2.18. SLOVAKIA

After a strong rebound in the third quarter, a second wave of the COVID-19 pandemic is expected to have suppressed economic activity in Slovakia towards the end of 2020, resulting in a 5.9% contraction of GDP compared to 2019. While prolonged pandemic-related restrictions are assumed to keep weighing on real output in early 2021, the gradual rollout of vaccination should enable a sharp rebound in the second half of the year, bringing annual GDP growth to 4%. The Slovak economy is forecast to reach its pre-pandemic output level by the end of 2021 and to grow by about 5.4% in 2022.

The deteriorating near term outlook mainly affects domestic spending. Despite continued fiscal measures cushioning the fall in private incomes and employment, closed businesses and travel restrictions are depressing private consumption, particularly in the service sector. In addition, prolonged uncertainty keeps precautionary savings of households high and also discourages investment spending. However, with the assumed lifting of most containment measures, a sharp rebound in domestic demand is expected from the second half of 2021.

In contrast to services, industry is proving to be more resilient, being largely shielded from domestic pandemic-related restrictions. This bodes well for Slovakia’s industry-heavy export sector, which should also benefit from improved foreign demand. Due to a large share of imported intermediate inputs, strong exports should also sustain faster import growth despite initially weaker domestic spending. On balance, net exports are forecast to contribute positively to GDP growth over the forecast horizon.

Inflation is expected to slow sharply at the beginning of 2021 due to a drop in administered energy prices. The deteriorating near-term outlook will act as an additional disinflationary force via weaker domestic demand, resulting in an annual inflation rate of 0.5% in 2021. The more dynamic rebound in the second half of 2021 is forecast to set off rising price pressures, mainly in the domestic service sector, leading to gradually increasing inflation rates, before stabilising around 1.6% in 2022.

Future spending related to the Recovery and Resilience Facility is not included in this forecast and constitutes an upside risk.

Graph 2.18: **Slovakia - Real GDP growth and contributions**