equity shares in subsidiary and affiliated accounting units and other shares and participating interests	108		305	92		213	
8. Non-current assets							5,712
9. Other assets	221	21	12	4	5		
Assets	1	16,811	440,603	339,918	100,401	284	5,712
1. Currency in circulation		155,154					
2. Liabilities to banks and central banks		328,126	4,421	30	4,391		
3. Liabilities from debt securities		67,712					
4. Derivatives			2,442		2,442		
5. Liabilities to the International Monetary Fund		13,311					
6. Liabilities to other international financial institutions		602	170	170			
7. Liabilities to clients		1,021	142	141	(5)	6	
8. Provisions and other liabilities		271	5	5			
Liabilities	2	566,197	7,180	346	6,828	6	
Open foreign exchange position at 31 Dec 2007	3=1-2	(549,386)	433,423	339,572	93,573	278	5,712
Assets	4	19,921	353,423	242,749	110,361	313	6,053
Liabilities	5	464,147	9,889	1,858	8,031		
Open foreign exchange position at 31 Dec 2006	6=4-5	(444,226)	343,534	240,891	102,330	313	6,053

Currency risk results from the open foreign exchange position of the NBS. The impact of exchange rate changes on NBS's performance is significant. This primarily results from the size of the open foreign exchange position and the volatility of the SKK/EUR and EUR/USD exchange rates.

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As at 31 December 2007, the exchange rate of SKK to EUR strengthened by 2.81% (from EUR 1 = SKK 34.573 as at 31 December 2006 to EUR 1 = SKK 33.603) and the exchange rate of SKK to USD strengthened by 12.86% (from USD 1 = SKK 26.246 as at 31 December 2006 to USD 1 = SKK 22.870).

The open foreign exchange position as at 31 December 2007 increased by 26.17% compared to 31 December 2006, from SKK 343,534 million to SKK 433,423 million.

F. Interest rates on assets and liabilities

The following table summarizes the interval (in percentages) of the average interest rates on assets and liabilities for 2007 and 2006, by the main currencies:

2007	EUR	USD	XDR	SKK
Assets				
Gold		0.01 - 0.1		
Debt securities in foreign currency	3.62 - 7.00	2.37 - 5.37		
Derivatives				
Receivables from banks and central banks	4.17 - 5.46			
Receivables from the IMF			0.00 - 4.38	
Receivables from clients				1.00 - 5.25
Liabilities				
Liabilities to banks and central banks	3.67 - 4.69			0.75 - 4.75
Liabilities from debt securities				4.05 - 4.25
Derivatives				
Liabilities to the IMF				
Liabilities to government and other clients				0.75 - 7.75
2006	EUR	USD	XDR	SKK
Assets				
Gold		0.02		
Debt securities in foreign currency	2.30 - 3.60	3.40 - 5.20		
Derivatives				
Receivables from banks and central banks	2.00 - 4.21			1.50 - 6.25
Receivables from the IMF			3.06 - 4.07	
Receivables from clients				1.00 - 5.75
Liabilities				
Liabilities to banks and central banks	1.60 - 3.71	4.25 - 4.50		0.50 - 4.75
Liabilities from debt securities				2.99 - 4.75
Derivatives				
Liabilities to the IMF				
Liabilities to government and other clients				0.50 - 7.75

NÁRODNÁ BANKA SLOVENSKA
Notes to the financial statements as at 31 December 2007
(in SKK millions)

G. Maturity of assets and liabilities

The structure of NBS's assets and liabilities by the remaining time to maturity as at 31 December 2007 is as follows:

