

## 18. SLOVAKIA

Slovakia's economy is recovering from the 2020 recession. However, intensifying supply-chain disruptions and resurging COVID-19 infections are expected to slow the recovery in the short term, before growth accelerates again from 2022 onwards, also boosted by Recovery and Resilience Facility-financed public investments. Inflation is forecast to rise sharply in 2021 and 2022 due to the combination of supply side bottlenecks and robust demand, but slow down thereafter. While fiscal policy is expected to remain supportive in 2021, declining budget deficits are forecast in the following years. In addition to economic growth and low interest rates, this also helps contain the public debt-to-GDP ratio.

### Recovery to slow down temporarily

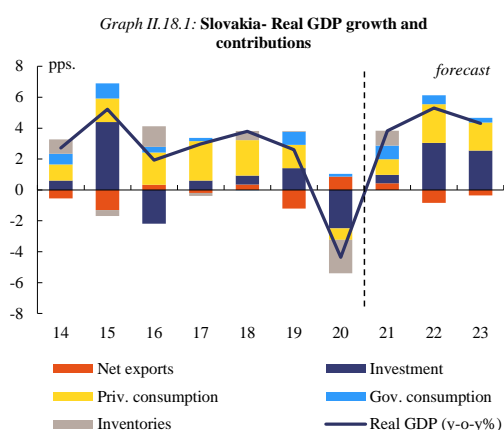
After a robust 2% q-o-q rebound in real GDP amid easing pandemic-related restrictions in the second quarter of 2021, economic growth in Slovakia is expected to moderate in the remainder of this year. Intensifying supply chain disruptions and resurging COVID-19 infections are assumed to weigh on economic activity, bringing annual GDP growth to 3.8% in 2021. The Slovak economy is forecast to reach its pre-pandemic output level by the end of 2021 and to continue expanding at an annual rate of 5.3% in 2022 and 4.3% in 2023, closing its output gap.

The easing of COVID-19 containment measures supported domestic demand in the second quarter. With more spending opportunities, private consumption bounced back sharply, which led to a fall in forced savings. Private investment also rebounded significantly. However, due to a rather low vaccination rate, domestic spending is expected to suffer somewhat from a new pandemic wave. After this temporary disruption, domestic demand is forecast to resume its robust expansion in the coming years, as spending by households and corporations catches up to its pre-crisis path. A boost to public investment from Next Generation EU funds is expected from 2022 onwards.

### Supply-chain disruptions hurt trade

Despite being largely shielded from domestic pandemic-related restrictions, and benefiting from robust foreign demand, Slovakia's industry-heavy export sector has been adversely affected by severe supply-chain disruptions. Global semiconductor shortages are assumed to persist throughout 2022, and to constrain Slovakia's automotive industry, resulting in markedly lower export levels during that period. Due to a large share of imported intermediate inputs, weaker exports should also go along with lower import growth. On balance, net

exports are forecast to contribute positively to GDP growth in 2021 and negatively thereafter, as domestic spending gains speed and boosts imports.



### Labour market to recover from 2022

The impact of the crisis on the labour market has been mostly reflected in declining hours worked, as public job retention schemes have shielded employment. As the recovery gathers pace and fiscal support measures are withdrawn, hours worked are set to increase first, followed by an increase in new vacancy postings only afterwards. Despite aggregate labour market indicators still being weaker than prior to the pandemic, certain sectors already face labour shortages, while skill mismatches reduce readily available labour supply, thereby contributing to a tightening market.

On average, employment is projected to increase by 0.3% in 2021, while the unemployment rate at 6.8% is expected to stay slightly higher than in 2020. Further improvement is forecast as from 2022, with employment growing by around 1% annually, and the unemployment rate falling to 5.6% in 2023. Wage growth is expected to gather pace as labour market slack diminishes, productivity rebounds, and inflation increases.

### Inflation to rise amid supply bottlenecks

Inflationary pressures have intensified recently, driven mainly by rising commodity prices and strong services inflation, as rebounding aggregate demand faces supply-side bottlenecks. Strong price dynamics are forecast to persist in 2021, leading to an annual HICP inflation rate of 2.8%. As regulated energy prices are expected to rise at the beginning of 2022, quarterly inflation is assumed to decelerate only thereafter, bringing average annual inflation to 4.3% in 2022. Well-anchored inflation expectations should prevent temporary price pressures from becoming permanent, and allow inflation to slow to 2.2% in 2023.

