B. REPORT ON MONETARY DEVELOPMENT IN THE SR IN 1999

1. ECONOMIC DEVELOPMENT

Economic development in 1999 was marked by numerous conflicting tendencies. On the one hand, the pace of economic growth slowed, the rates of inflation and unemployment increased, while the country's external and internal balance was gradually restored. Some of the macroeconomic indicators deteriorated as a result of the impacts of unfavourable trends from previous years and the measures adopted by the Government in May 1999, to bring about economic recovery. The measures, which were designed to cut public spending and mobilise revenues, caused the deficit of trade to diminish by almost 50% and the performance of public finances to improve.

The unbalanced development of the economy in previous years and the measures adopted for its stabilisation led to a slowdown in the rate of year-on-year growth in gross domestic product (GDP) from 4.4% in 1998 to 1.9% at constant prices. On the expenditure side of GDP, a crucial factor was the export of goods and services, while on the side of GDP creation, the weight of industry and agriculture increased. An important aspect of economic transformation was the continued growth of GDP in the private sector, when its share of GDP increased year-on-year by 1.9 percentage points, to 84.3%.

In 1999, the dynamics of price increase accelerated considerably in comparison with 1998. The 12-month rate of inflation, expressed in terms of the consumer price index, reached 14.2% in December 1999. The average annual rate of inflation was 10.6%.

A key factor in the development of consumer prices was the adoption of administrative measures by the Government for the elimination of macroeconomic imbalances. In addition to adjustments to regulated prices, the price increase was also affected by the introduction of a surcharge on imports, adjustments to value added tax rates and excise duties on hydrocarbon fuels and tobacco, and by the exchange rate of the Slovak crown.

The rise in the price of fuels, mainly oil, the introduction of a surcharge on imports and administrative measures by the Government, were the main factors that affected the level of producer prices. They led to an accelerated increase in industrial producer prices and construction prices. The rate of increase in the prices of building materials showed a slowdown, while the year-on-year fall in agricultural prices increased in comparison with 1998.

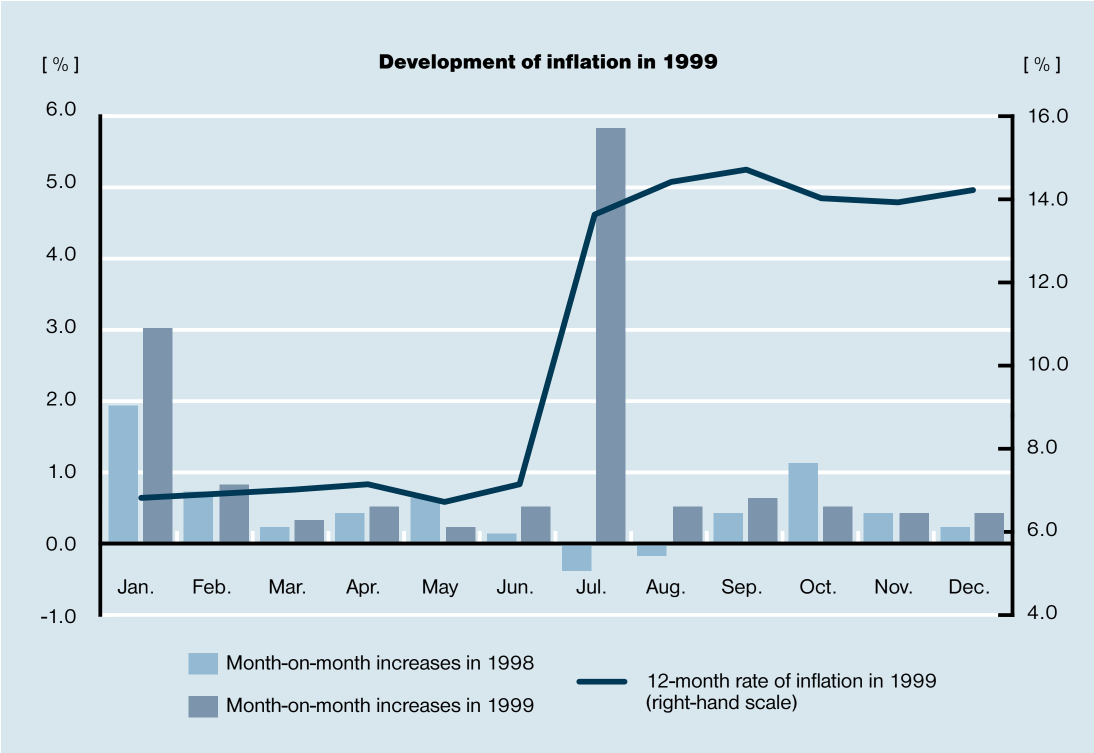
The average nominal wage in the Slovak economy reached Sk 10,728 in 1999. It increased year-on-year by 7.2%, but its rate of growth slowed by 2.4 percentage points compared with 1998. The level of real wages recorded a fall of 3.1%, for the first time since 1993.

