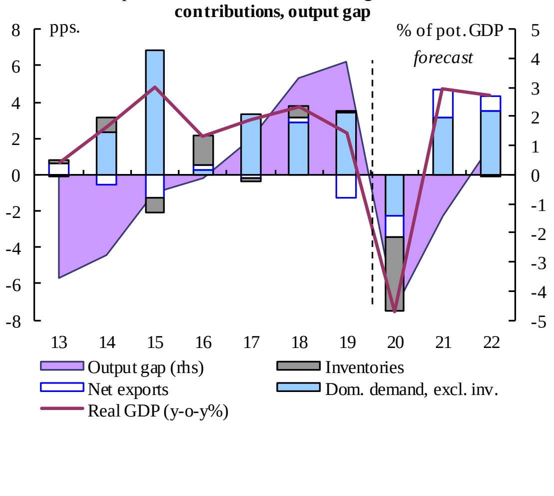
18. SLOVAKIA

The COVID-19 pandemic is expected to push Slovakia's economy into a deep and broad-based recession in 2020. Investment, private consumption and net exports have all contracted significantly. A recovery in all components is expected in 2021 and 2022. Consumer price inflation is forecast to moderate substantially over the forecast period due to lower energy prices and less demand-pull inflation. Public finances are expected to go into significant deficit in 2020, due to the loss of revenues and sizeable fiscal support measures cushioning the socio-economic impact of the pandemic, but should improve slowly as the economy recovers.

A deep recession and an uncertain recovery

Slovakia's real GDP is forecast to contract sharply by 7½% in 2020, but to then recover and grow by 4¾% in 2021 and 4¼% in 2022, returning to its pre-crisis income level in mid-2022. The lockdown in spring due to COVID-19 severely suppressed domestic demand, which is projected to remain subdued well into 2021, following a resurgence in infections and new restrictions. Sizeable fiscal support measures are expected to cushion the impact. Private consumption is projected to drop in 2020 as consumers withhold spending amid continued uncertainty and restrictions. It is expected to recover in 2021 and 2022 when it will surpass its pre-crisis level, but not fully return to its previous growth trajectory due to relatively weaker employment and wage growth. Uncertainty, liquidity constraints and restrictions to business activity are projected to weigh even more heavily on investment growth in 2020. Both private and public investment are expected to grow strongly in 2021 and 2022, even as support measures such as loan deferrals expire. Trade activity is also projected to decrease sharply in 2020 but to recover swiftly.

Graph II.18.1: **Slovakia - Real GDP growth and contributions, output gap**



Exports are expected to recover swiftly

The lockdown in spring will take its toll on exports in 2020 amid supply chain disruptions and weaker foreign demand, particularly so for Slovakia's large, export-oriented automotive sector. Nevertheless, goods exports, the bulk of Slovakia's trade activity, are expected to recover relatively quickly alongside resumed industrial production, with particularly high growth rates in 2020-Q3. While the recovery in trade remains subject to significant uncertainties amid rising infections and depends on prospects in Slovakia's key trading partners and the automotive sector, Slovakia is well-positioned to regain market shares.

Employment to fall in 2020 and 2021, but partially recover in 2022

Public support measures are expected to mitigate the impact of the crisis on the labour market. Nevertheless, after years of strong employment growth, Slovakia's economy is expected to shed jobs amid the recession. The unemployment rate is projected to rise from a record low of 5.8% in 2019 to 6.9% in 2020 and to climb to 7.8% in 2021, partly due to the scheduled expiration of protective measures such as short-time work schemes. Strong economic growth should improve the labour market in 2022 when the unemployment rate is forecast to decrease to 7.1%. Real wages are expected to decrease slightly in 2020 but to grow again in 2021 and 2022, albeit at lower rates than before the crisis. While these developments weigh on household disposable income, the latter remains relatively robust, thanks in part to public support.

Inflation to slow substantially

HICP inflation is forecast to slow down substantially from 2.8% in 2019 to 2% in 2020 and to 0.7% in 2021, before picking up again and growing by 1.4% in 2022. Energy prices contribute markedly to the slowdown, as the collapse in fuel prices earlier this year is expected to have a strong, lagged effect on regulated energy prices in 2021. Service price inflation is also expected to slow as the recession weighs on demand and wage growth. Food prices are likely to grow more swiftly than overall inflation.

