3.25 Slovakia

Note: Early data for "% of broadband lines with speed ≥ 30 Mbps" refer to 2011.
3.25.1 Introduction and performance

Slovakia is a small, open economy, well integrated into the global economy and the single market. Based on unit labour costs, its industry is among the most competitive in the ‘catching-up’ group of Member States. It has a significant export market share in cars and car components, consumer electronics, and machinery and metal products. Slovakia has a competitive advantage in terms of FDI and technology transfer, production process sophistication and extent of marketing. However, the short-term potential for further leaps seems limited. Good external competitiveness and lower imports brought the current account into balance in 2012, and the production of some export-driven manufacturing sectors reached record levels. Services constitute a relatively small part of the economy and their productivity gains are lower than those in the manufacturing sector. Relatively high electricity prices, in particular for SMEs, continue to hamper the competitiveness of Slovak industry.

Manufacturing continues to play a prominent role in the economy. Capital-intensive and technology-driven industrial sectors such as electronics and machinery, automotive and transport, and chemicals and pharmaceuticals, have increased their share in total EU manufacturing from 0.63 % in 2007 to 0.82 % in 2012. Foreign direct investment has primarily gone to export-oriented manufacturing and has significantly contributed to restructuring the economy. Trade surplus was over 6 % of GDP in 2013, and Slovakia's share in total EU exports of goods and services went up from 0.98 % in 2007 to 1.18 % in 2012, with some stagnation at 1.2 % in 2013. The growth of the export market share increased from 0.9 % in 2012 to 3.9 % in 2013. Main exports include cars and car components, consumer electronics, and machinery and metal products. The proportion of high-tech goods in total exports increased slightly to 6.6 % in 2011. In comparison to similar-sized economies in the EU, the domestic value-added content of exports is relatively low, as imports are essential for sustaining export capacity.

3.25.2 Access to finance and investment

Slovakia has improved SMEs’ access to finance, but has made limited progress in moving towards a financing model based less on grants and more on financial instruments. According to the World Economic Forum Global Competitiveness Report 2013-2014, Slovakia has a competitive advantage in terms of availability and affordability of financial services, and ease of access to loans, but is considerably lagging behind in terms of financing through the local equity market and venture capital availability. Despite the decrease in lending rates, the year on year growth of loans to non-financial corporations turned negative in both 2012 and 2013. However, the share of loan applications rejected by banks is still higher than the EU average. There is limited growth in venture capital financing: of the
three JEREMIE (1) instruments available in the 2007-2013 financing period, only the First Loss Portfolio Guarantee has become fully operational, and its effectiveness has yet to be seen. In order to see a sizeable effect on company investment, given Slovakia's market size limitation, more ambitious and effective measures are needed for improving access to finance, including encouraging cross-border investment.

3.25.3 Innovation and skills

While Slovakia has made little progress in encouraging innovation, its smart specialisation strategy nevertheless identifies the knowledge-intensive sectors that could push the country up on the value chain. However, the smart specialisation strategy is only the first step in putting in place a system that encourages innovation and more cooperation between academia and the business sector; its proper implementation is critical for boosting these sectors and thus leading to economic growth. The implementation plans are currently being discussed, but cooperation between ministries is not smooth and business stakeholders have not been invited to take part in these deliberations. In addition, there is a high risk that implementation will attract only a low level of private investment, while the incentives for research and development activities continue to be limited.

Slovakia is well below the EU average in terms of innovation performance (Innovation Union Scoreboard) and company spending on R&D (0.25 % of GDP in 2011). According to the WEF Global Competitiveness Report 2013-2014, Slovakia has a competitive advantage in terms of FDI and technology transfer, production process sophistication and extent of marketing, but it is considerably lagging behind in terms of capacity for innovation, firm-level technology absorption, cluster development, business-academia collaboration in R&D and government procurement of advanced technology. Fragmented R&D measures have had a limited effect on encouraging companies to use the research facilities of universities and have reportedly increased the administrative burden on companies. The incomplete legal framework on intellectual property protection and the university financing system do not motivate universities to create spin-offs and increase the number of contracts with companies. The innovation vouchers programme has finally been initiated, but its ambition has so far been limited: the small contracts are just a first step towards fully fledged R&D activities. The existing competence centres have made limited progress in encouraging business-academia cooperation, and the effectiveness of the incubators programme and the revolving Innovation Fund has been modest. There has been no progress in creating an agency for applied research. The recent creation of business-academia collaborative research centres is a more appropriate and ambitious initiative that has the potential to become an important tool for encouraging innovation.

