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Národná banka Slovenska
Imricha Karvaša 1, 813 25 Bratislava
Slovakia

Contact:
+421/2/5787 2146

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Abbreviations

CPI	Consumer Price Index
EA	euro area
ECB	European Central Bank
EC	European Commission
EIA	Energy Information Administration
EMU	Economic and Monetary Union
EONIA	euro overnight index average
ESA 95	European System of National Accounts 1995
EU	European Union
Eurostat	Statistical Office of the European Communities
FDI	foreign direct investment
Fed	Federal Reserve System
EMU	Economic and Monetary Union
EURIBOR	euro interbank offered rate
FNM	Fond národného majetku – National Property Fund
GDP	gross domestic product
GNDI	gross national disposable income
GNI	gross national income
HICP	Harmonised Index of Consumer Prices
IMF	International Monetary Fund
IPI	industrial production index
IRF	initial rate fixation
MFI	monetary financial institutions
MF SR	Ministry of Finance of the Slovak Republic
MMF	money market fund
NARKS	National Association of Real Estate Offices of Slovakia
NBS	Národná banka Slovenska
NEER	nominal effective exchange rate
NPISHs	Non-profit Institutions serving households
OIF	open-end investment fund
p.a.	per annum
p.p.	percentage points
qoq	quarter-on-quarter
PPI	Producer Price Index
REER	real effective exchange rate
SASS	Slovenská asociácia správcovských spoločností – Slovak Association of Asset Management Companies
SO SR	Statistical Office of the Slovak Republic
SR	Slovenská republika – Slovak Republic
ULC	unit labour costs
VAT	value-added tax
yoy	year-on-year

Symbols used in the tables
. – Data are not yet available.
- – Data do not exist / data are not applicable.
(p) – Preliminary data

1 Summary[1]

The recently published detailed national accounts data for the first quarter of 2014 confirmed the flash estimate and projected composition of economic growth in both the euro area and Slovakia. The sources of growth are the same, with exports making the largest contribution and domestic demand a smaller one. The increase in private consumption was a particularly positive development.

The latest monthly data for the euro area indicate that activity continues to be driven mainly by exports. This view is supported by the growth in industrial production in April. Private consumption is expected to continue rising, with monthly retail sales figures pointing to a faster rate of growth. Price movements in the euro area remain subdued and, with the pass-through of low imported inflation, they will have a downward effect on prices in Slovakia. Forward-looking indicators for the euro area are so far signalling moderate quarter-on-quarter growth in the second and third quarters.

The pass-through of positive trends from the euro area as a whole to Slovakia has been limited so far. The Slovak economy is probably affected to a greater extent by geopolitical tensions. According to 'hard' indicators, activity decelerated in the second quarter, although this was projected in the latest NBS forecast. The drop in industrial production growth in April weighed on exports. They fell in April for a third successive month, with lower car production being the main cause of their decline. On the other hand, short-term forward-looking indicators in May provide evidence of a modest improvement in key sectors, and therefore output and exports are expected to correct upwards from their current weaker figures. Business sentiment edged above its long-run average and consumer confidence was at its highest level since 2008.

Despite a moderate slowdown in economic activity, the labour market situation continues to improve. Monthly figures for April pointed to further growth in employment, with job creation increasing again in industry, as well as in the services, information technology and trade sectors. In addition to employment growth, April saw a notable increase in nominal wages. But while their growth was quite high, it is expected to correct slightly downwards in the next period. Low inflation is expected to boost private consumption growth in the second quarter through its effect on real wages.

The deflationary trend in year-on-year prices was halted in May, with the headline inflation rate remaining flat at 0%. In month-on-month terms, inflation increased as projected. That increase was driven mainly by volatile food prices, which increased substantially in May. Energy price inflation (fuel prices) rose in May, reflecting oil price increases caused by disruptions in oil-exporting countries.

Monthly indicators suggest there is a risk, if exports remain weak, that trends projected in the current NBS forecast will not materialise. That scenario would, however, be partially offset by stronger than projected domestic demand.

1 *All month-on-month and quarter-on-quarter changes mentioned in the text have been seasonally adjusted using internal seasonal models.*

2 REAL ECONOMY

2.1 'HARD' INDICATORS OF ECONOMIC ACTIVITY

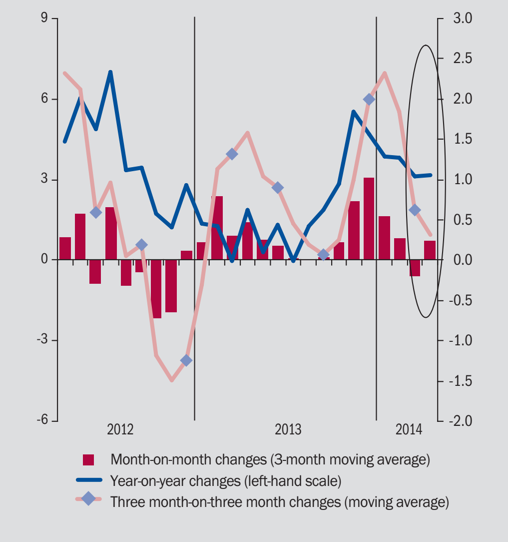
April's monthly figures for economic activity showed a further slowdown in thee month-on-three month growth, and so continued the gradual correction following January's positive figures. The cooling of activity is particularly evident in export and sales figures, and to a lesser extent in the correction of the previous growth in industrial production.

Slowdown in April sales growth moderated by trade sales

Looking at total sales in the economy, their three-month moving average for February-April was 0.3% higher than that for the previous three months (down from an increase of 0.6% in the average for January-March). Since the positive contribution of industry sales faded in April, the main driver of overall sales growth was domestic trade, particularly wholesale trade and retail trade. Compared with the previous month, overall sales increased by 0.4% in April.

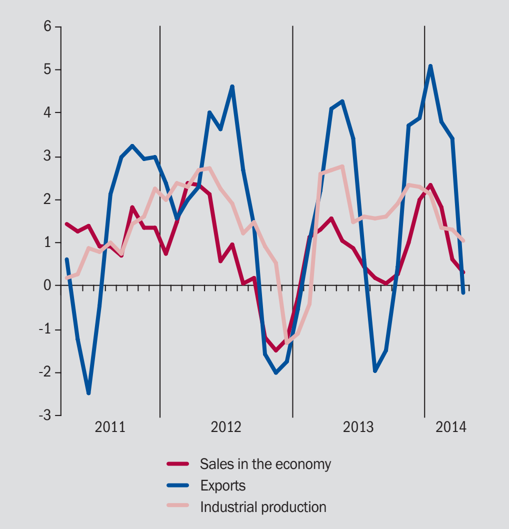
On the one hand, the trajectory of trade sales is in line with NBS projections that quarter-on-quarter growth in final consumption will decline in the second quarter of 2014. On the other hand, however, consumer sentiment improved in May to reach its highest level this year. Coming months may see a greater than expected impact from households' more positive assessments of

Chart 2 Total sales at constant prices (%)



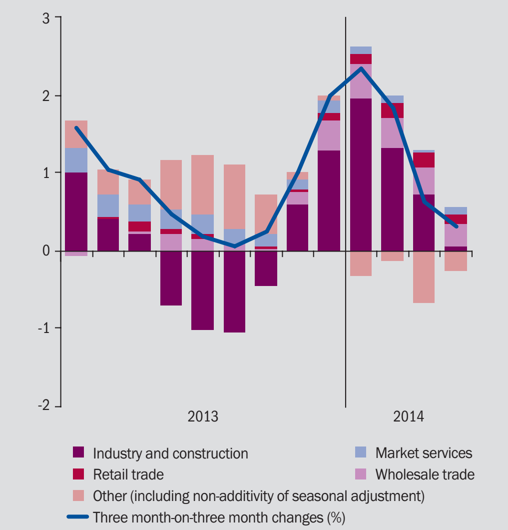
Source: SO SR, NBS calculations.

Chart 1 Sales, industrial production and exports (percent; three-month moving average compared against average for previous three months)



Source: SO SR, NBS calculations.

Chart 3 Total sales by contributions of selected sectors to three-monthly rate of change (p.p.; constant prices)



Source: SO SR, NBS calculations.

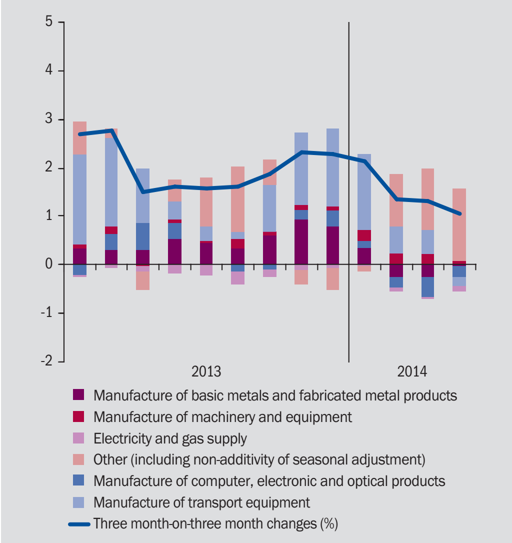
their financial situation, savings, and prospects for making large purchases, as well as from projected wage growth and employment growth in the first quarter. Similarly, overall confidence in retail trade has improved moderately on the basis of stronger assessments of the current situation.

Slowdown in industrial production growth caused mainly by automotive industry

Industrial production's three-month moving average for February-April was 1.1% higher than the average for the previous three months; however, this was down from an increase of 1.3% in the average for January-March, owing mainly to results in car production. That negative contribution was slightly offset by increased production in metals and electronics. Electronics production began to reflect a marked upturn in business sentiment in this sector, which itself is probably related to the FIFA World Cup (major sporting events are typically accompanied by a spike in television sales). Compared with the previous month, industrial production in April increased by 0.8%.

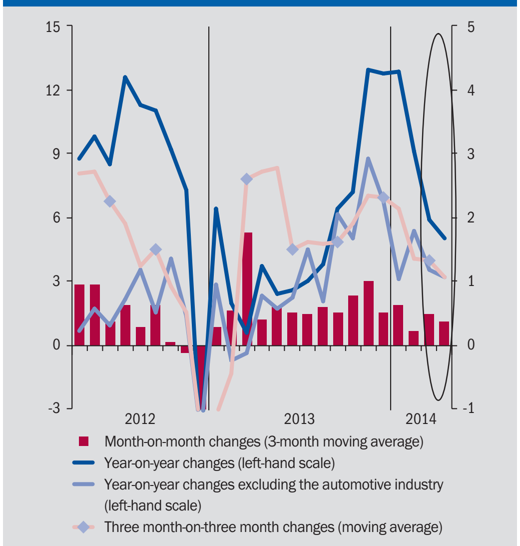
Construction production recorded a three-month moving average for February-April that was -5.1% lower than the average for the previous three months. This exceeded the decline in the average for January-March, owing mainly to lower domestic construction activity and in particular a marked drop in new construction. Despite mild weather in the first quarter and a gradual stabilisation in the sector, there are still no signs of significant positive impulses for construction production. According to construction firms, the major production-limiting factors are weak demand and their own financial situation.

Chart 5 Industrial production – principal contributions to three-monthly rate of change (p.p.; moving average)



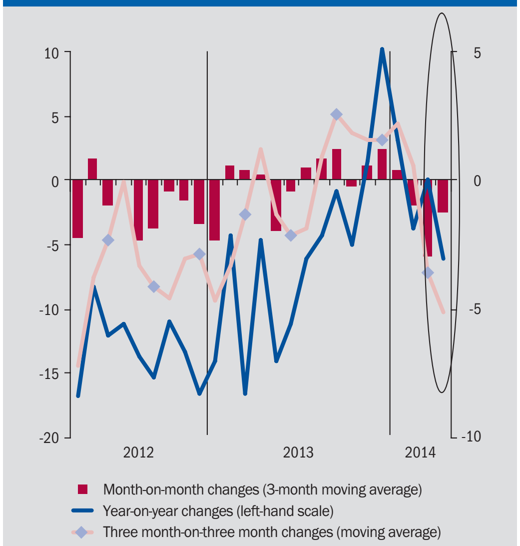
Source: SO SR, NBS calculations.

Chart 4 Industrial production (%)



Source: SO SR, NBS calculations.

Chart 6 Construction production (%)



Source: SO SR, NBS calculations.

Chart 7 Construction production (trend; constant prices; index: average for 2010 = 100)

Source: SO SR, NBS calculations.
Note: Building construction accounts for around 70% of total construction production.

Chart 9 Annual rate of change in exports (3-month moving average; percent; current prices)

Source: NBS, ECB and SO SR.

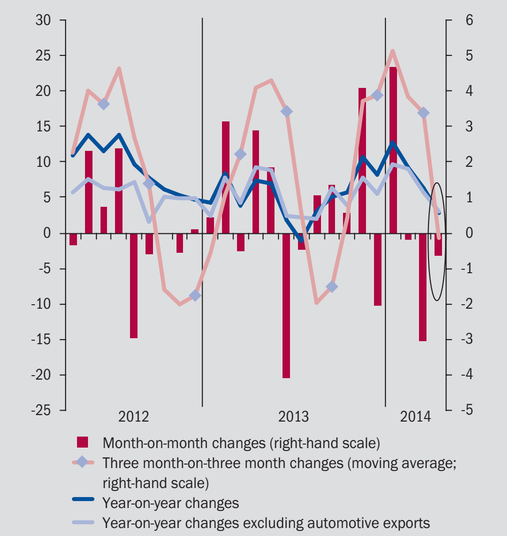
Exports fell moderately

Turning to goods exports, converted into constant prices, preliminary figures show that their three-month moving average for February-April was 0.1% lower than the average for the previous three months. Export growth continued its downward trajectory, owing to falling car exports and the fact that exports in the rest of the economy did not increase sufficiently to compensate for that decline. At the same time, electronics exports remained relatively stable.

Geopolitical risks alone cannot explain the weakening of Slovak exports, although their impact probably became more pronounced in April. This is evident from 'soft' indicators in the German market, which show that one-sixth of firms see geopolitical developments as adversely affecting their business. The bad news for Slovak exports is that most of these firms operate in the automotive industry. German exports to Russia declined in the first quarter of 2014 by 12.9% year-on-year, and the lagged pass-through of that drop may weaken German demand for products from the central European supply chain.

In the same period, Slovakia's goods exports to Germany increased by 16% year-on-year. However, Slovak exports to three other countries of Germany's supply chain declined (exports to the Czech Republic, Hungary and Austria fell, respectively, by 4.4%, 6.2% and 9.5%). Exports to Russia and Ukraine also decreased, by 13.4% and 24.3%. Although those were double-digit declines, their direct negative impact on overall Slovak exports was not significant given that the share of Slovak exports destined for these countries is only 4%.

Chart 8 Goods exports (percent; constant prices)

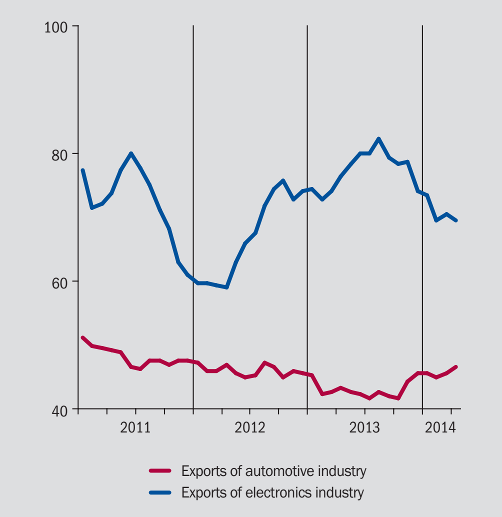


Source: SO SR, NBS calculations.
Note: Converted by NBS into constant prices.