### Fiscal support to weaken as from 2022

The general government deficit is projected to widen from 5.5% in 2020 to 7.3% of GDP in 2021, driven by temporary pandemic-related support measures, including short-time work schemes, health spending and support to selected sectors, as well as by permanent measures. Nevertheless, the expected deficit is significantly lower than in the adopted 2021 budget, due to higher tax revenues resulting from the economic rebound (mainly VAT and corporate income tax). Capital expenditures and expenditures on goods and services are also set to be lower than originally projected. However,

social transfers, subsidies, investments and expenditure on goods and services are assumed to grow fast in 2021.

In 2022, the government budget deficit is expected to narrow to 4.2% of GDP, as economic growth gains pace and most temporary support measures are phased out. The deficit is projected to further decline in 2023, to 3.2% of GDP. While tax revenues should grow broadly in line with GDP, expenditures are expected to shift away from pandemic-related emergency measures towards public investment aimed at facilitating the green and digital transformation. The drawdown of EU funds from the current programming period is assumed to peak in 2023. The forecast also incorporates expenditures financed by RRF grants, for a cumulative amount of 1.9% of 2019 GDP over the forecast horizon.

The government debt-to-GDP ratio is projected to edge up to 61.8% in 2021, before gradually declining to 59.1% by 2023, helped by moderating primary budget deficits as well as by strong nominal GDP growth and persistently low interest rates.

Table II.18.1:

#### Main features of country forecast - SLOVAKIA

	2020			Annual percentage change						
	bn EUR	Curr. prices	% GDP	02-17	2018	2019	2020	2021	2022	2023
GDP	92.1	100.0		4.0	3.8	2.6	-4.4	3.8	5.3	4.3
Private Consumption	53.6	58.3		3.1	4.1	2.7	-1.3	1.7	4.3	3.2
Public Consumption	19.8	21.5		2.5	-0.1	4.6	0.9	4.1	2.7	1.4
Gross fixed capital formation	18.1	19.6		2.7	2.8	6.7	-11.6	2.8	15.7	12.1
of which: equipment	6.8	7.4		3.6	1.9	13.9	-26.9	5.4	23.3	16.5
Exports (goods and services)	78.7	85.4		8.8	5.1	0.8	-7.3	11.7	6.5	5.9
Imports (goods and services)	77.8	84.5		7.0	4.8	2.1	-8.2	11.3	7.4	6.3
GNI (GDP deflator)	91.0	98.9		3.9	4.3	2.2	-3.8	3.6	5.8	4.5
Contribution to GDP growth:										
Domestic demand				2.9	2.9	3.8	-3.0	2.4	6.1	4.7
Inventories				0.0	0.6	0.0	-2.2	1.0	0.0	0.0
Net exports				1.2	0.3	-1.2	0.9	0.4	-0.8	-0.4
Employment				1.0	2.0	1.0	-1.9	0.3	1.2	1.0
Unemployment rate (a)				13.5	6.5	5.8	6.7	6.8	6.4	5.6
Compensation of employees / head				5.3	6.0	6.8	3.6	5.0	5.9	5.4
Unit labour costs whole economy				2.2	4.2	5.2	6.3	1.5	1.8	2.0
Real unit labour cost				0.5	2.1	2.6	3.8	0.1	-2.8	-0.2
Saving rate of households (b)				7.3	10.3	9.8	10.9	12.2	9.5	10.1
GDP deflator				1.7	2.0	2.5	2.4	1.4	4.7	2.2
Harmonised index of consumer prices				2.7	2.5	2.8	2.0	2.8	4.3	2.2
Terms of trade goods				-0.7	-0.9	-0.3	-0.5	-1.7	1.6	0.1
Trade balance (goods) (c)				-0.4	1.1	-0.5	0.1	-0.5	-0.5	-0.4
Current-account balance (c)				-2.7	-0.3	-2.0	-0.8	-1.7	-1.0	-1.1
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-2.1	-0.3	-2.0	-0.8	-1.5	-0.2	1.5
General government balance (c)				-3.8	-1.0	-1.3	-5.5	-7.3	-4.2	-3.2
Cyclically-adjusted budget balance (d)				-3.7	-1.8	-2.2	-4.1	-6.5	-4.3	-3.6
Structural budget balance (d)				-2.2	-1.8	-2.2	-4.1	-6.5	-4.3	-3.6
General government gross debt (c)				43.2	49.6	48.1	59.7	61.8	60.0	59.1

(a) Eurostat definition. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.