

REPORT ON MONETARY DEVELOPMENT FOR THE FIRST HALF OF 2004

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INTRODUCTION

Macroeconomic development in Slovakia in the first half of 2004 was influenced by several significant factors. On 1 January 2004 a tax reform came into effect, in the framework of which value-added tax rates were unified at 19% and the rates of income tax for private and legal entities also at 19%. On 1 May 2004 the Slovak Republic became a member of the European Union. Slovakia thus became a participant in Economic and Monetary Union as a member state with derogation. This means that Slovakia acquired the status of a member state with derogation, i.e. through accession to the EU Slovakia accepted the commitment to become, in the future, a member of the Monetary Union. At the same time, the National Bank of Slovakia became a part of the European System of Central Banks (ESCB), with all the rights and obligations that this entails. In connection with accession to the European Union the SR also adopted the Common Agricultural Policy (CAP), which represents a set of economic, financial, legislative and institutional instruments for ensuring a single market in agricultural produce, the aim being to ensure efficiency, stability and financial solidarity in the agricultural sector.

From the aspect of the development of consumer prices, the first half of 2004 was, in accordance with the expectations of the NBS, influenced primarily by domestic cost factors, which were to a significant extent connected with administrative measures in the field of regulated prices and indirect taxes (excise duties and value-added tax) and related secondary cost effects. Administrative measures in June contributed to the rate of year-on-year inflation growth through a share of more than 78% (in December 2003 the figure was 75%). The increase in consumer prices was also partly a consequence of the implementation of the Common Agricultural Policy. At the same time, the year-on-year rate of consumer price growth was influenced also by the basic effect, related to the increase in excise taxes on tobacco, beer and mineral oils in August last year. From the aspect of external factors influencing domestic price development, a main component in the first months of the year was the increase in oil prices in connection with growing worldwide demand. The year-on-year rate of core inflation for June 2004 recorded a 0.7-percentage-point decline in comparison with December 2003 to 2.3%.

In the tradable goods sector the development of prices over the course of the first half year was influenced primarily by volatile development in fuel prices. Prices of tradable goods, excluding fuel prices, throughout the whole period recorded a slowdown in their year-on-year growth. The year-on-year rate of price growth of market services in comparison with last year increased especially in connection with the change in methodology, when fees for compulsory third-party liability motor vehicle insurance were shifted from regulated prices into market services prices. The relatively high rate of price growth for market services in the first half of 2004 was also connected with the realisation of secondary effects of the influence of the growth in regulated prices. In January 2004 regulated prices for electricity, gas, heat, personal bus and railway transport, water and sewerage charges increased. However, in comparison with the previous year lower growth in regulated prices was recorded, due to the smaller scope of their adjustments.

In the field of foreign trade in the first half of the year the current account deficit of the balance of payments increased, in the framework of which the favourable development of the balance of trade was eliminated by a deepening deficit in the balance of revenues and the development in the balance of current transfers. The decline in the foreign trade deficit, in

comparison to the past year, resulted mainly from the higher rate of growth in exports than that of imports. The most significant export commodities included machinery and transport equipment. In imports a change in the structure toward such products as machinery and tools was recorded. In contrast to the preceding year, the import of technological equipment grew markedly for individual sectors of the national economy, where this could have a direct influence on the economy's restructuring with future effects on a growth in exports. In comparison with the favourable development of the trade balance in the first half of 2004 the deficit in the balance of revenues increased in consequence of a growth in revenues paid out to direct investors, as well as the balance of current transfers, influenced by contributions made to the EU budget. In the field of the capital and financial account a growth in foreign direct investment in comparison with the same period last year was recorded, which was connected with an increase in the stakeholdings of foreign investors in the SR. The greatest volume of investments in stakeholdings was, from the aspect of sectoral structure, directed toward industrial production.

The real economy's development in the first half of 2004 was characterised by acceleration in GDP growth. In accordance with the NBS's expectations the structure of the growth was more balanced, as a gradual recovery in domestic demand was seen, in particular in household final consumption as well as capital investment demand. The growth in consumer demand was influenced by a growth in real wages, as well as the realisation of deferred consumption from the previous year. Relatively fast growth of foreign demand continued, the pro-growth influence on GDP of which in the second quarter was moderated by acceleration in the growth in imports. The realised increase in imports was connected to a large extent with capital investment imports.

Current budgetary performance recorded in the first half year a positive development, which was probably influenced both by favourable macroeconomic development as well as by the tax reform. In the framework of public finance, a new system of debt and liquidity management was launched on 1 January 2004 in the form of the Agency for Debt and Liquidity Management (ARDAL). With regard to the founding of ARDAL a new division of activities and responsibilities has been made between the Ministry of Finance of the SR (MF SR), ARDAL, the State Treasury and the National Bank of Slovakia (NBS) pursuant to Act No 575/2001 Coll. on the organisation of the activities of government and the organisation of central state administration. The NBS as the agent of the MF SR is currently commissioned to issue and repay government securities, including revenues on treasury bonds.

The realisation of the NBS's monetary policy in the first half of 2004 took place in an economic environment characterised by an accelerated rate of economic growth, a favourable development of the balance of trade, as well as continuing consolidation of public finance. This, together with the absence of demand-side pressures for an increase in prices and an appreciating Slovak koruna exchange rate, was the reason for a decrease in NBS key interest rates in March, April and June 2004, in total by 1.50 percentage points. In accordance with the process of harmonising the NBS's monetary instruments with the set of monetary instruments of the ECB, the National Bank of Slovakia, with effect from the beginning of 2004, reduced the ratio of minimum required reserves for the banking sector by 1 percentage point from 3% to 2%. The level of the reserve requirement ratio was thus harmonised with that of the eurozone. The basis for calculating the compulsory minimum reserves, their interest accrual and the period of their evaluation remained unchanged.

In the first half of 2004 the volume of liquidity in the banking sector grew, where a significant source of this increase lay in NBS operations on the foreign-exchange market aimed at countering the inappropriate appreciation of the Slovak koruna exchange rate, which was not in accordance with its equilibrium development. The beginning of 2004 saw a strengthening of the Slovak koruna exchange rate, connected primarily with an inflow of short-term capital, which for the first four months of the year exceeded the level of 2003. One of the reasons for this inflow was an attempt to exploit the existing positive interest rate differential, which over the course of the first half-year remained at a relatively high level. At the same time, this was caused also by the expected further appreciation in the exchange rate as a result of foreign investors' upbeat expectations.

By and large, the execution of NBS monetary policy was in line with the forecasts of the NBS Monetary Programme, as well as its update. The development of consumer prices has in recent months continued to be in line with NBS expectations, where no signals in the economy of the potential emergence of demand-side pressures for an increase in inflation have been identified. Current indicators of the real economy indicate continuing positive development in the growth in industrial production and receipts, which has been accompanied by a gradually lessening growth in nominal wages. In the field of foreign trade an increase in the import of technology is predicted, primarily in connection with the realisation of foreign direct investment. In the development of the balance of trade it is therefore possible in the coming period to expect a progressive deepening of the 12-month cumulative deficit. This should be influenced primarily by the lapsing of the favourable influence of the basic effect on the 12-month cumulative deficit in the balance of trade, whereby the longer-term trend of decline in its cumulative deficit would be halted. In connection with the development of the exchange rate the NBS, continuing in accordance with its policy, is prepared to intervene with the aim of ensuring the appropriate development of the exchange rate and eliminating any risk of an excessive strengthening of the Slovak koruna.

As at 30 June 2004 eighteen banks, three branches of foreign banks, nine subjects – providers of free cross-border banking services and seven representative offices of foreign banks operated in the Slovak banking sector. As at 30.6.2004 the banks reported a net profit of SKK 6.9 billion. In a year-on-year comparison this represents a growth of SKK 3.7 billion (11.9%). No bank reported a loss as its economic result for the current period to 30.6.2004 (likewise as at 30.6.2003 no bank had a loss as an economic result). In connection with the Slovak Republic's Treaty of Accession to the European Union, entering into force on 1 May 2004, the provisions of Articles 11 to 20 of Act No 483/2001 Coll. on banks and on the amendment and supplementing of certain acts entered into force, on the basis of which credit institutions seated in the European Economic Area may perform banking activities (other than providing mortgage loans under Article 67(1) of the Act on Banks and the performance of the function of a depository under the Act on Collective Investment) in the territory of the Slovak Republic without a banking licence granted by the National Bank of Slovakia, provided such a banking licence has been granted to them in their domestic country.

1. ECONOMIC DEVELOPMENT

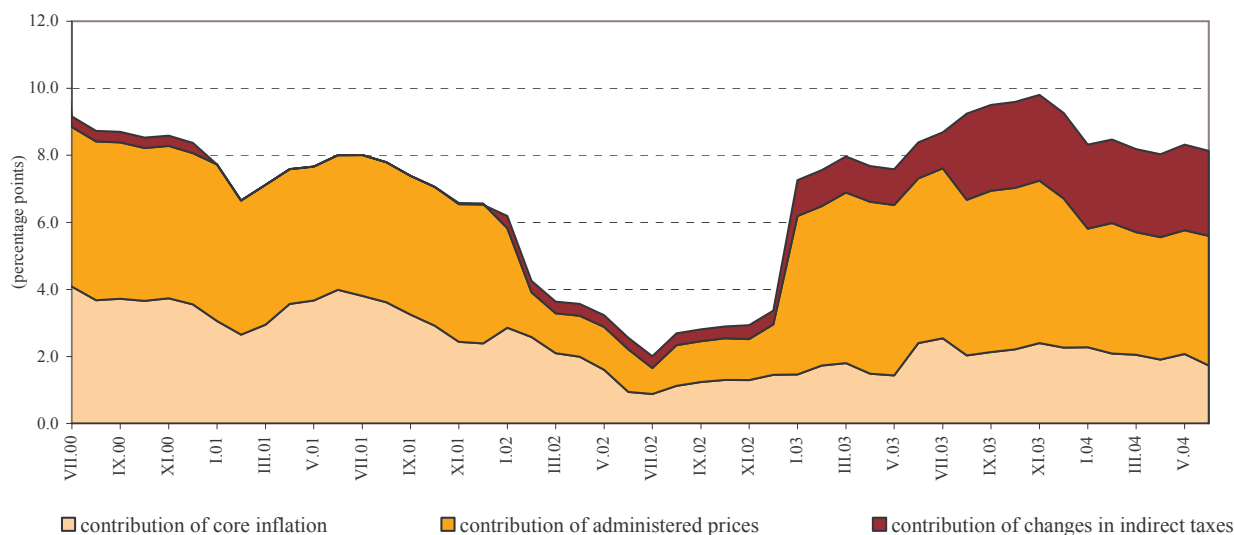
1.1 Price Development

Consumer prices

The year-on-year rate of inflation as measured by the consumer price index in June 2004 reached 8.1%, which compared to December 2003 (9.3%) represents a decline of 1.2 percentage points. The sector of regulated prices contributed to the year-on-year increase in consumer prices by 3.86 percentage points, the impact of changes in indirect taxes was 2.54 percentage points, and core inflation contributed 1.73 percentage points. The average annual rate of inflation in the first half of 2004 reached 8.2% (against 7.7% in the same period of the preceding year).

From the aspect of the development of inflation, the first half of 2004 was determined primarily by domestic cost factors, which were to a significant extent connected with administrative measures in the field of regulated prices and indirect taxes (excise duties and value-added tax). External factors included a growth in oil prices in connection with growing worldwide demand, the situation in Iraq, Venezuela, Nigeria and Russia. On the other hand the strengthening of the Slovak koruna exchange rate had a dampening effect on price development, primarily in the tradable sector.

Structure of Annual Inflation



Consumer prices – year-on-year growth

Consumer prices – year-on-year growth

	Constant weights in %	XII-03	I-04	II-04	III-04	IV-04	V-04	VI-04
Total	100.0	9.3	8.3	8.5	8.2	8.0	8.3	8.1
Regulated prices in %	19.9	18.7	14.4	15.8	14.7	14.7	14.9	15.7
<i>share in total in percentage points</i>		4.45	3.54	3.89	3.65	3.65	3.69	3.86
Impact of changes in indirect taxes on non-regulated prices – share of total in percentage points		2.54	2.51	2.49	2.48	2.48	2.55	2.54
Core inflation in %	80.1	3.0	3.1	2.8	2.8	2.6	2.8	2.3
<i>share of total in percentage points</i>		2.27	2.27	2.09	2.05	1.91	2.08	1.73
of which: Food prices in %	21.4	2.7	2.3	1.9	1.6	0.7	0.7	0.5
<i>share of total in percentage points</i>		0.54	0.44	0.37	0.31	0.14	0.13	0.10
Tradable goods in % /1	39.6	1.2	1.0	0.5	0.7	1.1	1.6	0.7
<i>share of total in percentage points</i>		0.44	0.37	0.17	0.25	0.39	0.57	0.24
Market services in % /1	19.1	7.0	7.7	8.2	7.8	7.2	7.2	7.3
<i>share of total in percentage points</i>		1.30	1.46	1.55	1.49	1.38	1.38	1.40
Net inflation (excl. the impact of changes in indirect taxes)	58.7	3.1	3.3	3.1	3.2	3.2	3.6	3.0
<i>share of total in percentage points</i>		1.73	1.83	1.72	1.74	1.77	1.95	1.63

Source: Statistical Office of the Slovak Republic (SO SR)

/1 Calculations made by the NBS based on the SO SR data

Net inflation – includes price increases in tradable goods (excluding foods) and market services.

Core inflation

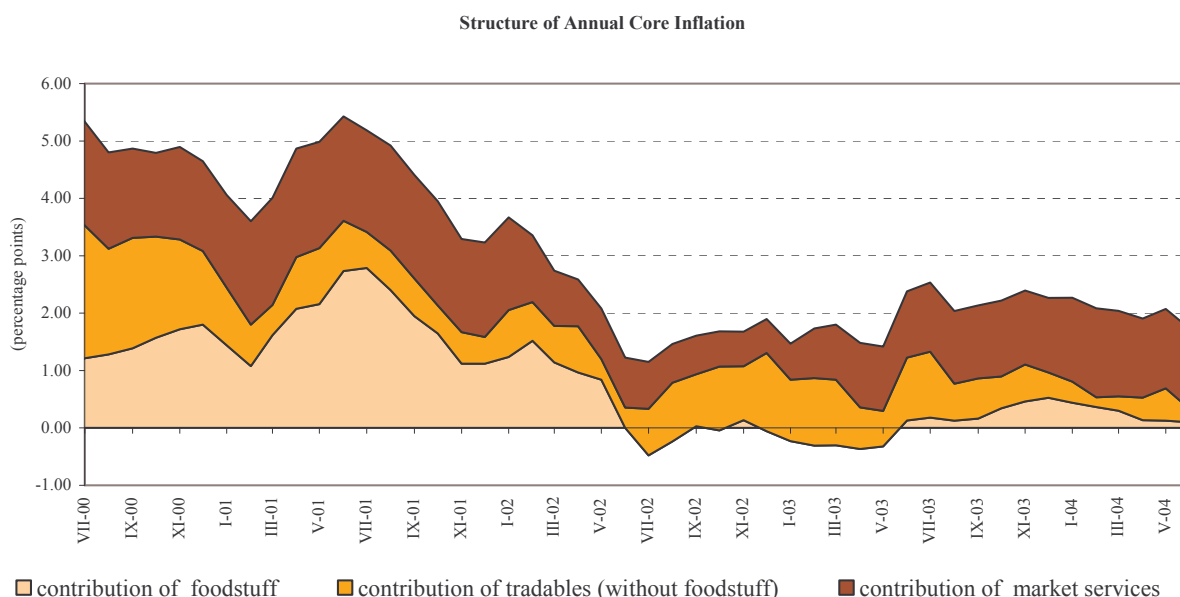
The year-on-year rate of core inflation in June 2004 fell by 0.7 percentage points against December 2003 to 2.3%. Price development in its individual segments was differentiated.

The year-on-year rate of food prices over the course of the first half of the year gradually fell, in connection with the slowdown in year-on-year growth, or the year-on-year fall in the prices of agricultural primary producers in crop and animal production. The same tendency was recorded in prices of processed and un-processed foods.

Prices in the tradable sector in June increased on a year-on-year basis by 0.7% (in December 2003 by 1.2%). The development over the course of the first half of the year was uneven and reflected the volatile development of fuel prices. These on a year-on-year basis in the first three months of the year recorded a deepening decline. Conversely, in the following three months - fuel prices grew on a year-on-year basis and their growth accelerated. In June 2004 - fuel prices had grown on a year-on-year basis by 12.2%. The prices of tradable goods excluding fuel prices recorded a slowdown in their year-on-year growth. This year-on-year low price growth of tradable goods in June was caused in part by an increase in cigarette prices in the same period of the preceding year (in consequence of growing demand prior to the expected August increase in excise duties).

The year-on-year price growth in market services accelerated slightly from 7.0% in December 2003 to 7.3% in June 2004. The highest level was recorded in February (8.2%), where over the course of the whole first half year it moved above 7%. The year-on-year rate of growth in prices of market services, in comparison with the preceding year, increased in particular in connection with the change in methodology, when charges for motor third-party liability insurance were shifted from regulated prices to market services. Its acceleration was also

partially a result of administrative measures in the form of changes of regulated prices and indirect taxes and the related secondary effects.



Regulated prices and indirect taxes

The year-on-year rate of growth in regulated prices in June 2004 slowed to 15.7%, where in December of the preceding year its growth reached 18.7%. The regulated prices sector was thus the most significant component of price growth, where in June its share in the year-on-year rate of inflation represented more than 47% (in December 2003 this figure stood at 48%).

The lower rate of growth in regulated prices was influenced by the smaller scope of their adjustments in comparison with those of 2003. In January regulated prices for electricity, gas, heat, personal bus and railway transport, water and sewerage charges were increased. Catering prices in school canteens and accommodation charges at university residences were also raised. In further months rent prices rose in state- and municipal-owned apartments, as did prices for urban public transport and prices in the field of healthcare.

Since January 2004 the rates of VAT were unified at 19% (from 20% to 19% and from 14% to 19%). The year-on-year rate of growth in consumer prices was affected also by the increase in excise duties on tobacco, beer and mineral oils from August last year. The contribution of the indirect taxes to the growth in consumer prices in the first six months of this year represented 2.54 percentage points (similarly as in December 2003).

Administrative measures in total (changes to regulated prices and indirect taxes) in June contributed more than 78% to the year-on-year rate of inflation (in December the figure was 75%).

Producer prices

Industrial producer prices for the domestic market

Industrial producer prices in the first half of 2004 were influenced both from the aspect of

costs as well as from the demand side, where the decisive role was played by cost factors. The influence of domestic cost factors in the form of an increase in energy prices was significantly lower than the previous year, when electricity, gas, steam and hot water prices grew on a year-on-year basis by 3.8%. This fact was reflected also in the development of prices of manufactured products, the growth in which compared to the first half of 2003 was 1 percentage point lower at 1.9%. Raw minerals prices increased the most, by 7.9%.

Development of producer prices

Average price index (same period last year = 100)	First half year	
	2003	2004
Industrial producer prices (domestic market)	108.4	102.8
- prices of manufactured products	102.9	101.9
- prices of raw minerals	104.0	107.9
- prices of electricity, gas, steam, and hot water	117.2	103.8
Industrial producer prices (export)	99.7	98.0
- prices of manufactured products	99.7	98.0
Prices of construction work	105.2	105.7
Prices of construction materials	103.7	103.7
Prices of agricultural products	93.0	102.0
- prices of crop production	95.1	115.1
- prices of animal production	92.6	100.0

The price growth of manufactured products was affected, besides domestic energy costs, also by the high price of oil on world markets. On the other hand, the depreciation of the American dollar against the Slovak koruna to a certain extent dampened the pro-inflationary effect of the high oil price. Owing to the above development, prices rose in particular in those sectors dealing with the processing of energies from raw materials, where the prices of refined petroleum products grew most markedly (by 5.8%). Prices of basic metals and fabricated metal products also grew faster (3.1%) than the average for the sector, which was probably connected with a period of expansion on world steel markets. Besides the high demand for steel, domestic producer prices were also influenced by the higher prices of certain input materials (e.g. scrap iron, coke), which developed in line with steel prices.

Within the manufactured products the prices of food products, beverages and tobacco recorded relatively fast growth (by 3.0%). With regard to the situation in agricultural primary production prices of mill products, starch and starch products, dairy products and beverages grew notably. Conversely, a dampening component were prices for meat and meat products, which fell by 3.1%.

Industrial producer prices for export

Prices of manufactured products intended for export in the first half of 2004 recorded a decline by 2.0%, which was influenced by lower prices in most sectors, in particular however prices of refined petroleum products (a fall of 8.8%), chemical products (a fall of 4.5%) and transport equipment (a fall of 2.3%). Prices of metals and fabricated metal products and textile products prices were higher than those in the same period last year.

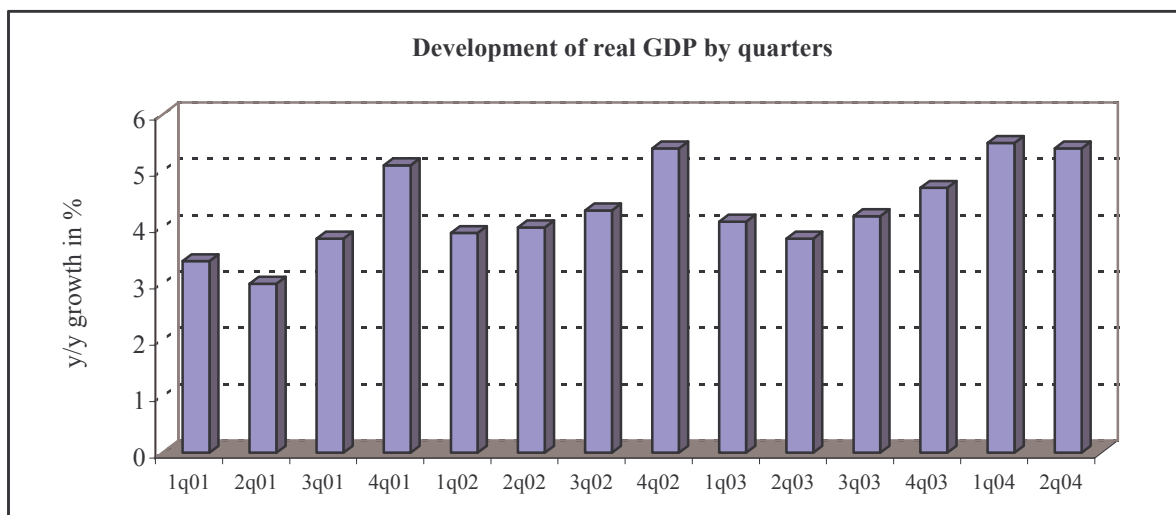
Agricultural products prices

Prices of farming products in the first half of 2004 were, on a year-on-year basis, 2.0% higher, where prices of crop production grew by 15.1%, whereas prices of animal production remained unchanged. A contrary development was seen in the development of prices of animal production, where in particular prices of pigs for slaughter (as a result of low demand on the domestic market) and cattle for slaughter fell, on the other hand prices of milk, eggs and poultry for slaughter were higher than the year before. Growth in the prices of crop production was affected by higher prices in all types monitored. The prices of potatoes and cereals grew most markedly (by 21.5% and by 16.7% respectively), where in the prices of cereals the consequences of poor harvest under the influence of adverse weather in 2003 was reflected.