As at 31 December 2007	Due within 1 month incl.	Due within 1-3 months incl.	Due within 1 year incl.	Due within 1-5 years incl.	Due in 5+ years	Not defined	Total
1. Gold	9,551		4,303		7,656	28	21,538
2. Debt securities in foreign currency	54,220	68,674	135,222	121,684	7,489		387,289
3. Derivatives	29	18			271		318
4. Receivables from banks and central banks	31,216	85	217	751	1,564	11	33,844
4.1 Current accounts, deposits and loans in foreign currency	31,090	9	3				31,102
4.2 Loans related to monetary policy operations in SKK							
4.3 Receivables not related to monetary policy operations in SKK	126	76	214	751	1,564	11	2,742
5. Receivables from the International Monetary Fund						13,454	13,454
6. Receivables from clients	14			5	297		316
7. Equity shares in subsidiary and affiliated accounting units and other shares and participating interests						413	413
8. Non-current assets						5,712	5,712
9. Other assets	17	168	18			39	242
TOTAL ASSETS	95,047	68,945	139,760	122,440	17,277	19,657	463,126
1. Currency in circulation						155,154	155,154
2. Liabilities to banks and central banks	328,126	76	11	2	4,332		332,547
2.1 Current accounts denominated in SKK	2,536						2,536
2.2 Overnight deposits, loans and deposits in SKK and minimum reserves	325,590						325,590
2.3 Current accounts, deposits and loans in foreign currency		76	11	2	4,332		4,421
3. Liabilities from debt securities	13,661	54,051					67,712
3.1 Denominated in SKK	13,661	54,051					67,712
3.2 Denominated in foreign currency							
4. Derivatives					2,442		2,442
5. Liabilities to the IMF						13,311	13,311
6. Liabilities to other international financial institutions	169					603	772
7. Liabilities to clients	511	8	177	467			1,163
8. Provisions and other liabilities	121	21	19	15	47	53	276
TOTAL LIABILITIES	342,588	54,156	207	484	6,821	169,121	573,377

Overnight bank deposits (item 2.2. under Liabilities) amounted to SKK 45,034 million.

These Notes are an integral part of the financial statements of Národná banka Slovenska.
Translation of the financial statements originally issued in the Slovak language.

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NÁRODNÁ BANKA SLOVENSKA
Notes to the financial statements as at 31 December 2007
(in SKK millions)

The structure of NBS assets and liabilities by the remaining time to maturity as at 31 December 2006 is as follows:

As at 31 December 2006	Due within 1 month incl.	Due within 1-3 months incl.	Due within 1 year incl.	Due within 1-5 years incl.	Due in 5+ years	Not defined	Total
1. Gold	5,828	5,005	1,250		6,677	28	18,788
2. Debt securities in foreign currency	7,637	65,129	99,718	123,735	16,145		312,364
3. Derivatives	2	7			217		226
4. Receivables from banks and central banks	21,987	88	241	240	757	1,841	25,154
4.1 Current accounts, deposits and loans in foreign currency	21,839	10	10	13			21,872
4.2 Loans related to monetary policy operations in SKK							
4.3 Receivables not related to monetary policy operations in SKK	148	78	231	227	757	1,841	3,282
5. Receivables from the International Monetary Fund						15,870	15,870
6. Receivables from clients	14		2	44	185		245
7. Equity shares in subsidiary and affiliated accounting units and other shares and participating interests						437	437
8. Non-current assets						6,053	6,053
9. Other assets	31	15	7	26	34	147	260
TOTAL ASSETS	35,499	70,244	101,218	124,045	24,015	24,376	379,397
1. Currency in circulation						143,518	143,518
2. Liabilities to banks and central banks	264,163	18	18	31	8,008		272,238
2.1 Current accounts denominated in SKK	2,560						2,560
2.2 Overnight deposits, loans and deposits in SKK and minimum reserves	261,603						261,603
2.3 Current accounts, deposits and loans in foreign currency		18	18	31	8,008		8,075
3. Liabilities from debt securities	500	36,935					37,435
3.1 Denominated in SKK	500	36,935					37,435
3.2 Denominated in foreign currency							0
4. Derivatives					1,382		1,382
5. Liabilities to the IMF						15,833	15,833
6. Liabilities to other international financial institutions						2,462	2,462
7. Liabilities to clients	303	13	205	342			863
8. Provisions and other liabilities	190	47	15	51	12	(10)	305
TOTAL LIABILITIES	265,156	37,013	238	424	9,402	161,803	474,036

NÁRODNÁ BANKA SLOVENSKA
Notes to the financial statements as at 31 December 2007
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Overnight bank deposits (item 2.2. under Liabilities) amounted to SKK 8,738 million.

H. Post-balance-sheet events

After 31 December 2007, there were no significant events that would require adjustments or disclosures in the 2007 financial statements.