There has been limited progress in terms of adapting the skills base of the workforce to market needs. Slovakia does not produce an adequate supply of employable graduates either in science, technical, engineering and mathematics, or in vocational education and training. The university financing system based on headcount puts technical universities at a disadvantage and does not generate appropriate incentives for attracting students in science, technical, engineering and mathematics. ICT, entrepreneurship and transversal skills, especially management and marketing, are in high demand but severely lacking. Although industry needs have not been clearly quantified, some stakeholders(2) report that some 300 000 technical jobs cannot be filled. Most initiatives have been ad-hoc and thus not very ambitious or effective. The existing re-training courses seem to have targeted neither the right categories of people nor the right skills. Given that the public availability of training is limited, multinational companies have designed and implemented their own training programmes and have only recently started to cooperate with universities on creating some training centres.

3.25.4 Energy, raw materials and sustainability

Slovakia is one of the most energy-intensive Member States, due partly to its high share of industry. In terms of the market functioning of the energy sector,

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(1) Joint European Resources for Micro to Medium Enterprises was an initiative of the European Commission for 2007-13, developed together with the European Investment Fund; it promoted the use of financial engineering instruments to improve access to finance for SMEs.

(2) The Automotive Industry Association of the Slovak Republic (ENTR mission to Slovakia, Jan 2014).
a non-transparent tariff-setting mechanism and the low accountability of the regulator remain weak points, despite recent efforts to liberalise the energy market. Relatively high electricity prices, due to high network charges, are hampering the competitiveness of companies, in particular SMEs. The 2014 attempt to correct the unfair practices of some distribution companies by introducing price regulation for SMEs did not address the problem, as the obligations were applied to both new entrants and operators with a significant degree of market power. The transport sector comes second in terms of energy consumption, and is characterized by an insufficiently developed public network. The tax on motor vehicles introduced in 2012 has the potential to improve the energy efficiency of cars.

Slovakia has made some improvements in cross-border energy connections with Poland and Hungary, which alleviates some of the upward pressure on energy prices. However, further measures are needed in terms of greater transparency and accountability of regulatory decisions, improving the security of supply and setting more ambitious targets for energy efficiency. For geopolitical reasons, a North-South gas connection in Central Europe is being considered, which has the potential to considerably improve energy security in the EU. Even though alternative funding should be considered, the EU funds for 2014-2020 remain critical, as measures proposed for EU financing include: energy audits in enterprises, renovation of buildings, reducing energy losses in heat distribution networks etc. In spite of the 2013 amendments of the waste law targeting increases in the landfill tax, considerable measures are still to be taken with a view to reach the country’s 2020 targets to significantly decrease landfilling of municipal waste.

3.25.5 Access to markets, infrastructure and services

The quality of transport infrastructure remains critical for the export-oriented manufacturing. The rail and road transport infrastructure are relatively underdeveloped. The unit costs of new and/or renovated infrastructure are high, reflecting poor planning and inefficient public procurement. Infrastructure charges for rail transport have been decreased recently, thus encouraging competition, but there are still considerable obstacles for new market entrants, including administrative burden. EU structural funding remains the main source of financing. A transport master plan is being drafted, aiming at identifying key priorities, in line with the Trans-European Transport Network.

3.25.6 Public administration and business environment

The business environment has been deteriorating, in part due to the introduction of measures increasing tax compliance. At the same time, Slovakia has made only limited progress towards supporting fast-growing firms. According to the World Bank Doing Business 2014 Report, Slovakia’s ease of doing business ranking and business environment score have worsened; the tax burden on SMEs has increased, including through the VAT pre-payment obligation, and starting a business has become more difficult – a new procedure involving a financial guarantee has been added for establishing a limited liability company. A 2013 SME Survey by the American Chamber of Commerce in Slovakia emphasises that recent legislative changes have led to a sizeable increase in companies' negative opinion on the business environment, especially concerning SMEs.

E-government services for companies and one-stop-shops (KAMO) are not yet fully operational, and there are no plans to integrate them with the tax administration. There is no SME test yet and the impact assessment for new regulatory and legislative initiatives is not conducted systematically according to a unified, thorough methodology. The number of SMEs accessing e-commerce and foreign markets continues to be low. In terms of companies’ access to justice, insolvency cases remain lengthy, and alternative dispute resolution mechanisms are barely used. No data is collected on the number of cases of mediation or arbitration. Some of the measures taken have been appropriate and effective. Setting fixed transfer fees has made it easier to register property. Since November 2013, companies’ communication with the authorities has become electronic-only and registers have been unified, so that companies are not asked to provide the same information twice. The protection of investors has been improved by allowing access to all corporate documents during trials. Initiatives such as ‘helping hand for the young’, organized by the Slovak Business Agency and ‘start-up weekends’ and ‘start-up awards’ have been effective in supporting innovative companies with
high growth potential. However, the measures supporting start-ups and entrepreneurship have been fragmented and not very ambitious, thus failing to create real eco-systems for companies.