1.2 Gross Domestic Product

Gross domestic product

According to preliminary data from the Statistical Office of the Slovak Republic gross domestic product in the first half of 2004 grew on a year-on-year basis by 5.4% at constant prices, whereby the economy achieved growth 1.5 percentage points faster than in the first half of 2003. This dynamic and even economic growth in the first half of 2004 (5.5% in the first quarter, 5.4% in the second quarter) was the consequence of both domestic and foreign demand. Domestic supply reacted to the growth in aggregate demand by increased value-added creation. The volume of GDP created at current prices stood at SKK 636.6 billion, which was 11.4% more than the year before.



Demand

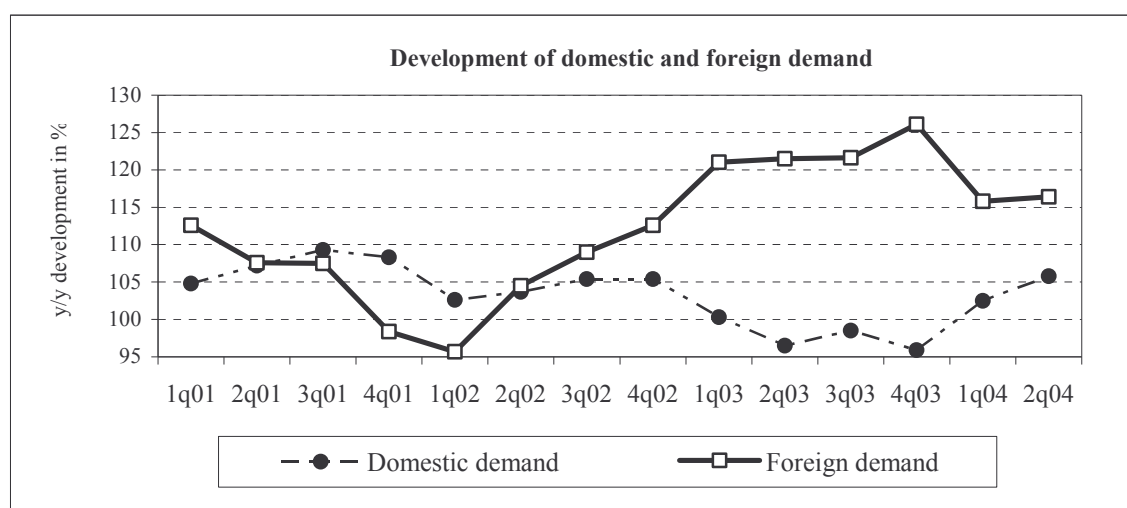
From the aspect of use, the growth in GDP was influenced by domestic (69%) as well as foreign demand (31%), where in the first quarter the pro-growth influence of foreign demand was more significant, and which in the following quarter moderated and was replaced by a higher contribution of domestic demand. Besides the recovery in domestic demand (growth of 4.2% at constant prices) foreign demand also maintained a relatively high growth rate, where

the export of goods and services grew on a year-on-year basis by 16.1% in the first half of 2004.

Development of gross domestic product according to use (index, same period last yr.=100, 1995 prices)

Indicator	<u>1.-2.Q 03</u>	<u>2003</u>	<u>1.Q 04</u>	<u>2.Q 04</u>	<u>1.-2.Q 04</u>
	<u>1.-2.Q 02</u>	<u>2002</u>	<u>1.Q 03</u>	<u>2.Q 03</u>	<u>1.-2.Q 03</u>
Gross domestic product	103.9	104.2	105.5	105.4	105.4
Domestic demand	98.3	97.7	102.5	105.8	104.2
Final consumption	100.8	100.5	101.8	102.8	102.3
Final consumption of households	101.2	99.4	103.0	102.8	102.9
Final consump. of general government.*	99.1	102.9	97.7	102.4	100.2
Non-profit institutions serving for households	110.4	111.9	104.2	105.8	105.0
Gross capital formation	92.2	90.3	104.4	113.8	109.4
Gross fixed capital formation	98.9	98.8	100.9	103.5	102.4
Export of goods and services	121.2	122.6	115.8	116.4	116.1
Import of goods and services	114.7	113.8	112.0	117.0	114.6

* preliminary data, estimate of the Statistical Office of the SR

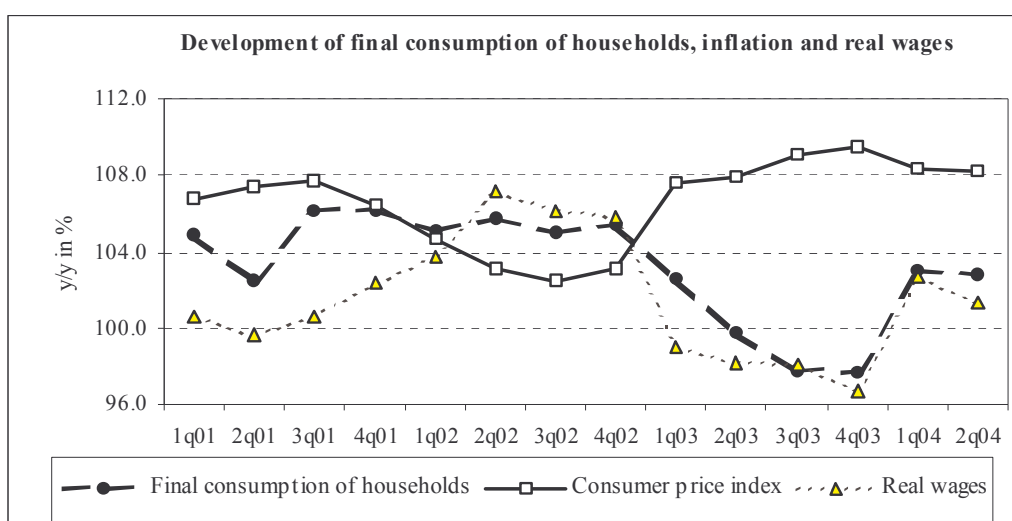


The recovery in domestic demand in the first half of 2004, following its temporary decrease in 2003, occurred primarily through a growth in gross capital formation and the final consumption of households. While in the first quarter only an increase in private consumption was significant, in the second quarter the growth in domestic demand accelerated in particular under the influence of investment.

Final consumption at constant prices grew on a year-on-year basis by 2.3%, where its development was positively influenced by the final consumption of households and non-profit institutions serving for households, whereas the final consumption of general government remained at the same level as the previous year. The development of the final consumption of general government in the first half of 2004 was probably influenced by the fiscal discipline of institutions financed via the state budget, as well as the possible more efficient use of resources. The year-on-year growth in consumption by non-profit institutions serving for households (5.0% at constant prices) and the unchanged level of public consumption is probably connected with the transformation of some subjects of the public sector into organisations of a non-profit nature that perform services for households.

Final consumption of households in the first half of 2004 achieved year-on-year growth of 2.9% at constant prices, representing a year-on-year increase in the rate of growth by 1.7

percentage points. The relatively even growth of private consumption in both quarters was connected with an increase in real wages, where the stronger purchasing power of demand was supported also by the efforts of a part of the population to satisfy their needs from the period of declining real wages. Changes to income taxation and lower interest rates on a year-on-year basis probably contributed to the growth in private consumption. Also a wide range of consumer loans and various forms of hire-purchase were available to the households. In consequence of the adjustments to regulated prices, expenditures on housing, water, electricity, gas and other fuels increased, and which together with expenditures on foods and non-alcoholic beverages constituted half (48.8%) of final household consumption. From the aspect of the structure of private consumption the highest rate of growth (36.4%) was seen in expenditures on health, where their share represents approx. 2% of total consumer expenditure of households.



Gross capital formation (including changes in inventories) grew on a year-on-year basis by 9.4% at constant prices. This development reflected primarily the growth in inventories by SKK 11.6 billion, as well as a higher level of fixed investment (a growth of 2.4%), which grew for the first time since 2001.

In terms of distribution by sectors, gross fixed capital formation grew proportionally in all sectors, with the exception of non-profit institutions and households, whose investment activity in the first half of 2004 did not reach the level of the previous year. The largest volume of investment resources was realised by non-financial corporations, primarily in the form of new fixed asset formation.

In terms of classification by production, the contributions made to overall growth in gross fixed capital formation came in the form of investments in machinery, which grew on a year-on-year basis by 5.4%, whereas investments in constructions, primarily in consequence of the lower allocation of investment resources into other structures (structures of an infrastructure nature), fell by 4.4%. In the framework of gross fixed capital formation in the field of machinery, the investment activity of investors in metal products and machines grew most (by 7.2%), where investment in transport equipment reached the same level at constant prices as in the first half of 2003.

Structure of gross fixed capital formation in the first half of 2004*

	Gross fixed capital formation (SKK million.)	Share (%)		Index
		1.-2.Q 2003	1.-2.Q 2004	$\frac{1.-2.Q 2004}{1.-2.Q 2003}$
SR economy total	153 999	100.0	100.0	102.4
<i>of which by production classification:</i>				
Structures	49 297	34.4	32.0	95.6
of which: residential buildings	8 653	5.7	5.6	98.3
other structures	40 644	28.7	26.4	95.0
Machinery	95 045	59.4	61.7	105.4
of which: metal products and machines	72 460	45.0	47.1	107.2
transportation equipment	22 585	14.4	14.7	100.1
<i>of which by sectors:</i>				
Non-financial corporations	98 746	63.6	64.1	103.2
Financial corporations	20 743	13.6	13.5	101.6
General government	11 376	7.3	7.4	103.6
Households	22 914	15.4	14.9	98.8
Non-profit institutions	220	0.1	0.1	99.3

* volume and share at current prices, index at constant prices

From the aspect of financing investment demand in the first half of 2004 the share of domestic sources in capital financing increased. The gap between gross domestic savings – unconsumed part of GDP and gross investments narrowed, where with regard to the higher year-on-year rate of savings in the national economy the savings-to-investment ratio reached 97.4%. This creates room for an acceleration in investment activity also from domestic sources in the coming period.

Development of investment and savings (%)

	1 st half of 2003	2003	1 st half of 2004
<i>Constant prices of 1995</i>			
Savings rate ¹	29.4	27.3	31.5
Gross investment rate ²	25.9	24.6	26.9
Fixed investment rate ³	24.7	25.4	23.9
Savings-to-investment ratio ⁴	113.6	111.1	117.4
<i>current prices</i>			
Savings rate ¹	24.6	23.3	26.0
Gross investment rate ²	26.8	25.3	26.7
Fixed investment rate ³	25.5	25.8	24.2
Rate of investment coverage by savings ⁴	91.8	92.1	97.4

¹ a ratio of gross domestic savings (GDP minus total final consumption) to GDP

² a ratio of gross capital formation to GDP

³ a ratio of gross fixed capital formation to GDP

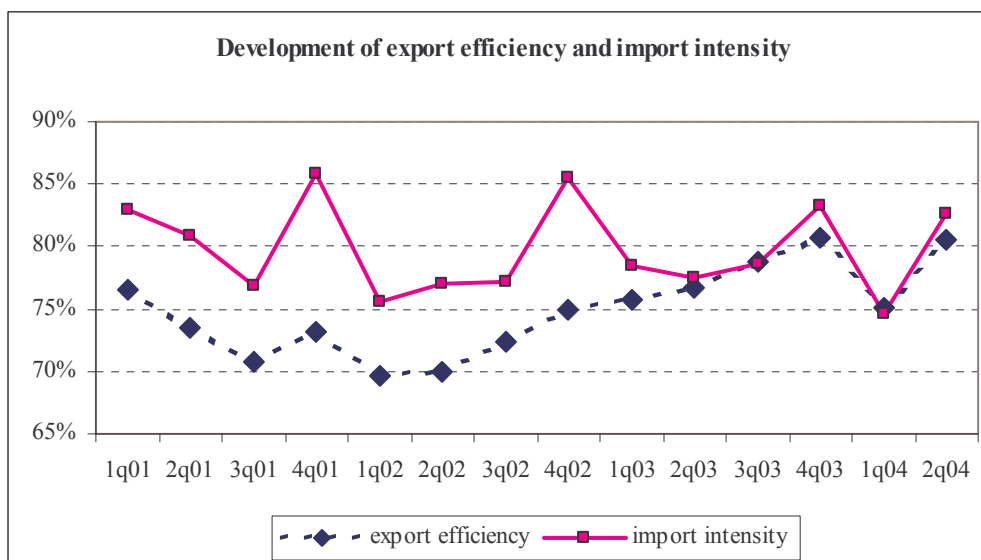
⁴ a ratio of gross domestic savings and gross investments

Net exports

The export and import of goods and services in the first half of 2004 achieved double-digit rates of growth, where the higher rate of growth in exports than imports was reflected in the year-on-year improvement in the trade balance. The net export at current prices reached a deficit of SKK 5.5 billion, which was approximately SKK 4.5 billion better than the results for the preceding year. After taking into account the negative year-on-year growths of the trade balance deflators, primarily under the influence of the exchange rate development, the net export at constant prices recorded a surplus in the amount of SKK 15.8 billion (in the first half of 2003 a surplus of SKK 9.4 billion).

The improvement in the trade balance of goods and services, including the statistical estimate of the grey economy, was a result of the mutual relationship of exports and imports, where the export of goods and services at constant prices grew relatively faster (16.1%) than imports (14.6%). The development in individual quarters was varied. While in the first quarter the difference in the year-on-year rates of growth of exports and imports was approximately 4 percentage points, in the second quarter the volume of imported goods and services increased, whereby the rate of growth of imports had overtaken that of exports.

The relatively high export efficiency of the Slovak economy has been maintained even despite the high comparison base of the year before, where the volume of exported goods and services reached 77.9% of GDP at current prices. The higher level of export efficiency brought about, in consequence of Slovak industry's export sectors' dependence on imports, a growth in import intensity, which reached 78.8%. The Slovak economy's openness, measured by the share of exports and imports of goods and services in GDP, increased slightly in the first half of 2004, reaching 156.7% (154.2% for the previous year).

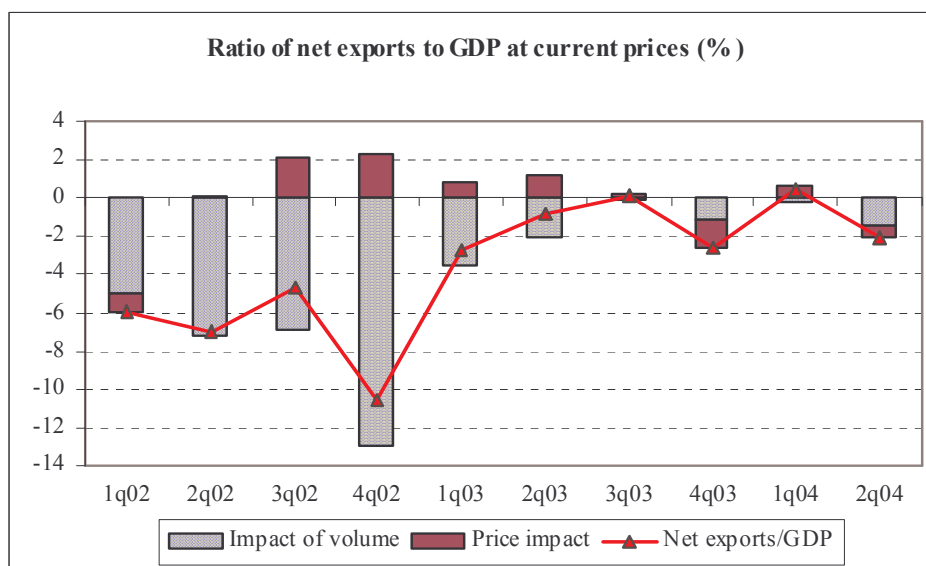


Besides the volume of exported and imported goods and services, the development of the net export of goods and services at current prices may also be influenced by the development of import and export prices, which take account of changes in the exchange rate. While price development a year ago ameliorated the net export deficit ensuing from the relationship of the exported and imported volumes of goods and services, in the first half of 2004 price changes did not result in a lower net export deficit at current prices.

Contributions of price and volume to the development of exports and imports (percentage points)

	2003		2004		
	1.-2.Q	year	1.Q	2.Q	1.-2.Q
Export of goods and services (y/y growth in %, current prices)	18.1	18.5	12.4	15.2	13.9
Contribution of volume	21.2	22.6	15.8	16.4	16.1
Contribution of price	-3.1	-4.1	-3.4	-1.2	-2.2
Import of goods and services (y/y growth in %, current prices)	10.6	9.9	7.8	16.9	12.6
Contribution of volume	14.7	13.8	12.0	17.0	14.6
Contribution of price	-4.1	-3.9	-4.2	0.0	-2.1
Ratio of net export to GDP (% ratio, current prices)	-1.7	-1.5	0.5	-2.1	-0.9
Contribution of volume	-2.8	-1.7	-0.2	-1.4	-0.8
Contribution of price	1.0	0.2	0.7	-0.7	0.0

discrepancies in sub-totals are due to rounding



In terms of structure of GDP, both domestic demand as well as net export operated in a pro-growth manner. The contribution of the positive balance of goods and services (at constant prices) represented 1.7 percentage points. Domestic demand through its contribution of 4.1 percentage points accelerated the year-on-year rate of growth in real GDP to 5.4%. As regards domestic demand, both the positive contribution of gross capital formation and private consumption operated together.

Contributions to GDP growth*

(percentage points, 1995 prices)

Indicator	1.-2.Q 03	2003	1.Q 04	2.Q 04	1.-2.Q 04
	1.-2.Q 02	2002	1.Q 03	2.Q 03	1.-2.Q 03
Gross domestic product	3.9	4.2	5.5	5.4	5.4
Domestic demand	-1.7	-2.4	2.4	5.6	4.1
Final consumption	0.5	0.4	1.3	1.9	1.6
Final consumption of households	0.6	-0.3	1.6	1.4	1.5
Final consumption of general government.	-0.2	0.6	-0.4	0.4	0.0
Final consumption of non-profit institutions serving for households	0.1	0.1	0.0	0.1	0.0
Gross capital formation	-2.3	-2.7	1.1	3.6	2.4
Gross fixed capital formation	-0.3	-0.3	0.2	0.9	0.6
Change in inventories	-2.0	-2.4	0.9	2.7	1.9
Net export	4.7	6.4	3.6	0.0	1.7
Export of goods and services	16.3	17.8	13.9	14.9	14.4
Import of goods and services	11.6	11.4	10.3	14.9	12.7
Statistical discrepancy	1.0	0.2	-0.5	-0.1	-0.3

* calculated from GDP figures in SKK mill., the contribution of the import of goods and services reduces the net export and GDP, differences in sub-totals are due to rounding

Supply

GDP growth from the production aspect was connected with the higher creation of value added in financial intermediation (by 19.5% at constant prices), other social services (by 7.9%) and industry (by 6.7%). Creation of value added fell most significantly in non-market service sectors in which restructuring processes are underway (healthcare, education, public administration and defence). A decline was recorded also by some market service sectors (hotels and restaurants, transport, storage, posts and communication).

Development of gross domestic product by sector

(index, same period last year=100, 1995 prices)

Branch of economic activity	1.-2.Q 03	2003	1.Q 04	2.Q 04	1.-2.Q 04
	1.-2.Q 02	2002	1.Q 03	2.Q 03	1.-2.Q 03
GDP	103.9	104.2	105.5	105.4	105.4
of which:					
Agriculture, hunting, fishing and forestry	109.2	104.4	99.8	111.4	105.7
Industry in total	110.5	109.5	106.0	107.4	106.7
Mining and quarrying	80.6	85.7	90.6	103.3	96.8
Manufacturing	107.5	106.6	101.9	108.3	105.2
Electricity, gas and water supply	149.8	150.7	132.6	100.5	118.9
Construction	106.3	106.9	108.4	103.4	105.8
Services in total	104.6	103.2	98.8	101.9	100.4
Wholesale, retail trade, repairs	101.3	100.1	105.4	105.8	105.6
Hotels & restaurants	73.8	78.7	91.1	105.9	99.2
Transport, storage, communication	104.7	96.2	92.9	99.4	96.1
Financial intermediation	115.8	129.4	130.0	109.5	119.5
Real estate, renting, & business activities	102.1	99.8	96.8	105.2	101.0
Public administration., defence, social security	113.8	104.2	94.2	92.6	93.3
Education	116.0	117.3	92.0	92.1	92.0
Health & social work	100.5	101.7	76.9	83.8	80.3
Other community, social and personal services	94.9	101.9	92.8	126.0	107.9
Other ¹	77.6	93.3	171.5	121.1	141.1

¹ value-added tax, excise duty, tax on imports less subsidies subventions and imputed production of banking services

The total increase in GDP resulted primarily from contributions from the sectors of industry, construction and agriculture, in which value added growth exceeded the overall performance

of the economy. The dynamic rate of growth in industry was supported by fast growth in value added in sector of electricity, gas and water supply (in the first quarter). The development in this sector was connected primarily with the energy provision for the economy's accelerating production performance, including production for export, as well as with an expansion in the range of services by economic subjects in the post-privatisation period. Significant growth was recorded in the manufacture of chemical, rubber and plastic and the manufacture of machinery, electrical and transport equipment as a consequence of intensive foreign demand.

The production of foods, beverages and tobacco fell almost by half, probably in connection with insufficient adaptation to European standards in the agro-foods industry. The current growth in value added in agriculture and the recovery in consumer demand are signals that a significant part of domestic production in the food-processing industry is saturated by production from imports.

The relatively stabilised position of construction in the Slovak economy was slightly disrupted by a slowdown in value added growth in the second quarter. A part of the construction production in this period was manifested by a growth in unfinished production in the form of inventories.

Within the sectors focused on providing services, financial intermediation and the sector of other social services (waste management, membership organisations, recreation, cultural and sports activities) contributed particularly to GDP creation. The growth in value added in financial intermediation is connected with an improvement in the efficiency parameters of the banking sector following the restructuring process. Within services value added also grew in wholesale, retail trade and the repair of vehicles and personal goods. The renewed growth in value added in this sector was a reaction to the recovery of the consumer demand of households. Other sectors of market and non-market services did not reach the level of the preceding year.

GDP growth, besides value added creation recorded in the sectors, was positively influenced by the higher collection of taxes on products (by 41.1%). The share of taxes (value-added tax, excise duty, tax on imports, excluding subsidies and the imputed production of banking services) in GDP in consequence of the tax reform increased from 6.9% in the first half of the preceding year to 9.3% in the first half of this year.

1.3 Labour Market

Wages

The average monthly nominal wage of an employee in the SR economy in the first half of 2004, at a relatively dynamic growth (of 10.3%), reached SKK 15 008. Its growth was 4.1 percentage points faster than in the previous year. Over the course of the half year the rate of growth of nominal wages slowed, where their growth of 11.2% in the first quarter moderated to 9.6% in the second quarter.

Nominal wages were higher in all sectors of the economy (apart from fishing, in which only 75 persons are employed) than in the first half of 2003. The fastest year-on-year growth in nominal wages was seen in the financial intermediation sector (15.5%), transport, posts and

telecommunications (14.6%) and real estate, renting and business activities (14.3%). Conversely, the slowest growth was in health and social work (2.6%).

From the aspect of the form of ownership, the most significant year-on-year growth in average monthly nominal wages was recorded in the business sector, in enterprises with 20 and more employees (12.9%), whereas in budgetary organisations growth stood at 8.3% and in -subsidised organisations 4.6%.

Real wages grew on a year-on-year basis by 1.9%, while in the same period last year they fell by 1.4%. Their development was influenced in a pro-growth manner by the growth in nominal wages, whereas the growth in average consumer prices (the rate of growth against the first half of 2003 accelerated by 0.5 percentage points to 8.2%) had a dampening effect on real wages.