A positive phenomenon, which is to a certain extent a reflection of an improvement in the competitiveness of the Slovak economy, was an increase in labour productivity based on real GDP, which increased year-on-year by 4.2% per employee in the Slovak economy.

At the end of December 1999, the absolute number of registered unemployed reached 535.2 thousand, 25% more than a year earlier. The rate of unemployment, calculated on the disposable number of registered unemployed, stood at 19.2% at the end of the year.

1.1. Price Development

In 1999, the increase in the general price level accelerated in comparison with 1998. The 12-month rate of inflation, expressed in terms of the consumer price index, reached 14.2% at the end of December, which was in line with the Revised Monetary Programme of the NBS for 1999 (13.5 to 15.5% at year-end). In 1999, the average annual rate of price inflation stood at 10.6%.



The acceleration in the year-on-year increase in consumer prices in 1999, was due primarily to the presence of external and internal cost factors. The effects of these factors were reflected in all sectors according to the structural breakdown of the consumer basket, which led to increases in their inflation rates in comparison with the previous year.

Apart from the adjustments to regulated prices, the price increase was also affected by the introduction of a surcharge on imports (7% as of 1 June 1999), adjustments to value added tax rates and excise duties on hydrocarbon fuels and tobacco, and by the exchange rate of the Slovak crown. After the adjustments to energy prices in January and July, the running expenses of households related to dwelling increased. This led to a slowdown in the rate of growth in consumer demand, which acted as a brake on the rise in price levels.

Of the total increase in consumer prices (14.2%), net inflation, i.e. share of market services and tradable goods (excluding foods) in total inflation, accounted for 6.06 percentage points and reached a value immediately above the lower limit of the projected interval (6.0 to 7.5 percentage points). Administrative adjustments to regulated prices were responsible for 6.87 percentage points of the total increase in consumer prices and food prices (excluding non-alcoholic beverages) for 1.26 percentage points. Despite a faster rate of increase than in 1998, food prices remained a factor with a stabilising effect on the development of consumer prices in 1999.

Net Inflation

Over the course of the year, the value of net inflation followed an upward trend and culminated at the end of the third quarter. It rose from 3.44 percentage points in January to 6.21 percentage points in September. After that period, the level of net inflation fell slightly. By the end of the year, however, it had almost doubled in comparison with the previous year. During 1999, the rate of net inflation was influenced significantly by cost factors, while domestic demand remained low and acted as a brake on the price increase.

The most significant external factor that affected the dynamics of consumer prices was the marked rise in oil prices on world markets, which was reflected directly in fuel prices. Net inflation was also affected by exchange rate developments during the year. From the beginning of January to May, the exchange rate of the Slovak crown depreciated, and thus affected the rate of increase in the prices of tradable goods. In June, however, the downward trend in the exchange rate changed into a trend of appreciation, which had an anti-inflationary effect and partly offset the effects of other factors. The internal cost factors, which affected the price increase, included the administrative measures of the Government of the SR. Those directly affecting the level of net inflation included the import surcharge and the adjustments to indirect taxes. The adjustments to excise duties on hydrocarbon fuels on two occasions and the rise in oil prices during the year caused the level of fuel prices to increase by 35% in 1999. Adjustments to regulated prices (mainly energy prices) eventually led to an increase in dynamics of prices in the sector of market services.

Food Prices

Food prices (excluding non-alcoholic beverages) recorded a year-on-year increase of 4.8% in 1999. This increase was only slightly higher than the figure a year earlier (4.6%), but the development of food prices followed a different course over the year. During the first two quarters, food prices increased at a slower rate than a year earlier. They rose during this period by only 0.2% (compared with 5.4% during the same period in 1998). On a year-on-year basis, they fell by 0.6 percentage points. The slowdown in the dynamics of food prices during