Public deficit to increase due to COVID-19

The general government headline deficit is expected to increase to 9½% of GDP in 2020 from 1.4% in 2019. This is due in part to weak tax revenues and social contributions as well as lower property income on the revenue side. No additional revenue is expected from the implementation of an online connection of cash registers to the financial administration. Expenditure is expected to increase by an estimated 2½% of GDP due to fiscal measures to cushion the socio-economic impact of the pandemic. The main measures encompass employment support, sickness and nursing benefits as well as subsidised rents. Worse fiscal developments than expected in spring are also partly due to expenditure measures previously not included in the budget including the cancellation of a bank levy, the establishment of a new ministry and a decrease in motor vehicle taxation, among others. Public guarantee schemes launched as a liquidity support to businesses are a potential downside risk if they materialise.

In 2021, the general government deficit is forecast to decline to around 8% of GDP on the back of the economic recovery. An increase in the tobacco excise duty together with subdued developments in wages, intermediate consumption and interest rates, should help lower the deficit. A majority of pandemic measures are expected to phase out in 2021. However, the budget also includes a reserve of more than 1% of GDP to cover risks from a second wave. In 2022, the headline deficit is forecast to decrease by almost 2% of GDP. Public investment is expected to grow, because the use of EU funding is projected to increase as the end of the programming period approaches. The projection for 2022 is based on a no-policy-change assumption. No measures related to the Recovery and Resilience Facility are included in the forecast, and hence represent an upside risk.

The government debt-to-GDP ratio is projected to increase rapidly from 48% in 2019 to more than 67% in 2022.

Table II.18.1:

Main features of country forecast - SLOVAKIA

	2019					Annual percentage change				
	bn EUR Curr. prices	% GDP	01-16	2017	2018	2019	2020	2021	2022
GDP	93.9	100.0	4.0	3.0	3.8	2.3	**-7.5**	**4.7**	**4.3**
Private Consumption	52.9	56.4	3.2	4.5	4.1	2.3	**-2.4**	**2.2**	**3.5**
Public Consumption	18.5	19.7	2.6	1.0	0.2	4.7	**8.9**	**0.3**	**-1.1**
Gross fixed capital formation	20.1	21.4	3.2	3.5	2.6	5.8	**-12.6**	**9.2**	**8.6**
of which: equipment	9.5	10.1	5.5	-6.0	1.2	15.6	**-20.0**	**13.3**	**12.1**
Exports (goods and services)	86.8	92.4	9.2	3.6	5.2	0.8	**-11.4**	**8.6**	**4.4**
Imports (goods and services)	86.4	92.0	7.9	3.9	4.9	2.1	**-10.2**	**6.8**	**3.5**
GNI (GDP deflator)	92.2	98.2	3.9	3.8	4.3	1.9	**-7.9**	**4.6**	**4.3**
Contribution to GDP growth: Domestic demand			3.1	3.4	2.9	3.4	**-2.3**	**3.2**	**3.5**
Inventories			0.1	-0.2	0.6	0.2	**-4.1**	**0.0**	**0.0**
Net exports			0.9	-0.2	0.3	-1.2	**-1.1**	**1.5**	**0.8**
Employment			0.9	2.2	2.0	1.0	**-1.6**	**-1.0**	**0.8**
Unemployment rate (a)			14.2	8.1	6.5	5.8	**6.9**	**7.8**	**7.1**
Compensation of employees / head			5.3	5.4	5.8	6.6	**1.5**	**3.5**	**3.7**
Unit labour costs whole economy			2.1	4.5	4.0	5.3	**8.1**	**-2.1**	**0.2**
Real unit labour cost			0.1	3.3	1.9	2.7	**4.6**	**-2.7**	**-1.5**
Saving rate of households (b)			7.4	8.9	10.7	10.2	**14.2**	**13.1**	**10.8**
GDP deflator			1.9	1.2	2.0	2.5	**3.3**	**0.6**	**1.7**
Harmonised index of consumer prices			3.1	1.4	2.5	2.8	**2.0**	**0.7**	**1.4**
Terms of trade goods			-0.7	-0.8	-0.9	-0.3	**0.1**	**0.0**	**0.0**
Trade balance (goods) (c)			-1.2	1.1	1.1	-0.5	**-1.6**	**-0.2**	**0.5**
Current-account balance (c)			-3.0	-0.9	-0.1	-1.7	**-3.1**	**-1.6**	**-0.9**
Net lending (+) or borrowing (-) vis-a-vis ROW (c)			-2.5	-1.6	-0.1	-1.8	**-3.2**	**-1.8**	**-1.1**
General government balance (c)			-4.2	-0.9	-1.0	-1.4	**-9.6**	**-7.9**	**-6.0**
Cyclically-adjusted budget balance (d)			-4.0	-1.4	-2.3	-2.8	**-7.8**	**-7.3**	**-6.4**
Structural budget balance (d)			-	-1.4	-2.3	-2.8	**-7.8**	**-7.3**	**-6.4**
General government gross debt (c)			43.2	51.7	49.9	48.5	**63.4**	**65.7**	**67.6**

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.