Foreword

The year 1995 has been an eventful year for the National Bank of Slovakia. The economic growth surpassed all expectations, whilst at the same time the primary objectives of monetary policy (i.e. reduction of inflation and stabilisation of the currency) were also achieved. Budgetary performance resulted in a deficit lower than had originally been forecast in the State budget draft, and even produced a surplus - for the first time since the beginning of the economic reform in 1990. The surplus in the balance of trade and the current account of the balance of payments, the increasing inflow of foreign capital, the achieved level of foreign exchange reserves, and the more efficient application of a stabilisation-oriented economic and monetary policy, made it possible for Slovakia to abandon internal convertibility and, with the support of the new Foreign Exchange Act, to liberalise transactions within the current account of the balance of payments in accordance with Article 8 of the IMF Agreement. In this way Slovakia took an important step towards full convertibility.

Liberalisation of foreign trade and foreign exchange policy is a prerequisite for Slovakia's admission to OECD, and later to the European Union. In this respect, Slovakia is faced with another demanding task: a gradual liberalisation the flow of capital according to the requirements of the Liberalisation Code of OECD, and to stabilise monetary development using market instruments.

Staff recruitment for the National Bank of Slovakia was virtually complete in 1995. Thanks to the staff, the Bank was able to strengthen the position of the Slovak crown in the economy, despite its short history as an independent central bank. In reviewing the past year, I should mention the work and professional contribution of RNDr. Ing. Štefan Adamec, CSc, Chief Executive Director of the Monetary Division and Member of the Bank's Board, who recently passed away.

In 1995, confidence in the Slovak crown and creditworthiness of the National Bank of Slovakia increased both at home and abroad. In recognition of this, the two most prestigious American rating agencies upgraded their ratings of the NBS. Standard and Poor's increased the Bank's long-term hard currency liability rating to BB+ with stable outlook, and Moody's Investors Service upgraded Slovakia's hard currency debt rating to Baa3 investment grade.

The last year was the year of a significant change in Slovakia's system of payment and settlement with the Czech Republic. The exchange rate deviation applied in mutual payments was gradually removed, and the Clearing Account Agreement with the Czech Republic was cancelled with effect from 30 September 1995. In October, Slovakia started to apply the standard method of a cross border payment. It is an indication of the maturity of the country's banking system that the change was effected smoothly, without serious problems.

Due to increasing confidence in the Slovak economy and expansion of the private sector, the inflow of foreign capital underwent a significant change in 1995. While foreign capital in the past was absorbed mainly by the State, the inflow of the foreign capital in 1995 was directed mostly to enterprises and commercial banks. The new situation has complicated the stabilisation of monetary development, though Slovakia's gross foreign debt remains relatively low, and the level of official debt was even reduced by debt service payments over the course of the year.

The first measure designed to get the inflow of foreign capital under control was taken already in the first quarter of 1995 with the launch of the first issue of NBS bills. The NBS bills issues have gradually paved the way for transition from the application of administrative tools to indirect monetary-policy instruments. The volume of the issue and the scope of operations on the open market increased steadily throughout the year. Open market operations were again employed in 1995 to correct excess liquidity and improve the situation on the money market. The introduction of interbank offered rates (BRIBOR) made a significant contribution to stabilisation of the money market.

In 1995, the National Bank of Slovakia continued working in close cooperation with foreign and international financial institutions. While funds obtained in previous years were used mainly to strengthen the country's balance of payments, in 1995 funds were mainly drawn for the support of specific development and restructuring projects. This involved cooperation with the IMF and the World Bank (Economic Recovery Loan, Enterprise and Financial Sector Adjustment Loan), the European Investment Bank (Apex Global Loan), and the EXIM Bank of Japan (Two Step Loan, Economic Recovery Loan). Technical assistance within the PHARE Programme was also of great importance.

The Bank's most significant achievement was a considerable reduction in consumer-price inflation. The average annual rate of inflation fell to 9.9%, and the annual inflation to the level of 7.2%. The favourable development of inflation made it possible for the NBS to lower the discount rate from 12% at the beginning of 1995 to 9.75% at the end of the year-end. Commercial banks took this as a signal to cut interest rates on the money market gradually. Since inflation has been so successfully dealt with in Slovakia for more than two years, this has done much to increase consumer confidence. Reducing inflation continues to be a priority for the NBS and the Slovak Government in the time ahead.

A key problem in Slovakia, in common with that in other transition economies, is the financial recovery of the business and banking sector. Commercial banks have gradually improved their capital adequacy and liquidity ratios. The improving financial position of the banking sector has made it possible for the Bank to commence a process of loan portfolio restructuring in the banking sector by stipulating regulations for evaluation of bank receivables and off-balance sheet liabilities according to risk exposure, and for the creation of reserve funds to cover such risk. It is essential to accelerate this process on account of the growing competition within the Slovak banking sector, where the number of branches and representative offices of foreign banks is steadily increasing, particularly in respect of increased competition in foreign investment.

With regard to the Bank's note issuing activity, the series of Slovak banknotes was completed in 1995 with new notes in Sk 200 and Sk 5,000 denominations. Further issuing activity will consist of new issues, withdrawals, and improvement of banknotes and coin in circulation. According to practical experience gained in recent years, Slovak banknotes are well protected against forgery.

The excellent results achieved by the NBS in the past year are in no small measure due to the coordination of financial and monetary policies based on respect for the Bank's freedom to set and implement monetary policy. We emphasise this, because we realise that the Bank will be able to meet the task of maintaining the stability of the recently liberalised currency only if the policy of cooperation continues to be developed.

Vladimír Masár
Governor

Bank Board of the NBS

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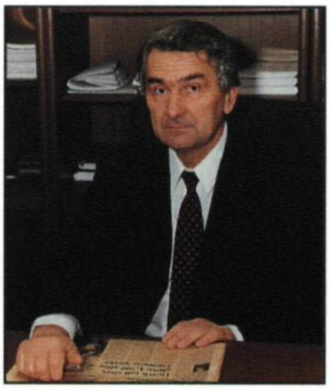

Štefan Adamec

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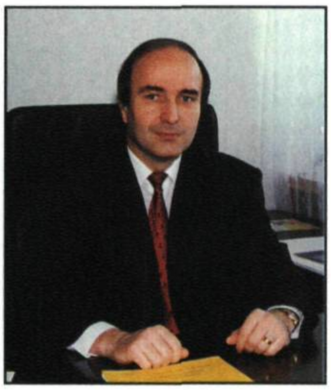

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