Development of consumer prices by sector

Increase in consumer prices in % since previous December *(contribution to the 12-month rate of overall inflation in % points)* [1/]	**Const. weight in %**	**December 1998**	**December 1999**	**Change in % points**
TOTAL	**100.0**	**5.6**	**14.2**	**8.6**
Tradable sector	66.9	5.2	7.6	2.4
		(3.45)	*(5.00)*	*(1.55)*
of which:				
Food prices	26.8	4.6	4.8	0.2
		(1.19)	*(1.26)*	*(0.07)*
Prices of other goods	40.2	5.6	9.3	3.7
		(2.26)	*(3.74)*	*(1.48)*
Non-tradable sector	33.1	6.5	27.1	20.6
		(2.17)	*(9.19)*	*(7.02)*
of which:				
Regulated prices	17.8	6.3	38.2	31.9
		(1.13)	*(6.87)*	*(5.74)*
Prices of market services	15.2	6.6	14.6	8.0
		(1.05)	*(2.32)*	*(1.27)*
Net inflation [2/]	**55.4**	**5.9**	**10.8**	**4.9**
		(3.30)	***(6.06)***	***(2.76)***
Non-regulated prices [3/]	82.2	5.5	8.9	3.4
		(4.50)	*(7.31)*	*(2.81)*

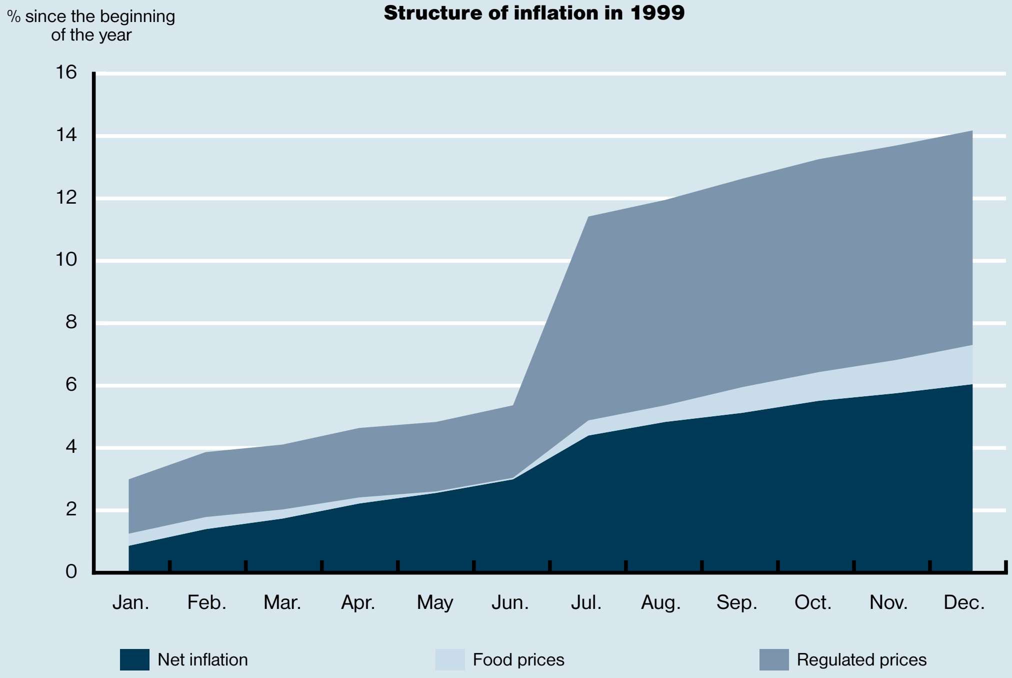
1/ NBS estimates based on data from the Statistical Office of the SR
2/ Other goods and market services
3/ Total excluding regulated prices

the first half of the year, was due to a fall in meat prices and a slight increase in the prices of milk and milk products. A substantial part of the year-on-year increase can, however, be attributed to the change in the lower rate of value added tax from 6% to 10% as of 1 July 1999, so that food prices recorded a month-on-month increase of 1.8%, instead of the characteristic seasonal fall. This administrative measure offset the effects of slower development in food prices during the fist six months of the year. During the following months, their development followed virtually the same course as in previous years. After the effects of changes in value added tax rates had been eliminated, food prices increased year-on-year by only 1.3%. The slow increase in food prices was also affected by the development of producer prices, when the average prices of agricultural products fell by 1.8% in 1999.

