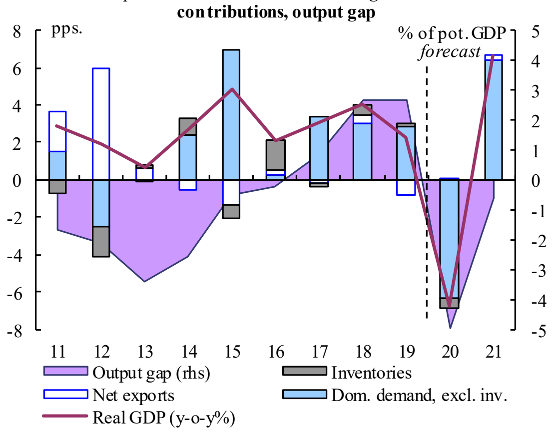
18. SLOVAKIA

In the wake of the COVID-19 crisis, Slovakia's economy is expected to enter into a deep recession in 2020 as private consumption, investment and trade suffer. As the impact of COVID-19 and the containment measures put in place to fight it are likely to subside in the second half of 2020, a swift recovery is expected in 2021. Consumer price inflation is projected to moderate substantially due to lower energy prices and less demand-pull inflation. Increased public spending should mitigate the recession and aid the recovery, but sharply increase the general government deficit in 2020 and 2021.

A deep recession and a swift recovery

After expanding by 2.3% in 2019, real GDP in Slovakia is forecast to contract sharply by 6¾% in 2020, but to then recover swiftly as containment measures are lifted and grow by 6½% in 2021. Despite substantial government measures put in place to cushion the impact, the COVID-19 crisis is projected to temporarily suppress domestic demand, the main driver of both the recession in 2020 and the recovery in 2021. Private consumption is expected to drop sharply in 2020 as consumers withhold spending due to closed stores, travel restrictions and higher precautionary savings. It is expected to recover in 2021, but not to fully return to its previous trajectory, as employment and wage growth are also impacted. The uncertainty, liquidity constraints and restrictions to business activity are projected to weigh even more heavily on investment growth in 2020. Trade is also projected to decrease sharply in 2020, but to offset most of the losses in 2021.

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



Trade outlook marked by recession

Supply chain disruptions and weaker demand in key EU trading partners are expected to take their toll on exports in 2020. However, goods, the bulk of Slovakia's exports, are expected to recover relatively quickly and post high growth rates in the second half of 2020 and in 2021. This is particularly the case for Slovakia's large automotive sector. As imports are expected to display a similar pattern, net exports are unlikely to act as a significant drag on growth. While the recovery in trade remains subject to uncertainties and depends on prospects in key trading partners and on demand in the automotive sector, Slovakia is well-positioned to regain export market shares.

Employment to fall in 2020 but partially recover in 2021

The limited duration of the crisis and public support are projected to mitigate the fallout 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 its record low of 5.8% in 2019 to 8¾% in 2020. Strong economic growth in 2021 is expected to bring a marked, but not full recovery to employment in 2021, with the unemployment rate decreasing to 7%. Wage growth is also expected to slow markedly from the high rates seen in recent years. While these developments weigh on household disposable income, the latter remains relatively robust, in part aided by government measures. The saving rate is expected to increase sharply in 2020 as consumers refrain from spending, though this development is projected to be largely reversed in 2021.

Inflation slows amid recession and lower energy prices

Headline inflation is forecast to slow substantially over the forecast horizon, moderating from 2.8% in 2019 to 1.9% in 2020 and 1.1% in 2021. Energy prices contribute markedly to the slowdown, as oil prices have recently collapsed. This is expected to sharply reduce regulated energy prices in 2021. Service price inflation is also expected to slow as the recession weighs on demand and on wage growth. Food prices are likely to grow more swiftly than overall inflation.

Deficit and debt to rise strongly

In 2019, the general government deficit of 1.3% of GDP turned out to be higher than the budget target of 0.5%. The worse-than-expected outturn was the result of the lower local governments' surplus, higher subsidies and public wages, higher spending on healthcare and social security systems, as well as military equipment purchases. Higher-than-expected expenditure was carried over from previous years and outpaced the solid growth in tax revenues, driven by robust labour market developments and buoyant household consumption.