An increase in real wages was recorded in the prevailing majority of sectors. A year-on-year decline was reported only in the health and social work (5.2%), hotels and restaurants (2%) and education (1.7%).

Despite the relatively dynamic growth of nominal wages, the growth in labour productivity at current prices kept ahead of the growth in nominal wages by 1.5 percentage points, where labour productivity (GDP per employee in the economy, according to statistical reporting) nominally grew by 11.8%. At constant prices labour productivity increased by 5.8% and surpassed the growth in real wages by 3.9-percentage-points. From the above it is clear that the growth in wages was covered by labour productivity growth and did not create inflationary pressures.

Development of average monthly wages and labour productivity in the SR economy
(index, same period last year =100)

	2003		2004		
	1 st half year	year	1.Q	2.Q	1 st half year
Nominal wage (SKK)	13 602	14 365	14 541	15 472	15 008
Nominal wage (index)	106.2	106.3	111.2	109.6	110.3
Real wage	98.6	98.0	102.7	101.3	101.9
Labour productivity, current prices	107.0	108.2	113.2	110.5	111.8
Labour productivity, constant prices	102.8	103.4	105.5	106.1	105.8
Real labour productivity – real wage (percentage points)	4.2	5.4	2.8	4.8	3.9
<i>Consumer prices (average for period)</i>	<i>107.7</i>	<i>108.5</i>	<i>108.3</i>	<i>108.2</i>	<i>108.2</i>

The development of labour productivity may also be assessed positively at the sectoral level, where in nominal terms year-on-year growth was recorded in all sectors, in real terms a decline was recorded only in the sector transport, storage communication and in the sector real-estate, renting and business activities.

Development of labour productivity and wages by selected sectors

In 1st half of 2004

(index, same period last year =100)

	Nominal		Real	
	labour productivity	wage	labour productivity	wage
SR economy total	111.8	110.3	105.8	101.9
of which				
Agriculture, hunting, fishing & forestry	120.0	110.7	118.9	102.3
Industry	106.7	109.5	107.3	101.2
mining and quarrying	116.2	107.4	107.4	99.3
manufacturing	103.4	109.4	105.1	101.1
electricity, gas and water supply	123.8	112.6	126.1	104.1
Construction	108.5	108.4	102.6	100.2
Wholesale, retail trade, repairs	109.8	110.5	106.1	102.1
Transport, storage, communication	110.1	114.6	98.4	105.9
Financial intermediation	121.5	115.5	116.8	106.7
Real-estate, renting and business activities	107.9	114.3	98.2	105.6

Source: Calculations made by the NBS based on the Statistical Office of the SR

A comparison of the year-on-year development of real labour productivity and real wages in the first half of this year shows that the growth in labour productivity outstripped the growth in wages in all productive sectors, and of market services in the sectors wholesale, retail, repairs, financial intermediation, whereas in the sector transport, storage, communication and in the sector real estate, renting and business activities, despite a decline in labour productivity, real wages recorded relatively dynamic growth. The significant advance of the growth in real labour productivity over the growth in real wages in the sectors of the electricity, gas and water supply (22 percentage points) and financial intermediation (10.1 percentage points) was influenced in particular by the high year-on-year growth in GDP in these sectors.

Household incomes and expenditures

According to preliminary data from the Statistical Office of the SR current household incomes in the first half of 2004 reached SKK 489 billion at a year-on-year nominal growth of 7.4% (falling in real terms by 0.7%). The rate of their growth was the same as in the first half of 2003. The volume of current household expenditures (expenditures which households pay to other sectors and do not directly consume themselves) reached SKK 119.4 billion, 1.4% more than in the previous year (a real decline of 6.3%). In comparison with the first half of 2003 their rate of growth slowed by 5.4 percentage points.

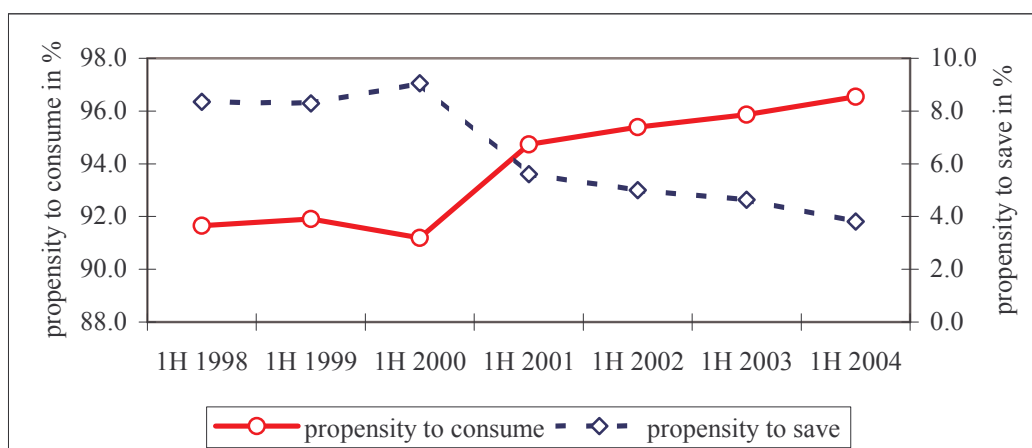
The development of current incomes was influenced in a pro-growth manner mainly by the growth in compensation of employee (8.3%) and the gross mixed income (8.8%), whereas the growth in social incomes as well as current income transfers slowed and property income (similarly as in the preceding year) fell. Property income result from the ownership of financial assets, i.e. deposits, bonds, etc., or from the ownership of land, underground resources, etc. that the owner has gained, if they have been made available to another institutional unit.

The year-on-year slowdown in growth in current expenditures was influenced in particular by the decline in current taxes on incomes and wealth (by 7.2%, compared to almost 6% in the same period of preceding year) and low growth in social contributions (by 1.1%, compared to 8.3% for the year before). The development of these items was probably influenced by new tax and social laws, as well as the fall in employment.

Development and distribution of gross disposable household income
(index, same period last year =100, current prices)

	2003		2004		
	1 st half year	year	1.Q	2.Q	1 st half year
Gross disposable income	107.5	106.2	109.1	109.9	109.5
Final consumption of households	108.7	107.1	110.5	110.1	110.3
Gross savings of households	90.8	96.1	94.2	101.2	90.1
Share of gross savings in gross disposable income in %	7.5	6.7	3.7	4.0	3.8

Following the settlement of current expenditures from current incomes, households were left with a gross disposable income of SKK 369.7 billion for other uses, which represented a year-on-year growth of 9.5% (compared to 7.5% for the year before). Households used 96.5% for final consumption (0.6% more than in the first half of 2003), the remainder was directed into gross savings (besides the deposits of households and small entrepreneurs, activities connected with purchasing tangible and intangible investments and additional pension insurance are also included). Faster growth of final consumption of households compared to the growth in current incomes was resulted in a year-on-year decline in the gross savings of households (by almost 10%) and subsequently also in a reduction in the rate of gross savings from 4.6% in the first half of 2003 to 3.8% in the first half of this year. The trend of decline in the propensity to save thus continued also this year.



Employment and unemployment

The trend of decline in employment, recorded in the first quarter of 2004, continued also in the second quarter, which was subsequently reflected also in the overall development for the first half year of 2004. According to the Labour force sample survey (LFSS), in the first half of 2004 on average 2 140.4 thousand persons worked in the SR economy, which in comparison with the same period last year represents a fall of 0.5%. This trend is confirmed also by data on the development of employment according to statistical reporting, which, on a year-on-year basis, was 0.4% lower.

Development of employment and unemployment	(average for the period)				
	2003		2004		
	1 st half year	year	1.Q	2.Q	1 st half year
Employees in the SR economy (according to statistical reporting) in thousand persons	2 016.5	2 025.0	1 996.6	2 022.1	2 009.4
index (same period last year=100)	101.2	100.8	100.0	99.3	99.6
Persons in employment according to the LFSS in thousand persons	2 150.5	2 164.6	2 128.8	2 151.9	2 140.4
index (same period last year=100)	101.9	101.8	99.9	99.2	99.5
Unemployment according to LFSS in thousand persons	464.8	459.2	511.5	489.4	500.5
index (same period last year=100)	93.4	94.3	106.0	109.5	107.7
Unemployment rate according to LFSS in %	17.7	17.4	19.3	18.5	18.9

The development of employment documents the fact that the dynamic economic growth is not accompanied by a sufficient supply of new job opportunities on the labour market. From the aspect of sectoral classification, in the first half of 2004 the decline in employment continued in particular in agriculture, transport, storage, communication, as well as education. The level of employment did not reach that of a year ago in healthcare, manufacturing and trade. On the other hand, employment developed favourably in particular in other community, social and personal services, construction, real estate, renting and business activities and in financial intermediation.

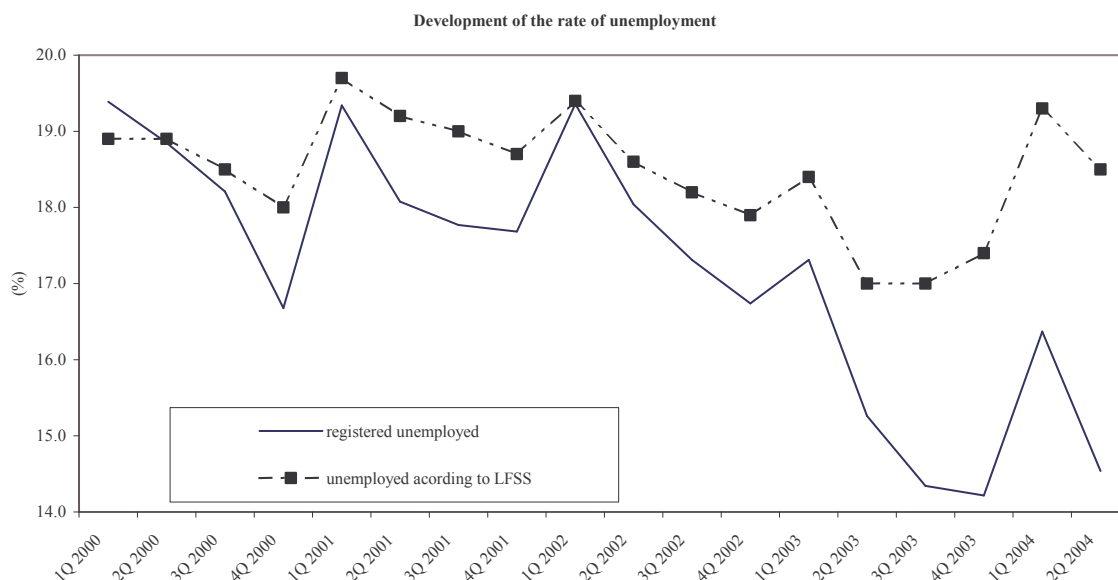
Development of employment by sector*	(index, same period last year =100)				
	2003		2004		
	1 st half year	year	1.Q	2.Q	1 st half year
Total	101.2	100.8	100.0	99.3	99.6
Agriculture, hunting, fishing and forestry	95.4	96.2	91.5	86.6	88.9
Industry	100.5	100.5	99.1	99.8	99.4
Mining and quarrying Mineral extraction	89.5	90.8	90.4	89.8	90.1
Manufacturing Industrial production	100.5	101.2	99.7	100.5	100.1
Electricity, gas and water supply	97.7	96.3	94.5	94.1	94.3
Construction	102.1	104.0	103.8	102.5	103.1
Wholesale and retail trade; repair of vehicles and personal goods	100.6	99.9	99.8	99.2	99.5
Hotels and restaurants	101.9	102.6	102.3	101.6	101.9
Transport, storage and communication	99.3	98.6	97.3	98.2	97.7
Financial intermediation	105.5	105.5	103.4	101.1	102.3
Real-estate, renting and business activities	103.0	103.2	102.4	103.3	102.9
Public admin. & defence; compulsory social security	103.2	103.9	102.1	100.5	101.3
Education	99.3	99.7	99.7	98.9	99.3
Health and social work	105.2	102.7	99.3	98.2	98.7
Other social and personal services	105.8	99.5	105.7	101.5	103.6

* according to statistical reporting

The decline in employment was accompanied by growth in the number of unemployed. According to the Labour force sample survey in the first half of 2004, the number of unemployed grew on a year-on-year basis by 7.7%. The average rate of unemployment reached 18.9%, which represented a year-on-year growth of 1.2 percentage points.

The unemployment rate according to labour office registers in the first half of 2004 represented on average 15.5% (in the first half of 2003 on average 16.0%). Its level against the data according to the Labour force sample survey is lower, which is connected with the different sampling methodology as well as with the definition of the unemployed. The long-term trend in unemployment according to both data sources, despite the gradually deepening difference, however does not principally differ.

The decisive factor in the different rate of unemployment according to the register of the Office of Labour, Social Affairs and the Family and according to the Labour force sample survey, which is carried out by the Statistical Office of the SR, was the adoption of administrative measures tightening the conditions for registered unemployed at labour offices. In the case of not fulfilling these conditions persons are removed from the labour office registers, but in the Labour force sample survey they continue to feature as persons without work and seeking work, i.e. as unemployed. Apart from this, in the Labour force sample survey pensioners and students actively seeking work may be included in the numbers of unemployed persons.



1.4 Financial results of corporations

Corporations of the non-financial and financial sector according to preliminary data created in the first half of 2004 a profit (gross profit before taxation) of SKK 96.5 billion, which in the same period last year was 6.1% higher. A substantial volume of the profit was to a decisive extent affected by the management of non-financial corporations, whose profit grew on a year-on-year basis by 4.6%. Financial corporations after a preceding loss created a profit of SKK 0.1 billion.

Financial results of corporations

(SKK mill., current prices)

	1 st half year of 2004	index $\frac{1^{\text{st}} \text{ half year of 2004}}{1^{\text{st}} \text{ half year of 2003}}$
Financial result (before tax)		
Non-financial and financial corporations in total	96 529	106.1
Non-financial corporations	96 406	104.6
Financial corporations	123	x

The financial result of non-financial corporations was influenced by the growth in profit in the electricity, gas and water supply; in transport, storage, communication; and in real estate and renting. A lower profit than last year was reported in manufacturing and construction, the loss in agriculture deepened.

Financial corporations, in comparison with the loss in the first half of 2003 (SKK 1.2 billion), created a profit of SKK 0.1 billion, where differing results in the management of individual entities persisted. A positive financial result was achieved by financial intermediaries (SKK 3.8 billion) and insurance corporations and pension funds (SKK 1.9 billion). The trend of negative financial result at financial institutions has persisted for the third year, which in the first half year created a loss of SKK 5.6 billion (this result was influenced by the loss of the NBS, which for the first half year reached SKK 13.1 billion).

2. BALANCE OF PAYMENTS

2.1 Current Account

In the first half of 2004 the current account deficit of the balance of payments reached SKK 16.8 billion, representing a growth on the same period last year of SKK 6.5 billion. Its increase was affected most by the development of the income balance (a growth in income of equity paid out to direct investors) and current transfers (contributions made to the EU budget). In contrast, an improvement was seen against the first half of 2003 in both the balance of trade and of services.

Current account of the balance of payments

SKK billion	1 st half year of 2004	1 st half year of 2003
Balance of trade	-9.4	-12.5
Balance of services	4.3	2.3
Income balance	-12.7	-5.3
Current transfers	1.0	5.2
Current account total	-16.8	-10.3
Share of current account in GDP in %	-2.6	-1.9

The balance of trade ended in a deficit of SKK 9.4 billion, representing a year-on-year decline of SKK 3.1 billion. The reduction in the balance of trade deficit was caused, in particular, by a higher rate of export growth in comparison with that of imports.

According to preliminary data from the Statistics Office of the SR, in the first half of 2004 goods exported were in the value of SKK 436.8 billion, which was 16.4% more than for the same period of the preceding year (in USD 33.3% more, in EUR 19.8% more).

Year-on-year change in the SR export and its individual segments and the contributions of these segments to the growth / decline of exports

	1 st half year of	1 st half year of	Contribution	Contribution
	2004	2 003	1 st half 2004	1 st half 2003
	in SKK bln.	in SKK bln.	in %ge points	in %ge points
Raw materials	4.4	2.5	1.2	0.8
Chemical products & intermediate products	9.7	11.7	2.6	3.8
Machinery & transport equipment	44.3	48.0	11.8	15.6
of which: machinery	18.8	11.7	5.0	3.8
transport equipment	25.5	36.3	6.8	11.8
Finished products	3.1	6.2	0.8	2.0
Total export	61.5	68.4	16.4	22.2

The SR's export in the first half of 2004 maintained a relatively high rate of growth, even despite the fact that in a year-on-year comparison its rate fell by more than 5 percentage points. The growth in the export was founded mainly on development in the group of machinery and transport equipment. Unlike in the preceding year in which the dominant position in the export growth of this group was held by means of transport, in the first half of 2004 the influence of the export of machinery and devices increased noticeably. The year-on-year export growth in the sub-group machinery and equipment, which was higher than in the first half of 2003, comprised machines for automatic data processing, machines for individual industrial sectors, white goods, televisions, electrical transformers, motors, cables, etc. An above-average rate of export growth was maintained also by means of transport, even if their rate of growth fell from last year's 58.5% to 26.2%. In the structure of the sub-group means of

transport the highest growth was recorded by personal automobiles, motor vehicle parts and accessories and coachworks’.

Chemical products and intermediate products, such as iron and steel and their products, rubber mixtures, plastics, aluminium and several wood products continued to sell on world markets. The change in the structure of the Slovak export is documented also by the fact that the dependence of export growth on the development of this group has been decreasing each year (while in 2001 the growth in the group chemical products and intermediate products formed 36% of the total export growth, in the first half of 2004 this figure had fallen to only 16%).

Exported production in the nature of finished products maintained a relatively stable development. Its year-on year growth did not achieve high values, comprising an increased export of relatively stable commodities such as: toys, footwear, clothing and certain foodstuffs.

The volume of imported goods in the first half of 2004 represented SKK 446.1 billion, a year-on-year growth of 15.0% (in USD 31.9%, in EUR 18.4%).

Year-on-year change in the SR import and its individual segments and the contributions of these segments to the change in imports

	1 st half year of	1 st half year of	Contribution	Contribution
	2004	2 003	1 st half 2004	1 st half 2003
	in SKK bln.	in SKK bln.	in %ge points	in %ge points
Raw materials	3.1	2.7	0.8	0.8
Chemical prod’s & intermediate products	16.0	11.9	4.1	3.4
Machinery & transport equipment	29.4	16.5	7.6	4.7
of which: machinery	19.9	6.6	5.1	1.9
transport equipment	9.5	9.9	2.5	2.8
Finished products	9.8	7.9	2.5	2.2
of which: agricultural	6.0	2.6	1.5	0.7
and industrial products				
personal automobiles	1.0	1.1	0.3	0.3
machinery and electrical equip.	2.8	4.2	0.7	1.2
consumer products				
Total import	58.3	39.0	15.0	11.1

Similarly as in exports, imports also saw amelioration in the strengthening of the share of machinery and transport equipment. The import of this group exceeded the overall year-on-year growth and reached 23.5%. Imports were oriented into the automobile industry, which was manifested in a growth in the import of transport equipment components and some machinery products, such as motors, etc. Above-average year-on-year import growth was achieved also in the sub-group of machinery and instruments. Within this sub-group, in contrast to the preceding year, also the import of technological equipment for individual sectors of the national economy grew significantly, which could have a direct influence on the economy’s restructuring with future effects on export growth (according to NBS calculations the import of technological equipment grew on a year-on-year basis by almost SKK 6.6 billion, where its share in the total import increased from last year’s 7.2% to 7.8%). This concerned primarily the import of machinery for the metallurgical, engineering, chemical and glass industries, as well as machines for automatic data processing.

The growth in the total import, besides the decisive engineering group, was due also to the group chemical products and intermediate products (year-on-year growth of 13.4%). The growth in the import of intermediate products was concentrated in increased imports of iron and steel and non-ferrous metals. In the chemical products group import growth was manifested in plastic products and related to the development of the automobile industry.

In the import of finished products (a year-on-year growth of 11.6%), which grew faster than in 2003, there was manifested mainly a growth in the import of industrial products (pharmaceuticals, furniture, footwear, clothing, toys and sports equipment) and in smaller amounts also certain foodstuffs (meat, milk, fruit, sugar, vegetables). The import for end consumption was influenced also by a growth in the import of consumer electronics.

In trade in services a surplus was created in the first half of 2004 in the amount of SKK 4.3 billion (a year-on-year growth of SKK 2.0 billion). Receipts for the export of services to abroad grew by SKK 0.5 billion and concurrently payments for their import fell by SKK 1.5 billion. The growth in the balance of services was due in part to “total other services” and transport services, whereas tourism services recorded a decline in their positive balance.

Balance of services

SKK billion	1st half year of 2004	1st half year of 2003
Transport	9.4	8.5
Tourism	1.7	4.2
Total other services	-6.8	-10.4
Balance of services	4.3	2.3

Incomes from the international transport of goods and persons reached SKK 25.2 billion (a year-on-year growth of SKK 0.7 billion) and expenditures of SKK 15.8 billion (a decline of SKK 0.2 billion). From the aspect of the size of volume, the largest item in the framework of transport services remained income from the transfer of natural gas and oil, which reached SKK 13.6 billion, representing almost 54% of overall transport incomes. Moderate growth, even despite the decline of the koruna exchange rate against the USD, was recorded also by the transit fee in SKK, where in USD this growth represented 18.4%.

In international transport services excluding transit (automobile, railway, aircraft and boat), including transport related services, a deficit was reported in the amount of SKK 4.2 billion, where 80% of this deficit comprised payments for other freight services, including trade costs.

The positive balance of foreign tourism fell on a year-on-year basis by SKK 2.5 billion. Foreign exchange incomes from foreign tourism reached SKK 12.0 billion, representing a decline against the first half of 2003 by SKK 3.0 billion. According to NBS calculations, the strengthening of the SKK against the basic currencies (EUR, USD) contributed to the decline in earnings by approximately one third. The remaining two thirds were a consequence of a change in the structure of foreign visitors, as well as in the number of days, which these tourists spent in the territory of the Slovak Republic.

Expenditures by Slovak citizens on foreign tourism fell by SKK 0.5 billion to SKK 10.3 billion.

Despite the fact that the balance in “total other services” (communication services, building services, insurance services, financial services, rental, computer equipment services, advertising, trade services, technical services, etc.) was, similarly as in the preceding year, in deficit, this deficit fell on a year-on-year basis by SKK 3.7 billion. Incomes for services provided grew on a year-on-year basis by SKK 2.8 billion, while expenditures declined by SKK 0.9 billion

In the first half of 2004 in the framework of “total other services”, the best development was seen in financial services, legal and accounting services, where the growth in the export was accompanied by a decline in their import. A decline in the deficit, made possible by higher growth in receipts as payments, was recorded also in intermediary services and services in the framework of representing foreign firms in the SR, which may be a sign of the increased interest of foreign businesses in presenting themselves in the SR’s territory. A negative impact on the overall balance has resulted mainly from the decline in receipts and the growth in payments in services of a trade nature, including consultancy in business and management; and services in the field of public relations.

In the first half of 2004 the income balance ended in a deficit of SKK 12.7 billion, which against the same period last year represents a worsening by SKK 7.4 billion. Incomes fell by SKK 1.4 billion and payments rose by SKK 6.0 billion.

During short-term working stays abroad Slovak citizens, according to NBS calculations, earned SKK 7.5 billion, where this value remained at approximately the same level as for the first half of 2003. Costs for the labour of foreign citizens working in the SR remained, also in 2004, at a very low level, reaching SKK 0.3 billion.