Public administration continues to suffer from governance weaknesses in terms of both quality and efficiency. Evidence-based policy-making is impaired by high staff turnover linked to the political cycle, weak human resource management and underperforming analytical capacities. Transparency and effectiveness in both public procurement and judiciary proceedings remain serious challenges.

There has been some progress in terms of public administration reform. The Government acknowledged the Framework Strategy for Public Administration Reform in December 2013. The reform aims at modernising human resources management, strengthening analytical capacities in ministries, improving tax management and public procurement and implementing user-friendly e-government applications for businesses and citizens. However, the framework strategy lacks an action plan with concrete measures accompanied by a timetable and a budget, and it does not envisage revamping the Civil Service Act in 2014. Given that reforming public administration requires serious political commitment from all parties involved, implementation remains critical, with a high degree of risk. The government has tentatively committed to adopting an Action Plan for Public Administration Reform by July 2014.

Slovakia ranks bottom of the EU in terms of the WEF Global Competitiveness Report indicator ‘irregular payments and bribes’, and the situation has worsened in 2013-2014 compared to 2012-2013. According to the EU Anti-Corruption Report, 90% of Slovaks perceive corruption to be widespread and 21% have personally experienced it in the past year. A highly sensitive and thus difficult point is making the civil service less vulnerable to the political cycle, especially in terms of limiting widespread staff changes. Equally challenging is smooth cooperation between ministries, for which there is political willingness, but which is much more difficult to put into practice. As for the newly-created analytical capacities, they are not operational in all ministries, and where they exist, there is as yet no evidence that they function well and are able to permeate the policy cycle at all levels. In addition, ministries still have very weak or non-existent impact assessment and smart regulation capacities.

Figure 3.25.2: Overall profile of public administration - Slovakia

Note: Values have been scaled so that the best observation (Member State) gets 1 and the worst gets 0.
Source: World Bank Doing business; Intrum Justitia; OECD; World Economic Forum; European Commission
In terms of improving the efficiency of the judicial system, limited progress has been made towards reducing the length of proceedings. The planned introduction of electronic communication between courts and parties could lead to fewer delays and thus shorter proceedings. A reform of the Code of Civil Procedure is ongoing, but the amended law is not expected to come into force before 2016. Further, a new act on arbitration, expected to come into force in 2014, separates commercial and consumer arbitration but does not promote alternative dispute resolution mechanisms. Perceived judicial independence has worsened and is the lowest in the EU, and the capacity of judicial authorities to investigate and prosecute corruption offences is weak. Similarly, public confidence in the functioning of the justice system is low: according to a recent Eurobarometer, only 25% of the Slovak respondents tend to trust the justice system, the second lowest percentage in the EU.

In terms of public procurement, the effectiveness of the 2013 reform seems to be rather limited, as no significant effect has been observed in increasing transparency of public procurement procedures and reducing the number of complaints against the decisions of contracting authorities. On the contrary, public procurement procedures have become lengthier, savings have decreased and the use of e-procurement has declined. These shortcomings are also observed in the implementation of EU structural funds.

3.25.7 Conclusions

While Slovakia has identified the growth areas that could boost its competitiveness at global level, the current mix of measures is insufficient to ensure the critical mass and the right skills for promoting an innovative, business-friendly economy. Slovakia has to step up its efforts to improve the business environment, especially in terms of alleviating the tax burden on SMEs, starting a business, and introducing a systematic impact assessment and SME test for new legislative initiatives. In terms of the energy market, the opaque regulatory framework and high electricity network charges affect the competitiveness of Slovak companies. Public administration in Slovakia remains a challenge, especially in terms of human resources management, insulation from the political cycle and analytical capacities. As Slovakia’s innovation performance is well below the EU average, it has to take coordinated measures to improve its capacity for innovation, firm-level technology absorption, cluster development, business-academia collaboration in R&D and government procurement of advanced technology.

\(^{(1)}\) Flash Eurobarometer 385: Justice in the EU: http://ec.europa.eu/public_opinion/archives/flash_arch_390_375_en.htm