In 2020, the general government deficit is expected to increase to 8½% of GDP. This is the result of both a sharp decline in tax revenue, reflecting the economic downturn, and the introduction of fiscal support measures to counteract the economic impact of the COVID-19 pandemic. The estimated decrease in tax revenues attributable to macroeconomic fundamentals is around 3% of GDP. The impact of the measures on the expenditure side is estimated at above 2¼% of GDP and of 1¼% of GDP on the revenue side in 2020. Key measures increasing the general government deficit include employment support schemes, as well as sickness and nursing benefits. An accelerated drawing and reallocation of EU funds offsets the cost of these measures by around 1% of GDP. Shifting payments in time, such as postponed employer social security contributions, waived income tax advance payments and the loss-carry forward used in tax returns for 2019, are likely to have a limited impact on the overall 2020 deficit. The general government balance is also negatively impacted by the delayed implementation of the online connection of all cash registers to the financial administration and the introduction of the regular 13th pensions at the beginning of the year.

In 2021, under a no-policy-change assumption, the general government deficit is forecast to decline to close to 4% of GDP. The use of EU funds is set to increase as the end of the programming period nears. The general government debt-to-GDP ratio is forecast to increase to nearly 60% of GDP in both 2020 and 2021.

Table II.18.1:
Main features of country forecast - SLOVAKIA

		2018		Annual percentage change						
		bn EUR Curr. prices	% GDP	00-15	2016	2017	2018	2019	2020	2021
GDP		89.7	100.0	4.0	2.1	3.0	4.0	**2.3**	**-6.7**	**6.6**
Private Consumption		50.2	55.9	3.1	3.9	4.3	3.9	**2.2**	**-7.1**	**7.2**
Public Consumption		16.7	18.6	2.7	1.9	1.0	0.2	**3.8**	**4.2**	**1.5**
Gross fixed capital formation		19.0	21.2	3.0	-9.3	3.9	3.7	**4.4**	**-14.7**	**10.7**
of which: equipment		8.4	9.3	4.3	-2.0	0.8	-3.5	**4.8**	**-24.1**	**18.7**
Exports (goods and services)		86.2	96.1	9.5	5.0	3.5	5.4	**1.7**	**-12.4**	**13.4**
Imports (goods and services)		84.4	94.1	8.0	4.8	3.9	5.0	**2.6**	**-12.6**	**13.3**
GNI (GDP deflator)		88.3	98.4	3.8	2.0	3.6	4.5	**2.3**	**-7.1**	**6.9**
Contribution to GDP growth:	Domestic demand			3.0	0.2	3.4	3.0	**2.9**	**-6.3**	**6.4**
	Inventories			0.1	1.6	-0.2	0.5	**0.2**	**-0.5**	**0.0**
	Net exports			0.9	0.3	-0.2	0.5	**-0.8**	**0.1**	**0.3**
Employment				0.6	2.4	2.2	2.0	**1.2**	**-3.4**	**2.0**
Unemployment rate (a)				14.7	9.7	8.1	6.5	**5.8**	**8.8**	**7.1**
Compensation of employees / head				6.0	2.2	5.4	5.6	**6.2**	**1.3**	**2.5**
Unit labour costs whole economy				2.5	2.5	4.5	3.5	**5.1**	**4.9**	**-2.0**
Real unit labour cost				0.0	3.0	3.3	1.4	**2.4**	**2.7**	**-3.2**
Saving rate of households (b)				7.5	8.6	8.2	8.4	**7.7**	**17.1**	**10.0**
GDP deflator				2.6	-0.5	1.2	2.0	**2.6**	**2.2**	**1.3**
Harmonised index of consumer prices				3.8	-0.5	1.4	2.5	**2.8**	**1.9**	**1.1**
Terms of trade goods				-0.5	-0.4	-0.8	-0.9	**-0.3**	**0.1**	**0.0**
Trade balance (goods) (c)				-1.7	2.3	1.1	1.1	**0.3**	**0.5**	**0.5**
Current-account balance (c)				-3.0	-2.0	-1.8	-1.6	**-2.6**	**-2.9**	**-2.4**
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-2.5	-2.1	-2.5	-1.3	**-2.3**	**-2.6**	**-2.2**
General government balance (c)				-4.9	-2.5	-1.0	-1.0	**-1.3**	**-8.5**	**-4.2**
Cyclically-adjusted budget balance (d)				-4.7	-2.4	-1.3	-2.1	**-2.3**	**-6.6**	**-4.0**
Structural budget balance (d)				-	-2.3	-1.3	-2.1	**-2.3**	**-6.6**	**-4.0**
General government gross debt (c)				43.1	52.0	51.3	49.4	**48.0**	**59.5**	**59.9**

(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.