Regulated Prices

In accordance with the measures adopted by the Government for the solution to the problems of macroeconomic imbalances and the low competitiveness of the Slovak economy, the process of making adjustments to regulated prices accelerated at the beginning of 1999. The items of the consumer basket, the prices of which were regulated in 1999, recorded a year-on-year increase of 38.2% in December 1999. In comparison with the previous year, when regulated prices made the most significant contribution to the slow rate of increase in consumer prices, they became a factor determining the rise in inflation in 1999. Adjustments to regulated prices were made in two stages (1 January 1999 and 1 July 1999). In January, increases were recorded in the prices of electricity (38.4%); heat energy (21.2%); water supply and sewage disposal (20.0%); and postal services (27.6%). In February, prices were increased in railway (25.6%) and bus transport (21.3%). The persistence of macroeconomic imbalances necessitated further administrative measures in July. Adjustments were again made to the prices of electricity (an increase of 38.8%), heat energy (45.0%), and water (3.8%). In addition, prices were increased in gas supply (53.8%) and telecommunications services (24.0%). As a result of large-scale adjustments, the share of regulated prices in the 12-month

Structure of inflation in 1999



rate of total inflation reached almost 50%. The increase in energy prices during the year not only affected the sectoral inflation of regulated prices, but also generated indirectly a gradual rise in prices in other sectors, especially in market services.

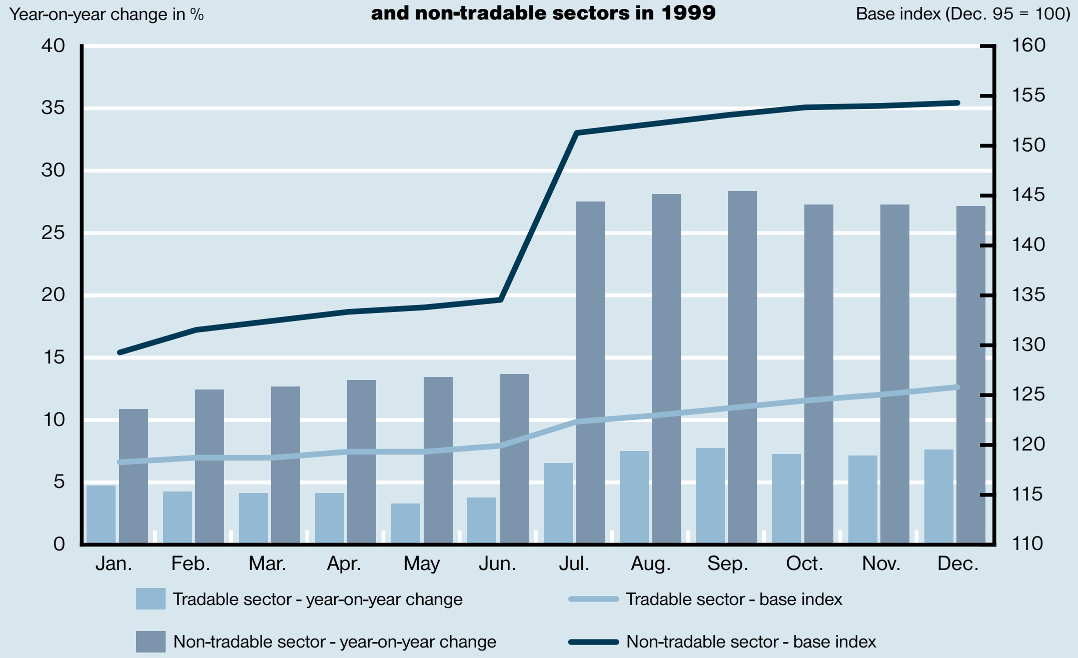
Price Development in the Tradable and Non-Tradable Sectors

According to the structure of the consumer basket by sector, the rate of inflation in the non-tradable sector reached 27.1%, well exceeding the figure for the tradable sector (7.6%). The differences between the sectoral rates of inflation (so-called 'dual inflation') deepened under the influence of large-scale administrative price adjustments. Although the weight of the non-tradable sector in the consumer basket is only 33.1% (in base weights), this sector accounted for nearly 65% of total inflation in 1999.

Prices in the tradable sector increased by 7.6%, which represented an acceleration of 2.4 percentage points in comparison with the increase a year earlier. The rate of year-on-year increase in prices in this sector slowed during the first five months of the year due to a downward trend in food prices. On the other hand, exchange rate development had an upward effect on the prices of other tradable goods, which was reflected in their accelerated dynamics of month-on-month increase in comparison with the previous year. The slowdown in the rate of price increase in the tradable sector came to a halt in June, when the rate of growth in this sector increased after the introduction of the import surcharge and the change in the lower limit for VAT rates. A factor that had a stabilising effect on the level of prices in the tradable sector, was the low demand for goods of non-food nature in particular. This resulted from a fall in real wages during the second half of the year and the subsequent slowdown in the rate of year-on-year growth in receipts from retail sales. Due to the extent of cost factors, the low level of consumer demand did not lead to a fall in prices.