Ing. Ivan Šramko
Governor



Ing. Viliam Ostrožlík, MBA
Deputy Governor



Ing. Katarína Taragelová
Director
Financial Management Dept.

These Notes are an integral part of the financial statements of Národná banka Slovenska.
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Abbreviations

ARDAL	Debt and Liquidity Management Agency
a.s.	joint stock company
ATM	Automated Teller Machine
BCPB	Bratislava Stock Exchange
BRIBOR	Bratislava Interbank Offered Rates
CPI	Consumer Price Index
CDCP SR	Central Securities Depository of the SR
DDP	Doplňková dôchodková poisťovňa – Supplementary Pension Insurance Company
DDS	Doplňková dôchodková spoločnosť – Supplementary Pension Company
EBOR	European Bank for Reconstruction and Development
EC	European Commission
ECB	European Central Bank
ECOFIN	Economic and Financial Affairs Council of the EU
EFT POS	Electronic Funds Transfer at Point of Sale
EMU	Economic and Monetary Union
ERM	Exchange Rate Mechanism
ESCB	European System of Central Banks
EU	European Union
EUR	euro/€
FDI	Foreign direct investment
Fed	Federal Reserve System
FNM	Fond národného majetku – National Property Fund
FRA	Forward rate agreement
GDP	Gross Domestic Product
HICP	Harmonised Index of Consumer Prices
IBEC	International Bank for Economic Cooperation
IBRD	International Bank for Reconstruction and Development
IFRS	International Financial Reporting Standards
IIB	International Investment Bank
IMF	International Monetary Fund
IPP	Industrial Production Index
IRB model	Credit risk model based on internal rating
IRS	Interest rate swap
MFI	Monetary Financial Institutions
MiFID	Markets in Financial Instruments Directive
NBS	Národná banka Slovenska – National Bank of Slovakia
NEER	Nominal Effective Exchange Rate
OECD	Organisation for Economic Co-operation and Development
OCP	obchodník s cennými papiermi – securities dealer
OPEC	Organisation of Petrol Exporting Countries
OPF	otvorené podielové fondy – Open-end Mutual Funds
p.a.	per annum
p.p.	percentage points
PPI	Producer Price Index
REER	Real Effective Exchange Rate
ROE	Return on Equity
RULC	Real Unit Labour Costs



SASS	Slovenská asociácia správcovských spoločností – Slovak Association of Management Companies
SAX	Slovak Share Index
SDX	Slovak Bond Index
SDXG	Slovak Bond Index Group
SEPA	Single Euro Payments Area
SIPS	Slovak Interbank Payment System
SKONIA	SlovaK OverNight Index Average
SSP	Single Shared Platform
SSS	Securities Settlement System
STATUS DFT	STATUS application software for financial market supervision
TARGET	Trans-European Automated Real-time Gross Settlement Express Transfer
ULC	Unit Labour Costs
USD	US dollar
WB	World Bank
WTO	World Trade Organization
ZBK SR	Bank Card Association in the SR



Glossary

Actuary – insurance mathematician responsible for the calculation of insurance premiums and reporting.

Autonomous liquidity factors – factors other than monetary policy operations influencing banking sector liquidity. Such factors are, in particular, net foreign assets held by the central bank, central government deposits with the central bank and currency in circulation.

Average value of currency mark – the total value of currency in circulation divided by the total number of banknotes and coins.

B5 – aircraft insurance.

B11 – insurance of the liability arising out of the ownership and use of aircraft including carrier's liability.

BRIBOR (Bratislava Interbank Offered Rate) – interest rate fixing in the interbank deposit market calculated from prices offered by reference banks for deposits with maturities ranging from 1 day to 12 months.

Central parity – the exchange rate vis-à-vis the euro of currencies of ERM II participant countries, around which the ERM II fluctuation margins are defined. The central parity for the Slovak koruna was set on 28 November 2005 at 38.4550 SKK per euro, with a fluctuation band of $\pm 15\%$.

Collateral – an asset used to secure a loan. In case of the debtor's default the asset can be sold and the proceeds used to settle the outstanding loan.