Imports, converted into constant prices, reported a three-month moving average for February-April that was 0.2% lower than the average for the previous three months. At the same time, however, in the sector manufacturing cars and motor vehicle accessories for export, the ratio of imports to exports increased, possibly reflecting an inflow of imports for the completion of large investment projects in this sector. The amount of consumer goods imported in April was close to the all-time high recorded in March. This is consistent with the gathering momentum in household consumption growth, which in coming months may put further upward pressure on imports.

The nominal trade surplus fell in April, to €345.8 million (seasonally unadjusted), which was €203 million lower compared to April 2013. Exports declined by 3.3% year-on-year and imports increased by 0.3%.

Chart 10 Import intensity of exports (6-month moving average; percent; current prices)



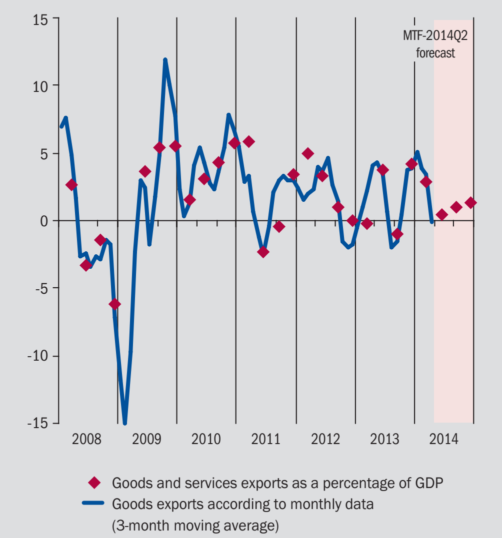
Source: NBS and SO SR.

2.2 FORWARD-LOOKING 'SOFT' INDICATORS

Favourable economic sentiment in the euro area

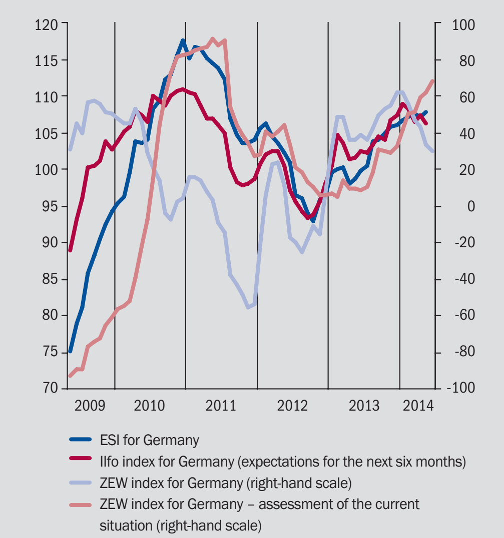
The economic sentiment indicators for the euro area and Germany were higher in May than in the previous month. The euro area saw confidence improve in all sectors apart from retail trade, where it remained flat. In Germany the pick-up in confidence was driven mainly by improved sentiment in industry and among consumers. Even so, the ZEW index for Germany fell in June for a sixth consecutive month (by 3.3 points, to 29.8). Confidence in the future situation nevertheless remains relatively high, and assessments of the current economic situation in Germany are also positive.

Chart 11 Exports (three month-on-three month percentage changes; constant prices)



Source: SO SR, NBS calculations.
Note: Converted by NBS into constant prices.

Chart 12 Economic sentiment indicators for Germany

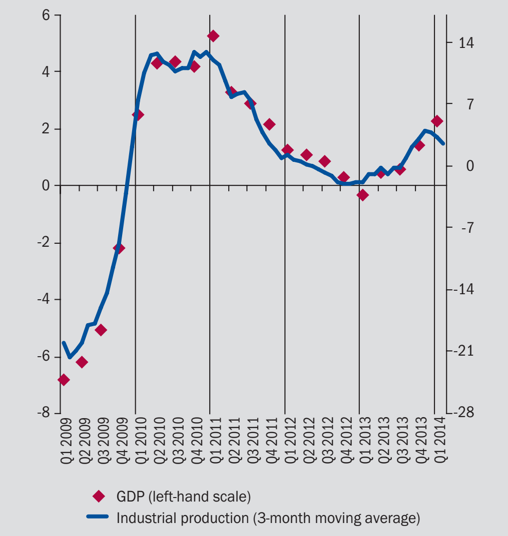


Source: European Commission, Ifo institute, ZEW Centre.
Note: ESI (long-run average = 100), Ifo index (2005 = 100), ZEW (balance of responses).

Chart 13 Economic sentiment indicator (long-run average = 100)

Source: European Commission.

Chart 15 GDP and industrial production in Germany (annual percentage changes)



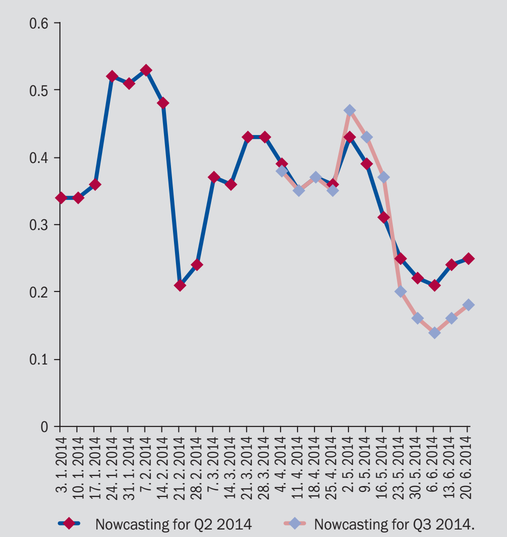
Source: Eurostat.

Given the continuing optimism in the euro area and the fact that expectations in Germany remain above their long-run average (despite having corrected somewhat), both the euro area and German economies are expected to maintain moderate quarter-on-quarter growth and therefore to match the assumptions used in the NBS forecast for the Slovak economy.

Confidence in the Slovak economy rises above its long-run average

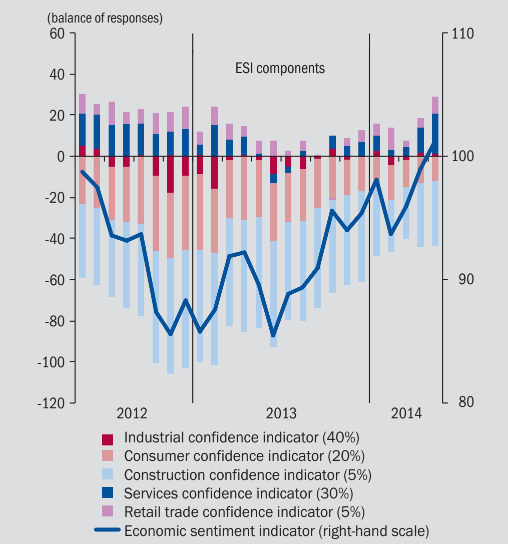
The economic sentiment indicator (ESI) for Slovakia increased month-on-month in May by 2.3 points, to 101.3, and therefore rose above its long-run average for the first time in 24 months. The improvement was driven by the services,

Chart 14 Euro-area GDP growth estimate for Q2 and Q3 2014 (quarter-on-quarter percentage changes)



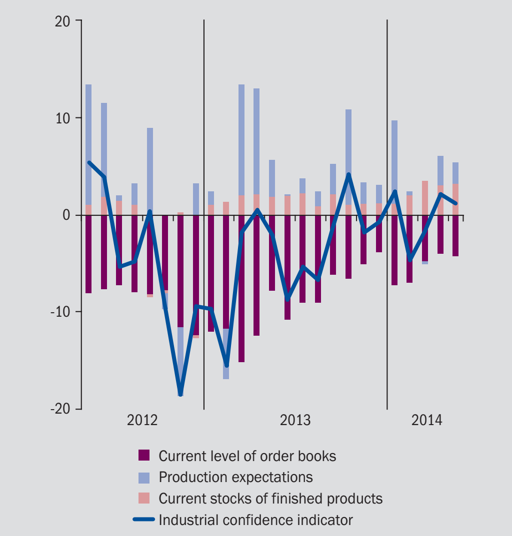
Source: Now-Casting.com

Chart 16 Economic sentiment indicator for Slovakia (long-run average = 100)



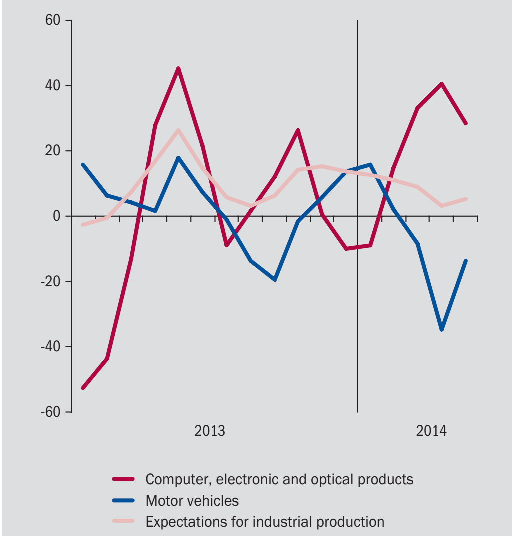
Source: European Commission.
Note: The percentages in the legend represent the weights of the respective components in the ESI.

Chart 17 Industrial confidence indicator for Slovakia (balance of responses)



Source: European Commission.

Chart 18 Industrial production expectations (balance of responses; 3-month moving average)



Source: European Commission and NBS.

retail trade and consumer confidence indicators, while sentiment in the industry and construction sectors deteriorated slightly.

The most marked improvement in confidence was in the services and retail trade sectors, based mainly on more optimistic appraisals of the current business situation. In services, the segments accounting for most of the greater optimism were information and communication, financial and insurance activities, and administrative services. Consumer confidence in May reached its highest level since October 2008, with improvements in all components apart from expectations for the future general economic situation. Industry confidence worsened slightly owing mainly to the expected decline in industrial production, particularly in manufacture of coke and refined petroleum products, manufacture of chemical products, and manufacture of computer, electronic and optical products. On the other hand, production expectations in the automotive industry increased quite sharply. The slight drop in the construction confidence indicator reflected negative views about employment growth in the sector, although their effect was mitigated

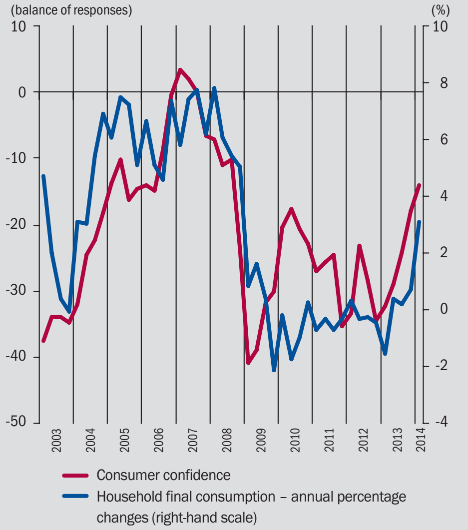
Chart 19 Export expectations and real exports

Source: SO SR, European Commission and NBS.

by brighter assessments of the level of order books.

Going forward, the improving economic sentiment, as well as the still relatively optimistic expectations in the euro area, could

Chart 20 Consumer confidence and household final consumption



Source: SO SR, European Commission and NBS.

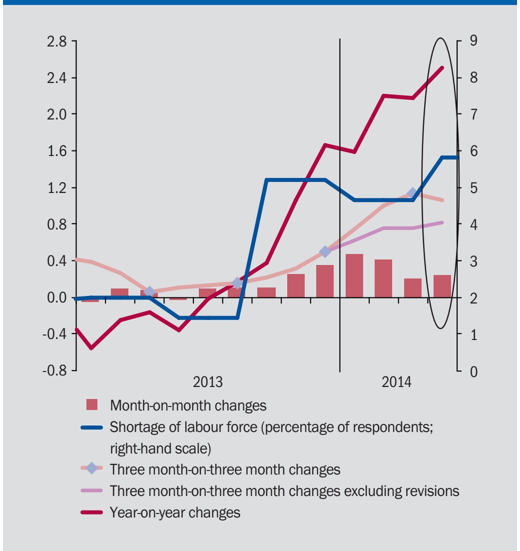
to some extent correct the recent deterioration of 'hard' figures for economic activity. At the same time, the firming of consumer confidence points to further growth in household final consumption.

3 Labour market

Employment data for April suggest that the acceleration of employment growth observed in the first quarter of the year continued in the second quarter. In the selected sectors, overall employment increased by 0.2% month-on-month and by 2.5% on a year-on-year basis (or around 2.1% after adjustment for methodological changes[2]). Greater balance is appearing in the contributions to employment growth; in April there were positive contributions from three of the four principal sectors (industry – mainly manufacture of machinery, metals, and paper and wood products; services – selected market services, and IT and communication; and trade). In the construction sector, employment remained depressed, with a moderate drop in both year-on-year and month-on-month terms. Employment expectations in recent months have remained at elevated levels, indicating further growth in job creation, particularly in industry and services.

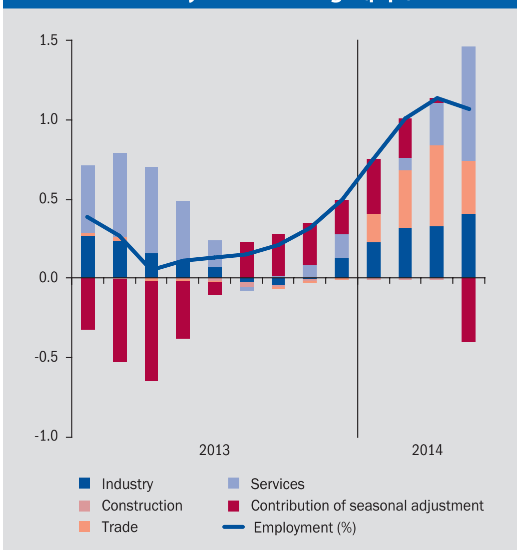
The first complete employment figures for the first quarter showed that employment grew by 0.3% quarter-on-quarter (up from the flash estimate of 0.2%). Employment growth across the selected sectors in April suggests that its rate in the second quarter could match that in the first quarter, as projected in the latest NBS forecast (MTF-2014Q2).

Chart 22 Rates of change in employment (%)



Source: SO SR, NBS calculations.
Note: The indicator 'shortage of labour force' is included in EC business survey. In January, upward revisions were made to employment growth in the segments of business activities, accommodation, and restaurants. At the same time, the figures for 2013 were not revised and hence there was probably no upward effect on the labour market situation.

Chart 21 Employment – sectoral contributions to three-monthly rate of change (p.p.)

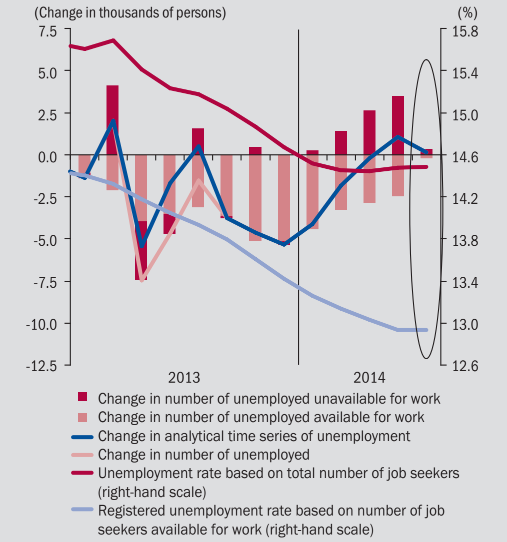


Source: SO SR, NBS calculations.