In the first half of 2004 dividend payments to direct investors grew most. Enterprises with a foreign stake holding were paid dividends in the amount of SKK 13.8 billion, representing a year-on-year growth of SKK 10.2 billion. The revenue of foreign investors from capital invested (the yield on foreign direct investments is calculated as the share of revenues from the assets and interest on the balance of the FDI) in the territory of the SR reached approximately 3.7%, representing a significant growth on the first half of 2003 (by 3.2 percentage points). Investment in foreign equity securities brought Slovak investors, similarly to last year, the revenue of SKK 0.2 billion.

Interest from banking sector assets (in the framework of portfolio investments) fell slightly on a year-on-year basis, which could have been connected with the strengthening of the koruna exchange rate and the development of interest rates on the financial markets. A decline was also recorded in interest paid out to non-residents in the framework of investment in domestic securities.

The balance of other investments remained at approximately the level of the same period last year, where no changes occurred either on the side of receipts or payments. Whereas a significant share on the side of receipts was formed by interest from short-term loans provided to non-residents by Slovak banks, on the side of payments this concerned long-term loans to the business sector, which were used in particular for covering their capital investment needs.

In the balance of current transfers a significant decline was seen in the first half of 2004 compared to the preceding year. The year-on-year decline in the surplus by SKK 4.2 billion

was caused primarily by the deficit created by government transfers. Within government transfers there were negatively reflected the contributions to the EU budget in June, whereas incomes from the EU have so far been made only in very small amounts. A decline in the surplus occurred also in the case of private transfers. The decline in incomes in the amount of SKK 0.6 billion was caused by lower non-capital investment subsidies provided to non-governmental organisations. Concurrently with the decline in incomes in consequence of the increased transfers of juristic persons to abroad, private transfer expenditures also increased by almost SKK 1.0 billion.

2.2 Capital and Financial Account of the Balance of Payments

The capital and financial account ended the first half of 2004 with a surplus of SKK 28.3 billion, and in comparison with the same period last year was SKK 0.7 billion lower. A change in the structure of the financial inflow was also seen, where in the first half of 2003 short-term capital of the banking sector played a decisive role, in the first half of 2004, besides direct investments, also an increased inflow of portfolio investments was evident.

Capital and financial account of the balance of payments

SKK billion	1st half year of 2004	1st half year of 2003
Capital account	-0.5	0.5
Direct investments	31.3	20.2
of the SR abroad	7.7	0.7
in the SR	23.6	19.5
of which: stakeholdings	19.9	20.8
of which: privatisation FDI	2.9	9.4
Portfolio investments and financial derivatives	32.7	-18.2
of the SR abroad	-12.2	-16.2
in the SR	44.9	-2.0
Other long-term investments	-16.7	-4.4
Asset	-3.5	8.7
Liability	-13.3	-13.1
Short-term investments	-18.5	30.9
Asset	0.2	-7.1
Liability	-18.7	38.0
Capital and financial account total	28.3	29.0

A structural change in the capital and financial account was seen also in its sectoral composition. While in the first half of 2003 the inflow of capital was made to the banking sector, in the first half of 2004 the largest recipient of capital was the government.

Structure of the capital and financial account by sector

Sector	1st half year of 2004		1st half year of 2003	
	SKK billion	EUR million	SKK billion	EUR million
Enterprises	-3.0	-74.1	-17.1	-413.1
Banking	2.1	52.5	35.7	861.0
Government sector and NBS	29.2	716.4	10.4	231.3
of which: government	49.6	1 266.6	4.7	91.6
NBS	-20.4	-550.2	5.7	139.7
CAPITAL & FINANCIAL ACCOUNT	28.3	694.8	29.0	679.2

The balance of foreign direct investment (FDI) in the the first half of 2004 reached SKK 31.3 billion, representing a year-on-year growth of SKK 11.1 billion.

In the first half of 2004 the low interest among Slovak enterprises in investing abroad persisted. The inflow of other capital in the structure of direct investment from abroad was the result of credit provided to the domestic enterprise from its subsidiary company abroad. Direct investments from abroad represented an inflow of funds in the amount of SKK 7.7 billion. This inflow was the result of the drawing of credit by a domestic enterprise, provided by its subsidiary company abroad, and which in the structure of direct investments from abroad was included into other capital. The interest of Slovak enterprises in investing abroad (stakeholdings) fell, where liquidation of already realised investments exceeded new investments made in the first half of 2004.

The growth in FDI to the SR was influenced by the development of other capital, where the year-on-year change in the trend from outflow to inflow was caused by the decline in the activities of Slovak entities in providing trade credit connected with the export of goods to parent companies.

The inflow of shareholder capital reached SKK 19.9 billion and remained slightly below the level of the same period last year. The structure of the inflow was different from the aspect of privatisation and non-privatisation investments. Higher foreign direct investments (excluding those of privatisation) against the same period last year were made in increases in foreign investors' stakeholdings in the SR. The greatest volume of investments in stakeholdings were directed, from the aspect of sectoral structure, into industrial production (production of coke, refined oil products, and motor vehicles). An increased interest of foreign investors persisted also in investing in trade and trade services.

On the other hand, the volume of the sale of state assets in 2004, compared to the preceding year, fell by SKK 6.5 billion (during the first half year only the completing sale of a 10% stake in Slovenská sporiteľňa was made in the amount of SKK 2.9 billion).

In the field of portfolio investments a net inflow of funds in the amount of SKK 32.7 billion was recorded. In comparison with the same period last year a change in the trend from outflow to inflow was seen.

Portfolio investments of Slovak subjects increased by SKK 12.2 billion. Domestic investors, both banking and non-bank subjects, invested their funds into long-term foreign bonds, where a net outflow was seen in the amount of SKK 12.5 billion. In the trading of foreign shares their sale prevailed over their purchase, and this mainly in the case of the business sector. Over the course of the period monitored foreign investors invested on balance SKK 44.9 billion, where non-residents increased their holding of debt securities of domestic entities by SKK 47.6 billion. A significant role in their structure was played by government activities. In the first half of 2004 the government issued on foreign market eurobonds in the counter-value of SKK 40.1 billion. Government liabilities ensuing from the repayment of eurobonds issued in 1999 represented SKK 20.0 billion. Demand by foreign investors for government securities issued in Slovak koruna over the course of the first half of the year had a growing tendency, and over the six months was manifested in an inflow of funds in the amount of SKK 24.5 billion. Interest in treasury bills also grew slightly. The balance of government debt securities over the first half of 2004 increased by SKK 47.6 billion and in comparison with the first half of 2003 grew by SKK 51.0 billion.

Similarly as in 2003, in the first half of 2004 no business sector issues were made on the foreign markets. Commercial and banking sector securities neither played a significant role in trading on the secondary market. On the other hand, the low interest in shares in Slovak enterprises continued, which alongside growing sales of shares acquired in previous years meant an outflow of capital. In sum, domestic securities of enterprises and banks recorded an outflow of funds in the amount of SKK 3.4 billion.

The balance of other investments ended with an outflow of funds to abroad in the amount of SKK 35.2 billion. The change in the trend from inflow to outflow was caused by the development of short-term liabilities in the government sector, the NBS and the banking sector.

Other long-term investments recorded an outflow of funds in the amount of SKK 16.7 billion. An outflow of long-term capital was seen both on the asset as well as liability side. Whereas on the asset side this concerned the provision of long-term funds from the banking sector, on the liability side it concerned mainly the excess of repayment over the drawing of financial credit in the business sector.

The drawing of financial loans by enterprises reached SKK 12.0 billion, which was 20% more than in the same period last year. The increased drawing was connected also with a renewal in the interest in obtaining foreign funds in the sectors the generation and distribution of electricity, gas and water; trade; transport; and financial intermediation. The inflow of credit funds to the individuals sectors of industry was very low, where significant credit activity was recorded only in the production of metals and metal constructions. The repayment of financial loans by the business sector reached SKK 26.6 billion, more than double its previous figure.

Short-term capital recorded an outflow in the amount of SKK 18.5 billion. NBS activities had a decisive influence on the fall in short-term liabilities by SKK 18.7 billion. Through the realisation of repo trades, in the framework of its strategy of managing foreign currency reserves, there occurred an outflow of funds in the amount of SKK 19.7 billion (this transaction did not have any impact on the net inflow, or outflow of capital, as it was manifested both as a fall in NBS foreign currency reserves, as well as in SR's foreign debt). The outflow of capital of commercial banks (SKK 2.6 billion) was a consequence of the development of other short-term liabilities, the decline of which was in large part compensated for by a growth in loans drawn and deposits of non-residents in Slovak banks. The inflow of short-term capital realised in the business sector (SKK 3.6 billion) was connected with the drawing of import and financial loans from abroad.

2.3 Foreign Exchange Reserves

The foreign exchange reserves of the NBS as at the end of June 2004 stood at USD 12.4 billion (EUR 10.1 billion) and from the beginning of the year had grown by USD 213.5 million (EUR 173 million). The total foreign exchange reserves of the National Bank of Slovakia were over the course of the half year influenced by various factors. Incomes were influenced by the borrowing activities of the government, as well as incomes relating to central bank interventions on the foreign exchange market. Expenditures were determined in particular by debt servicing repayments by the government. The development of NBS foreign exchange reserves over the course of the first half year was also influenced by the development of mutual exchange rates of freely tradable currencies on world financial

markets. The surplus in the balance of incomes and expenditures over the period monitored (USD 409.4 million) was partially compensated for by negative exchange rate differences (USD -195.9 million), which arose in consequence of the weakening of other freely tradable currencies (the euro especially) against the American dollar on world financial markets.

The income side of foreign exchange reserves in this period was determined by:

- revenues from deposits and securities in the NBS portfolio in the amount of USD 134.5 million,
- drawing of government loans from foreign financial institutions in the amount of USD 1 325.3 million, of which the May eurobond issue represented USD 1 199.8 million
- incomes resulting from interventions and direct trades on the interbank foreign exchange market in the amount of USD 454.4 million
- other incomes of the NBS in the amount of USD 119.6 million

The expenditures side of foreign exchange reserves in this period was influenced by:

- debt servicing repayments of the government in the amount of USD 805.7 million, of which repayments of principal and interest on government eurobonds issued in previous years represented USD 705.2 million,
- debt servicing repayments of the NBS in the amount of USD 20.9 million,
- other expenditures of the NBS in the amount of USD 179.4 million, ensuing in particular from payments in the framework of the foreign system of payments for NBS clients (USD 162.2 million),
- central bank expenditures ensuing from repo operations realised (a negative balance in the amount of USD 586.7 million).

The NBS foreign exchange reserves as at the end of June 2004 were sufficient to cover 4.9 times the average monthly import of goods and services to the Slovak Republic for the first six months of the year.

The foreign exchange reserves of commercial banks as at the end of the half year of 2004 stood at USD 1 388.2 million. The balance of foreign exchange reserves of the whole banking sector, including the NBS, at the close of June was USD 13 750.7 million.

2.4 Foreign Debt of the SR

The total gross foreign debt at the close of June 2004 stood at USD 18.7 billion (EUR 15.4 billion), representing a growth of USD 0.6 billion in comparison with the start of the year. The growth in the total foreign debt was due in large part to the borrowing activities of the SR government (the May issue of eurobonds by the Ministry of Finance of the SR in the amount of EUR 1 billion, equalling USD 1.2 billion). In June 5-year Ministry of Finance bonds were repaid in the amount EUR 0.5 billion (equal to USD 0.6 billion).

The total long-term foreign debt in the period monitored grew by USD 1.1 billion, where as at the end of June it stood at USD 11.4 billion. Over the course of the half year the long-term foreign debt of the government and the NBS grew by USD 1.6 billion, and the long-term debt of business subjects fell by USD 0.5 billion.

The total short-term foreign debt as at the end of June stood at USD 7.3 billion, which against the start of the year represents a fall of USD 0.5 billion. Short-term foreign liabilities of the government and the NBS fell by USD 0.5 billion, primarily due to the lower balance of repo

transactions by the central bank. In the commercial sector short-term liabilities of commercial banks fell slightly, alongside a concurrent growth in short-term liabilities of business entities.

The total gross foreign debt per capita in the SR at the end of June amounted to USD 3 478, which against the start of the year represents a growth of USD 15. The share of total short-term debt in the total gross foreign debt of the SR as at the end of the half year reached 39.1%, which is 3.9% less than the share reported at the start of 2004.

	in mill. USD		in mill. EUR	
	1.1.2004	30.6.2004	1.1.2004	30.6.2004
Total foreign debt of the SR	18 090.2	18 710.7	14 468.3	15 384.2
1) Long-term foreign debt	10 308.2	11 393.0	8 244.4	9 167.5
Government and NBS*	4 347.7	5 900.2	3 477.2	4 851.2
Commercial banks	323.1	340.4	258.4	279.9
Business entities	5 637.4	5 152.4	4 508.7	4 236.4
2) Short-term foreign debt	7 782.0	7 317.7	6 223.9	6 016.7
Government and NBS*	915.5	390.4	732.2	321.0
Commercial banks	2 738.6	2 604.3	2 190.3	2 141.3
Business entities	4 127.9	4 323.0	3 301.4	3 554.4
Foreign assets	18 907.5	19 587.8	15 122.0	16 105.3
Net foreign debt	- 817.3	- 877.1	-653.7	- 721.1

* including government agencies and municipalities

Net foreign debt, calculated as the difference between gross foreign debt in the amount of USD 18.7 billion (liabilities of the NBS, government, commercial banks, and business sector – excluding shareholdings) and foreign assets in the amount of USD 19.6 billion (foreign exchange reserves of the NBS, commercial banks' foreign assets, foreign assets of the business sector – excluding shareholdings) as at the end of June 2004 reached the creditor position of USD 0.9 billion.

3. PUBLIC SECTOR

Development of budgetary management in the first half of 2004

At the end of the first half of 2004 the state budget ended in a deficit of SKK 12.4 billion, which represented 15.9% of its total amount set for this year. In comparison with the previous year, this year's deficit represents an improvement in state budget management by SKK 15.2 billion.

Incomes to the state budget for the whole of 2004 were set at SKK 232.0 billion. According to the balance as at the end of June they had reached SKK 120.7 billion, i.e. 52.0% of the whole year's budget. The half-year budget forecast was exceeded by SKK 4.7 billion. In comparison with the same period last year incomes was SKK 19.8 billion higher. Tax revenues reached SKK 107.9 billion, representing a 55.3% fulfilment of the whole year's incomes. Compared to the same period last year, tax receipts recorded an increase of SKK 18.7 billion. Non-tax incomes in comparison with the same period last year similarly grew, reaching SKK 9.3 billion, i.e. a 71.5% fulfilment of the state budget. Other incomes totalled SKK 3.5 billion.

In the first half year value-added tax receipts reached 52.1% of their budgeted level. The unification of the VAT rates at 19% resulted in a growth in revenues from this tax, where this year's half-year collection increased by almost SKK 15 billion, to approximately SKK 51 billion. Following Slovakia's accession to the EU (in May 2004) a certain weakening in the collection of VAT was seen. This was caused by an administrative change in the collection of this tax. The tax shortfall is a one-off matter of this year, having arisen through the fact that value-added tax is no longer collected on imports from European Union countries at customs offices, but at tax offices.

Excise duties were not in line with the budgeted objective, where budgetary fulfilment represented 47.3%. This year's excise duties exceeded those of last year by SKK 2.8 billion. Similarly as in the case of value-added tax revenues, excise duty revenue, too, this year has been influenced by a one-off impact ensuing from Slovakia's accession to the EU.

The half-year revenue of natural person income tax was higher than the budget forecast, by SKK 1.9 billion, reaching SKK 11.2 billion (a 60% budgetary fulfilment). This year's revenue was below that of last year. Tax reform in the field of income tax, which entered into force on 1 January this year, resulted in a change in this tax's revenue. Its budgeted level is based on the introduction of a single tax rate, a new tax-deductible item, on changes in contribution rates and maximum measurement bases, and on a monthly child tax allowance.

In corporate income taxes SKK 19.2 billion was collected in the first half of 2004, representing an 87.0% budgetary fulfilment. In comparison with last year it can be said that there has been an improvement in collection by approximately SKK 5.5 billion. Similarly as in the case of natural person income tax, also in the case of this tax the budgeted level was based on the reduced rate from 25% to 19%.

State budget expenditures represented a 42.9% budgetary fulfilment. In a year-on-year comparison, this year's expenditures were SKK 4.6 billion higher.

State guarantees

Pursuant to Act No 386/2002 Coll. on state debt and state guarantees, the limit on the provision of state guarantees for 2004 was set at the level of SKK 4.6 billion. Over the course of the first half of 2004 this limit was not drawn on at all.

For 2004 the government, in Resolution No 974/2003, consented to the use of assets of the National Property Fund in the amount of SKK 2.3 billion for the settlement of realised state guarantees. At 30 June 2004 the realisation of state guarantees for Slovak Railways in the value of SKK 1.3 billion was settled from these resources.

Relationship of NBS and state budget of Slovak Republic

The period in question has been characterised by a movement of clients from the NBS to the State Treasury. As at the end of June the NBS administered accounts for only 12 budgetary chapters (out of a total of 38).

On the basis of the approved system of interest accrual, which is derived from the current one-day sterilisation rate announced by the National Bank Slovakia, the NBS for the first half of 2004 paid to the Ministry of Finance of the SR interest in the amount of SKK 466.1 million, of which interest on funds deposited in the state's summary suspense account represented SKK 237.4 million, and SKK 228.7 million on term deposits.

Interest expenses of the NBS due to administration of the annual term deposit intended for pension reform reached SKK 1 925.9 million.

Development of state financial assets and liabilities in the first half of 2004

State financial assets deposited in the form of deposits on accounts at the NBS as at the end of the first half year reached SKK 8.3 billion. Over the course of the half-year the level of assets grew against the initial balance for 2004 by SKK 0.9 billion.

State funds

Over the course of the first half of 2004 specific tasks, which were not ensured in the full amount from state budget expenditures, were fulfilled by two purpose-specific state funds. In the competence of the Ministry of the Economy of the SR there operates the State Fund for the Decommissioning of Nuclear Facilities and Handling of Spent Nuclear Fuel, and in the competence of the Ministry of Construction and Regional Development of the SR there operates the State Housing Development Fund.

At the close of the first half-year the financial balances on these funds' accounts at the NBS and commercial banks represented SKK 15.4 billion.

Budgetary Management of the National Property Fund of the SR as at 30.06.2004

For the first half of 2004 incomes of the NPF SR reached SKK 15.0 billion and expenditures SKK 4.0 billion. Incomes comprised prevalingly receipts from privatisation in the amount of SKK 5.0 billion (for the sale of Paroplynový cyklus, a.s. and the completing privatisation of Slovenská sporiteľňa, a.s.) and incomes from dividends totalling SKK 9.8 billion. On expenditures side of the NPF SR there was realised in particular the use of its assets in accordance with the Resolutions of the SR Government, according to which SKK 2.2 billion

was transferred to state financial assets and SKK 1.3 billion was used for the realisation of state guarantees for Slovak Railways.

4. MONETARY POLICY AND MONETARY DEVELOPMENT

The execution of monetary policy by the NBS in the first half of 2004 was realised in the environment characterised by an accelerated rate of economic growth, favourable development of foreign trade balance, as well as current budgetary management of the government sector and a continuing trend of appreciation of Slovak koruna against the EUR.

4.1 Monetary Aggregates

The money supply M2 (at fixed 1993 exchange rate) grew in comparison with the figure for the start of the year by SKK 5.5 billion and at the close of the first half-year had reached SKK 731.0 billion. Its year-on-year rate of growth in June represented 7.1%. At the current exchange rate, the money supply M2 grew by SKK 4.1 billion to SKK 742.7 billion in the first half year. Its year-on-year rate of growth at the close of June represented 6.3% (compared to 3.1% in June 2003).

The development of the money supply in the first half of 2004 was relatively volatile. The main factors responsible for this included the March date for the settlement of income taxes for natural and juristic persons for the previous year's tax periods and the disbursement of dividends by the corporate sector. These factors operated in individual months to a more intensive degree than in the previous year, since the effect of the income tax payment was concentrated into one month (in consequence of the cancellation of the option to extend the deadline for income tax payment for taxpayers whose tax returns are prepared by a tax adviser) and the volume of taxes collected and dividends paid out reached a higher level than in comparison with the previous year.

Money supply M2 (in SKK billion)	Volume as at the end of June 2004	Change since the beginning of year 2004
YEAR 2004		
- at current exchange rate	742.7	+4.1
- at fixed 1993 exchange rate	731.0	+5.5
YEAR 2003		
- at current exchange rate	698.7	-9.8
- at fixed 1993 exchange rate	682.3	-4.1

The fall in the difference between the growths in the money supply at the current and fixed exchange rate in the first half of 2004 against the same period last year was determined by the different development of deposits in foreign currency. While in the first half of 2003 foreign currency deposits declined, at the close of the first half of 2004 they had maintained their level from the outset of the year. Concurrently, the first half of 2003 saw a more significant appreciation of the SKK / USD exchange rate, at which a part of deposits in foreign currency in the sum of monetary aggregates is converted.

Sources of money supply formation in the first half of 2004 comprised, in the relatively stable development of net foreign assets, prevailing domestic factors, in particular the continuing growth in credits to enterprises and households.

Net foreign assets (at fixed 1993 exchange rate) grew in absolute terms against the start of the year by SKK 6.0 billion to SKK 161.0 billion, as foreign assets grew faster than foreign liabilities. The year-on-year rate of growth in net foreign assets at the end of the first half-year

reached 0.8%. While in the structure of foreign assets the growth of NBS foreign currency reserves and long-term foreign assets of commercial banks dominated most, on the side of foreign liabilities a growth was seen in the volume of government securities in holding of non-residents and long-term foreign liabilities of the NBS and government, as well as a decline in short-term foreign liabilities of commercial banks and the NBS.

Loans to enterprises and households (at fixed 1993 exchange rate) continued in their upward trajectory, as their volume over the course of the first half of 2004 grew by SKK 12.8 billion (SKK 12.9 billion in the first half of 2003) and at the close of June had reached SKK 394.5 billion at a year-on-year rate of growth of 14.6%. The growth in loans was influenced on a one-off basis by the realisation of a state guarantee for loan provided to a state enterprise, in consequence of which over the course of January 2004 the volume of loans to enterprises fell by SKK 4.6 billion to the debit of the central state administration's debt.

In contrast to the preceding year, when koruna loans dominated, the growth in loans to enterprises and households this year was due primarily to loans in foreign currency (preferred especially by enterprises). From the beginning of the year these increased by SKK 16.8 billion, whereas koruna loans to enterprises fell by SKK 17.9 billion. Koruna loans to households confirmed their growing trend also in the first half of 2004, as against the start of the year they grew by SKK 13.9 billion.

Fiscal field, net credit to the government

Net credit to general government (including the National Property Fund) at the end of June reached SKK 294.9 billion (at 1993 fixed exchange rate), which in comparison with the beginning of the year represented a fall of SKK 2.3 billion. This favourable development in the first half of 2004 was influenced to a significant extent by the change in the creditor position of the National Property Fund vis-à-vis the banking sector. This position was, especially under the influence of receipts from the sale of the remaining 10 percent shares in Slovenská sporiteľňa, a.s. and the sale of Paroplynový cyklus, a.s. (in total SKK 5 billion) and funds obtained from dividend payout (SKK 9.4 billion), increased by SKK 10.9 billion, thus leading to a reduction in the net credit to general government.