Common ESCB Training – a common training program of the European Central Bank (ECB) and national central banks of the European System of Central Banks (ESCB). The program covers manager training designed to learn new knowledge and work procedures, as well as the development of management skills focusing on the effectiveness and efficiency of decision-making in the ESCB and the Eurosystem, to foster a common ESCB culture through sharing of best practices.

Core inflation – measures the rate of growth of the price level on the basis of an incomplete consumer basket. The consumer basket excludes items with regulated prices and items with prices subject to other administrative measures (e.g. change of VAT, consumer taxes, subsidies). It is part of the national index of consumer prices.

Deflation – a decrease in the general price level, the opposite of inflation.

EFCB certificate (European Foundation Certificate in Banking) – an internationally accepted banking certificate awarded in an examination assessing the level of skills required as qualification for a bank employee, comparable within the EU banking sector; the only institution in Slovakia accredited to conduct EFCB training and examinations is the Institute of Banking Education of Národná banka Slovenska.

Effective exchange rates (nominal: NEER, real: REER) – weighted averages of bilateral SKK exchange rates against the currencies of the main trading partners. The weights used reflect the share of each partner country in Slovakia's foreign trade. Real effective exchange rates are nominal effective exchange rates deflated by a weighted average of foreign, relative to domestic, prices or costs. They are measures of price and cost competitiveness of a country.

Electronic money business – the issue and administration of electronic money and electronic money payment instruments.

Electronic money institution – a legal person other than a bank, foreign bank or Národná banka Slovenska, holding a license for electronic money business under the Payments Act.

Employee benefits – wage and wage compensations, bonuses, supplementary insurance, severance pay, exit pay, and other non-pecuniary benefits, such as health care.

ERM II (exchange rate mechanism II) – an exchange rate system providing a framework for exchange rate policy cooperation between the euro area countries and the EU Member States not participating in the third stage of the EMU. Membership in ERM II is one of the Maastricht criteria for the adoption of the euro.

ESA 95 – the European System of Accounts adopted in 1995. A common methodology for the compilation and reporting of GDP, employment and employee compensation data for all EU countries.

Euro area – the area encompassing those EU Member States in which the euro has been adopted in accordance with the Treaty. The responsibility for monetary policy in the euro area lies with the European Central Bank.

European Economic Area – comprises all EU Member States, Norway, Lichtenstein and Iceland.

European Payments Council – an organisation associating European Union banking associations.

EUROSIPS – a retail payment system that will be made up by the transformation of the present domestic SIPS payment system. It will be operated by Národná banka Slovenska as of the day of euro introduction.

Eurosystem – a system of central banks comprising the European Central Bank and the national central banks of those EU Member States that have adopted the euro.

Financial market (for the purposes of Part 4, entities regulated by NBS) – consists of four sectors: the banking sector (the main representatives are banks and branches of foreign banks), the capital market (the main representatives are securities dealers, asset management companies, the stock exchange, the Central Securities Depository, issuers and investment services intermediaries), the insurance sector (the main representatives are insurance companies and branches of foreign insurance companies), and the pension saving market (the main representatives are pension management companies and supplementary pension companies (pension insurance companies)).

Foreign direct investment – a category of international investments reflecting the objective of a resident entity in an economy (direct investor) to acquire a permanent interest in a company residing in an economy other than that of the investor (direct investment company). Direct investments include the initial transaction between these two entities – i.e. the transaction giving rise to the investment relationship – and all subsequent transactions between these two entities and affiliated companies.

Foreign exchange reserves – reserves of the Slovak Republic consisting of gold and other financial assets denominated in foreign currency held and managed by the central bank. They are used to directly finance payment imbalances, to indirectly regulate their size through foreign exchange market interventions in order to influence the exchange rate of the currency, or for other purposes.

Free provision of cross-border services – the conduct of banking activities by foreign entities based in the European Economic Area (foreign banks, foreign financial institutions or electronic money institutions) not present in the Slovak Republic.

GDP deflator – an aggregate price index reflecting developments in the price of products and services in an economy. It is calculated as a ratio of GDP at current prices to GDP at constant prices.

General government – a sector defined in ESA 95 as comprising resident entities that are engaged primarily in the production of non-marketable goods and services intended for individual and collective consumption and in the redistribution of national income and wealth. Included are central, regional and local government authorities as well as social security funds, and any budget-funded or subsidised organisations established by them, whose revenues cover less than 50% of their production costs.