The number of unemployed in May fell month-on-month by 5,100, while the registered rate of unemployment edged down to 12.8% (from 12.96% in April). Since, however, such a drop is typical in May (with the onset of seasonal work), the seasonally adjusted unemployment rate remained flat month-on-month after rising marginally in the previous month. The unemployment rate based on the total number of job seekers followed a very similar trend. The cautiousness of employers was reflected in the declining number of people who found work in May. At the same time, a majority of new job seekers who registered at labour offices had not previously been employed (they included students, people coming from abroad, and inactive persons). The inflow of these job-seekers was a further reason why the downward trend in unemployment was interrupted. On the positive side, however, the number of job seekers who found work was higher than the number

2 *In January there was an upward revision of employment growth in business activities, accommodation and restaurants. The figures for 2013 were not revised.*

Chart 23 Unemployment



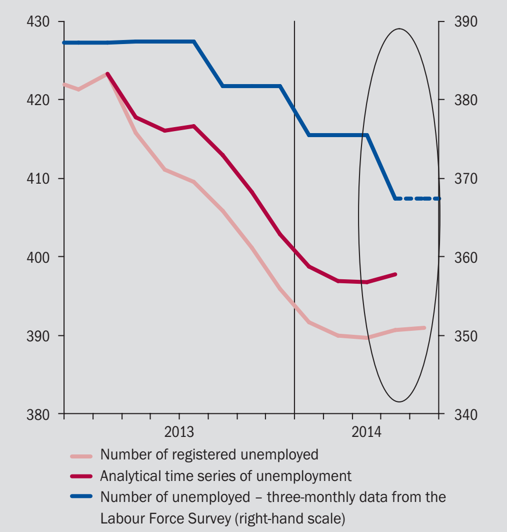
Source: Central Office of Labour Social Affairs and Family, NBS calculations.

who registered as unemployed after being made redundant. This was mirrored in the number of registered job vacancies, which recorded its largest month-on-month increase in the post-crisis period. If these vacancies are filled, it may be expected that labour market indicators will continue their moderate improvement in coming months.

Given the indications of a higher number of job vacancies, the unemployment rate may continue its downward trend in the second quarter, as projected in the MTF-2014Q2 forecast. That trend may be further supported by government efforts to expand work activation programmes for job seekers or newly announced projects for the employment of specified groups of job seekers.

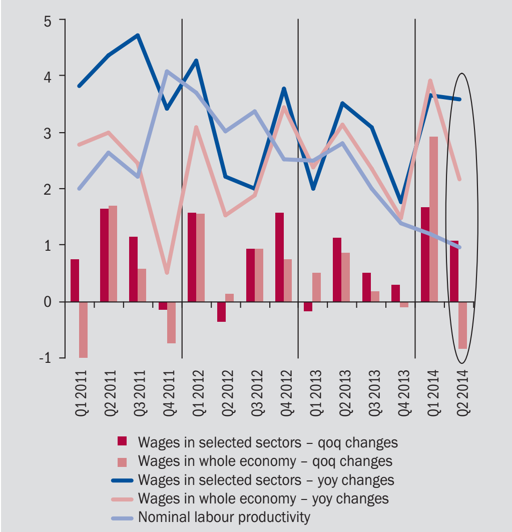
As economic growth picks up, wage growth is also accelerating. In April wages were 4.4% higher compared with the same month of 2013 and 1.3% higher month-on-month. In 2013 the average annual increase in nominal wages was 2.6% and in no month did it exceed 4%. Most of the growth was accounted for by wages in industry and, to a lesser extent, in business activities. In the construction sector, the average wage continued to decline in year-on-year terms, but it increased month-on-month. April saw wages fall in the IT and communication sector and in selected market services. Looking ahead, however, each of these sectors can potentially improve its economic

Chart 24 Number of unemployed (thousands of persons)



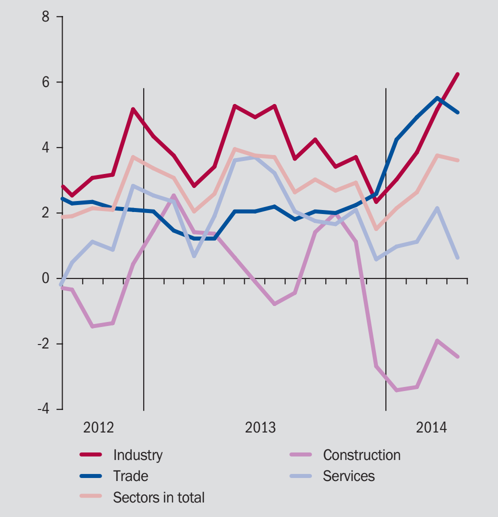
Source: Central Office of Labour Social Affairs and Family, SO SR and NBS calculations (seasonally adjusted).
Note: The number of unemployed (Labour Force Survey) for Q2 2014 is based on the MTF-2014Q2 forecast.

Chart 25 Wage developments in the economy (annual and quarter-on-quarter percentage changes)



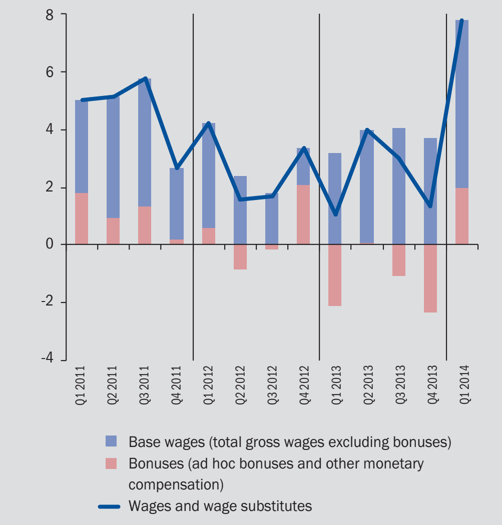
Source: SO SR.
Note: Wage growth in the selected sectors for Q2 2014 is calculated using the SO SR's monthly data and ARIMA modelling for May and June. Wage growth in the economy as a whole for Q2 2014 represents the current most plausible estimate for wages.
The figure for nominal labour productivity in Q2 is the projection from the MTF-2014Q2 forecast.

Chart 26 Wage growth (annual percentage changes; 3-month moving average)



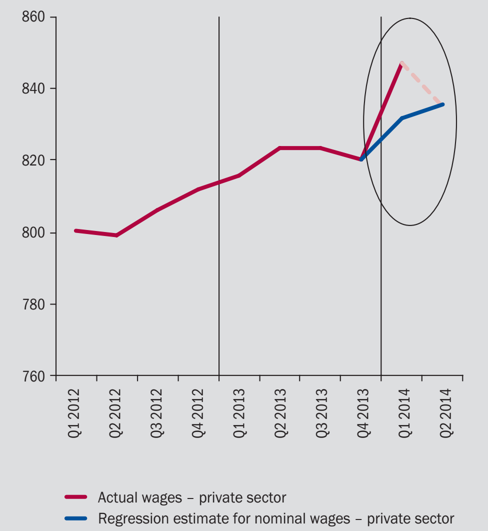
Source: SO SR.

Chart 28 Bonuses and principal wage components (annual percentage changes; components in p.p.)



Source: SO SR.

Chart 27 Projected adjustment of wages in Q2 2014 (EUR)



Source: SO SR.
Note: Regression for the nominal wage estimate are based on the following explanatory variables – value added in the private sector per employee, contribution wedge, and unemployment gap.

performance and therefore also its labour market indicators. It remains the case that low inflation may act as a partial brake on further wage growth, especially in the context of collective bargaining.

April's relatively strong wage growth might suggest that wages in the overall economy would increase appreciably in the second quarter. However, the first quarter saw wages in the overall economy increase by a substantial 2.9% over the previous quarter, driven largely by ad hoc bonuses (bonuses surged by 33% year-on-year, after falling by 10% in the fourth quarter of the previous year[3]). Consequently, in the second quarter, bonuses are expected to be more limited and the average wage level could fall (even after seasonal adjustment). Based on indicators such as nominal labour productivity and the unemployment gap, the annual growth rate of wages is expected to decelerate in the second quarter, from 4.1% to closer to 2%. There may be an upside risk to the wage growth outlook in the MTF-2014 forecast.

3 *Source: Statistical Office of the Slovak Republic. This data is from statistics on a sample firms that have 20 or more employees (including entities organisations performing financial intermediation and all non-business organisations regardless of their number of employees) and firms that have fewer than 20 employees and annual production worth €5 million or more.*

4 Prices

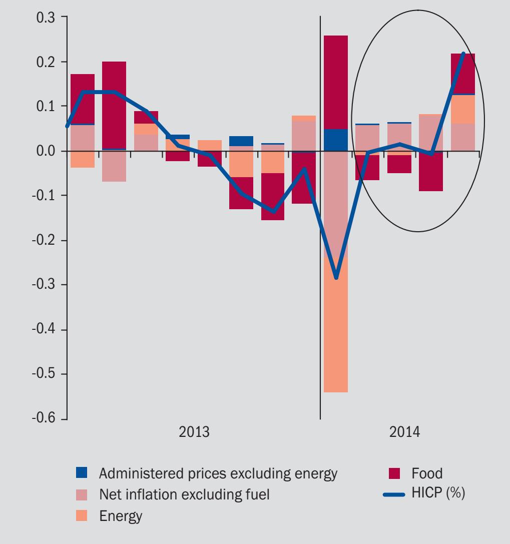
Downward trend in year-on-year prices stopped in May

Annual HICP inflation was 0.0% in May, almost 0.2 percentage point higher than its deflationary level in April. In month-on-month terms, consumer prices increased by 0.3%. The headline inflation rate exceeded NBS projections by 0.2 percentage points.

The shift in the annual inflation rate from negative territory to stagnation was largely accounted for by prices of processed food and fuel. The fact that processed food prices rose in May after declining month-on-month in April supports the view that during the holiday period retail chains were probably, paradoxically, reducing prices in order to compete for customers and increase sales. The subsequent price growth represents no more than a correction of retail chains' pricing policies after a weakening of demand.

The annual rate of decrease in prices of industrial goods continues to stabilise, which can be seen as relatively positive. The brightening of consumer sentiment may gradually put upward pressure on prices of semi-durable and durable goods as the profit margins of retailers and wholesalers widen. Services price inflation reached an all-time low of 0.7% in May 2014, but it is expected to accelerate in June due to the fading of the effect of the cancellation of

Chart 29 Contributions to month-on-month inflation (p.p.)



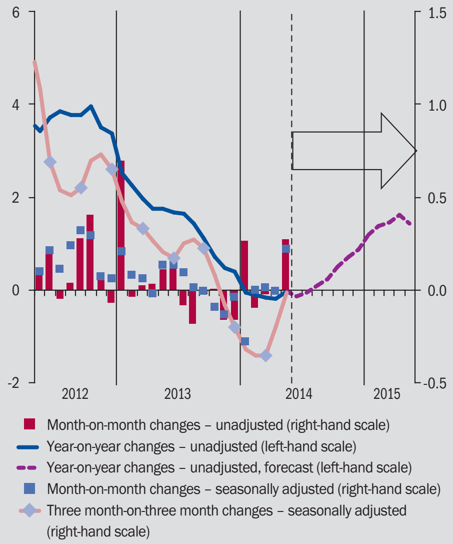
Source: SO SR, NBS calculations.

Table 1 HICP components – comparison of projected and actual rates of change (in percent unless otherwise stated)

			Non-energy industrial goods	Energy	Food	Services	HICP	Net inflation excluding fuel
Month-on-month change	A	May 2013 – actual figure	0.0	-0.2	0.6	0.0	**0.1**	0.0
	B	May 2014 – forecast	0.0	0.0	0.1	0.1	**0.0**	0.0
	C	**May 2014 – actual figure**	**0.0**	**0.4**	**0.9**	**0.0**	**0.3**	**0.0**
	BC	**Difference in contribution to month-on-month rate of change (p.p.)**	**0.00**	**0.06**	**0.20**	**-0.04**	**0.23**	**-0.02**
Year-on-year change	D	April 2014 – actual figure	-0.1	-2.3	-0.1	0.8	**-0.2**	0.2
	E	May 2014 – forecast	-0.2	-2.1	-0.6	0.8	**-0.3**	0.2
	F	**May 2014 – actual figure**	**-0.1**	**-1.7**	**0.2**	**0.7**	**0.0**	**0.2**
	AC	Base effect	moderate	**significant**	insignificant	insignificant	**moderate**	insignificant
	EF	**Difference in contribution to month-on-month rate of change (p.p.)**	**0.00**	**0.07**	**0.20**	**-0.04**	**0.22**	**-0.02**

Source: SO SR, NBS calculations.

Chart 30 Headline inflation rate (%)

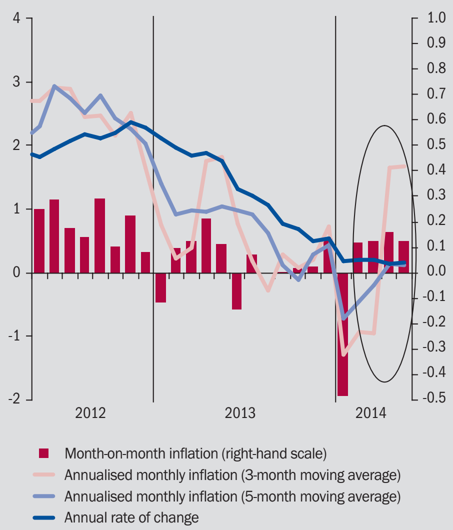


Source: SO SR, NBS calculations.

certain bank charges in June 2013. Subsequent movements in services prices will, with a lag, reflect external factors (via secondary effects), domestic consumer demand, and administrative prices. Services price inflation is expected to be kept relatively low by the projected year-on-year drop in energy prices and low food price inflation. On the other hand, rising consumer demand and wage growth could contribute to a gradually increase in services price inflation.

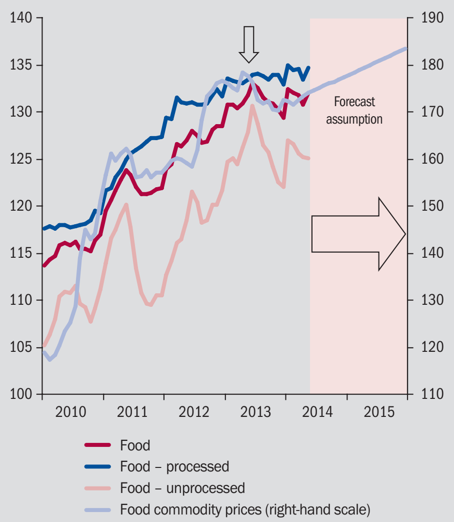
Over the next two months, the annual rate of change in HICP inflation is expected to fluctuate at close to 0%. Given current price developments and technical assumptions, the outlook is still that the average annual HICP inflation rate in 2014 will be very low and that the rate at the year-end will be just below 1%. A continuing risk to the inflation forecast is the movement of food and fuel prices in the second half of 2014. On the one hand, the uncertainty surrounding prices of agricultural and energy commodities (the current instability in the Middle East being an issue on the supply side) could be a major factor; on the other hand, depreciation of the euro's exchange rate against the dollar could be a factor.

Chart 31 Annualised net inflation excluding fuel prices (percent; seasonally adjusted)



Source: SO SR, NBS calculations.
Note: Net inflation comprises non-administered prices of services and non-administered prices of non-energy industrial goods.