The net credit to government (excluding the influence of the National Property Fund) over the course of the first half of 2004 deepened by SKK 8.6 billion in particular under the deficit budget management of central government. The state budget deficit in the first half of 2004 reached SKK 12.5 billion. In May the SR government realised the eurobond issue in the volume of EUR 1 billion with a maturity of 10 years, of which a part of the resources totalling EUR 500 million was used in June 2004 for the repayment of a eurobond issue dating from 1999. The remaining part of the funds acquired by the issue stayed deposited in the form of a term deposit of the Ministry of Finance of the SR with the NBS.

The more favourable conditions to raise funds for covering government debt on foreign markets in the first half of 2004 were manifested in a change in the structure of government debt in the form of a growth in the foreign part of debt alongside a concurrent decline in its internal part.

The trend towards reduction of the public sector's internal debtor position was caused by an improvement in the net position of local authority bodies, as well as in a growth of deposits of extra-budgetary funds of state bodies with commercial banks. The deepening of the

government's internal position resulted both from the current budgetary performance as well as the increased credit exposure of state bodies vis-à-vis commercial banks, and also a worsening in the budgetary management of the social security funds.

The development of net credit to the government in the first half of 2004, in its internal debt part, was favourably influenced also by the transfer of funds from extra-budgetary deposits of state bodies from accounts with the NBS to accounts at the State Treasury in relation to the gradual incorporation of clients to its system. The extra-budgetary deposits of state bodies, which had not hitherto been a component in the methodology of the net credit to general government, has through their transfer to the State Treasury become a part of government deposits with the banking sector, whereby they caused a reduction in the internal debt of the government (these deposits at the end of June amounted to approximately SKK 8 billion).

4.2 Structure of the Money Supply

The M2 money supply (at fixed 1993 exchange rate) grew in the first half of 2004 by SKK 5.5 billion, reaching at the end of June SKK 731.0 billion. The year-on-year rate of growth in the money supply accelerated from 6.4% in December 2003 to 7.1% in June 2004, where the money supply recorded relatively volatile development in the individual months of the first half-year.

Currency in circulation outside banks grew in the first half of 2004 by SKK 1.4 billion, where its year-on-year rate of growth fell from 9.0% in December 2003 to 7.6% in June 2004. Development in the individual quarters was varied, where in the first quarter the year-on-year rate of growth fell and gradually grew in the second quarter.

Total koruna deposits (demand and time) have fallen slightly since the start of the year, by SKK 0.2 billion, where in a year-on-year comparison they have stagnated (a fall in the rate of growth by 8.0 percentage points). Their development has been influenced by the fall in time deposits (by SKK 2.6 billion), which was compensated for by a growth in demand deposits (by SKK 2.4 billion). The year-on-year rate of growth of demand deposits accelerated from 13.4% in December 2003 to 14.7% in June 2004, while the rate of growth of time deposits fell from 5.4% to 3.1%. The increase in koruna deposits was due in part to deposits of enterprises, while those of households declined.

	Year-on-year change in %			Change on the beginning of year in SKK billion		
	June 2002	June 2003	June 2004	June 2002	June 2003	June 2004
<i>at fixed 1993 exchange rate</i>						
Household deposits	5.4	0.6	-3.3	-1.0	-6.9	-3.5
<i>koruna total</i>	3.1	2.7	-2.2	-4.5	0.3	-0.6
demand	15.5	14.7	9.5	2.8	6.3	6.5
time	0.0	-1.5	-6.1	-7.3	-6.0	-7.1
<i>foreign currency</i>	22.1	-7.8	-10.5	3.5	-7.2	-2.9
<i>at current exchange rate</i>						
Household deposits	5.5	-1.6	-4.3	-0.4	-11.0	-5.1
of which: in foreign currency	17.6	-17.8	-16.0	4.1	-11.3	-4.5
<i>at fixed 1993 exchange rate</i>						
Deposits of enterprises	12.7	12.8	24.6	-1.1	0.4	7.6
<i>koruna total</i>	12.2	16.8	21.7	-3.9	2.1	0.4
demand	15.3	18.4	19.9	-11.2	-7.4	-4.1
time	10.1	15.7	23.0	7.3	9.5	4.5
of which insurance co's	-10.7	-37.2	10.9	0.6	-2.1	0.0
<i>foreign currency</i>	15.3	-9.3	44.9	2.8	-1.7	7.2
<i>at current exchange rate</i>						
Deposits of enterprises	12.0	9.7	23.7	-0.4	-1.2	7.8
of which: in foreign currency	11.1	-18.9	35.6	3.5	-3.3	7.4

Koruna deposits in the first half of 2004 were determined by a preference for holding short-term deposits and demand deposits by various economic sectors. This trend is characteristic primarily for deposits of enterprises, where demand deposits together with short-term deposits comprise approximately 99% (their share in comparison with the end of 2003 is essentially unchanged). Within deposits of enterprises the most significant growth was seen in overnight deposits, by SKK 13.3 billion and time deposits with a maturity of one year by SKK 3.3 billion, while one-month deposits fell by SKK 9.3 billion, 7-day deposits by SKK 6.5 billion and demand deposits by SKK 4.1 billion. Other maturities did not record any significant changes. The interest rate differential between demand and time (including savings accounts) deposits of enterprises fell by 0.8 points to 3.0 percentage points in consequence of the fall in average interest rates on time deposits (by 1.0 percentage point) as well as on demand deposits (by 0.2 percentage points).

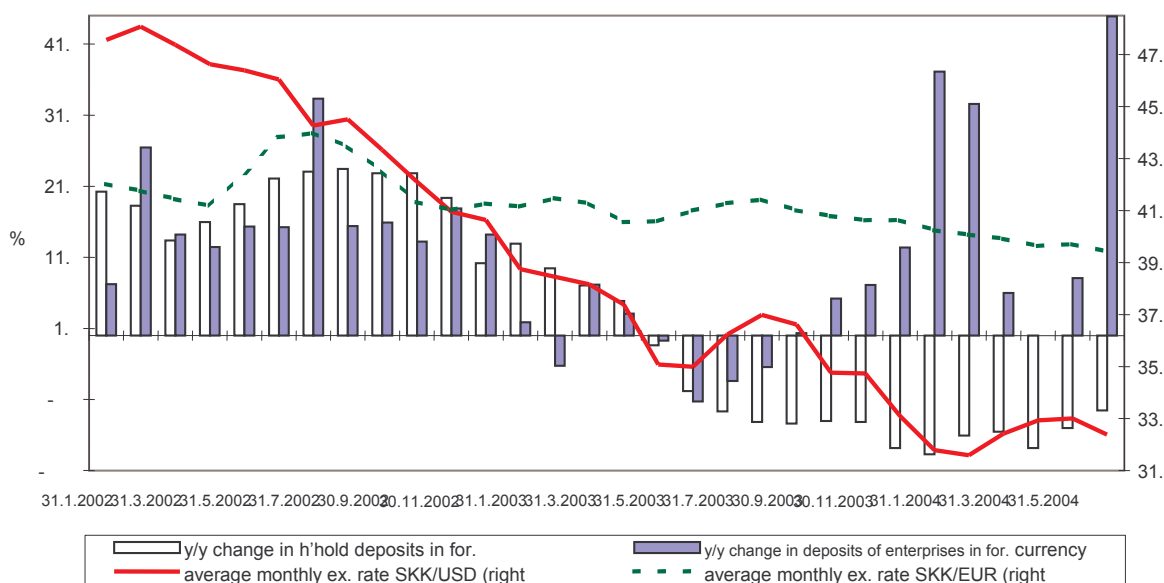
Household deposits have also continued to be characterised by a persistent preference for highly liquid funds, where the share of demand and short-term deposits in total household koruna deposits in the first half of the year increased by 1.0 percentage point to 80.4% as a result of an increase in demand deposits. Time deposits in the first half of 2004 fell by SKK 0.3 billion and savings deposits by SKK 6.8 billion. In the structure of time deposits the most significant change was seen in deposits with a maturity of up to one month, which fell by SKK 2.7 billion and 3-month deposits, which conversely grew by SKK 2.6 billion. Savings deposits recorded a relatively significant decline (of which home savings deposits fell only slightly by SKK 0.2 billion), where one-year deposits fell by SKK 4.3 billion and medium-term deposits by SKK 2.6 billion. The interest rate differential, i.e. the difference between the interest rate on demand and time deposits for households fell (by 0.4 percentage points) to 1.6 percentage points in consequence of a more significant fall in interest rates on time deposits (by 0.7 percentage points) than demand deposits (by 0.3 percentage points).

In the development of koruna deposits households continued in their trend of declining interest in time deposits, influenced primarily by level of the return offered on individual bank products. The falling interest rate differential concurrently acts to lower the attractiveness of time deposits in comparison with demand deposits. The growing use of mutual funds continued, where in the first half of 2004 the net value of assets allocated to open mutual funds operating in the Slovak financial market grew by SKK 16.4 billion.

Foreign currency deposits (at fixed 1993 exchange rate) grew in the first half of 2004 by SKK 4.3 billion, where their year-on-year rate of growth reached 9.5% (compared to a 6.1% fall in December 2003 on a year-on-year basis). Foreign currency deposits over the course of the first half-year were characterised by relatively volatile development, influenced primarily by the development of foreign currency deposits of enterprises. This is documented also by the development of the year-on-year rate of growth of foreign currency deposits of enterprises, which rose from 12.4% in December 2003 to 44.9% in June 2004 (where in individual months the rate of growth moved in a range from 0% to 44.9%). Foreign currency deposits of enterprises for the first half of 2004 grew by SKK 7.2 billion, while foreign currency deposits of households fell by SKK 2.9 billion. In the development of foreign currency household deposits there is a clear declining interest in holding such deposits, which is manifested in their falling volume since May 2003. The year-on-year rate of decline in foreign currency household deposits reached 10.5% in June (15.8% in December 2003).

After taking into account the change in the exchange rate in the first half of 2004 (a 3.0% appreciation against the euro and 0.2% against the USD), foreign currency deposits at the current exchange rate grew by SKK 2.9 billion and their year-on-year rate of growth increased from -13.9% in December to 2.7% in June. This growth was due to the deposits of enterprises, which from the start of the year grew by SKK 7.4 billion (the year-on-year rate of growth increasing from 3.3% to 35.6%), while household deposits recorded a decline of SKK 4.5 billion (the year-on-year rate of decline lessening from 22.8% to 16.0%).

Comparison of the development of foreign currency deposits (at fixed exchange rate 1.1.1993) and Slovak koruna exchange rate



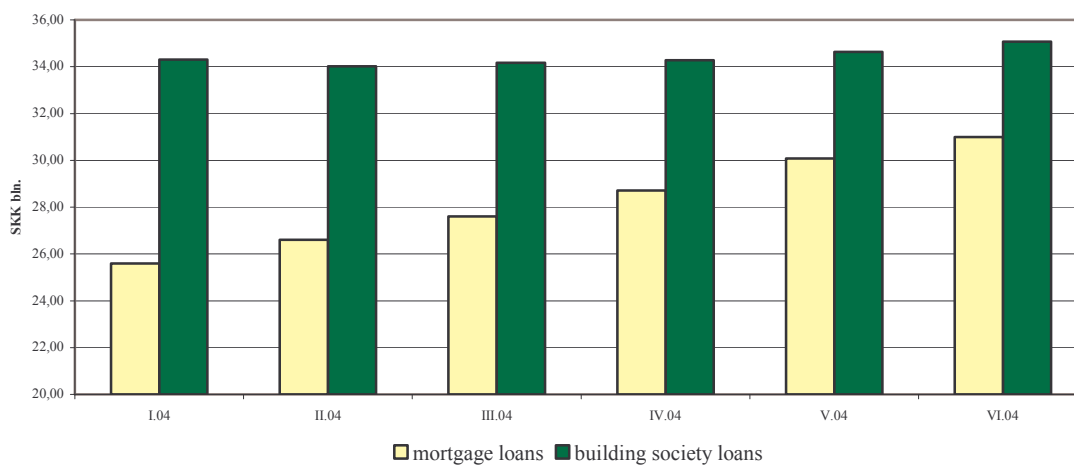
4.3 Lending Activity

Total credits (koruna and foreign currency at the current exchange rate) provided to the corporate sector, households, central and local authorities for non-budgetary needs represent credits statistically reported for the whole banking sector. From the methodological aspect this is not identical to loans to enterprises and households according to the monetary survey, which does not include the government sector.

The volume of credit in June 2004 had grown against the figure for the beginning of the year by SKK 15.4 billion, where this growth was influenced solely by foreign currency loans, which grew by SKK 17.3 billion, whereas koruna loans recorded a decline of SKK 1.9 billion. As at the end of the period monitored total credit reached SKK 427.8 billion, of which koruna loans represented SKK 328.8 billion and foreign currency loans SKK 99.1 billion.

In the framework of the sectoral structure the development from last year continued also in the first half of 2004, this being characterised by a significant growth in foreign currency loans and a decline in koruna-denominated loans to the corporate sector. The drawing of foreign currency credit was probably connected with the persistent interest-rate differential, as well as with the Slovak koruna's appreciation and expectations of a continuation of this trend. The more significant decline in koruna-denominated loans to enterprises in comparison with the beginning of the year (by SKK 17.5 billion) was influenced by a reduction in loans for current assets and of other loans (in total by SKK 12.4 billion). A relatively significant decline by SKK 15.9 billion was recorded also by classified loans. Their influence on the overall reduction of loans however represented only approximately SKK 6 billion (of which SKK 3.5 billion was the sale of loss-making receivables). At the same time, classified loans declined also due to the reclassification of long-term standard conditioned loans (SKK 9.9 billion) to standard loans (for current assets and for investment loans), which did not have an influence on the overall volume of loans. The total volume of loans was affected in a pro-growth manner by the household sector, in the framework of which koruna loans increased by SKK 13.9 billion, mainly in consequence of the development of mortgage lending. Even despite the fact that its growth in comparison with the second half of 2003 slowed slightly, (probably also in consequence of the reduction to the state contribution from 2.5% to 1.0%), the average monthly growth in mortgage lending represented approximately SKK 1 billion (in the first half of 2003 this figure stood at SKK 0.8 billion and in the second half of 2003 increased to more than a SKK 1.4 billion).

Households - mortgage lendings



From the aspect of industrial sector structure, the development of koruna-denominated loans in the first half of 2004 was influenced mainly by a decline in loans in industrial production, by SKK 7.6 billion (a share in credit of 12.6%), of which SKK 5.3 billion in metallurgy and engineering. A more significant decrease in the volume of koruna-denominated loans, by SKK 5.5 billion, was recorded in the generation and distribution of electricity, gas and water (a share in credit of 8.6%) and a decline of SKK 5.4 billion in koruna loans also occurred in the transport, warehousing, posts and telecommunications sector (a share in credit of 5.6%). The sector “other” acted in a pro-growth manner on koruna-denominated loans (by SKK 14.9 billion, a share in total credit of 46.0%). Koruna-denominated loans recorded a growth also in the sector trade, repair of consumer goods and motor vehicles; hotels and restaurants (by SKK 2.9 billion, a share in total credit of 13.2%).

Within the koruna-denominated loans, from the aspect of time structure, only long-term loans grew (by SKK 4.1 billion) against the figure for the start of the year. Of total koruna-denominated loans as at the end of June 62% comprised loans to the corporate sector, 30% loans to households, 7% loans to public administration and 1% other loans.

Foreign currency loans grew in all maturities. Short-term loans grew most significantly (by SKK 8.2 billion) and long-term loans (by SKK 6.5 billion). Of the total volume of loans denominated in foreign currencies 87% were to the corporate sector, 10% to non-residents and 3% to public administration.

Time structure of loans in SKK and foreign currency (June 2004)

	Loans in SKK		Foreign currency loans		Total loans (SKK + f.c.)	
	Change on 1.1.2004 (SKK bln.)	Share (%)	Change on 1.1.2004 (SKK bln.)	Share (%)	Change on 1.1.2004 (SKK bln.)	Share (%)
Short-term loans	-3.6	29.4	8.2	39.0	4.6	31.6
Medium-term loans	-2.4	29.5	2.6	28.7	0.2	29.4
Long-term loans	4.1	41.1	6.5	32.3	10.6	39.0
Total loans	-1.9	100.0	17.3	100.0	15.4	100.0

4.4 Interest rates

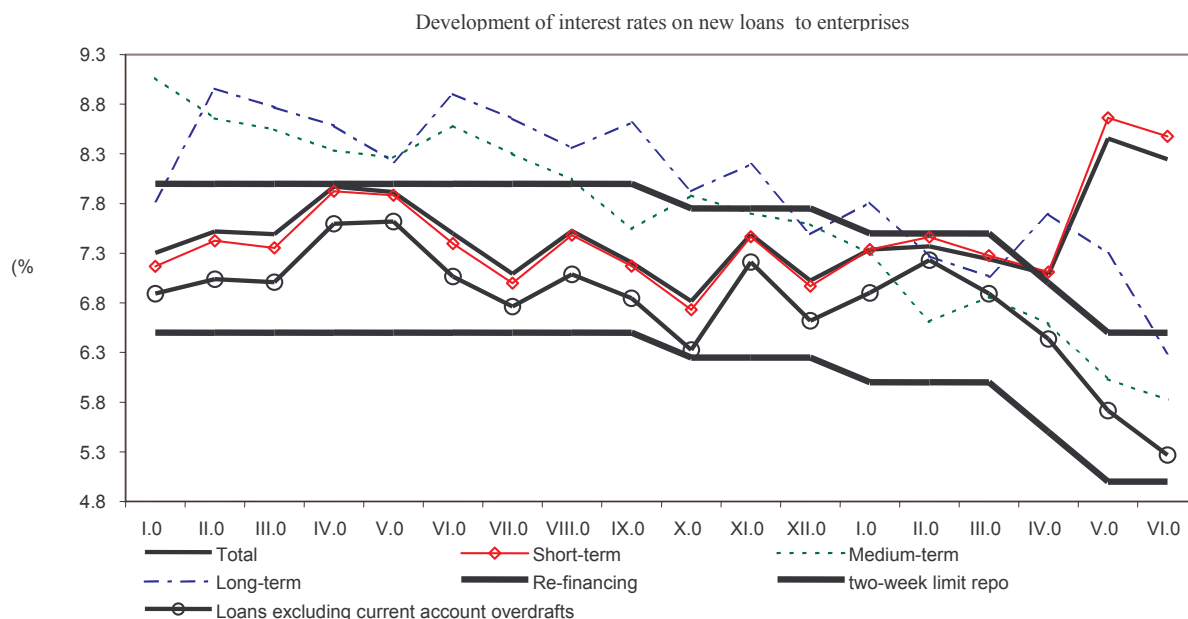
The development of customer interest rates in the first half of 2004 was determined by the reduction of NBS key interest rates in December 2003, March and April 2004 in total by 1.25 percentage points. Similarly, at the end of June the Banking Board of the NBS decided on a further reduction in key rates by 0.5 percentage points, which should be manifested in the development of customer interest rates in the coming months. The reduction of key NBS rates was reflected variously in customer rates. An obvious reaction is clear primarily in interest rates on deposits both of households as well as enterprises. The average interest rate on total deposits, of both households and enterprises, was over the course of the whole half-year below the level of the NBS sterilisation rate. In comparing the interest accrued on time deposits and that on savings deposits, however, the difference is clear. The accrual of interest on time deposits of enterprises over the course of the first half-year moved above the level of the sterilisation rate, while household deposits accrued interest below this level. A different development was recorded by the interest rates on new loans (excluding current account overdrafts). In the case of new loans to households interest rates increased and their level moved above that of the refinancing rate, while interest rates on new loans to enterprises over the course of the first half-year declined, where these moved below the level of the refinancing rate.

Average interest rates on new loans

The average interest rate on new loans (with the exception of loans at an interest rate of 0%) had increased in June 2004 in comparison with the end of 2003 by 1.3 percentage points to 8.5%. The development of the interest rate on new loans has however in 2004 been significantly determined by the change in the methodology for calculating the interest rate on current account overdrafts, where since 2004 the method of cumulative debit turnovers has been applied in its calculation. This has been manifested in a significant growth in the current account overdrafts share in total new loans, with a subsequent impact on the level of the average interest rate. With regard to the fact that short-term credit has a critical share (approx. 85%) in total new loans, the influence of the change in methodology is reflected significantly in the level of the average interest rate on the total new loans. Concurrently, current account overdrafts have a significant share also in new short-term loans, where they represent approximately 34% (the average for the period January to June). The average interest rate on total new loans, excluding the influence of current account overdrafts, the average rate in June, in comparison with December 2003, had fallen by 1 percentage point. In a comparison of interest rates on short-term loans, this difference is even more marked, where against December 2003 the rate had increased by 3.6 percentage points, while excluding current account overdrafts a decline of 1.4 percentage points was recorded. New Medium-term loans recorded a reduction in the average interest rate by 0.4 percentage points to 8.2%, where their cumulative share in total new loans was 10.0%. The average interest rate on new long-term loans fell by 0.1 percentage points to 6.9%, their share however formed only 5.0%.

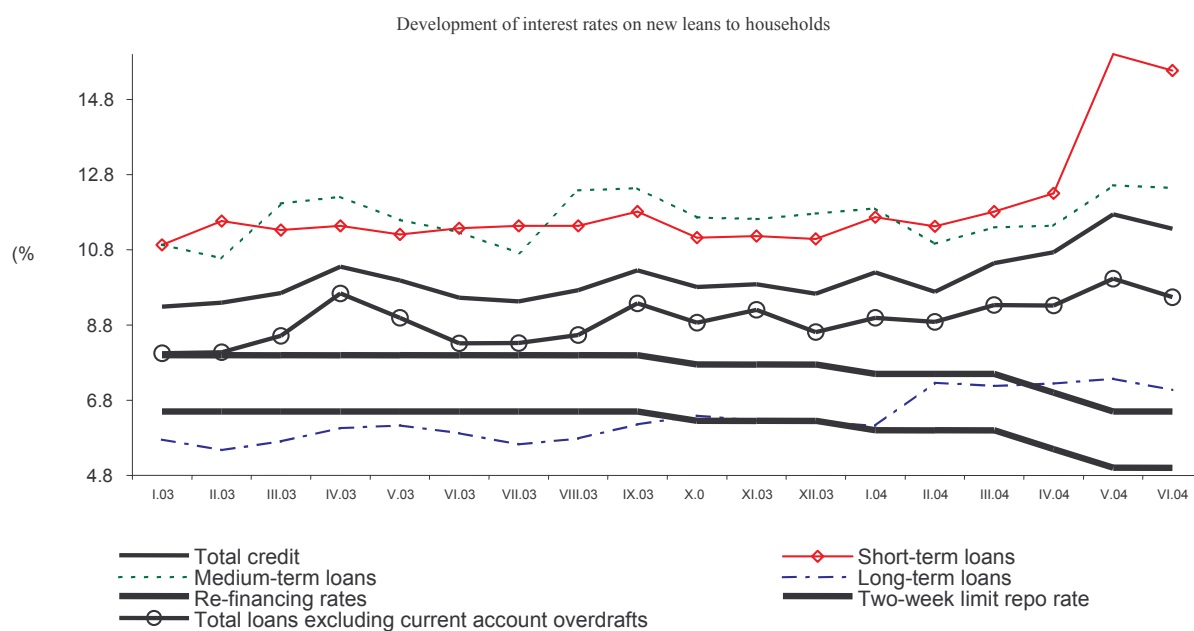
The development of the average interest rate on new loans to enterprises was in the first half of 2004 determined primarily by the development of prices of short-term loans, the share of which in total new loans is approximately at the level of 90%. The influence of the change in methodology on the level of interest rates on new loans to enterprises is significant, with regard to the fact that the of current account overdrafts represents approximately 35% of new credit (the average for the first half of 2004). The average interest rate on new loans to enterprises had in June, in comparison with the end of 2003, increased by 1.2 percentage points to 8.2%, though when removing current account overdrafts this rate fell by 1.4

percentage points to 5.4%, where its level over the course of the first half of the year was below the level of the NBS refinancing rate. From the aspect of loan-use purpose (with a decisive influence on the level of the interest rate) other loans¹ recorded a decline in their interest rate by 1.3 percentage points to 5.2%, investment loans by 0.8 percentage points to 5.9%, while the cost of an current account overdrafts, primarily in consequence of the change in methodology, increased by 3.8 percentage points to 12.4%.