General government debt – gross debt (deposits, loans and other debt securities other than financial derivatives) of the general government at nominal value. A debt-to-GDP ratio under 60% is one of the Maastricht convergence criteria for the adoption of the euro.

General government deficit – the difference between total revenues and total expenditures of the general government sector, if expenditures exceed revenues. A deficit-to-GDP ratio under 3% is one of the Maastricht convergence criteria for the adoption of the euro.

Gross domestic product (GDP) – the total output of goods and services in an economy in a given period. The main expenditure aggregates that make up GDP are household final consumption, government final consumption, gross fixed capital formation, changes in inventories, and imports and exports of goods and services.

Harmonised Index of Consumer Prices (HICP) – a consumer price index measured on a comparable basis across all EU Member States, which accounts for differences in national definitions. The HICP is one of the indicators used to assess price stability in a country (one of the Maastricht convergence criteria).

IBAN (International Bank Account Number) – an international bank account number format allowing unique customer identification and automated payment processing (mostly cross-border payments at present). In Slovakia, IBAN consists of 24 alpha-numerical characters (ISO country code, control number, account number including bank code).

Implied volatility – expected volatility (i.e. standard deviation) in terms of change in the price of an asset (for example, a bond or share). It can be derived from the price of the asset, maturity date and the exercise price of an option for the asset, as well as from a risk-free rate of return using an option valuation model (e.g. the Black-Scholes model).

Inflation – an increase in the general price level.

M1 – a narrow monetary aggregate comprising currency in circulation and overnight deposits with MFIs and central government (e.g. post office or the State Treasury).

M2 – an intermediate monetary aggregate that comprises M1 plus deposits repayable at notice of up to 3 months (short-term saving deposits) and deposits with an agreed maturity of up to 2 years (short-term time deposits) with MFIs and central government.

M3 – a broad monetary aggregate that comprises M2 plus negotiable instruments, i.e. repurchase agreements, money market fund shares and units as well as debt securities issued by MFIs with a maturity of up to two years.

Maastricht criteria – convergence criteria set out in the Maastricht Treaty that must be fulfilled before a country can join the euro area. There are four criteria regarding: public finances (deficit and debt of the general government sector), inflation, long-term interest rates, and exchange rate.

MFI claims on residents – MFI claims from residents other than MFIs (including the general government sector and the private sector) and securities issued by residents other than MFIs (stocks and other equity and debt securities) held by MFIs.

Minimum reserve requirement – financial reserves held by banks, branches of foreign banks, building societies and electronic money institutions on accounts with the central bank. It is a monetary policy tool with the level set individually by the central bank for each minimum reserve holder.

Monetary financial institutions (MFI) – financial institutions which together form the money-issuing/generating sector. These comprise the central bank (NBS), credit institutions (banks and branches of foreign banks) and all other financial institutions whose business is to receive deposits or redeemable funds from entities other than MFIs and, in their own name and for their own account, to grant credit and invest in securities (in particular money market funds).

NBS base rate – the interest rate limit applied to the marginal deposit facility of NBS – its main monetary policy operation. NBS has published the base rate since 1 January 2003; whenever the term “discount rate of the National Bank of Slovakia” or “discount rate of the Czecho-Slovak State Bank” appears in older legislation, it means the NBS base rate.

Net currency issuance – the difference between the amount of currency put into circulation and currency received in a given period.

Overnight refinancing operation of NBS – a facility which counterparties (banks) may use to receive overnight credit from the central bank against eligible assets. The overnight refinancing rate is one of the NBS key rates.

Overnight sterilisation operation of NBS – a facility which counterparties (banks) may use to make overnight deposits with the central bank. The overnight sterilisation rate is one of the NBS key rates.

Own funds adequacy – the ratio of own funds to risk-weighted assets (must not fall below 8%). The adequacy of own funds is an indicator of smooth functioning of a financial institution in the future, i.e. an indicator of its financial strength and credibility.

Parent company – a legal person controlling, i.e. holding over 50% of equity or voting rights in another legal person, or the right to appoint or dismiss the majority of the members of its statutory body, supervisory board or another managing, supervisory or controlling body.