Chart 32 Food prices (index: 2005=100)

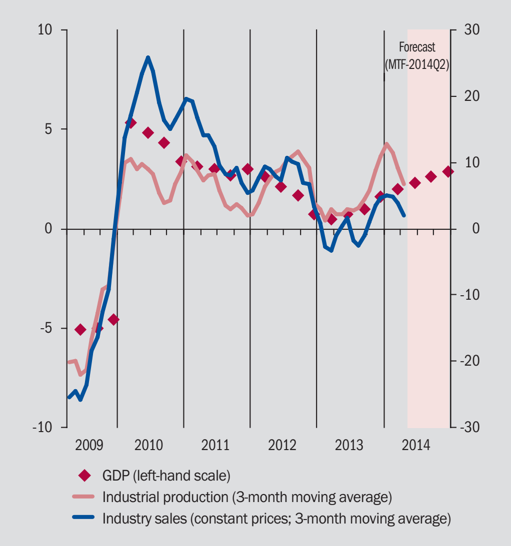


Source: SO SR, NBS calculations.

5 Qualitative impact on the forecast

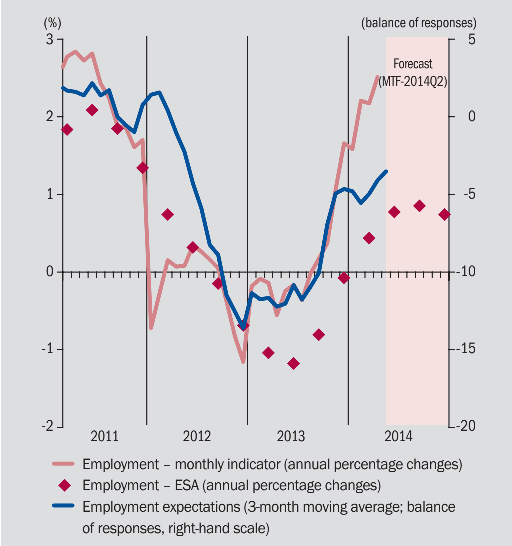
The detailed national accounts data for the first quarter broadly confirmed the projections of the current NBS forecast (MTF-2014Q2) for the composition of economic growth. Based on these data there was no need to revise the forecast. Looking at monthly figures for the real economy, however, the possibility of a further decline in exports represents a downside risk to the forecast

Chart 33 GDP, industrial production and sales (annual percentage changes)



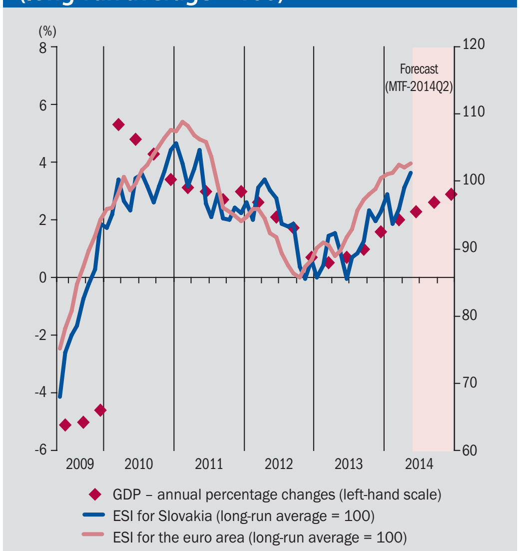
Source: SO SR and NBS.

Chart 35 Employers' expectations and the annual rate of change in employment



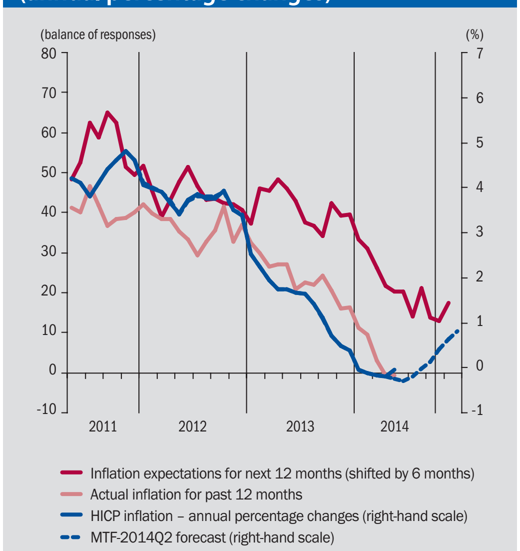
Source: SO SR, NBS and European Commission.

Chart 34 GDP (annual percentage changes) and the economic sentiment indicator (long-run average = 100)



Source: SO SR, NBS and European Commission.

Chart 36 Consumers' inflation perceptions (balance of responses) and HICP inflation (annual percentage changes)



Source: SO SR, NBS and European Commission.

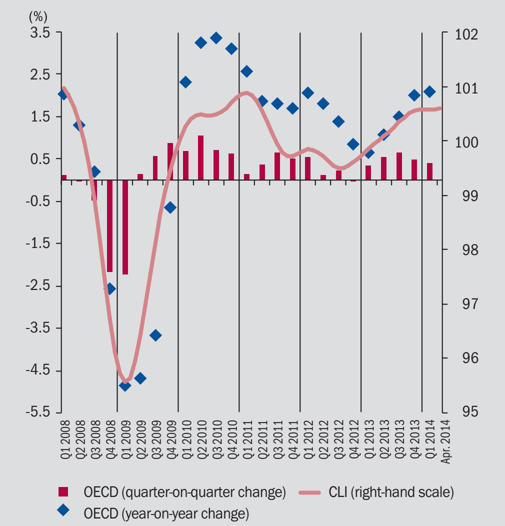
for moderate economic growth in the second quarter. Other monthly indicators pointed to a continuing recovery of domestic demand. These trends were further supported by forward-looking indicators showing improvement in both business and consumer sentiment. Export performance continues to be a risk, although one that may be partially offset by a pick-up in domestic demand. Hence there is no expectation of having to revise down the forecast for economic growth. Labour market figures were in line with expectations and the projections for these indicators did not need to be adjusted in the current forecast. Wage growth and inflation were slightly higher than expected, although the annual inflation rate is still not expected to rise until the last quarter of 2014.

QUARTERLY REPORT ON THE INTERNATIONAL ECONOMY

THE GLOBAL ECONOMY

The pace of growth in the global economy slowed somewhat in the first quarter of 2014. Overall, the trend of gradual revival in advanced economies and slowdown in emerging economies, which began in the second half of 2013, continued in the quarter under review. While the improving financial situation of households and supportive domestic policies had a positive impact on economic activity in advanced countries, the weaker domestic demand, coupled with stricter financial conditions and geopolitical tensions in certain regions, had a dampening effect on economic growth in emerging countries. Economic developments in certain countries (advanced or emerging) were also affected by one-off and non-standard factors. On the one hand, the US economy suffered a marked decline as a consequence of the harsh winter and the Chinese economy slowed down owing to the closedown of several enterprises in the heavy industry on environmental grounds. At the same time, economic activity in Russia weakened severely as a result of the conflict with the Ukraine. On the other hand, the global economy profited from the positive trend in Great Britain, where private household consumption was growing dynamically as a result of a steady rise in consumer confidence. Private consumption also increased considerably in Japan, but this was probably only a temporary effect of the turnover tax increase planned for April. Economic growth in the euro area remained below expectations, but was stimulated by all parts of the economy (except for net exports).Overall, economic activity in OECD countries slowed to 0.4% in the first quarter of 2014, from 0.5% in the previous quarter. In year-on-year terms, economic growth remained virtually unchanged (it accelerated by only 0.1 percentage point, to 2.1%). The modest revival in the global economy over the short-term horizon was also confirmed by the Composite Leading Indicator (CLI)[4] of economic sentiment, which stagnated in all OECD countries over the first quarter of 2014 and then rose slightly in April.

Chart 37 GDP as implied by CLIs



Source: OECD.
Note: CLIs – Composite Leading Indicators.

In the first three months of 2014, consumer price developments in OECD countries were determined by energy prices in particular. While the year-on-year dynamics of food prices increased only slightly and core inflation remained relatively stable (it rose from 1.6% in December 2013 to 1.7% in March 2014), energy prices were rather volatile in that period. Their increase in January led to a slight rise in inflation to 1.7%, from 1.6% as at the end of 2013. The subsequent fall in energy prices in February, which dampened the consumer price increase (1.4%), was only temporary. Energy prices continued to rise in March and consumer-price inflation returned to its December level. The current inflation rates of OECD countries indicate that the level of consumer price inflation rose to 2.0% in April. This rise was caused by energy prices, food prices, as well as by core inflation, which reached 2.0%. Price developments in OECD countries in April were influenced primarily by the turnover tax rate increase in Japan (from 5% to 8%[5]), as well as by the accelerated inflation in the United States as a result of energy prices.

Global economic activity is expected to increase gradually, but such revival will be very moderate in the short run. The slower restructuring in the

4 *The CLI indicators are published by OECD on a monthly basis – the latest available data, released in June 2014, are for April 2014.*

5 *The annual inflation rate in Japan rose by 1.8 percentage points in April (to 3.4%), compared with the previous month.*

private sector and the gradual fiscal consolidation, coupled with improved labour market conditions, are expected to support the growing demand in advanced economies. In the case of emerging economies, the gradual slowdown is likely to continue, while a dampening effect will be exerted by structural factors and, in certain countries, by monetary policy normalisation in the United States. A risk to the global economy is posed by uncertainty regarding the geopolitical conflict between the Ukraine and Russia.

COMMODITIES

The Brent oil price fluctuated over the first quarter of 2014 between USD106 and 111 per barrel. The average price stood at USD108/barrel and was only slightly lower than in the previous quarter (USD109/barrel). In January, oil prices showed a rising tendency in reaction to the growing concerns regarding the safety of supplies from Libya and Iraq. The improved demand and supply conditions, however, led to a correction in oil prices at the end of the month. The subsequent short-term rise in oil prices at the beginning of February turned into a falling trend owing to the expected decline in global demand for oil. The fall in oil prices in that period was also influenced by subdued activity in the Chinese industry. The falling trend in oil prices continued until the beginning of April, when the level of oil prices started to be pushed up by the Ukrainian crisis and the possible disruption of gas supplies from Russia, as well as the oil supply outages in Libya and Nigeria.

Non-energy commodity prices were stagnant at the beginning of the quarter under review. This was followed by a slowly rising trend as from February, mainly in food commodities. Metal prices declined in month-on-month terms throughout the quarter, reflecting the falling demand in China. The continuing rise in food commodity prices in April was a reaction to the unfavourable weather conditions in the United States and Brazil. An upward effect on non-energy commodity prices in this period was also exerted by metal prices.

UNITED STATES

The US economy was greatly influenced in the first quarter of 2014 by the unexpectedly harsh winter. For the first time since the first quarter of 2011, the annualised quarter-on-quarter rate of growth entered negative territory in the quarter under review, when the originally estimated fall of 0.1% was revised upwards to 1.0%[6]. This change also caused a slowdown in the year-on-year rate of growth, from 2.6% to 2.0%. The current positive labour market data on employment growth and the decreasing amount of unemployed benefits paid have confirmed that the economic downturn in the United States was caused by temporary one-off factors and that economic activity is returning to its previous level.

The downturn in the US economy was determined by all of its components, except for private consumption. The strongest negative impact was exerted by gross private investment, in particular by inventories, the decrease of which implied a negative contribution of 1.6 percentage points to growth. Private fixed investment declined, too. Consumption and investment also declined somewhat in the government sector. The weather conditions also had a profound impact on foreign trade. Owing to a sharp fall in exports and a slowdown in imports, the contribution of net exports to the annualised growth rate was negative. Overall, these components dampened the pace of economic growth by 3 percentage points. A pro-growth effect was only exerted by private consumption, mainly in the services sector (spending on housing and health care). The cold winter affected household consumption in terms of the structure of goods purchased, where spending on durable consumer goods slowed down.

In March 2014, inflation in the United States remained at the level of December 2013 (1.5%). Food prices increased more dynamically over the first quarter of 2014, but the overall trend in consumer prices was set primarily by the volatile developments in energy prices. Energy prices rose in year-on-year terms throughout the quarter under review, except in February, when they had a dampening effect on inflation. In March, core inflation also remained at the level of December (1.7%). In April, the price increase in the United States accelerated to a significant extent. The rise in inflation to 2.0% was caused by the continuing acceleration in food prices, as well as by the faster rise in energy prices. The dynamic increase in consumer prices was also supported to some extent by core inflation, which rose to 1.8% in April.

6 *In the fourth quarter of 2013, the US economy grew by 2.6% on an annualised basis.*

At its meetings in January, March, and April, the Federal Open Market Committee (FOMC) decided to leave its target range for the federal funds rate unchanged, at 0% to 0.25%. At its January meeting, the FOMC reaffirmed its intention to keep the target range for the federal funds rate at the current exceptionally low level at least as long as the unemployment rate remains above 6.5%, inflation between one and two years ahead is projected to be no more than 0.5 percentage point above the Committee's 2% longer-run goal, and longer-term inflation expectations continue to be well anchored. In determining how long to maintain a highly accommodative stance of monetary policy, the Committee will also consider other information, including additional measures of labour market conditions, indicators of inflation pressures and inflation expectations, and readings on financial developments. The Committee continues to anticipate, based on its assessment of these factors, that it likely will be appropriate to maintain the current target range for the federal funds rate well past the time that the unemployment rate declines below 6.5%, especially if projected inflation continues to run below the Committee's 2% longer-term goal. At its January meeting, the Committee also announced that the monthly amount of asset purchases would be reduced by USD10 billion to USD65 billion (with effect from February) in view of the current economic developments, accompanied by a steady improvement in labour market conditions. At its March and April meetings, the Committee signalled that, in determining how long to maintain the current 0% to 0.25% target range for the federal funds rate, the FOMC would assess progress – both realised and expected – towards its objectives of maximum employment and 2% inflation. The Committee continues to anticipate that it likely will be appropriate to maintain the current target range for the federal funds rate for a considerable time after the asset purchase programme ends, especially if projected inflation continues to run below the Committee's 2% longer-term goal, and provided that longer-run inflation expectations remain well anchored. Within the asset purchase programme, the Committee decided at its March and April meetings to reduce the amount of asset purchases by USD10 billion with effect from April or May. Thus, after the April meeting, the amount of asset purchases was reduced to USD45 billion.

Chart 38 Economic growth (at 2005 constant prices, percentage changes)

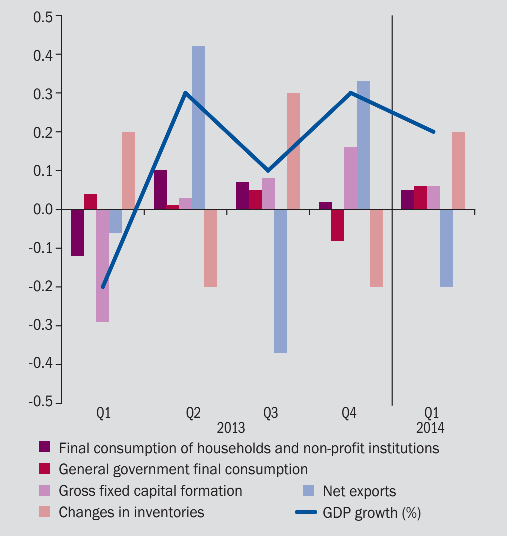
Source: Eurostat.

THE EURO AREA

The euro area economy continued to grow in the first quarter of 2014, for the fourth quarter in a row. Compared with the previous quarter, however, the pace of economic growth slowed to 0.2%, from 0.3% in the last quarter of 2013. This result was a disappointment to some extent, because the majority of forward-looking indicators pointed to somewhat faster economic growth. Although the relatively mild winter was beneficial to construction activity, it was also responsible for the markedly lower consumption of energy, especially of natural gas. This was mainly reflected in the Dutch economy, where gas consumption, production, and exports declined considerably. The Netherlands is the fifth biggest exporter of natural gas in the world, so this commodity is of great importance for the economy. Among the leading euro area economies, the Netherlands recorded a major economic decline in the quarter under review (1.4%). In year-on-year terms, the pace of economic growth accelerated to 0.9%, from 0.5% in the last quarter of 2013.