Similarly, the development of average interest rates on new loans to households was influenced significantly by the change in methodology as regards current account overdrafts. In comparison with December 2003 the average interest rate on total new loans rose by 1.7 percentage points to 11.4%, and excluding the effect of current account overdrafts, it rose by 0.9 percentage points to 9.5%, where throughout the whole half-year this average rate remained above the level of refinancing rate. When classifying new loans by maturity, the representation of constituent maturities is more balanced than that in the case of loans to enterprises, where the share of short-term loans represented 40%, medium-term loans 28% and long-term loans 32% (the average for the first half of 2004). In classifying loans according to purpose of use (with a critical influence on the level of the interest rate), interest rates on mortgage loans over the course of the half-year were characterised by a progressive growth from 5.2% in December 2003 to 6.0% in June 2004, which was probably connected with the reduction in the state contribution from 2.5% to 1%. The cost of overdrawing current accounts rose by 5.1 percentage points to 16.3% in June 2004 (in particular under the influence of the change in methodology) and bridging loans by 0.2 percentage points to 7.4%. The average interest rate on consumer credit fell from 14.3% in January 2004 to 14.0% in June 2004 (with regard to the change in methodology made in 2004, it is not possible to make a comparison with the end of 2003).

¹ Though the change in methodology in other loans occurred in 2004, with regard to the types of loans drawn within this group by enterprises, the influence of the methodological change should not be significant.



Average interest rates on the volume of loans

The development of interest rates on the volume of loans over the course of the first half of the year was characterised by a gradual decline. The average interest rate on the volume of loans (with the exception of loans at an interest rate of 0%) had decreased in June in comparison with the end of 2003 by 0.4 percentage points to 6.9%. The decline in average interest rates on short-term loans represented 0.7 percentage points to 7.1%, on the medium-term loans 0.5 percentage points to 8.3%. The price of long-term loans fell by 0.4 percentage points to 6.5%.

In a comparison of interest rates on loans to enterprises and households an opposing trend can be seen. While interest rates on the volume of loans to enterprises in the first half of 2004 fell by 0.8 percentage points, in the case of loans to households they increased by 0.4 percentage points.

Interest rates on the volume of loans to enterprises at all maturities had fallen in June in comparison with the December 2003, where the interest rate on medium-term loans fell by 1.0 percentage point, on short-term loans by 0.9 percentage points and on long-term loans by 0.4 percentage points. From the aspect of loan-use purpose (with a critical influence on the level of the interest rate) the most significant decline in rates was recorded by “other” loans, current account overdrafts (both declining by 1.0 percentage point) and capital investment loans (a decline of 0.6 percentage points).

On the other hand, interest rates on loans to households in the first half of the year increased, where the interest rate on total loans grew by 0.4 percentage points, on short-term loans by 1.2 percentage points, on medium-term loans by 0.6 percentage points and on long-term loans by 0.3 percentage points. In the framework of the purpose of use of loans having the highest share in total loans, the cost of current account overdrafts rose by 0.7 percentage points, the cost of mortgage loans with a state premium by 0.3 percentage points, bridging loans by 0.2 percentage points and the price of building society loans remained unchanged.

Average interest rates on deposits

The average interest rate on deposits over the course of the whole half-year remained below the level of the sterilisation rate, where its development was characterised by a general decline. The reduction in key NBS rates over the course of the first half-year was reflected in interest rates on deposits, where the average interest rate on deposits in June 2004 had declined against that of December 2003 by 0.5 per cent points to 2.5%. The interest rate on demand deposits recorded a decline of 0.4 percentage points to 1.1%, on time deposits by 0.8 percentage points to 3.6% and on savings accounts by 0.7 percentage points to 2.0%.

From the aspect of the time structure of time and savings deposits, the most significant decline in the average interest rate was on medium-term savings deposits (by 1.3 percentage points) and short-term savings deposits (by 1.2 percentage points), while interest rates on daily deposits grew (by 0.8 percentage points).

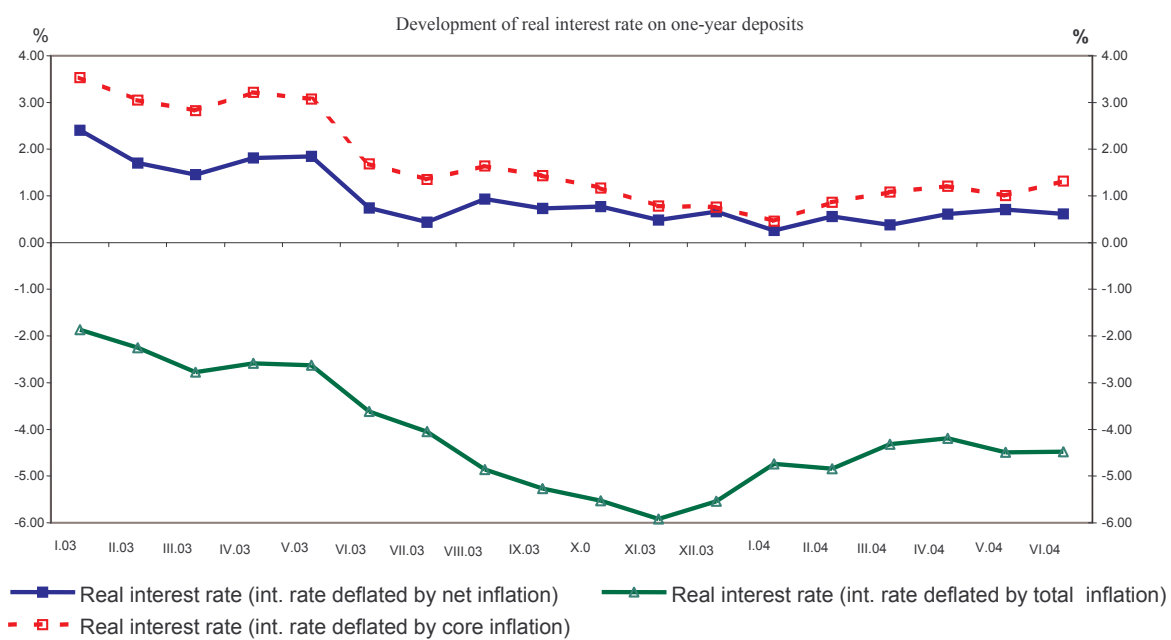
From a comparison of the development of interest rates on deposits there is a clear persistent difference between the interest accrued on deposits of enterprises and those of households. The reduction in key interest rates has undoubtedly been reflected in interest rates on household deposits, which over the course of the half-year recorded a gradual decline. In the case of interest rates on deposits of enterprises, this influence was apparent primarily in the second quarter. Even though interest rates on deposits of enterprises fell by approximately the same rate as those in the case of household deposits, the interest accrued on deposits of enterprises remains significantly higher than that on household deposits, a fact that is connected with the volume of funds on a single account, as well as with the structure of their investing.

	Total			Households			Enterprises		
	Dec 03	Jun 04	Diff.	Dec 03	Jun 04	Diff.	Dec 03	Jun 04	Diff.
Total deposits	3.0	2.5	-0.5	2.6	2.0	-0.6	3.5	2.8	-0.7
demand	1.5	1.1	-0.4	1.1	0.9	-0.2	1.3	1.1	-0.2
time and savings deposits	3.9	3.2	-0.7	3.2	2.5	-0.7	5.1	4.1	-1.0
time	4.3	3.6	-0.7	3.5	2.8	-0.7	5.1	4.1	-1.0
savings	2.8	2.0	-0.8	2.7	2.0	-0.7	3.2	2.4	-0.8
Short-term deposits	4.1	3.3	-0.8	3.2	2.4	-0.8	5.1	4.1	-1.0
Medium-term	3.1	3.1	0.0	3.0	2.0	-1.0	4.4	3.6	-0.8
Long-term	3.1	3.0	-0.1	3.1	3.0	-0.1	3.1	3.0	-0.1

(%)

The real interest rate on one-year deposits in June 2004 grew, compared to the end of 2003, by 1.0 percentage point, reaching the negative value of 4.5%. The increase in the real interest rate was influenced by a faster fall in year-on-year inflation than the fall in interest rates on one-year deposits.

By deflating the interest rate on the volume of deposits with a maturity up to one year by net, or respectively core inflation, the real interest rate in June 2004 reached the positive value of 0.6%, or respectively 1.3%. In comparison with the end of 2003 this represented no change, or respectively a growth of 0.6 percentage points as a result of the reduction in the average interest rate on one-year deposits by 0.2 percentage points alongside the fall in net and core inflation (by 0.1 and 0.7 percentage points respectively).



5. FINANCIAL MARKETS

5.1 Money Market

Treasury bills

The Agency for Debt and Liquidity Management (ARDAL), which since 2004 has on behalf of the Ministry of Finance of the SR decided on the issue conditions of government securities as well as the results of auctions, began issuing treasury bills (T-bills) in February. In accordance with the Time Schedule for Issuing Government Securities for 2004, ARDAL over the course of the first half-year invited tenders for 10 issues with a maturity of 364 days, and which were placed on the market via a Dutch auction. Following several years' practice of the American auctions, the change in the form of the primary sale was required by the reform of the tax law. The new tax law defines the exceptions in the case of which revenue from securities is not a part of the tax base, but subject to withholding tax. These subjects have access enabled to the market in T-bills and in the case of an American auction it was not possible on the maturity date to quantify their revenue and thus neither to ensure the deduction of withholding tax. Therefore a Dutch auction is presently the necessary form of realising the auction manner of the primary sale of T-bills.

In the period assessed ARDAL placed on the market T-bills in the total value of SKK 19.7 billion, representing 20.6% of the investors' total demand. This low percentage of demand satisfaction was caused by the favourable development of the state's budgetary management.

The foreign investors' share in the primary purchase was 11.2%. Purchases by domestic commercial banks represented 71.3%. The share of other domestic investors formed 17.5%.

The average yield accepted reached 4.964%. Yields throughout the period assessed were below the level of interest rates on the domestic money market of a comparable maturity. T-bills in the first half of 2004 placed on market were on average 17 base points below the level of BRIBOR at a comparable tax burden.

T-bill yields over the period assessed recorded a falling trend. At first the decline was only slightly apparent, becoming more significant only from April onwards, where this was due to the double reduction in key interest rates. Accepted T-bill yields began to fall still more markedly in June. This was a result of the increased interest in government securities due to the non-acceptance of demand in the NBS T-bill auction and the shortening of interest in repo tenders. This situation developed pressure for lower interest requirements by investors.

Realisation of monetary policy and money market rates

In the first half of 2004 the Banking Board of the NBS at its meetings in March, April and June repeatedly reduced key rates by 50 base points.

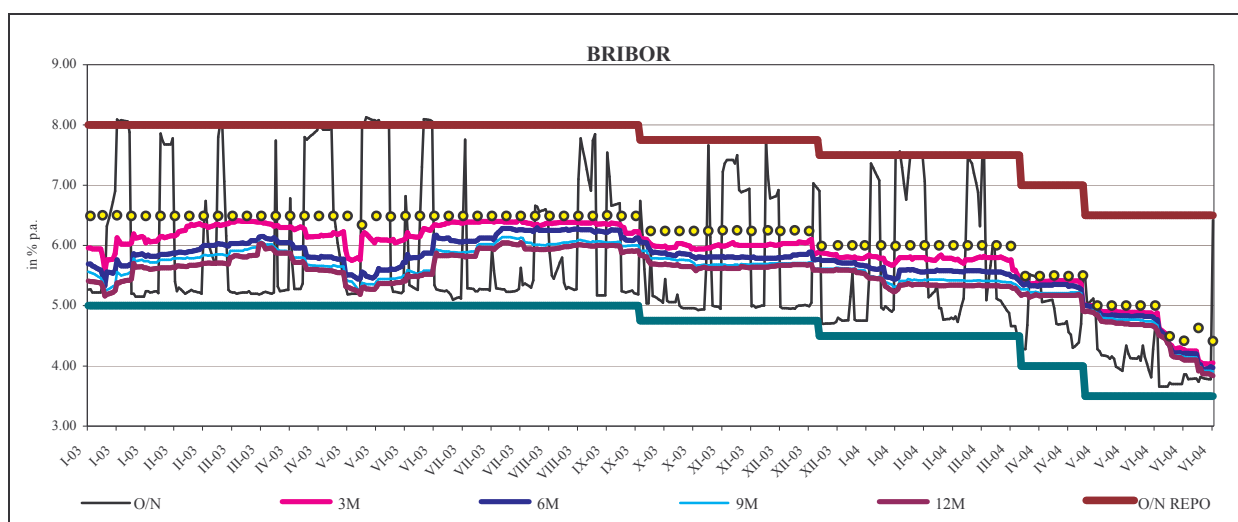
Despite the high volatility of the shortest rates there was already in January noticeably lower sensitivity to changes in the demand for daily liquidity. The reason was the introduction of the possibility of drawing interest-free intra-day credit at the NBS backed by securities registered at the central register of short-term securities administered at the NBS. The use of intra-day credit has ensured the smoother course of the system of payments and reduced the transmission of demand for the shortest deposits at the time of a daily liquidity sub-balance. A

further stabilising factor was the introduction of a change, made at the start of the year, in the calculation of the volume of funds for accruing interest on compulsory minimum reserves. The change concerned the cancellation of the calculation of the accrual of interest on compulsory minimum reserves on a daily basis on the balances on the clearing account, and the introduction of an average balance for the period. In this way banks are not forced to settle up their position on a daily basis and increase demand for the shortest deposits in a period of a persistent daily liquidity sub-balance. A more significant decline in interest rates in January on maturities of 3 to 12 months was influenced by the opening of domestic and foreign banks' positions and the depositing of funds, also via swaps, ensuing from this.

The reduction in NBS key interest rates in March showed through in interest rate prices on the money market to a lesser extent. The reason was the partial incorporation of expectations resulting from a reduction in NBS interest rates even before the meeting of the Banking Board of the NBS. The most significant decline was recorded in the case of one-month to three-month maturities and to a lesser degree in the case of maturities from 6- to 12-months.

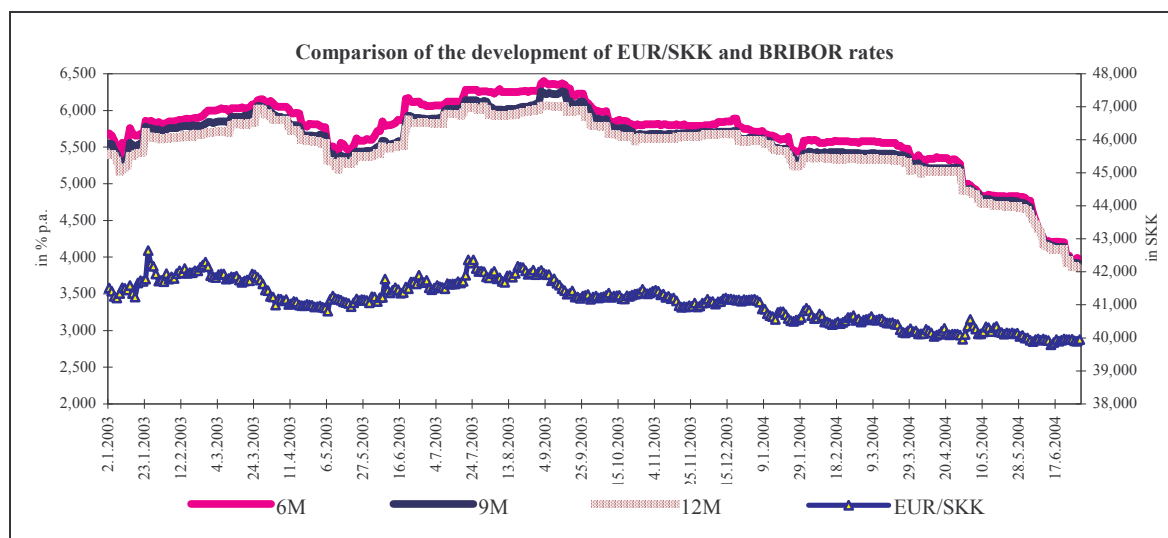
The development of prices of the shortest rates in April was influenced by the activities of the Agency for Debt and Liquidity Management (ARDAL) on the State Treasury account, to under the competence of which also tax offices passed from the beginning of the month. The sending of payments to the State Treasury clearing account and the subsequent endeavours of ARDAL to valorise the funds thus acquired on the interbank market have removed significant deviations in the volume of interbank liquidity at the dates of tax payments, which has led to a reduction in the volatility of the cost of the shortest rates and maintaining their quotations prevalingly in the lower part of the corridor, defined by the one-day rates of the NBS. The April fall in interest rates on maturities above three months was connected with expectations of the results of a referendum and those of presidential elections, to which foreign banks reacted by purchasing Slovak koruna on the foreign exchange market and its subsequent depositing on the money market. To the reduction in NBS key interest rates in April, BRIBOR rates reacted with an appropriate decline.

The growth in the volume of funds on the State Treasury account in May raised the banking sector's dependence on State Treasury funds, and ARDAL in an effort to improve their valorisation on the money market succeeded, through its activities, in keeping the cost of one-day deposits above the 4% level.



For the purpose of eliminating excessive pressures for an appreciation of the Slovak koruna, the NBS in June proceeded to change the use of its monetary instruments. Under the influence of a shortening of demand in two-week repo-tenders and the rejection of bids in an NBS T-bill auction, a significant growth in surplus liquidity occurred, having the aim of weakening speculative pressures on the exchange rate. The effort to deposit the surplus liquidity on the interbank market led to a sharp decline in the whole yield curve on the money market. The repeated shortening of demand in tenders thus left the banking sector in a significant surplus of daily liquidity and kept the price of deposits across the yield curve below 4.5%. Reference banks reacted to a verbal announcement by the NBS at the end of the month on the probable reduction of key rates by a temporary halting of BRIBOR rate quotations. After the renewal of their quotation the prices of deposits with a maturity from six to twelve months fell below 4% and remained at this level through until the end of the half-year. Uncertainty over further development of rates on the money market led banks to an increase in the spread between buy and sell prices, to 50 base points. The money market did not react to the reduction in NBS key rates on the last day in June, as it had already incorporated their decline into prices.

In 2004, too, there continued the interconnection of the foreign exchange and money market. The strengthening of the Slovak koruna against the euro brought about by its purchasing on the foreign exchange market was subsequently manifested in the depositing of funds thus acquired on the money market, usually by means of swaps. At the same time domestic banks in which foreign banks deposited the Slovak koruna sold these funds on the interbank market, which initiated a further decline in interest rates.



The management of banking sector liquidity by means of trades on the free market was effected through the use of unchanged basic instruments for trades on the free-market. The development of averages of surplus interbank liquidity deposited at the NBS recorded over the first half of 2004 a growth of SKK 39.4 billion. The main factors contributing to this increased volume of liquidity were NBS activities on the foreign exchange market (SKK 14.7 billion), a transfer of the resources of the State Fund for the Decommissioning of Nuclear Facilities and Handling of Spent Nuclear Fuel from an account administered at the NBS into the banking sector (SKK 10.8 billion), and a reduction in required minimum reserves at the start of the year (SKK 6.3 billion). Cyclical changes in the quantity of liquidity were dealt with by changes in the volume of issued currency in circulation and changes in expenditures and incomes of the state budget.

The NBS continued in the regular renewal of payable issues of three-month NBS T-bills. From the start of 2004 the NBS proceeded to change the form of the primary sale from that of a Dutch auction to an American auction. In this way all participants in the auction are satisfied at the price they stated in their application to the auction. This change in the form of auction was enabled by the amendment to the Income Tax Act. No less substantial a change was the decision of the NBS Banking Board to limit the share of NBS T-bills in the total sterilisation so that the volume of issued NBS bills moved approximately at the level of 25%.

in SKK billion

Form of intervention	2003		2004					
	1st half year	2 nd half year	January	February	March	April	May	June
SRT	-107.426	-116.176	-113.061	-107.185	-115.526	-125.040	-131.546	-149.067
O/N	-2.793	-3.594	-1.408	-2.456	-3.408	-647	-1.471	-8.553
NBS T-bills	-50.999	-44.387	-66.837	-81.164	-77.160	-70.047	-70.000	-43.000
TOTAL	-161.218	-164.157	-181.306	-190.805	-196.094	-195.734	-203.017	-200.620

In the first half-year the NBS announced 26 sterilisation repo tender (SRT) auctions with a two-week maturity. Demand was shortened in five tenders. The NBS shortened demand for the first time due to a predicted lack of liquidity in the banking sector. In the other four tenders it concerned a change of approach at the NBS by means of monetary instruments in June. The average yield achieved in repo tender auctions achieved a deviation of 0 – 1 base points against the repo tender limit rate throughout the first five months. The situation in June was reflected in an increase in the deviation from the tender limit rate to 37 – 59 base points.

Banks reacted to fluctuations in daily liquidity by using both sides of one-day trades with the NBS. Over the first three months banks used refinancing repo trades to the greater extent. Under the effect of a growth in the influence of ARDAL's activities this situation gradually changed and resulted in a smaller refinancing need and a growth in the volume of deposits at the NBS. The maximum level of refinancing reached SKK 11.5 billion and was realised on the last day of the half-year, which was connected with the acceptance of greater demand following a preceding significant shortening of the demand in tenders. The greatest deposit, in the volume of SKK 23.5 billion, was deposited by banks over the course of June.

In accordance with the process of harmonising the monetary instruments of the NBS with those of the ECB, the National Bank of Slovakia, with effect from the start of the year, reduced its rate of compulsory minimum reserves (CMR) for the banking sector by 1 percentage point from 3% to 2%. The level of the CMR rate was thus harmonised with its counterparts in the eurozone. The basis for calculating the CMR, its interest accrual, and the period of its valorisation remained unchanged.

The reduction in the CMR rate was manifested in a fall in the level of these reserves by approximately SKK 6.3 billion. The actual fulfilment of the CMR for the whole banking sector over this first half of 2004 was in line with the more significant volume in April. In conditions of significant surplus liquidity and continuing sterilisation interventions by the NBS, the set volume of CMR in each month of the first half of 2004 was adhered to and was not greatly exceeded. The average monthly surplus reserves following NBS interventions moved in the range from SKK 0.02 to 0.32 billion.

Fluctuations in daily money reserves in individual periods moved from SKK 20.7 billion of surplus reserves through to insufficient reserves of SKK 11.25 billion. The most significant

variability measured by standard deviation in the development of money reserves for the first half of 2004 was in June.

(in SKK bln. and in %)

	Set CMR	Actual fulfilment of CMR plnenie PMR		
		average	% fulfilment	standard deviation
January	15.59	15.70	100.70	5.85
February	15.61	15.63	100.13	5.76
March	16.01	16.03	100.14	5.67
April	15.84	16.15	101.99	3.95
May	15.53	15.57	100.27	3.45
June	16.16	16.23	100.45	6.10

In the first half of 2004 non-fulfilment of the set compulsory minimum reserves did not occur once.