Pension Pillar II – old-age pension saving, part of the compulsory state pension system based on a fund system financed through contributions.

Pension Pillar III – supplementary pension saving. A fund system financed through voluntary contributions and supported by the State through tax relieves.

Persons related to National Bank of Slovakia – legal or natural persons which are subsidiary accounting units of the NBS, affiliated accounting units, members of the NBS Bank Board, close relatives of a member of the NBS Bank Board, accounting units controlled, co-controlled or subject to the influence or significant voting rights exercised or held by members of the NBS Bank Board or their close relatives.

Portfolio investment – net transactions by residents and their holdings of securities issued by non-residents (assets) and net transactions by non-residents and their holdings of securities issued by residents (liabilities). They comprise equities and debt securities (bonds, bills of exchange and money market instruments). For investments to be considered portfolio investments, the interest in the company concerned must be lower than the equivalent of 10% of ordinary shares or voting rights.

Price stability – a year-on-year increase in consumer prices lower than a limit set by the NBS. As a medium-term target, the NBS seeks to maintain consumer price growth as measured by the HICP below 2% at the end of 2007 and 2008.

Regulated prices – prices and fees set by ministries or regulators (Network Industries Regulation Office, Slovak Post Office, Slovak Telecommunications Office, etc.) or by regional or local governments. They are included in the national consumer price index.

Reinvested earnings – consist of the share of a direct investor (relative to a direct participating interest) in profit not distributed as dividends by subsidiaries or affiliates and in profit of branches not distributed to the direct investor.

Repo operation – the granting or receiving of a loan against collateral in form of securities.

RTGS (Real Time Gross Settlement) – a real-time gross settlement system.



SEPA (Single Euro Payments Area) – a single euro payments area the objective of which is to create a single internal market for cross-border euro payments.

Single banking licence (single European passport) – regulated foreign entities are allowed to perform activity on the territory of other member states of the European Economic Area, provided they have been granted a licence in a member state of the European Economic Area. These entities may provide services on the basis of an established branch or via free provision of cross-border services.

Single banking licence principle (single European passport principle) – applies to all banking activities explicitly stated in the Banking Act. In order to provide mortgage loans pursuant to Article 67(1) of the Banking Act and to act as a depositary under the Collective Investment Act, a special licence from Národná banka Slovenska is required.

SIPS – an interbank payment system operated by Národná banka Slovenska.

Stability and Growth Pact – was designed to ensure sound public finances during the third stage of the Economic and Monetary Union in order to facilitate price stability and a strong sustainable growth contributing to job creation. To that end, the Pact requires Member States to set medium-term fiscal targets. It also defines a specific excessive deficit procedure. The Pact consists of the resolution on the Stability and Growth Pact adopted at the Amsterdam summit of the European Council on 17 June 1997 and two Council regulations, namely (i) Regulation 1466/97/EC of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies as amended by Regulation 1055/2005/EC of 27 June 2005 and (ii) Regulation 1467/97/EC of 7 July 1997 on speeding up and clarifying the implementation of the excessive deficit procedure as amended by Regulation 1056/2005/EC of 27 June 2005.

STEP2 – a European automated clearing system operated by the Euro Banking Association Clearing, designed to process cross-border euro payments.

Subsidiary – a legal person subject to control (a holding of over 50% of equity or voting rights in the legal person).

TARGET (Trans-European Automated Real-time Gross Settlement Express Transfer) – a real-time gross settlement system for euro payments. It is a decentralised system made up of 15 national RTGS systems, the ECB payment mechanism and the interlinking mechanism.

TARGET2 – a new generation of TARGET in which the current decentralised technical structure will be replaced by a single shared platform.

TARGET2-SK – a payment system that will be operated by Národná banka Slovenska as the national component of TARGET2 as of the day of euro introduction.

Two-week repo tender of the NBS – a standard 14-day repo operation of the central bank consisting in lending or borrowing against collateral in form of securities. This repo operation is conducted as a tender. The two-week repo tender rate is the NBS base rate.

Yield curve – a graphic representation of the relationship between the interest rate/yield and the maturity of an asset with the same credit risk, but different maturities at a specific point in time. The slope of the yield curve can be expressed as the difference between interest rates applied to two selected maturities.