In terms of structure, economic growth in the first quarter was driven mainly by domestic demand. The most significant contribution to economic growth came from inventories, but fixed investment, government and private consumption also increased somewhat. Both investment

Chart 39 Contributions to quarterly GDP growth by component (percentage points)



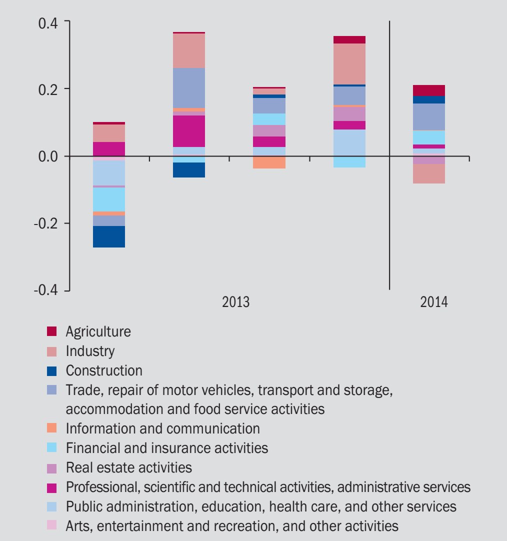
Source: Eurostat and NBS calculations.

demand and private consumer demand grew for the fourth consecutive quarter. Despite this, consumer demand was still subdued. The exports of goods and services continued to grow, but the rate of growth slowed considerably in comparison with the previous quarter. By contrast, the rate of import growth accelerated and consequently net exports made a negative contribution to economic growth.

On the supply side of the economy, value added increased by 0.1%. This increase took place mainly in trade, repair of motor vehicles, transport and storage, accommodation and food service activities. Value added also rose in financial and insurance activities, and in construction. By contrast, industry recorded a marked fall in value added (-0.3%). The fall in value added in industry was probably due to subdued value added creation in the energy sectors (the breakdown is not available), while value added in manufacturing continued to rise (by 0.6%).

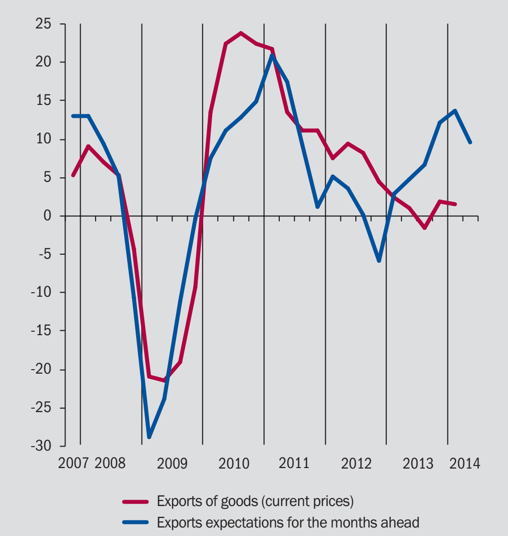
Manufacturing production, which is a key export sector, continued to grow in the first quarter of 2014. The annual rate of growth in manufacturing accelerated in the quarter under review in line with the sector's strengthening competitive position. In the second quarter of 2014, however, the growth in positive expectations regarding the sector's competitive position came to a halt and its perception in EU markets and non-EU markets deteriorated somewhat. The manufacturing sector's competitive position as perceived in the domestic market improved in that period. At the same time, export expectations in industry weakened slightly in the second quarter. Their level, however, remained relatively high, which indicates that the moderate growth in goods exports may continue.

Chart 40 Contributions of value added by sector to quarterly GDP growth (percentage points)



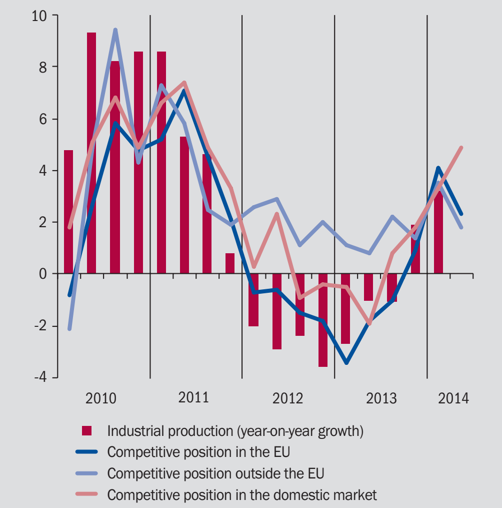
Source: Eurostat and NBS calculations.

Chart 41 Export expectations in industry (balance of responses) and goods exports (%, current prices)



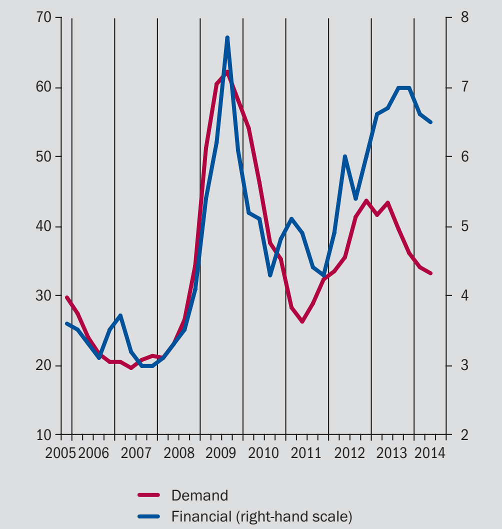
Source: European Commission, Eurostat and NBS calculations.

Chart 42 Competitiveness in industry (balance of responses) and industrial production (%)



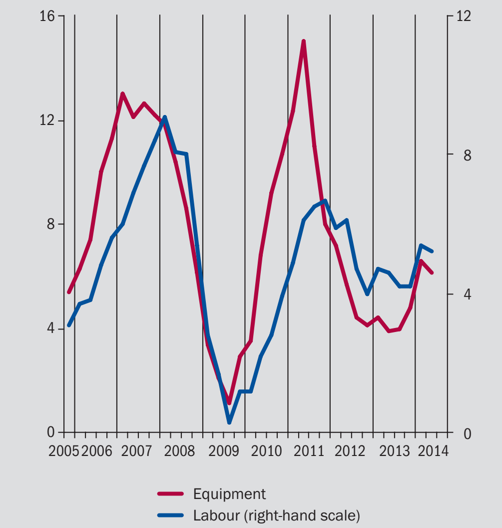
Source: European Commission, Eurostat and NBS calculations.

Chart 43 Production-limiting factors in industry (%)



Source: European Commission.

Chart 44 Production-limiting factors in industry (%)



Source: European Commission.

Demand in the euro area remained subdued in the period under review. Although the perception of demand as a production-limiting factor weakened in the second quarter, it weakened to a lesser extent than in the previous three quarters. The perception of financial factors as production-limiting factors decreased somewhat, but remained at a relatively high level. The perception of equipment and labour as production-limiting factors weakened in line with the weaker perception of production capacity utilisation. The individual indicators in industry suggest that production will continue growing, but probably at a more moderate pace.

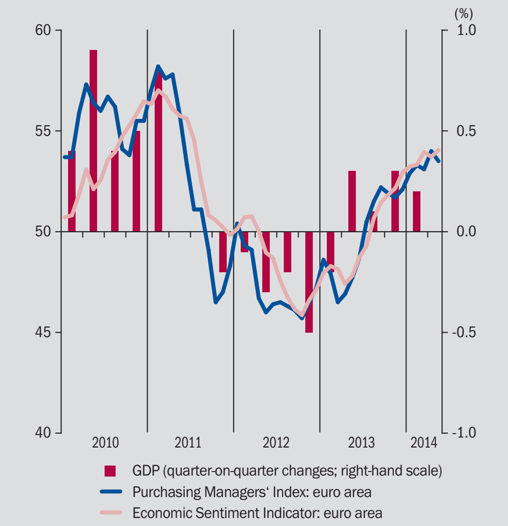
The labour market still represents a weak link in the economy. Unemployment has been falling since October 2013, but only marginally. Over the first quarter of 2014, the unemployment rate remained unchanged, at 11.8%. A slight fall was recorded in April, specifically a fall of 0.1 percentage point to 11.7%. Although the moderate fall in unemployment is expected by consumers to continue, the outlook for employment growth in the individual sectors is uncertain. In the period to date, employment in industry has been expected to follow a more or less falling trend. After a certain improvement, the expectations regarding employment in services and retail trade became slightly more pessimistic in May. Construction activity remained subdued in the quarter under review.

Most of the forward-looking indicators suggest that the euro area economy will continue growing in the quarter to come. The Economic Sentiment Indicator (ESI) rose throughout the first quarter. Its value fell slightly in April, but this fall was corrected in May. By contract, the Purchasing Managers' Index (PMI) recorded a slight fall in May,

Chart 45 The unemployment rate (%) and consumers' expectations regarding the economic situation and unemployment in the next 12 months (balance of responses)

Source: European Commission and Eurostat.

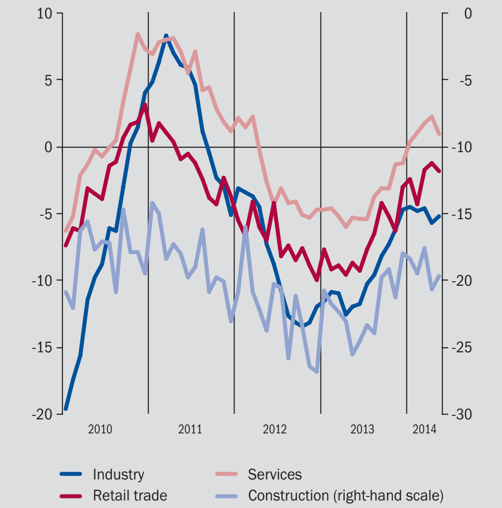
Chart 47 Euro area forward-looking indicators and GDP growth



Source: European Commission, Eurostat, Bloomberg, and NBS calculations.

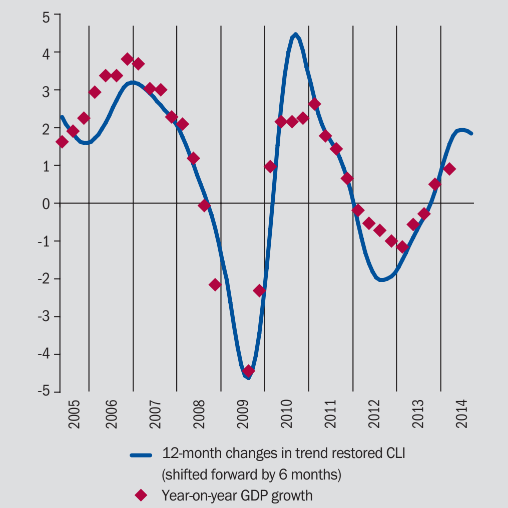
but continued to indicate relatively strong growth. The OECD Composite Leading Indicator (CLI) for the euro area pointed to continuing economic growth, without acceleration. Among the economic indicators for Germany, the ZEW index decreased gradually, as over the first five months of the year. The ZEW index, however, remained at a relatively high level, signalling the continuation of economic growth. The IFO index strengthened in the first two months, then weakened in March and May. Its value remained above the level of end-2013 and indicated further economic growth. Overall, it is possible to state that the level of optimism fell somewhat in both Germany and the euro area as a whole. This was undoubtedly influenced by the existing geopolitical tensions,

Chart 46 Employment expectations by sector (balance of responses)



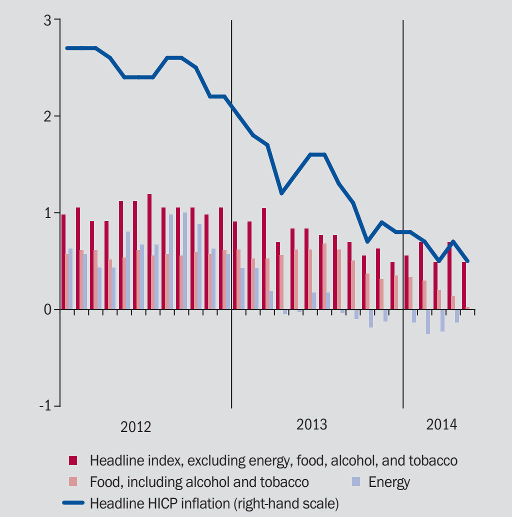
Source: European Commission.

Chart 48 OECD Composite Leading Indicator (expectations) and annual GDP growth (%)



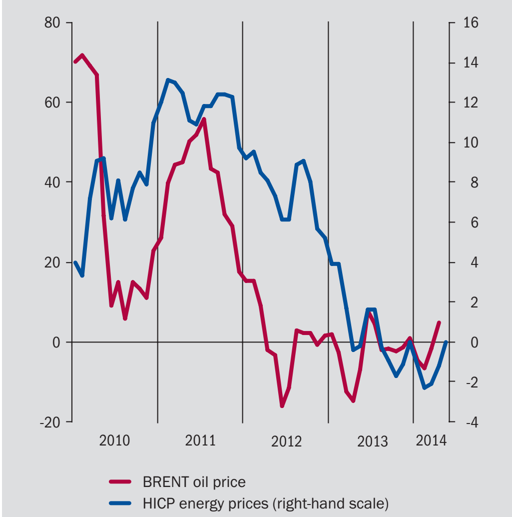
Source: OECD and Eurostat.

Chart 49 Annual headline HICP inflation (%) and contributions of selected components (percentage points)



Source: Eurostat and NBS calculations.

Chart 50 Oil and energy prices in the HICP index (%)



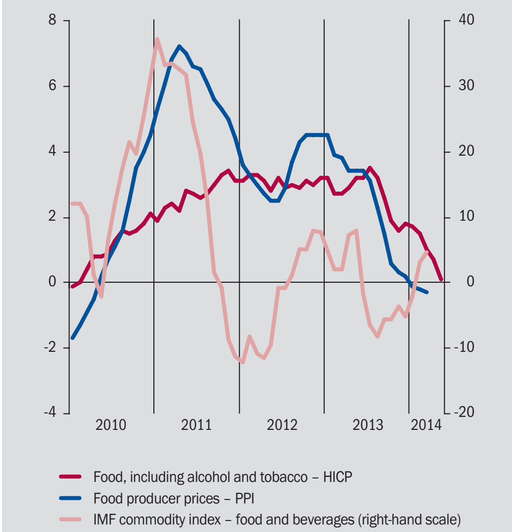
Source: Eurostat and EIA.

coupled with uncertainty regarding the impact of this situation on the economy.

The falling trend in inflation from the previous year continued in the first quarter of 2014. This trend was influenced first and foremost by energy and food prices. The rise in non-energy industrial goods prices and services prices slowed, too. During the first quarter, the HICP inflation rate fell from 0.8% in December 2013 to 0.5% in March 2014. Inflation also remained low in the following two months, when it rose slightly in April on account of the timing of the Easter holiday, but then in May it returned to the level of March.

Energy price inflation continued to reflect the year-on-year dynamics of oil prices on world markets. In the first two months of the year, the deepening year-on-year decline in oil prices was almost immediately reflected in energy prices for consumers. The moderating year-on-year decline in oil prices or their restored rise in the following months was also reflected in energy price inflation, which rose from negative territory to 0% in May. By contrast, the restored rise in food commodity prices was not yet reflected in the dynamics of food producer prices, nor in consumer food prices. The rise in consumer food prices slowed in the first quarter, as well as in the following two months.