Development of banking sector liquidity

The first half of 2004 saw a continuation of the sterilization nature of monetary policy. The volume of funds sterilised moved within the range of SKK 170 billion to SKK 220 million, having a tendency of slight growth.

A substantial source for the increase in the banking sector's liquidity included the NBS operations in the foreign exchange market against the inappropriate appreciation of the Slovak koruna exchange rate, the cumulative volume of which in the first half-year amounted to SKK 14.7 billion.

The increase in liquidity was also stimulated by the current budgetary performance, which with the exception of March and April ended in deficit and which, under the influence of an overhanging in current expenditures of the state budget to commercial banks (including expenditures on government bond's coupons in the volume of SKK 9.7 billion) above current incomes, increased in the first half-year the banking sector's liquidity on a cumulative basis by approx. SKK 4 billion.

The gradual transfer of state funds from accounts with the NBS to the State Treasury in connection with the commencement its activity as of 1 January 2004, the releasing of funds from selected asset accounts with the NBS and the moderately growing volume of currency in circulation also acted to increase liquidity.

Liquid funds of the banking sector were also increased by some one-off impacts. The latter included a reduction in the CMR rate from 1 January 2004 by 1 percentage point (compared to December 2003, an increased need for sterilisation by SKK 6.3 billion) and the January transfer of resources from state funds from the NBS into the banking sector (liquidity inflow in the volume of SKK 10.8 billion).

The pro-liquid effect of the factors above was partially compensated for by the overhang in the volume of issued government securities above their repayments, which drew off liquidity in the volume of approx. SKK 13 billion, and by the realisation of daily deposits by the Agency for Debt and Liquidity Management at the NBS. The main part of surplus liquidity was sterilised via open market operations.

Under the conditions of the persistent impact of pro-liquidity operating factors, the first half of 2004 saw an increase in the NBS's sterilisation position vis-à-vis the banking sector from SKK 176 billion (as at 31 December 2003) to SKK 215.6 billion (as at 30 June 2004) and its average level for the 6 months of 2004 amounted to approx. SKK 196 billion (in 2003 the respective figure was SKK 162.7 billion).

5.2 Capital Market

Primary market

Treasury bonds

The Ministry of Finance SR (MF SR) in the Time Schedule of Treasury Bond Issues for 2004 stipulated that all issues will be reopening and with a maximum total issue of SKK 40 billion.

On 1 January 2004 a new system of debt and liquidity management by the Agency for Debt and Liquidity Management (ARDAL) was launched. The establishment of ARDAL resulted in a new division of activities and responsibilities between the Ministry of Finance SR, ARDAL, State Treasury and the National Bank of Slovakia, pursuant to Act No 575/2001 Coll. on the organisation of activities of the government and central state administration bodies. The NBS as an agent of the MF SR is currently entrusted with the issuing and repayment of government securities, including revenues on treasury bonds.

In the first half of 2004 in total 5 issues of treasury bonds in the total value of SKK 48.0 billion took place. Compared to the same period last year, this represented an decrease in the amount of treasury bonds issued by 47.7%, i.e. a fall of SKK 43.7 billion. All issues were limited with the maximum amount of each issue of SKK 40.0 billion, and all were reopening.

Over the course of the second quarter of 2004 an issue of treasury bonds denominated in EUR in the value of EUR 1 billion was made. A part of the funds obtained from this issue was used for repaying foreign issues of treasury bonds from 1999.

In 2004, for the first time in the history in the issuing treasury bonds, a 15-year issue with a fixed coupon of 5.30% p.a. was opened.

Structure of treasury bond issues by maturity

	1 st half of 2003 in SKK billion	Number of issues	1 st half of 2004 in SKK billion	Number of issues
1-year	15.3	3	-	-
1.5-year	18.0	3	-	-
2-year	16.4	2	-	-
3-year	-	-	25.9	1
5-year, flexible coupon (12M BRIBOR)	-	-	2.3	1
5-year, fixed coupon	16.4	1	7.7	1
7-year	16.4	1	-	-
10-year	17.5	2	4.8	1
15-year	-	-	7.3	1

Of the total volume, the largest share pertained to the 3-year issue (53.9%), followed by the 5-year issue with a flexible coupon 4.7%, 15.9% was formed by the 5-year issue with a fixed

coupon, the 10-year issue represented a share of 10.1% and the 15-year issue 15.3%. All five issues were increased by total amounts of SKK 40.0 billion. Overall in the first half of 2004 13 auctions were held.

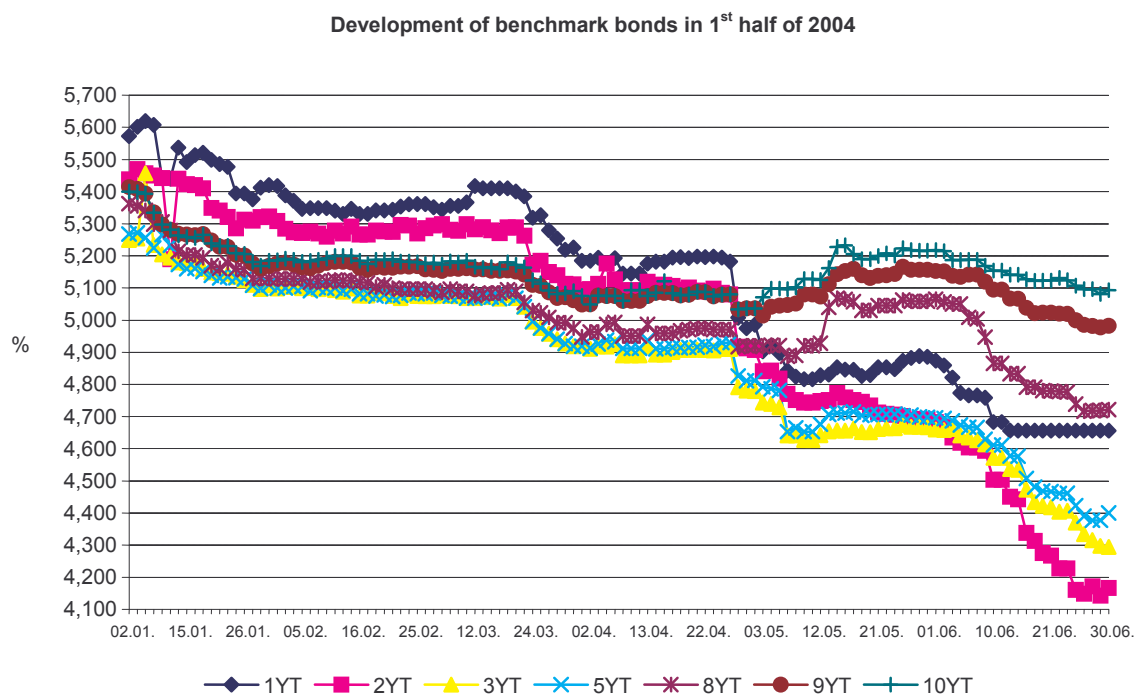
ARDAL in the first half of 2004 cancelled 2 issues planned according to the Time Schedule of Issues for 2004 with regard to the non-functioning of the operation at the Central Securities Depository, due to which it was not possible to credit, or respectively execute transfers of securities at this depository.

The total demand for treasury bonds in the first half of 2004 was SKK 95.2 billion, representing, against the same period of 2003 (SKK 168.6 billion) a fall of 43.5%. The average value of an issue was SKK 3.7 billion, where in the first half of 2003 this figure stood at SKK 5.1 billion. This significant decrease in the size of issues in comparison with the first half of 2003 was a consequence of inviting tenders to issues of T-bills.

The greatest interest was expressed in treasury bond issue no. 200 with a zero coupon. Investors' demand for this issue was SKK 6.6 to 19.8 billion, moving in relative terms within the range of 113.9% to 201.4%. Investors' demand for treasury bonds by individual maturity period was as follows: 5-year issues (treasury bond nos. 201 and 203) up to 669.8%, 10-year issue (treasury bond no. 202) up to 303.2%, and in the case of the 15-year issue (treasury bond no. 204) demand was up to 301.7%.

At 30 June 2004 27 foreign investors, forming 19.1% of the total number, were registered on the primary market in treasury bonds.

Since the beginning of 2004 the treasury bond benchmark has been fully functioning at the NBS, in which the banks – contributors quote daily, on a voluntary basis, selected treasury bonds with a maturity from 1 to 10 years. The aim of this is to have a benchmark curve created from the average of banks' quotations for the prices of individual securities contained in that curve. The manner of creating the benchmark curve is determined by the "Rules for Creating the Benchmark Yield Curve". 8 entities participated in its creation. The reduction in key NBS interest rates was apparent also in the benchmark yield curve.



Payout and repayments of treasury bonds

In the first half of 2004 revenues from treasury bonds were paid out in the total sum of SKK 13.6 billion, of which SKK 1.9 billion (13.9% of the total volume) to foreign investors, to domestic investors SKK 11.7 billion (86.0% of the total sum), of which to bond creditors SKK 0.1 billion (0.7% of the total sum).

Against the first half of 2003, the first half of 2004 recorded a fall in the total revenues paid out from treasury bonds (SKK 16.9 billion in the first half of 2003) by 19.5%, to foreign investors by 82.9% (SKK 11.1 billion in the first half of 2003), where in the payout to domestic investors revenues increased by 101.0% (SKK 5.8 billion in the first half of 2003) and to bond creditors 66.7% fewer revenues were paid out (SKK 0.3 billion in the first half of 2003).

In the first half of 2004 9 issues in the nominal value volume of SKK 31.1 billion were repaid. To foreign investors the nominal value of SKK 8.2 billion was paid out (26.4% of the total volume), to domestic investors almost SKK 22.9 billion (73.6%), of which bond creditors were received SKK 0.09 billion (0.3%). Overall, revenues and the nominal value paid out in the first half of 2004 were in the amount of SKK 44.8 billion.

In the first half of 2004, compared to the same period last year, the nominal value paid out to domestic investors was almost 10 times higher, where the volume paid out to foreign investors fell by 82.9%. In the framework of domestic investors, the nominal value payout to bond creditors fell by 92.5%.

Non-treasury bonds

The first half of 2004 saw 9 issues of mortgage bonds. Compared to the same period of 2003 this represented an increase of 5 issues. The total sum of mortgage bonds issued reached SKK

6.5 billion, representing an increase of SKK 2.5 billion on the same period of 2003. Issuers were Tatra banka, Slovenská sporiteľňa, OTP Banka, VÚB, Unibanka, Istrobanka.

Secondary market

On 1 January 2004 the new act on collective investment No 594/2003 Coll. entered into force, taking into account all existing EU standards. Likewise, on 1 January 2004 an amendment to act on the stock exchange No 429/2002 Coll. entered into force, where this deals with the manner of approving company prospectuses.

General overview of stock exchange trading

During 124 trading days the Bratislava Stock Exchange (Burza cenných papierov Bratislava (BCPB)) in the first half of 2004 made 7 762 transactions, representing a fall of 53.1%. The total financial volume reached SKK 161.5 billion, which compared to the same period of 2003 is a decline of 66.6%. Trades in equity securities reached SKK 18.4 billion and their share in the total volume of trades was 11.4%. Price-setting transactions represented SKK 14.2 billion and in the total volume achieved a share of 8.8%.

Bond trading

The total financial volume of trades in bonds for the first half of 2004 declined markedly, to SKK 142.6 billion (a year-on-year fall of 69.5%). This fall in the financial volume was caused also by the amendment to the income tax act which prevents the transfer of securities to foreign entities for tax advantage purposes.

The share of the volume of treasury bond trades represented 98.6% in 933 transactions. The most traded titles were treasury bonds – the series 142 (SKK 50.6 billion, 45 deals), series 200 (SKK 34.1 billion, 170 deals), and series 191 (SKK 9.0 billion, 79 deals). From among non-treasury bond issues the most successful were the listed bonds of Istrobanka II. (SKK 416.5 million, 5 deals), Železiarne Podbrezová (SKK 327.5 million, 3 deals). The most traded security from the aspect of number of the transactions concluded (170) was the treasury bond series 191.

The total number of issues on the BCPB markets at 30 June was 68, of which 42 on the listed main market, 18 on the listed parallel market, none on the listed new market and 8 issues on the regulated free market. Of this total number 1 issue on the free market were Eurobonds.

The share of foreign investors in the total BCPB turnover for the first half of 2004 represented 53.6%, of which 61.3% pertained to purchases and 45.9% to sales.

As at the last trading day of the half-year in the module of market makers trading was in the following issues of treasury bond series 131, 133, 166, 174, 187, 188, 189, 200 and 202; in the issues of commercial bonds - B.O.F. 04, B.O.F. 04, Železiarne Podbrezová II; and in the issues of mortgage bonds – VÚB VI, VÚB VII, Tatra banka 01, Istrobanka I, Istrobanka II. The volume of trades in the above, in the market maker module, reached SKK 449.0 million in 32 transactions, representing a 7.5% share in all price-forming transactions in bonds.

The market capitalisation of debt issues at the last day of trading of the half-year represented SKK 334.2 billion, of which SKK 311.5 billion pertained to listed issues, in the case of which an increase of 8.4% on an annual basis was recorded.

SDX Index

The SDX bond index for bank and company bonds closed the last day of trading of the half-year with a 7.1% gain on the closing value for June 2003 at the average value of 248.639% of the nominal value of its portfolio, with an average yield to maturity of 5.441% and a duration of 1.95 years. The minimum of 239.076% was reached on 7 January and the maximum 248.639% on 30 June.

The average price of the state bond portfolio on the SDX basis as at the end of June was 227.966%, representing an increase of 11.9% for the year, where the value of the average yield represented 4.324% and the duration 3.87 years. The minimum of 217.410% for this component was reached on 7 January, and the maximum 228.035% on 28 June.

Equities trading

On the last day of trading in June deals in 439 issues of shares (of 349 issuers), including mutual fund certificates, were concluded, of which 6 issues on the listed main market, 8 issues on the listed parallel market and 425 issues on the free market. None of the stock issues succeeded in being accepted on the listed new market during the half-year period.

The volume of trades in the first half of 2004, compared to the same period of the preceding year, increased by 27.3% reaching SKK 18.4 billion in 6 530 transactions. The financial volume of traded shares lagged behind the volume of debt securities. The most successful stock titles from the aspect of the financial volume achieved in trades were the shares of Nafta (SKK 2.5 billion, 140 deals), Slovnaft (SKK 1.7 billion, 302 deals) and shares of Zentiva (SKK 356.5 million, 67 deals). On the regulated free market of the stock exchange successful titles were shares of Inžinierske stavby Košice with a volume of SKK 1.1 billion in 70 transactions. The highest number of deals for the period in question (463) was recorded for shares in Všeobecná úverová banka, which concurrently were the most traded stock title in the framework of price-forming transactions from the aspect of the financial volume of trades.

SAX Index

The SAX Index opened the year 2004 with a slight weakening (0.2%) against the closing value of the preceding year, at the level of 177.33 points. On 23 June the index recorded its half-year maximum at the level of 198.96 points (the closest higher value of 201.88 had been recorded on 14 April 1997). The index closed the six-month period at the level of 195.65 points.

5.3 Foreign Exchange Market

Foreign exchange market operations

The SKK / EUR exchange rate at the close of June strengthened in comparison to the end of 2003 by 2.95%, from EUR/SKK 41.161 to EUR/SKK 39.946. The average exchange rate in the first half of 2004, compared to the first half of 2003, appreciated by 2.8%.

Balance of spot trades of foreign banks against domestic banks in the first half of 2004 was positive (USD 850.1 million), i.e. foreign banks sold domestic currency more and purchased foreign currency.

The SKK / USD exchange rate strengthened at the end of the first half-year in comparison with the close of 2003 by 0.23%, from USD/SKK 32.92 to USD/SKK 32.844. The average exchange rate in the first half of 2004, compared to the first half of 2003, appreciated by 12.7%.

The National Bank of Slovakia accepted several bids by commercial banks for buying foreign currency and during the first half-year purchased in the form of direct deals EUR 364 million.

	<u>30 June 2004</u> 31 December 2003	<u>average for June 04</u> average for June 03	<u>1st half-year of 04</u> 1 st half-year of 03
	%	%	%
EUR/SKK	-3.0	-3.8	-2.8
USD/SKK	-0.2	-7.3	-12.7

-means appreciation of SKK

+means depreciation of SKK

Interbank foreign exchange market (IFEM)

The total volume traded on the IFEM in the first half of 2004 reached USD 226 362.8 million (USD 209 400.6 million in the second half of 2003) and compared to the preceding six month grew by 8.1%. In the framework of types of deals 91.3% comprised swap transactions, of which the prevailing part were made in USD (90.8%). Spot deals contributed a share of 8.6% to the total volume, where 96.3% of these deals were made in EUR. The average daily turnover on the spot market was USD 153.5 million, with the size of one deal averaging USD 1.99 million.

The volume of trades between the Slovak domestic banks in the first half of 2004, compared to the preceding half-year, grew from USD 41 018.5 million to USD 41 261.6 million. Trading in USD had the largest representation at 79.6% (82.8% in the second half of 2003), followed by EUR with a share of 19.5% (16.6% in the second half of 2003) and other currencies formed a share of 0.9%.

In the total interbank foreign exchange market in the first half of 2004 trading by domestic banks had a 18.4% share (in the second half of 2003 the figure was 19.6%). From the aspect of the types of deals, 87.7% (89.2% in the second half of 2003) of the total volume of deals between domestic banks was made in the form of swap operations, spot deals had a 12.3% share (10.8% in the second half of 2003).

Trading with foreign banks grew by 9.7% from USD 168 332.3 million in the second half of 2003 to USD 184 655.1 in the first half of 2004. The maximum volume was also reached in USD, representing 83.9% (80.7% in the second half of 2003), followed by EUR with a share of 10.5% (10.7% in the second half of 2003) and other currencies formed 5.6%. Trades with foreign banks continued to represent the more significant part of the total foreign exchange market, with a share of 81.6%.

Both in deals between domestic banks as well as in trading with foreign banks the decisive part of trades was formed by swaps, up to 92.1% (93.3% in the second half of 2003), spot deals represented 7.7% (6.7% in the second half of 2003) and forwards 0.2% (0.1% in the second half of 2003).

6. BANKING SECTOR

6.1 Banking Sector

As at 30 June 2004 there were eighteen banks, three branch offices of foreign banks, nine subjects – providers of cross-border banking services and seven representative offices of foreign banks operating in the Slovak banking sector. Of these eighteen banks, three are home-savings banks: ČSOB stavebná sporiteľňa, a. s., Prvá stavebná sporiteľňa, a. s. a Wüstenrot stavebná sporiteľňa, a. s. Out of the fifteen universal banks nine banks and one branch office of a foreign bank held a mortgage banking license (HVB Bank Slovakia a. s., Dexia banka Slovensko a. s., ISTROBANKA, a. s., ĽUDOVÁ BANKA, a. s., OTP Banka Slovensko, a. s., Slovenská sporiteľňa, a. s., Tatra banka, a. s., UniBanka, a. s., Všeobecná úverová banka, a. s. and Československá obchodní banka, a. s., a branch office of a foreign bank in the SR).

In connection with the Slovak Republic's Treaty of Accession, which entered into force on 1 May 2004 provisions of Articles 11 to 20 of Act No 483/2001 Coll. on banks and on amendments to certain laws entered into force, on the basis of which credit institutions with a registered office in the European Economic Area may perform banking activities (except for the provision of mortgage loans under Article 67 (1) of the Act on Banks, and the function of a depository under the Act on Collective Investment) in the territory of the Slovak Republic without a banking licence granted by the National Bank of Slovakia, provided such a banking licence has been granted to them in their country of origin. On the basis of notifications from foreign supervisory authorities in Austria, the United Kingdom and Denmark delivered pursuant to Article 11 (2) of the Act on Banks and Article 21 (2) of Directive 2000/12/EC relating to the taking up and pursuit of business of credit institutions, on the intention of a foreign bank to perform, or provide banking activities listed in Annex 1 to the Directive, the banking supervision division registered as at 30 June 2004 nine subjects, or respectively foreign banks providing cross-border banking services.

On 13 February 2004 the National Bank of Slovakia granted prior approval to the Istrokapitál, a. s., Bratislava to increase its holding in the share capital and voting rights of Poštová banka, a. s., by 50% in connection with an increase in the bank's share capital by the mentioned company.

The National Bank of Slovakia granted on 15 March 2004 prior approval to the National Property Fund of the SR to acquire from the Ministry of Finance of the SR, a 10% holding in the share capital and voting rights of Slovenská sporiteľňa, a. s. This share was (according to the extract from the Central Securities Depository at 30 April 2004) transferred to ERSTE BANK DER OESTERREICHISCHEN SPARKASSEN AG, Vienna, whose total share in the share capital of Slovenská sporiteľňa, a.s., represents 80.01%.

On 23 April 2004 the decision of the National Bank of Slovakia the revoke the permit to operate as a bank from DEVÍN BANKA, a. s., entered into force.

On 3 February 2004 the National Bank of Slovakia registered ABN AMRO Bank N. V., Amsterdam, AG, a representative office of a foreign bank with a registered office in Bratislava. On 5 March 2004 the National Bank of Slovakia cancelled for COMMERZBANK Aktiengesellschaft, Frankfurt am Main, on the basis of its own request, the registration of the representative office of this bank. On 14 May 2004 the National Bank of Slovakia cancelled

for Dresdner Bank AG, Frankfurt am Main, on the basis of its own request, the registration of the representative office of this bank. The number of representative offices of foreign banks as at 30 June 2004 totalled seven.

In the following period the business name of Stavebná sporiteľňa VÚB-Wüstenrot, a. s. was changed to Wüstenrot stavebná sporiteľňa, a. s. and that of CREDIT LYONNAIS BANK SLOVAKIA, a. s. to CALYON BANK SLOVAKIA a. s.

The volume of the subscribed share capital of banks (excluding the NBS) increased by SKK 0.8 billion compared with the volume as at 31 December 2003, from SKK 40.4 billion to SKK 41.2 billion. The development of share capital was affected by the subscription of new shares in Poštová banka, a. s.

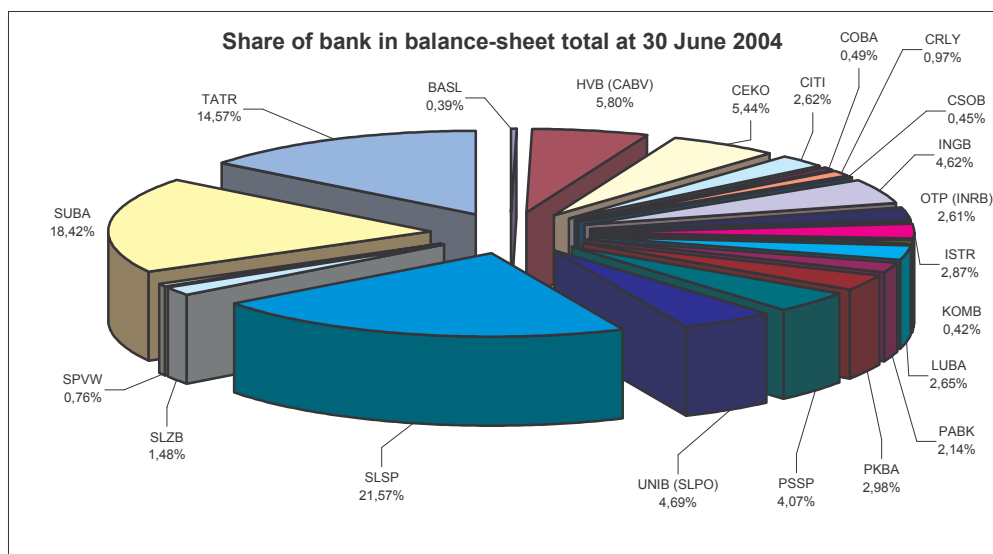
The amount of funds provided by foreign banks to their branch offices did not change, and at 30 June 2004 represented SKK 2.8 billion.

The share of foreign investors in the total subscribed share capital of banks and funds provided by foreign banks to their branch offices grew, compared to the preceding half-year, from 88.9% (at 31 December 2003) to 89.5% (at 30 June 2004). This increase was influenced by the entry of a foreign investor to Banka Slovakia, a. s., by the increase in foreign investors' share in the share capital in LUDOVÁ BANKA, a. s., Slovenská sporiteľňa, a. s., Tatra banka, a. s. and Wüstenrot stavebná sporiteľňa, a. s.. Furthermore, the mentioned share was affected by the reduction in the share capital of Tatra banka, a. s. and its increase in Poštová banka, a. s. by a domestic investor.

6.2 Economic Results of the Banking Sector

The balance-sheet total (sum total of the net value of assets) for the twenty-one banks of the Slovak banking sector at 30 June 2004, compared to the end of 2003, grew by SKK 60.7 billion (by +6.2%) to the volume of SKK 1 046.2 billion.

The development of the banking sector's balance-sheet total was affected both by the increase in secondary (SKK + 44.7 billion) as well as primary funds (SKK + 45.3 billion). The volume of non-anonymous deposits grew by SKK 12.9 billion (by 3.2 %) to SKK 418.7 billion.



The reported volume of earning assets in the banking sector increased against the end of 2003 by SKK 71.0 billion to SKK 979.6 billion. The share of earning assets over the course of the first half of 2004 also had a growing trend, and at 30 June 2004 reached 93.6%, which is 1.4% more than at the end of 2003.

Total loans reported by twenty banks as at 30 June 2004 represented a volume of SKK 413.2 billion. Classified loans fell by SKK 3.6 billion to SKK 32.3 billion, i.e. by 10.0 %. Banks created provisions for them in the value of SKK 27.5 billion. Coverage of classified loans by created provisions as at the close of the period reached 85.2%. The share of classified loans in total loans fell to 7.8%.

As at 30 June 2004 banks reported a net profit of SKK 6.9 billion. In a year-on-year comparison this represents an increase of 3.7 billion (+11.9%). None of the banks reported a loss for the current period as at 30 June 2004 (likewise, as at 30 June 2003 no bank reported a loss).

SR banking sector	31.12.2003	30.6.2004	Difference 30/06-12/03	in SKK
				thous.
				% change 30/06-12/03
Number of employees	19 797	19 850	53	0.27%
Number of banks in the SR	18	18	0	0.00%
Number of branch offices of foreign banks in the SR	3	3	0	0.00%
Number of representative offices of foreign banks in the SR	8	7	-1	-12.50%
Number of branch offices in the SR	553	570	17	3.07%
Number of sub-branches in the SR	504	519	15	2.98%
Number of branch offices in other countries	1	1	0	0.00%
Number of sub-branches in other countries	2	2	0	0.00%
Number of representative offices in other countries	1	1	0	0.00%
Total assets	985 445 707	1 046 193 365	60 747 658	6.16%
Earning assets	908 597 027	979 561 801	70 964 774	7.81%
Total foreign exchange assets	146 048 650	171 768 419	25 719 769	17.61%
Securities	358 364 029	340 115 024	-18 249 005	-5.09%
Receivables from loans	395 154 645	413 201 839	18 047 194	4.57%
Of which: classified loans	35 868 781	32 273 564	-3 595 217	-10.02%
Share of class. loans in total loans (%)	9.08	7.81	-1.27	x
Uncovered estimated loss	510 688	122 448	-388 240	-76.02%
Provisions loans	29 093 617	27 501 808	-1 591 809	-5.47%
Statutory reserves	2 733 706	6 455 215	3 721 509	136.13%
Share capital	40 442 576	41 233 475	790 899	1.96%
Own funds	105 875 293	99 012 266	-6 863 027	-6.48%
Secondary funds	96 466 762	141 167 220	44 700 458	46.34%
Primary funds	708 292 274	753 590 555	45 298 281	6.40%
- of which non-anonymous deposits	405 802 712	418 678 199	12 875 487	3.17%
Current period profit*	11 548 335	6 924 523	735 652	11.89%
Current period loss*	231 918	0	0	0.00%
Net profit and loss *	11 316 417	6 924 523	735 652	11.89%
Cumulative profit/loss*	34 577 036	34 682 543	8 358 993	31.75%
Adequacy of own funds (%)	21.59	21.63	0.04	x

*) year-on-year comparison

6.3 Performance of Banking Supervision and Prudential Banking Assessment

The main task and mission of banking supervision is to support the stability and healthy development of banks, the banking system and protect depositors' interests.

The number of inspections performed by the banking supervision division in the first half of 2004 is given in the following table:

	1 st quarter		2 nd quarter		1. 1 st half of 2004	
	begun	finished	begun	finished	plan	outcome
comprehensive	2		2	2	4	4
completing			1	1	1	1
thematic	1	1			0	1
total	3	1	3	3	5	6

In the period monitored the banking supervision division of the National Bank of Slovakia issued 81 decisions in the field of licensing activity, including decisions on suspending proceedings and proceedings for violation of the law.

One of the basic regulatory instruments of the banking supervision are rules of the prudential business conduct by banks and limits set by such rules.

Adequacy of own funds of the Slovak banking sector, compared to the end of 2003, as at June 2004 had grown by 0.04%, reaching the value of 21.6%. The adequacy of own funds limit (8%) during the first half of 2004 was complied with by all banks.

Over the course of the whole period in question the fulfilment of large exposure limits did not record any significant changes. The limit on bank's large exposure to a parent or subsidiary company, or to a group of economically connected persons, whose member the bank is (20% of own funds) was not fulfilled over the course of the half-year by 1 bank.

The limit on a bank's large exposure to other person, a group of economically connected persons or to countries and central banks (25% of own funds) was not met by four banks. The remaining four prescribed limits, or ratios, were fulfilled by all banks.

The limit on the indicator of fixed assets and non-liquid assets of a bank, which is at most 1, set by the new NBS Measure No 3/2004 on the liquidity of banks and branch offices of foreign banks and on the process of liquidity risk management of banks and branch offices of foreign banks, with effect as of 31 January 2004, was fulfilled by all banks.

6.4 International Co-operation

Bilateral cooperation agreements in the area of banking supervision

On 12 February 2004 an Agreement on co-operation was concluded and signed with the Malta Financial Services Authority.

Currently negotiations are under way on the concluding of a Memorandum of understanding with the supervisory authorities of Poland, Belgium, Latvia and Estonia. In the final phase, an amendment is to be approved and signed to the co-operation agreement with the Ministry of the Interior and the Presidium of the Police Corps.

7. TEXT APPENDICES

7.1 European Union Enlargement

On 1 May 2004 the Slovak Republic together with nine other countries – Cyprus, the Czech Republic, Estonia, Hungary, Lithuania, Latvia, Malta, Poland, Slovenia – became a member of the European Union. The decision on the accession of these ten countries was adopted at the Copenhagen European Council Summit in 2002, and was confirmed by the ceremonial signing of the Accession Treaties on 16 April 2003 in Athens. The enlargement to 25 member states brought about an important institutional change from the aspect of the acceding countries as well as from the aspect of the European Union itself.

In the case of Slovakia the beginning of the integration process may be dated from 1993 when the SR signed an Association Agreement with the EU member states. This Agreement entered into force on 1 February 1995 and set out the basic framework of economic cooperation between the SR and EU. An important milestone in the integration process was the submission of an official request for acceptance as EU member at the European Council Summit in June 1995 at Cannes. Even though the European Council passed at its meeting in December 1997 in Luxembourg a division of candidate countries into two groups (Slovakia was listed in the 2nd group of countries, whose immediate negotiations on the accession to the EU were to be initiated at a later date), on 15 February 2000 the representatives of the 15 EU member states, in line with the conclusion of the Helsinki Summit (December 1999) opened the Intergovernmental Conference on the Slovak Republic's Accession to the European Union also with Slovakia, whereby its official negotiations on the accession were commenced.

Membership in the EU requires the ability of the country to fulfil political and economic criteria on the one hand and, on the other hand, the ability to accept existing as well as future rights and obligations of the Union, contained in its *acquis communautaire*. The negotiations themselves were officially held within the 31 negotiation chapters (the NBS participated directly in preparation in the framework of Chapter 3 – the free movement of services, 4 – the free movement of capital, 11 – Economic and Monetary Union, 12 – Statistics, and 31 – Miscellaneous).

Through signing the Treaty of Accession the SR undertook that through its accession to the EU it will become a contractual party of the treaties on which the Union is founded. Thus on the date of accession it became a participant in Economic and Monetary Union as a member state with derogation – i.e. having this status, the SR in the future is expected to enter the monetary union. At the same time, the National Bank of Slovakia became a part of the European System of Central Banks (ESCB) with all the rights and obligations this entails. Following the fulfilment of convergence criteria a member state with a derogation will be able to introduce the common currency euro and its central bank will become a part of the eurosystem.

According to its statute the European System of Central Banks (ESCB) is formed by the European Central Bank (ECB) and national central banks of the member states of the EU. The primary goal of the ESCB is to maintain price stability. The basic functions fulfilled by the ESCB are as follows:

- setting and realising Community monetary policy,
- performance of foreign exchange operations,
- holding and management of foreign currency reserves of the member states,

- ensuring a the smooth activity of payment systems.

According to its statute the ESCB is managed by the managing bodies of the ECB, which include the Governing Council, Executive Board and the General Council. The ECB Governing Council comprises members of the ECB Executive Board and governors of national central banks of the eurozone member states. Executive Board is formed by the president, vice-president and four other members with various terms of office. The General Council members comprise the president and vice-president of the ECB and governors of national central banks of the EU member states.

Following the European Council Decision in Copenhagen on the accession of the 10 new member states to the EU, taken in December 2002, and the subsequent signing of Accession Treaties in April 2003, it was decided that governors of central banks of the acceding countries, and thus also the NBS governor, would as of June 2003 take part at the meetings of the ECB General Council, having the status of observers, i.e. not having the right to vote. Through the accession of these countries to the EU, the governors of the acceding countries' central banks automatically acquired voting rights as of 1 May 2004.

Representatives of the NBS participate at meetings of the following committees and the working groups subject to them:

- Accounting and Monetary Income Committee,
- Banknote Committee
- Banking Supervision Committee
- External Communications Committee
- Information Technology Committee
- Internal Auditors Committee
- International Relations Committee
- Legal Committee
- Market Operations Committee
- Monetary Policy Committee
- Payment and Settlement Systems Committee
- Statistics Committee.

As the SR became as of the date of acceding to the EU a participant of Economic and Monetary Union as a member state with derogation, under Council Regulation No 1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies it is obliged to submit to the European Commission each year its convergence programme. It submitted to the European Commission its first Convergence Programme for 2004 - 2010 on 14 May 2004. It was prepared under the auspices of the Ministry of Finance of the SR in cooperation with the relevant institutions, i.e. also in cooperation with the NBS. The Convergence Programme presents goals of economic policy up to 2010 and is a natural continuation of the hitherto prepared Pre-Accession Economic Programme (PEP).

According to Article 104 of the EC Treaty, the SR, as a member of Economic and Monetary Union, began as of the date of entering the EU to be subject to the obligation to avoid excessive deficits, and on the basis of this obligation it is possible to initiate against the country a specific procedure (Council Regulation No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure). Compliance with budgetary discipline

means fulfilling two criteria: public finance deficit / GDP ratio must not exceed 3% and the government debt / GDP must not exceed 60% (Protocol on the Excessive Deficit Procedure). On the basis of the deficit and debt notification submitted the European Commission began to monitor the budgetary situation in the SR and subsequently on 12 May 2004 passed a report on the non-fulfilment of the public finance deficit / GDP criterion. On 24 June 2004 the EC passed an opinion on the budgetary situation in Slovakia and subsequently to that, on 5 July 2004, the Council of the EU decided on the existence of an excessive deficit and passed recommendations for its removal.

7.2 Monetary Policy Instruments

1. Interest rate policy

a) *basic interest rate of the NBS² (interest rate for two-week repo tenders)*

as of 22 December 2003	6.00%
as of 29 March 2004	5.50%
as of 29 April 2004	5.00%

b) *interest rate for overnight refinancing operations*

as of 22 December 2003	7.50%
as of 29 March 2004	7.00%
as of 29 April 2004	6.50%

c) *interest rate for overnight sterilisation deals*

as of 22 December 2003	4.50%
as of 29 March 2004	4.00%
as of 29 April 2004	3.50%

2. NBS monetary policy instruments

2.1 Open market operations

a) *main instrument*

- *Standard repo tender with a two-week maturity* – is made by the NBS with commercial banks regularly once a week. The NBS at the same time declares an interest rate for these standard operations (the basic interest rate).

b) *instrument for longer-term liquidity management*

- *Issue of NBS T-bills* to the portfolios of commercial banks – the NBS instrument for longer-term management of commercial banks' liquidity. Auctions of NBS T-bills were held at least once a month, as a rule in the Dutch method.

c) *fine tuning instrument*

- *Quick tender* - the NBS instrument serving for the gentle operative adjustment of commercial banks' liquidity.

d) *structural operations*

- *Individual deals* – the NBS instrument enabling the direct purchase or sale of government securities and NBS T-bills to and from the NBS portfolio.

e) *foreign exchange swaps*

- An instrument serving for temporarily liquidity adjustment in the koruna field using foreign exchange transactions with future settlement.

2.2 Standing facilities

(a) *Overnight refinancing operations*

² On 12 December 2002 the Bank Board of the NBS decided on setting the basic interest rate of the NBS with effect from 1 January 2003. The basic interest rate of the NBS is identical to the limit interest rate for standard two-week repo tenders of the NBS. Where in generally binding legal regulations the terms “discount interest rate of the National Bank of Slovakia” or “discount interest rate of the State Bank of Czecho-Slovakia” are used, they are understood to mean the basic interest rate of the National Bank of Slovakia.

- commercial banks have an automatic access to financial resources (under the condition of sufficient eligible assets) at an announced interest rate.

(b) *Overnight sterilisation operations*

- commercial banks have the possibility to deposit surplus funds in the form of non-collateralised deposits at an announced interest rate

3. *Other instruments*

(a) *redistribution loan*

- traditional - interest rate = *rate for two-week repo tender* + 0.5%

- soft loan - interest rate = *rate for two-week repo tender* - 2% + 0.5%

(b) - with a view to maintain a bank's liquidity the NBS may exceptionally provide to a bank a short-term loan, for a period of at most three months.

4. *Minimum required reserve*

Commercial banks, branches of foreign banks, home savings banks and electronic money institutions create from 1 January 2004 minimum reserves in the amount of 2% from non-term and term deposits and credits received, from deposits and credits received with a notice period, from debt securities issued except for mortgage bonds in Slovak korunas and in foreign currencies, and from deposits of foreign banks branches acquired from their headquarters abroad. The maintenance period for the minimum reserves in 2004 is one calendar month. Minimum reserves bear an interest at the rate of 1.5%, up to the set amount for the corresponding month.

5. *Exchange rate and foreign exchange policy*

(a) *exchange rate regime*

The National Bank of Slovakia also in the first half of 2004 applied a floating exchange rate regime. The Slovak koruna exchange rate was determined in relation to the reference currency – the euro. Its development depended on the supply and demand for Slovak koruna development on the foreign exchange market. The National Bank of Slovakia used the possibility to intervene on the foreign exchange market in order to correct an excessive volatility of the Slovak koruna exchange rate, or in the case when exchange rate development did not correspond to the development of macroeconomic fundamentals.

(b) *nominal exchange rate of the SKK*

The nominal exchange rate of the Slovak koruna against euro in the first half of 2004 appreciated by 2.95%, where as at 30 June 2004 it reached the value of 39.946 SKK/EUR.

The development of the Slovak koruna exchange rate against the American dollar recorded an appreciation of 0.23% to the level of 32.844 SKK/USD.

(c) *nominal and real effective exchange rate of the SKK³*

³ The methodology of calculating the nominal and real effective exchange rate of Slovak koruna indices (NEER and REER) is taken from the IMF. This uses the average monthly exchange rates of the Slovak koruna and partners currencies against the dollar. Furthermore, it is based on the producers' price index PPI (the prices of manufactured articles PPI manufacturing), the base year 1999 and sixteen important trading partners of the SR, representing together roughly 86 to 89% of the Slovak foreign trade turnover in 1993-2002: Germany, the Czech Republic, Italy, Austria, France, the Netherlands, the USA, the UK, Switzerland, Poland, Hungary, the Ukraine, Russia, Japan, China and Turkey.

The development of the index of the nominal effective exchange rate of the Slovak koruna (NEER) during the first half of 2004 was affected in particular by the declining average year appreciation of the koruna exchange rate against USD (by 12.7%, against 20.8% in the first half of 2003), which represented a pro-growth factor for price competitiveness of domestic producers-exporters. On the other hand, however, a slightly higher appreciation rate of SKK against EUR (in a year-on-year comparison of 2.8% against 2.6%) implied higher SKK/USD appreciation rate than was the dollar exchange rates appreciation of the SR's main trading partners currencies and thus to a certain degree this dampened the mentioned price competitiveness impact. The average year-on-year NEER index growth rate during the first half of 2004 fell to 5.5% against 6.9% in the same period last year.

The real effective exchange rate index (REER) based on the producers' price index on average on a year-on-year appreciated by 4.2%, representing a lower growth rate against the growth of 12.6% in the first half of 2003. Likewise, a slowdown was also recorded in the REER growth rate based on the prices of manufactured articles, i.e. excl. mineral raw materials prices and energy prices, which in the first half of 2004 grew by 3.2% (against a growth of 7.0% in the first half of 2003).

(d) Currency structure of foreign exchange receipts and payments of the Slovak Republic

The overall turnover of foreign exchange receipts and payments for payment titles of groups 1 to 6 in convertible currencies for the first half of 2004 was in the amount of SKK 770.4 billion. The average monthly turnover for the 6 months (SKK 128.4 billion) against the same period last year grew by 7.1%. Foreign exchange receipts and payments reached a debit balance of SKK 13.2 billion, representing a marked increase compared to the first half of 2003 (against SKK 1.4 billion).

The overall turnover was influenced, on a long-term basis, to a decisive degree by the EUR and USD, where however the euros share since the single currency's introduction has been continuously growing and, conversely, those of the USD and CZK have been falling. The share of other currencies in recent years have stagnated at a low level.

Currency structure development of foreign exchange receipts and payments in 1999-2003 and the half-year of 2004

	2001	2002	1-6/2003	2003	1-6/2004
Total turnover (in SKK bln.)	1 277.9	1 385.6	719.2	1 536.8	770.4
Of which: EUR (incl. Former currencies of EMU countries)	61.3%	63.7%	68.1%	69.8%	70.7%
CZK	8.7%	9.3%	8.2%	7.8%	7.5%
USD	26.4%	23.2%	20.4%	19.0%	18.5%
Other currencies *	3.6%	3.8%	3.3%	3.3%	3.3%
Share of turnover in GDP (at current prices)	126.5%	126.4%	125.8%	128.5%	121.4% **

* HUF, DKK, NOK, SEK, CHF, GBP, AUD, JPY, CAD and other currencies

** As yet only data for the first quarter of 2004 is available.

7.3 Monetary Calendar

January

- The rating agency Fitch increased the rating of the Slovak Republic's long-term liabilities in foreign currency from BBB to BBB+ and in those in domestic currency to A. The agency, through its positive outlook for long-term liabilities in foreign currency, emphasised the confidence in maintaining the current trend of the country towards the single European currency adoption.

March

- The international rating agency Standard & Poor's (S&P) increased Slovakia's credit rating in foreign currency from BBB/A-3 to BBB+/A-2. The rating outlook remains positive.

- The South Korean automobile manufacturer Kia Motors officially announced decision to build its first factory in Europe for the production of 200 000 cars annually in Slovakia for EUR 700 million.

April

- The Slovak government discussed the starting points for the public administration budget for 2005 to 2007. The Ministry of Finance of the SR assumes for the following year a budget deficit without including the fiscal costs of pension reform at the level of 3.2% of GDP. Revenues should represent SKK 287.5 billion and expenditures SKK 344.9 billion. The state budget deficit should be SKK 57.4 billion and the deficit for the whole sphere of public finance SKK 54 billion. Together with the proposal of starting points it discussed also the Convergence Programme.

- The World Bank released for Slovakia the third and last tranche of EUR 70 million from the EFSAL loan for restructuring domestic business and financial sectors, and thereby confirmed that the Slovak government is successfully completing reform steps throughout the whole economy. Funds in the total volume of EUR 20 million were released on the basis of the progressive fulfilment of strict conditions.

May

- The Bank Board of the NBS approved the Updated Monetary Programme for 2004. The NBS in its monetary programme increased the estimate for economic growth, reduced the forecast rate of inflation and foreign trade deficit. The end-of-year level of inflation is expected to be in the interval of 5.7 – 7.0%. The original interval of the prediction for core inflation of 1.2 – 3.5% has been narrowed to 1.9 – 3.4%. Risks to the estimate remain the development of world oil prices, the koruna exchange rate, as well as the adoption of the Common Agricultural Policy with an impact on the food price levels development. The current account deficit of the balance of payments should reach 1.2% of GDP against the previous estimate of 2.3%. The favourable development of foreign trade has been also reflected in the increased economic growth forecast in the interval of 3.8% - 4.4%; previous GDP growth estimates have been increased by 0.1%.

June

- The rating agency Moody's Investors Service changed outlook for Slovakia from stable to positive. It assigned Slovakia the rating A3. The change in the outlook reflects results of structural reforms, pricing policy liberalisation, the banking sector privatisation, introduction of pension reform and also reforms in education and health care. Moody's through its rating change also reacted to the introduction of the flat-rate income tax for private and legal entities, through which the SR created one of the most liberal economic environments in the Central and Eastern Europe.

7.4 NBS Foreign Exchange Licensing and Foreign Exchange Supervision

The competence of the National Bank of Slovakia as the foreign exchange authority, ensuing from the Act of the National Council of the SR No 202/1995 Coll. (Foreign Exchange Act) as later amended, as well as from the Act of the National Council of the SR No 566/1992 Coll. on the National Bank of Slovakia was in the first half of 2004 oriented, in the fields of the licensing and supervision as follows:

Licensing activity

As at 30 June 2004 the National Bank of Slovakia had granted 43 foreign exchange licences in the following structure:

- 39 foreign-exchange licences for foreign exchange offices activity, i.e. the purchase or sale of foreign currency for Slovak currency in cash,
- 2 foreign exchange licences for non-cash trading in foreign currency assets,
- 2 foreign exchange licences were issued for the provision of foreign exchange financial services.

Performance of foreign exchange supervision

In accordance with the approved objective, the supervision activity of the National Bank of Slovakia was oriented in particular on the business entities compliance control of the foreign exchange reporting obligations. Besides this, focus also centred on the performance control of other obligations limited by foreign exchange regulations and the control of compliance with conditions set out in foreign exchange licences.

In total 34 inspections were carried out at business entities and foreign exchange offices. In all cases foreign exchange supervision were further planned inspections.