Chart 51 Effect of food commodity prices on producer prices and consumer prices (annual percentage changes)

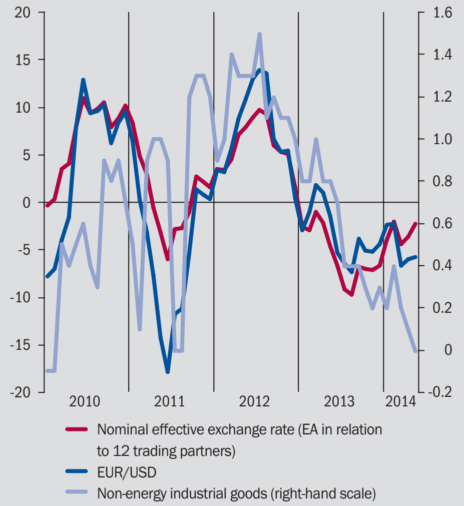


Source: Eurostat and IMF.

Consumer price inflation, excluding energy, food, alcohol, and tobacco prices (i.e. which are highly sensitive to demand-side developments) remained unchanged in March, at the level of end-2013 (0.7%). After a temporary rise in April, inflation returned to the same level in May.

The competitive economic environment, coupled with the persistently weak consumer demand, determined the prices of demand-sensitive inflation components. The rise in prices for services and non-energy industrial goods remained subdued. By the end of May, non-energy price inflation had slowed to 0%. Non-energy industrial goods prices were affected by the relatively strong euro exchange rate, which dampened the dynamics of import prices as well as the overall price increase in this segment. Services prices followed a more volatile course. At the beginning of the year, the rise in services prices accelerated as a result of an increase in indirect tax rates in France. The more volatile developments in the following months were influenced mostly by the timing of the Easter holiday (April 2014, compared with March 2013). In May, the rise in services prices remained virtually unchanged, at the end-2013 level (1.1%). Compared with the long-term average, however, services prices rose at a much slower pace in economies that were hit by the crisis in public finances or in the banking sector, where consumer demand contracted more significantly in reaction to the consolidation measures taken.

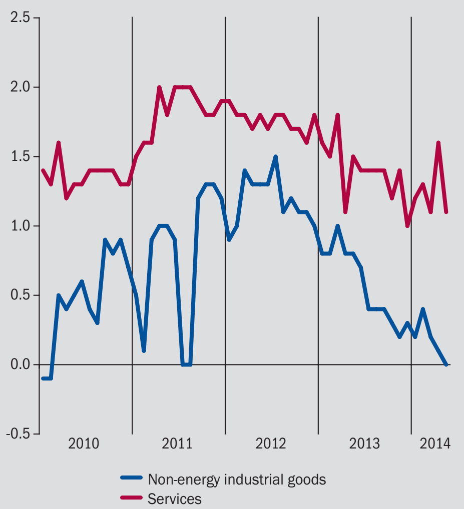
Chart 53 Non-energy industrial goods prices and the nominal exchange rate (annual percentage changes)



Source: Eurostat a ECB.

Selling price expectations remained rather low in the quarter under review. Compared with their end-2013 level, these expectations fell mainly in retail trade and industry. Both sectors had previously recorded an upward trend in these price expectations. The price expectations of consumers, reacting rather sensitively to changes in the prices of frequently purchased items, decreased to a significant extent, too. The prices of frequently purchased items have been rising at a slackening pace since the end of 2011.

Chart 52 Goods and services prices (annual percentage changes)

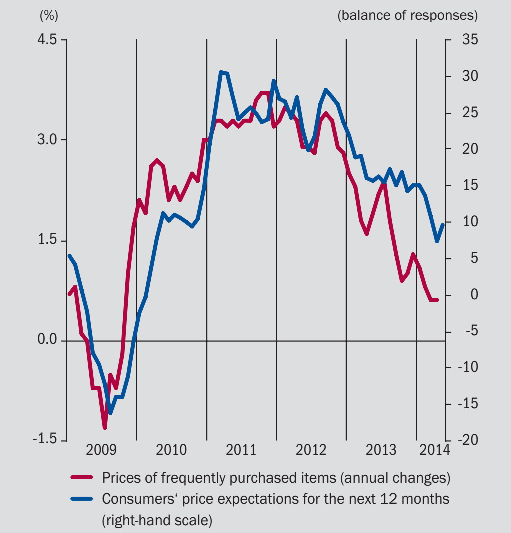


Source: Eurostat.

Chart 54 Price expectations in industry, services and retail trade (balance of responses)

Source: European Commission and Eurostat.

Chart 55 Prices of frequently purchased items and consumers' price expectations



Source: European Commission and Eurostat.

At its monetary policy meetings held in the first quarter of 2014, the Governing Council of the European Central Bank (ECB) decided to leave its key interest rates unchanged. Thus, the interest rate on the main refinancing operations of the Eurosystem remained at 0.25%, the rate on the marginal lending facility at 0.75%, and the rate on the deposit facility at 0.00% (throughout the first quarter). After its first meeting in June, the Governing Council of the ECB decided, with effect from 11 June 2014, to lower the interest rate on the main refinancing operations by 10 basis points to 0.15%, the rate on the marginal lending facility by 35 basis points to 0.40%, and the rate on the deposits facility by 10 basis points to -0.10%. This negative rate will apply to the deposit facility (overnight sterilisation operations), as well as to average reserve holdings in excess of the minimum reserve requirements and to other deposits held with the Eurosystem[7].

In view of the considerably improved US dollar funding conditions, the Governing Council of the ECB, in cooperation with the Bank of England, the Bank of Japan and the Swiss National Bank, has decided that the ECB will cease to conduct three-month US dollar liquidity-providing operations as of April 2014. One-week US dollar liquidity-providing operations will continue to be conducted at least until 31 July 2014.

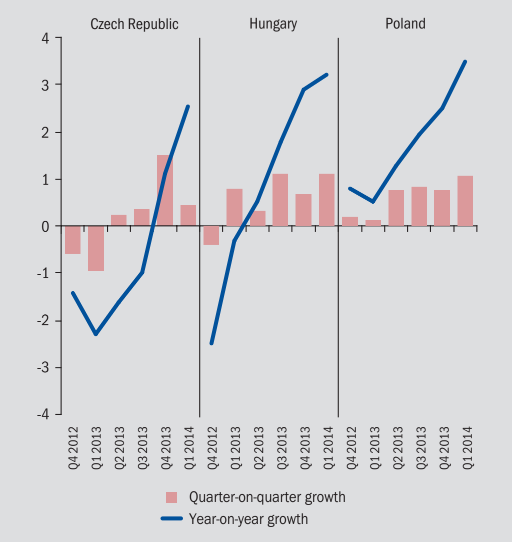
At its meeting on 5 June 2014, the Governing Council of the ECB adopted further monetary policy measures to enhance the functioning of the monetary policy transmission mechanism by supporting lending to the real economy within the scope of its mandate to maintain price stability. In particular, the Government Council decided to conduct a series of targeted longer-term refinancing operations (LTROs) aimed at improving bank lending to the euro area non-financial private sector, excluding loans to households for house purchases, over a window of two year. The Governing Council also decided to intensify preparatory work related to outright purchases of asset-backed securities (ABS). The Governing Council decided to continue conducting its main refinancing operations (MROs) as fixed rate tender procedures with full allotment for as long as necessary, and at least until the end of the Eurosystem's reserve maintenance period ending in December 2016. Furthermore, the Governing Council decided to conduct the three-month longer-term refinancing operations (LTROs) to be allotted before the end of the Eurosystem's reserve maintenance period ending in December 2016 as fixed rate tender procedures with full allotment. The rates in these three-month operations will be fixed at the average rate of the MROs over the life of the respective LTRO. In addition, the Governing Council decided to discontinue the Eurosystem's special-term refinancing operations with a maturity of one maintenance period, following the operation to be allotted on 10 June 2014. Finally, the Governing Council decided to suspend the weekly fine-tuning operation sterilising the liquidity injected under the Securities Market Programme, following the operation to be allotted on 10 June 2014.

DEVELOPMENTS IN POLAND, THE CZECH REPUBLIC AND HUNGARY

In the first quarter of 2014, all three countries under review recorded a year-on-year improvement in economic performance: the Czech economy grew by 2.5% (in the previous quarter by 1.1%), the Hungarian economy grew by 3.2% (0.3 percentage point more than in the previous quarter), and the Polish economy expanded by 3.5% (1.0 percentage point more than in the previous quarter).

7 *More detailed information is available at www.ecb.europa.eu*

Chart 56 GDP growth (%)

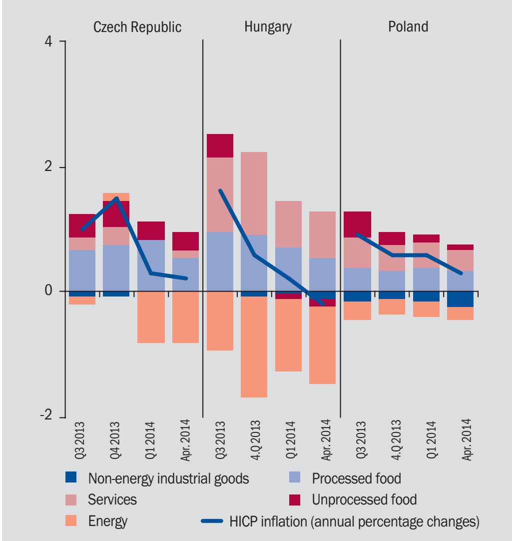


Source: Eurostat.

A marked slowdown in quarter-on-quarter terms was recorded in the Czech economy, which grew by 0.4% in the first quarter of 2014, representing a slowdown of 1.1 percentage points compared with the previous quarter (caused largely by one-off factors). By contract, the rates of growth in the Hungarian and Polish economies accelerated equally by 0.4 percentage point to 1.1%. GDP growth in the Czech Republic was influenced in the first quarter by the uneven excise tax collection on tobacco products in connection with the stocking up with tobacco products at the end of 2013. The main pro-growth factor was net exports, caused by accelerated growth in exports, which exceeded the growth in imports. GDP growth was positively influenced by both consumer demand (with government consumption rising too) and investment demand. By contrast, inventories had a dampening effect, which was connected with the aforementioned stocking up with tobacco products. In Hungary, the accelerated GDP growth in the first quarter of 2014 was attributable largely to growth in domestic demand, consumer demand (mainly in the public sector), and investment demand. By contrast, net exports had a negative effect as a result of slower growth in exports than in imports. The Polish economy was driven in the first quarter by the escalating investment demand. Household final consumption also increased, but more moderately than in the previous quarter. At the same time, general government consumption decreased. The pace of economic growth was dampened by net exports.

At the end of the first quarter of 2014, the 12-month rate of consumer-price inflation slowed in quarter-on-quarter terms in the Czech Republic and Hungary, while it remained unchanged in Poland. The slowdown in inflation in the Czech Republic (by 1.2 percentage points, to 0.3%) was caused primarily by energy prices, which, after rising slightly at the end of the previous quarter, fell to a significant extent. The consumer price increase was also dampened by services prices, which stagnated towards the end of the first quarter. The effects of processed and unprocessed food prices on headline inflation offset one another. The overall consumer price dynamics in the Czech Republic weakened somewhat in April. Consumer-price inflation in Hungary slowed by 0.4 percentage point, to 0.2% as at the end of the first quarter. This slowdown was caused mainly by services prices, which slowed considerably in comparison with the end of the previous quarter. Inflation was also dampened by food prices, with unprocessed food prices falling and processed food prices showing weaker dynamics. At the same time, the energy price decline moderated considerably. April saw a fall in the level of consumer prices

Chart 57 Contributions to HICP inflation (percentage points)

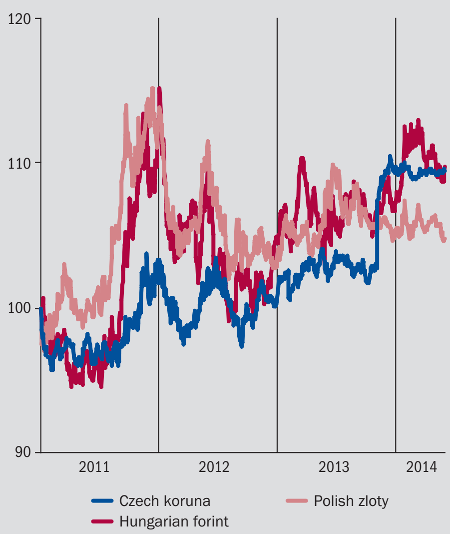


Source: Eurostat and NBS calculations.

in Hungary. Poland's headline inflation rate as at the end of the first quarter (0.6%) corresponded to the figure recorded a quarter earlier. In the quarter under review, the decline in non-energy industrial goods prices deepened, and thus compensated for the modest fall in energy prices. Food prices followed a similar trend: the slowdown in unprocessed food prices offset the faster rise in processed food prices. Services prices maintained the same dynamics as in the previous quarter. Poland's headline inflation rate slowed in April.

In the first quarter of 2014, the Hungarian forint showed a slightly depreciating tendency in quarter-on-quarter terms, while the Polish zloty followed a highly volatile course. The exchange rate of the Czech koruna tended to strengthen as a result of the central bank's November decision to make foreign exchange interventions in order to maintain the eased monetary policy conditions. The exchange rates under review were influenced in this period first and foremost by tensions in emerging markets persisting since the beginning of the year and resulting from concerns about the possible suspension of qualitative easing by the Fed and from signs of a slowdown in emerging economies, especially in China. The ongoing crisis in the Ukraine also contributed to these tensions.

Chart 58 Exchange rate indices of the V4 currencies vis-à-vis the euro (3 January 2011 = 100)

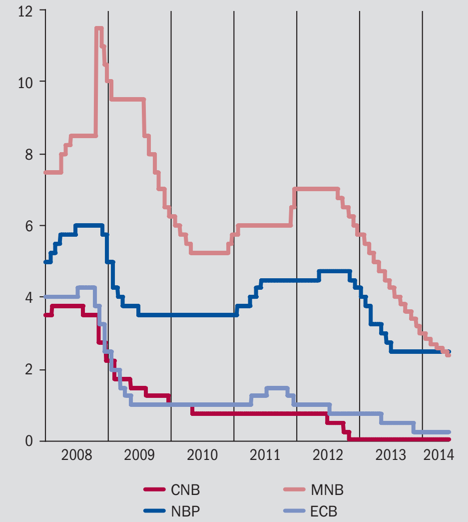


Source: Eurostat and NBS calculations.
Note: A fall in value denotes appreciation.

The Czech koruna fluctuated around the level of CZK/EUR 27.5 throughout the quarter under review, when the effect of any positive information on the Czech economy that may lead to exchange range appreciation was more than offset by the asymmetrical commitment of CNB to prevent the exchange rate from strengthening below the level of CZK/EUR 27. This commitment should be maintained until the beginning of 2015 or longer. The Hungarian forint was negatively influenced by global factors (the financial markets of emerging economies) and was rather volatile over the first quarter, until the middle of March. As from the middle of March, the forint began to appreciate gradually. The exchange rate of the Polish zloty was also affected by market tensions at the beginning of the year. The zloty depreciated somewhat in January, then appreciated in February, then weakened again. The exchange rate of the zloty vis-à-vis the euro was rather volatile over the first quarter, but had the potential for a stable appreciation, mainly as a result of a steady revival in the Polish economy.

In the first quarter of 2014, the only central bank within the group of countries under review to use its base rate to change the monetary policy conditions was the Hungarian central bank. In the Czech Republic, the central bank rate remained unchanged, at 0.05% (technical zero). At its meetings held in the first quarter of 2014, Česká národní banka (CNB) confirmed its decision to use the exchange rate as a monetary policy tool through foreign exchange interventions with the aim of maintaining price stability in the Czech economy in line with the inflation target. The exchange rate of the koruna is to be maintained at a level close to CZK/EUR 27. According to the latest data, this exchange rate commitment should be maintained at least until the beginning of 2015. Hungary's Magyar Nemzeti Bank (MNB) cut its base rate on three occasions in the first quarter of 2014: twice by 0.15 percentage point and once by 0.1 percentage point to 2.60% as at the end of the quarter. The rationale behind this decision was the persisting low inflation environment, dampened by inflationary pressures over the medium-term horizon and by the high degree of free capacities in the economy. Inflation is expected to remain below the central bank's inflation target throughout 2014, with a gradual return to the target level after 2015. The deeper and more permanent perception of risks posed to the Hungarian economy may create room for a further easing of monetary policy. The Hungarian central bank lowered its base rate in April and May 2014 still further. In April, however, the Hungarian central bank decided to change its monetary policy tools in order to improve the structure of the country's external debt (debt financing from domestic sources, instead of external sources). With effect from 16 June 2014, MNB has introduced a rate for swap operations in forints, a floating interest rate for long-term collateralised loans in forints, and swap operations in assets. With effect from 1 August 2014, two-week operations in MNB bills have been replaced with two-week deposit operations. In the first quarter of 2014 and the following two months, Narodowy Bank Polski (NBP) kept its base rate unchanged at 2.50%, because this rate was appropriate for the recovery of the Polish economy, return to the inflation target, and financial market stabilisation. The NBP also confirmed its commitment to maintain the base rate at this level at least until the third quarter of 2014.

Chart 59 Key interest rates of the V4 national central banks (%)



Source: National central banks and ECB.

QUARTERLY REPORT ON THE REAL ECONOMY

THE REAL ECONOMY IN THE FIRST QUARTER OF 2014

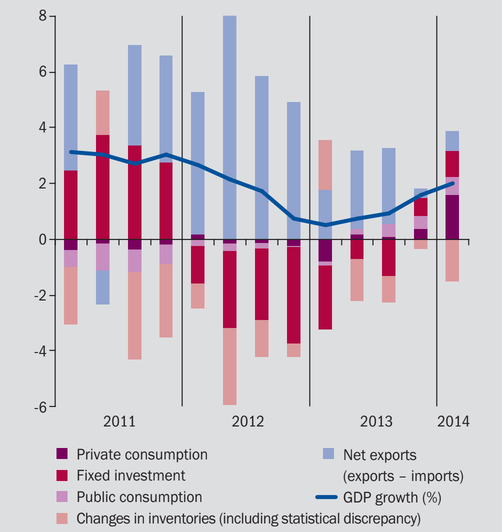
GROSS DOMESTIC PRODUCT

The Slovak economy grew in the first quarter of 2014 by 0.6%, compared with the previous quarter. Thus, economic growth continued to accelerate slightly for the second quarter in a row.

While GDP growth in the previous quarter was driven by investments, the main contributor in the quarter under review was private consumption. In year-on-year terms, the rate of GDP growth (seasonally unadjusted) accelerated from 1.5% in the fourth quarter of 2013 to 2.4% in the first quarter of 2014.

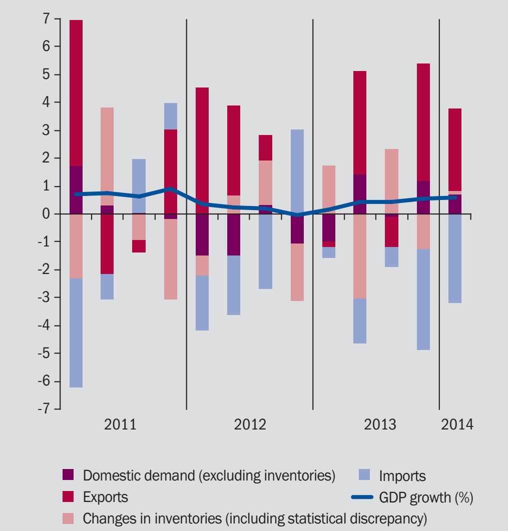
The ongoing revival in the countries of our trading partners led to an upturn in the Slovak economy's export performance. As a result, the growth dynamics of exports of goods and services again exceeded the estimated dynamics of foreign demand for Slovak products. This

Chart 60 Contributions to annual GDP growth (percentage points)



Source: SO SR.

Chart 61 Contributions to quarterly GDP growth (percentage points)



Source: SO SR.

Table 2 GDP by expenditure (quarter-on-quarter percentage changes; at constant prices)

	2013					2014
	Q1	Q2	Q3	Q4	Year	Q1
Gross domestic product	**0.1**	**0.4**	**0.4**	**0.5**	**0.9**	**0.6**
Final consumption	-0.4	0.7	0.4	0.6	**0.3**	1.0
Households and NPISHs	-0.8	1.2	-0.1	0.4	**-0.1**	1.5
General government	0.3	0.6	1.6	0.4	**1.4**	1.4
Gross fixed capital formation	-3.0	3.7	-1.8	4.5	**-4.3**	-1.5[1)]
Exports of goods and services	-0.2	3.7	-1.0	4.2	**4.5**	2.8
Imports of goods and services	0.4	1.9	0.8	4.1	**2.9**	3.5

Source: SO SR.
1) If the last quarter of 2013 were adjusted for one-off investments (estimate), fixed investments in the first quarter of 2014 would increase by more than 1% quarter-on-quarter.

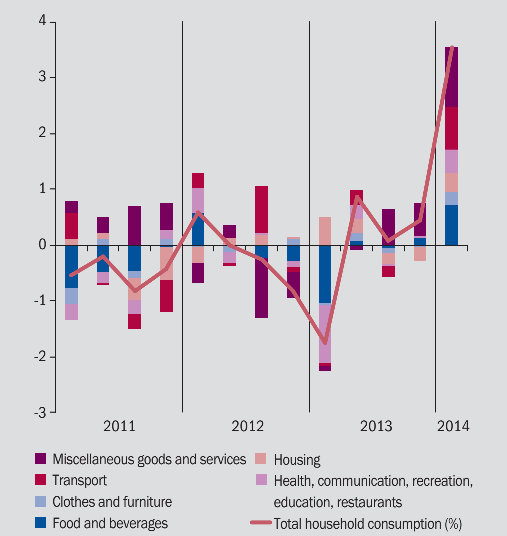
Chart 62 Developments in Slovakia's export markets compared with Slovak exports (year-on-year percentage changes)

Source: SO SR and NBS calculations.

indicates that Slovak exporters increased their market share still further in the first quarter of 2014, mainly in the market for motor vehicles and components.

Although exports contributed almost 3 percentage points to the quarterly rate of GDP growth in the first quarter, the Slovak economy was not driven exclusively by exports in that period. After more than five years of deferred consumption and occasional tentative rises in consumer spending, household consumption noticeably increased in the quarter under review and contributed 0.5 percentage point to GDP growth. Household consumption began to show clear signs of revival as a result of low inflation and growing wages. Prices fell somewhat, particularly for food and energy, i.e. vital commodities the consumption of which cannot be reduced considerably. Owing to the lower food and energy prices, households could satisfy their needs for these vital commodities at lower costs and could thus spend more on other goods. They probably purchased non-durable and semi-durable consumer goods, luxury goods, and services, rather than durable goods. The share of food, transport, miscellaneous goods and services increased to almost three-quarters of the year-on-year increase in consumption.

Chart 63 Contributions of consumer groups to year-on-year growth in household consumption (percentage points)



Source: SO SR and NBS.

Government consumption also contributed to the growth in domestic demand, mainly as a result of growth in employee compensation and health insurance payments (these contributed 0.2 percentage point to GDP growth). Domestic demand would have been even higher if investments had not fallen quarter-on-quarter owing to the base effect of a high basis of comparison from the last quarter of 2013. Thus, investments dampened the rate of GDP growth by 0.3 percentage point. Excluding the marked one-off effect of investments in the automobile industry from the end of last year, investments would have increased slightly in the first quarter of 2014. Although there were no massive imported investments as in December, the revival of domestic demand and persisting export growth helped to maintain a relatively high level of imports. Imports dampened the rate of GDP growth by 3.2 percentage points.

The low-inflation environment in the consumer market and the current decline in producer prices, as well as in export and import prices, caused the year-on-year GDP deflator to fall.

On the production side, GDP growth at constant prices was generated mostly by value added (almost 90%), the remaining 10% came from net taxes on products.

Table 3 GDP and its components (year-on-year percentage changes; at constant prices)

	2013					2014
	Q1	Q2	Q3	Q4	Year	Q1
Gross domestic product	**0.5**	**0.8**	**0.9**	**1.5**	**0.9**	**2.4**
Gross output	-3.7	0.0	0.9	3.1	**0.1**	5.3
Intermediate consumption	-5.9	-0.2	1.5	4.1	**-0.1**	7.3
Value added	0.2	0.4	-0.1	1.5	**0.5**	2.0
Net taxes on products[1)]	3.8	4.9	11.4	2.3	**5.6**	6.8

Source: SO SR.
1) Value added tax, excise tax, import tax, less subsidies.

WAGES AND LABOUR PRODUCTIVITY

Supported by the impact of accelerating economic growth, the situation in the labour market continued to improve in the first quarter of 2014. Employment increased somewhat, while unemployment decreased according to both the Labour Force Survey (LFS) and statistical reports. The number of vacancies for employees increased, while the number of active self-employed persons decreased slightly. The number of hours worked in the economy increased, too. Following the stabilisation of labour costs in relation to productivity, wages increased considerably in both the public and private sectors. Since this increase was caused mostly by irregular remuneration payments, the wage dynamics may weaken in the period to come. The higher wages led to an increase in both final household consumption and savings.

The beginning of this year saw relatively strong wage growth. The year-on-year dynamics of wages and salaries reached 4.1% (the highest level since the first quarter of 2009) and their quarter-on-quarter growth accelerated to 2.9% for the economy as a whole and to 3.3% for the private sector (the highest figures in the post-crisis period). Wages in the public sector and health care increased by 4.4% year-on-year. Although a certain stimulus could also come from the improved real economic situation, labour productivity increased slowly in nominal terms as a result of falling producer prices. An important accelerating effect could be caused in this quarter by one-off remuneration payments in larger companies, which could distort the rate of growth. Irregular remuneration payments increased by 33% year-on-year, representing the steepest increase since the beginning of the time series used.[8] Owing to the absence of a price rise, real wages increased in the first quarter by 4.2% year-on-year. This increase created conditions for growth in private household consumption.

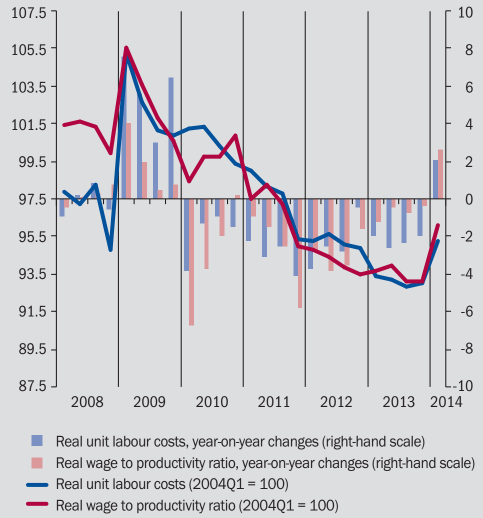
Contributions to growth in quarter-on-quarter terms were made by the following sectors: manufacturing, trade, administrative and support service activities, and sectors related to the general government (public administration, education and health care). In the public sector, an increase was expected on the basis of the anticipated increase in wage tariffs. A slightly negative trend in wages (quarter-on-quarter decline) was only recorded in water supply and in professional activities.

Developments in compensation per employee corresponded to wage developments, which was natural, because there had been no major changes in the amounts of compulsory payments of employers since the beginning of the year. Employee compensation thus increased in the first quarter by 2.6% quarter-on-quarter and by 3.6% year-on-year, compared with 0.4% and 0% respectively in the last quarter of 2013. Contributions to this increase were made by the same sectors as in the case of wages. In the case of compensations, however, marked increases were also recorded in agriculture, real estate activities, professional activities, arts and entertainment. Real compensation per employee increased, like wages, by 4.4% year-on-year.

As in the previous two quarters, productivity increased only slightly (by 0.3% quarter-on-quarter), after new employees had been hired after a longer period. By contrast, real labour costs, expressed in terms of compensation per

8 Source: Statistical Office of the Slovak Republic. This data is from statistics on a sample firms that have 20 or more employees (including entities organisations performing financial intermediation and all non-business organisations regardless of their number of employees) and firms that have fewer than 20 employees and annual production worth €5 million or more.

Chart 64 Real labour productivity and real labour costs (index 2004Q1 = 100)



Source: SO SR and NBS calculations.
Note: Real unit labour costs as defined in the ESA 95 methodology. CPI deflated real wages from quarterly statistical reports. All data are seasonally adjusted.

employee or real wages, grew more dynamically. This contributed to the growth in unit labour costs. On the basis of these facts concerning irregular remuneration payments, it is possible to assume that this is only a one-off phenomenon, which will not affect the competitiveness of the Slovak economy in the long run.

HOUSEHOLD INCOME AND EXPENDITURE

The current income of households increased by 2.6% year-on-year, to €14.3 billion in the first quarter of 2014. Compared with the last quarter of 2013, the annual growth rate accelerated by 1.6 percentage points. This acceleration was caused mainly by the strong year-on-year growth in employee compensation, accompanied by a modest increase in gross mixed income. By contrast, the negative dynamics of current income were influenced by social benefits, which dampened the annual growth rate.

Table 4 Generation and use of income in the household sector (current prices)

	EUR billion		Annual rate of change (%)		Percentage share	
Item	Q1 2013	Q1 2014	Q1 2013 / Q1 2012	Q1 2014 / Q1 2013	Q1 2013	Q1 2014
Employee compensation (all sectors)	6.6	6.9	1.4	4.1	47.6	48.3
of which: gross wages and salaries	5.2	5.5	1.9	4.6	37.5	38.2
Gross mixed income	3.8	3.9	2.5	1.8	27.2	26.9
Property income – received	0.4	0.4	12.2	-5.9	2.9	2.6
Social benefits	2.6	2.7	2.9	1.4	18.9	18.6
Other current transfers – received	0.5	0.5	2.1	2.9	3.5	3.5
Current income in total	**13.9**	**14.3**	**2.3**	**2.6**	100.0	100.0
Property income – paid	0.1	0.1	-20.3	24.8	2.8	3.3
Current taxes on income, property, etc.	0.5	0.5	3.7	4.5	13.5	13.6
Social contributions	2.6	2.7	1.2	3.2	68.2	67.9
Other current transfers – paid	0.6	0.6	6.2	1.2	15.5	15.2
Current expenditure in total	**3.8**	**3.9**	**1.5**	**3.7**	100.0	100.0
Gross disposable income	**10.2**	**10.4**	**2.6**	**2.3**	-	-
Adjustment arising from changes in net assets of households in pension fund reserves	0.1	0.1	-46.9	-6.6	-	-
Household final consumption	10.0	10.2	0.5	2.5	-	-
Gross household savings	0.3	0.3	42.6	-9.1	-	-

Source: SO SR.

Table 5 Gross disposable income (index, same period a year earlier = 100, at current prices)

	2013					2014
	Q1	Q2	Q3	Q4	Year	Q1
Gross disposable income (1)	102.6	102.6	101.9	101.2	102.0	102.3
Adjustment (pension funds) (2)	53.1	43.1	51.9	60.7	51.3	93.4
Household final consumption (3)	100.5	102.3	101.2	101.2	101.3	102.5
Gross household savings (4)	142.6	83.7	93.0	97.5	96.5	90.9
Savings ratio [%, (4)/((1)+(2))]	3.2	6.1	6.2	16.4	8.3	2.8

Source: SO SR and NBS calculations.

The current expenditure of households (expenses paid to other sectors and not used for direct consumption) increased year-on-year by 3.7%. Compared with the previous quarter, the growth rate accelerated by 3 percentage points. This was due mainly to tax payments, social contributions paid, and, to a lesser extent, to income from property.

The gross disposable income of households (current income less current expenditure) amounted to €10.4 billion, representing a year-on-year increase of 2.3%. This represented an acceleration of 1.1 percentage points compared with the previous quarter. A seasonal adjustment by NBS pointed to a quarter-on-quarter increase of 1.2%. The year-on-year decline in gross savings deepened to -9.1%. In quarter-on-quarter terms, however, gross savings increased somewhat (the seasonally adjusted savings ratio rose in nominal terms from 8.1% to 8.4%). This was due to the fact that household final consumption increased in the first quarter to a lesser extent than disposable income did.

EMPLOYMENT AND UNEMPLOYMENT

Employment grew at a slightly accelerated pace in the first quarter of 2014, when, according to the ESA methodology, its level increased by 0.3% quarter-on-quarter. Thus, the gradual revival in employment, which had begun in the second half of 2013, continued in the quarter under review. In year-on-year terms, employment grew by 0.6%, representing an acceleration of 0.5 percentage point compared with the previous quarter. According to the Labour Force Survey (LFS), employment increased by 0.1% quarter-on-quarter and by 0.2% year-on-year. This was due partly to the number of people working abroad, which decreased year-on-year for the first time since the second quarter of 2012 (by 5,200 persons, i.e. 3.8%). By contrast, according to statistical reports (based on reports from domestic enterprises), employment increased by 0.5%[9] quarter-on-quarter and by 0.6% year-on-year. Despite the methodological differences, the individual measurements clearly indicate that the number of new jobs created in the quarter under review increased.

According to the ESA 95 methodology, employment growth in the first quarter was caused mainly by an increase in the number of employees (by 0.4% quarter-on-quarter). The number of self-employed fell by 0.4%, but this category made a limited contribution to overall employment owing to its low weight. In year-on-year terms, the number of employees increased by 0.7 percentage point (to 1%) and the number of self-employed decreased, as in the previous quarter, by 1.3%.

In quarter-on-quarter terms, employment growth according to the ESA methodology was supported by transport and trade, and, to a lesser extent, by manufacturing, information technology and communications, professional and support service activities, public administration, education, and health care. Negative contributions came from agriculture, construction, and the entertainment industry.

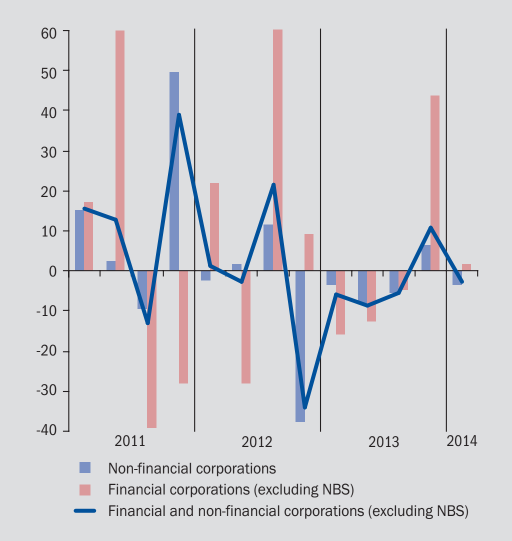
The number of hours worked in the economy broadly reflected the trend in employment. The number of hours worked by employees increased by 0.4%, while the number of hours worked by self-employed persons decreased by 0.8%. The trends in the number of hours worked began in the second quarter of 2013. In year-on-year terms, the number of hours worked increased

9 *Seasonally adjusted by NBS.*

by 1.1%, representing an improvement of 2.2 percentage points compared with the previous quarter. The average weekly number of hours worked decreased slightly, from 36.9 to 36.8 hours, and was influenced by the self-employed.

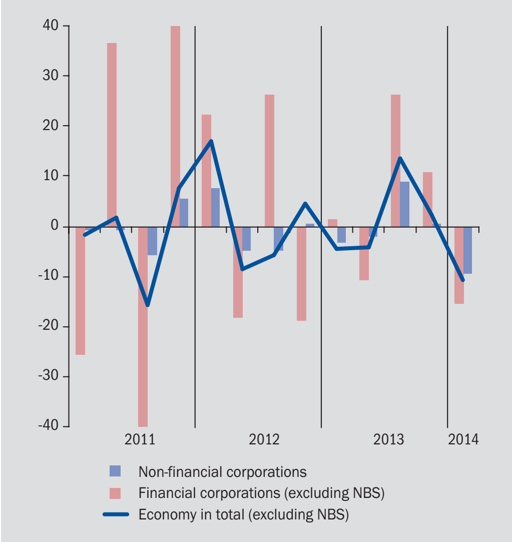
According to the Labour Force Survey (LFS), the number of unemployed decreased by 3.2% year-on-year to 382,900 in the first quarter of 2014. Thus, the positive trend that began at the end of last year continued in the period under review. In quarter-on-quarter terms, the number of unemployed dropped by 6,200 persons (after seasonal adjustment).This number is higher than the increase in the number of people employed (1,900 persons according to the LFS methodology), which indicates that an important role is played here by the demographic trend (falling number of economically active people), which creates vacancies in the labour market. The number of economically active people decreased by 4,300. As a result of this trend, the seasonally adjusted unemployment rate fell by 0.2 percentage point quarter-on-quarter, to 13.9%. The number of unemployed registered by labour offices showed a favourable tendency: it dropped by 10,400 (after seasonal adjustment). The average registered unemployment rate reached 13.46%, representing an improvement of 1.3 percentage points year-on-year and 0.5 percentage point quarter-on-quarter (after seasonal adjustment).

Chart 65 Total profits in the economy (excluding NBS) (year-on-year percentage changes)



Source: SO SR and NBS calculations.

Chart 66 Total profits in the economy (quarter-on-quarter percentage changes)



Source: SO SR and NBS calculations.

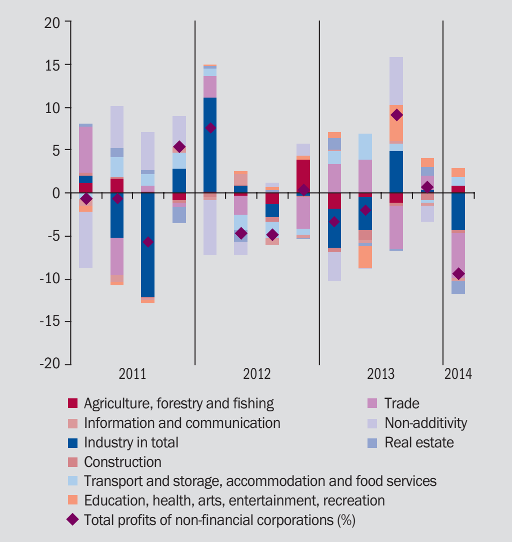
FINANCIAL RESULTS

In the first quarter of 2014, the total profits of financial and non-financial corporations (excluding NBS), expressed in seasonally adjusted terms, declined by 2.8% year-on-year, after growing in the previous quarter by 10.8%. In quarter-on-quarter terms, however, total profits fell by 10.6%, after rising in the last

Chart 67 Investments and profits of non-financial corporations (%)

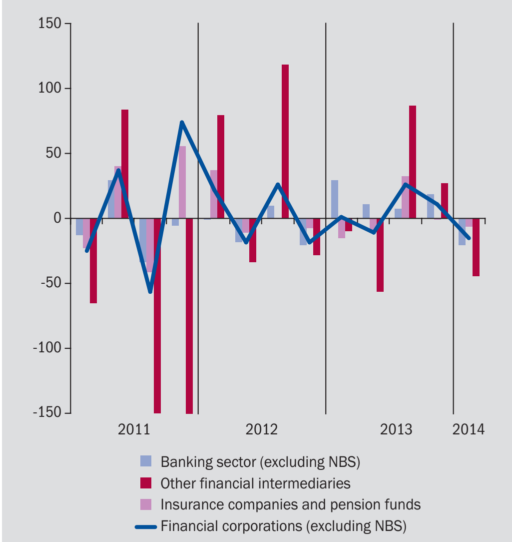
Source: SO SR and NBS calculations.

Chart 68 Total profits of non-financial corporations by sectoral contributions to their quarterly rate of change



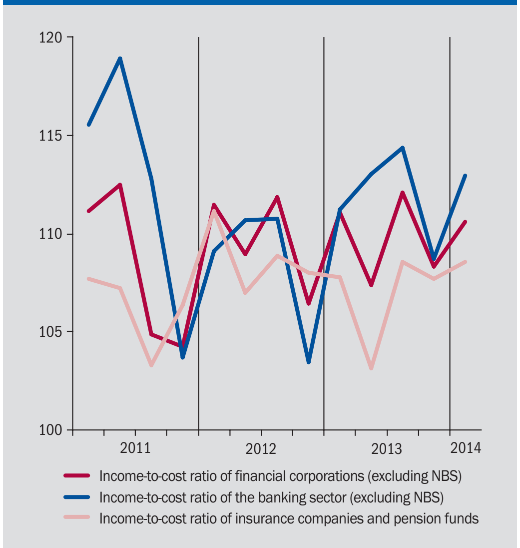
Source: SO SR and NBS calculations.

Chart 70 Total profits of financial corporations (%)



Source: SO SR and NBS calculations.

Chart 69 Income-to-cost ratios of financial corporations (%)



Source: SO SR and NBS calculations.

quarter of 2013 by 2.3%. Negative developments were recorded in both the financial corporations and non-financial corporations sectors.

The financial results of **non-financial corporations** continued to worsen in the first quarter of 2014 (the quarter-on-quarter growth rate dropped to -9.4%, from 0.6% in the last quarter of 2013). The fall in profits was caused by the negative financial results of corporations in trade, construction, and manufacturing (mainly in the food and chemical industries). This was partly offset by an increase in profits in the wood processing and textile industries. The fall in profits was, to some extent, offset by an increase in profits in agriculture, mining and quarrying, electricity and gas supply, transport and accommodation services, and in education.

Like non-financial corporations, the **financial sector (excluding NBS)** also recorded substantially worse financial results in the first quarter of 2014 (a quarter-on-quarter fall of 15.3%, compared with a rise of 10.7% in the previous quarter). This deterioration was reflected in the falling profits of all types of institutions, mostly in the *other financial intermediaries* sector, where profits dropped by 45% quarter-on-quarter.

Overview of main macroeconomic indicators for Slovakia

Table 6 Selected economic and monetary indicators for the SR

(annual percentage changes, unless otherwise indicated)

	Gross domestic product	HICP	Industrial producer prices	Employment ESA 95	Unemployment rate (%)	Industrial production index	Total receipts of sectors	Economic sentiment indicator (long-term average =100)	M3 for analytical purposes[1]	Loans to non-financial corporations	Loans to households	State budget balance (EUR mil.)	General government balance as % of GDP	Debt ratio (general government gross debt as % of GDP)	Current account (% GDP)	Balance of trade (% GDP)	USD/EUR exchange rate (average for the period)
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
2006	8.3	4.3	6.4	2.1	13.3	15.6	-	112.5	15.3	-	-	-1,051.5	-3.2	30.5	-7.8	-4.7	1.2556
2007	10.5	1.9	1.8	2.1	11.0	16.7	-	114.6	12.9	25.4	28.6	-781.0	-1.8	29.6	-5.3	-1.2	1.3705
2008	5.8	3.9	6.1	3.2	9.6	2.9	-	99.1	4.9	15.3	25.3	-704.2	-2.1	27.9	-6.0	-1.1	1.4708
2009	-4.9	0.9	-2.6	-2.0	12.1	-15.4	-18.6	78.0	-2.8	-3.3	11.0	-2,791.3	-8.0	35.6	-2.6	1.5	1.3948
2010	4.4	0.7	-2.7	-1.5	14.4	8.0	7.9	98.7	7.8	1.6	12.5	-4,436.1	-7.5	41.0	-3.7	1.2	1.3257
2011	3.0	4.1	2.7	1.8	13.6	5.4	8.9	98.6	2.9	7.6	11.1	-3,275.7	-4.8	43.6	-3.8	1.5	1.3920
2012	1.8	3.7	3.9	0.1	14.0	7.7	5.2	94.0	8.8	-2.3	10.3	-3,810.7	-4.5	52.7	2.2	5.0	1.2848
2013	0.9	1.5	-0.1	-0.8	14.2	5.3	2.1	90.6	5.2	1.7	10.2	-2,023.3	-2.8	55.4	2.1	5.9	1.3281
2013 Q2	0.8	1.7	0.1	-1.3	14.0	3.0	2.5	89.1	7.4	-0.1	10.0	-	-2.1	57.9	4.8	8.6	1.3062
2013 Q3	0.9	1.4	-0.7	-0.9	14.1	4.5	1.8	89.7	6.2	0.4	10.3	-	-1.4	57.1	1.1	4.5	1.3242
2013 Q4	1.5	0.5	-1.7	0.1	14.2	10.8	4.3	95.0	5.2	1.7	10.2	-	-4.8	55.4	-0.9	3.6	1.3610
2014 Q1	2.4	-0.1	-3.4	0.6	14.1	7.6	4.3	95.9	4.1	0.8	10.7	-	.	.	3.2	7.3	1.3696
2013 June	-	1.7	-0.3	-	14.3	2.7	0.6	85.5	7.4	-0.1	10.0	-63.4	-	-	-	-	1.3189
2013 July	-	1.6	-0.5	-	14.0	3.0	1.6	88.8	5.7	-2.2	10.1	39.1	-	-	-	-	1.3080
2013 Aug.	-	1.4	-0.7	-	13.7	3.9	0.4	89.4	6.3	-0.5	10.2	-291.0	-	-	-	-	1.3310
2013 Sep.	-	1.1	-0.8	-	13.8	6.5	3.2	91.0	6.2	0.4	10.3	-61.4	-	-	-	-	1.3348
2013 Oct.	-	0.7	-1.4	-	13.7	7.2	3.0	95.6	9.0	1.0	10.2	6.5	-	-	-	-	1.3635
2013 Nov.	-	0.5	-2.0	-	13.5	12.9	4.2	94.0	6.5	-0.6	10.3	8.7	-	-	-	-	1.3493
2013 Dec.	-	0.4	-1.7	-	13.5	12.7	5.9	95.4	5.2	1.7	10.2	-60.5	-	-	-	-	1.3704
2014 Jan.	-	0.0	-2.5	-	13.6	8.1	4.9	98.1	4.8	2.8	10.2	-122.9	-	-	-	-	1.3610
2014 Feb.	-	-0.1	-3.7	-	13.5	9.0	3.9	93.7	5.0	0.0	10.5	-754.2	-	-	-	-	1.3658
2014 Mar.	-	-0.2	-4.0	-	13.3	5.9	4.0	95.9	4.1	0.8	10.7	-208.7	-	-	-	-	1.3823
2014 Apr.	-	-0.2	-4.4	-	13.0	5.1	1.2	99.0	3.6	-2.2	10.0	-430.4	-	-	-	-	1.3812
2014 May	-	0.0	.	-	12.8	.	.	101.3	.	.	.	-362.8	-	-	-	-	1.3732

Sources: Statistical Office of the Slovak Republic, MF of the SR, the European Commission and NBS.
1) Currency in circulation in M3 refers to money held by the public (according to methodology in place prior to 2008).

More detailed time series for selected macroeconomic indicators
http://www.nbs.sk/_img/Documents/_MonthlyBulletin/2014/StatisticsMB0614.xls