The higher dynamics of inflation in the non-tradable sector was caused by the increased

Development of consumer prices in the tradable and non-tradable sectors in 1999



rates of inflation in both sectors (regulated prices and market services). The year-on-year increase accelerated steeply in the months when the adjustments to regulated prices were made. The steepest increases in the prices of services also took place in these months. The weak competition in the sector of market services allowed companies to transfer the increased costs of their services directly to prices.

Producer Prices

The increase in the prices of fuels (mainly oil), the import surcharge, and the administrative measures of the Government, were the main factors that affected the development of producer prices in 1999. They caused the dynamics of increase in industrial producer prices and price of construction work to accelerate. A slowdown in the dynamics of increase was recorded in the prices of building materials, while the prices of agricultural products showed a sharper year-on-year fall than in 1998.

Though commodity prices (mainly oil) followed a favourable trend on world markets in 1998, oil prices rose steeply throughout the world in 1999, as a result of the restriction on oil supplies. The continued rise in oil prices, coupled with measures taken by the Government to increase excise duties and adjustments to the regulated prices of electrical and heat energy, were the main factors that accelerated the rate of increase in industrial producer prices, particularly during the second half of the year. The rise in oil prices was mirrored in the costs of producers and subsequently in output prices, particularly in manufacturing sectors with a large share of oil refinery products (coke production and oil refining). Of the other sectors in manufacturing, marked year-on-year increases were recorded in the prices of transport equipment (9.1%) and other industrial products (9.7%). Outside the manufacturing industry, a year-on-year increase was recorded in the prices of electricity, gas, hot water and steam (6.0%). The increase took place mainly in the second half of the year due to an increase in the maximum price of electrical energy for entrepreneurs. The prices of basic metals and finished metal products, which have the largest weight in the structure of industrial producer prices, remained below the level of last year (after a fall of 0.6%) and thereby acted as a brake on the rise in industrial producer prices.

In the long term, the highest level and dynamics among producer prices were propped up by the price of construction work, which increased year-on-year by an average of 11.0%. The producer prices of materials and products used in construction rose by only 1.8%, which represented a marked slowdown in the rate of year-on-year increase (5.5 points).

On average, the prices of agricultural products were 1.8% lower than in 1998. This was due to a fall in prices in both animal and plant production. The excess of supply over demand persisted throughout the year, mainly on the grain market, which led to a fall of 4.9% in prices (cereals including corn). Marked price fluctuations during the year were recorded in the prices of potatoes and fruit.

Development of consumer and producer prices

Average annual price index same period of last year = 100	1995	1996	1997	1998	1999
Consumer prices	109.9	105.8	106.1	106.7	110.6
Industrial producer prices	109.0	104.1	104.5	103.3	103.8
Prices of construction work	112.0	115.0	109.7	108.9	111.0
Building material prices	112.2	107.4	107.6	107.3	101.8
Prices of agricultural products	103.3	105.4	105.6	99.7	98.2
GDP deflator	109.7	104.5	106.6	105.1	106.6

The prices of animal products fell by 1.2%, due primarily to a fall in the prices of animals for slaughter (excluding poultry), especially pigs for slaughter, as a consequence of pork imports. The average prices of poultry and eggs also fell in 1999.

GDP Deflator

The development of the GDP deflator was affected by the accelerated dynamics of consumer and producer prices. The deflator increased by 6.6% (in 1998 by 5.1%) on a year-on-year basis. The most significant increases were recorded in the deflator of final household consumption (9.3%) and the formation of gross fixed capital (7.6%).

1.2. Gross Domestic Product

In 1999, gross domestic product was influenced by two major factors, the first of which was the effect of unbalanced economic development in previous years and the second was represented by the measures adopted by the Government for the elimination of macroeconomic imbalances and the stabilisation of the economy. The effects of the above factors led to a slowdown in the pace of economic growth and to changes in its structure. The slowdown in GDP creation was due primarily to a deceleration in the rate of growth in added value in market services and a sharp decline in the creation of added value in construction. With regard to the utilisation of GDP, the slowdown in GDP growth was due mainly to a fall in domestic demand, caused by a pronounced decline in gross fixed capital formation.

On the one hand, the gradual stabilisation of the economy resulted in a slowdown in the rates of growth in aggregate demand and aggregate supply, and on the other hand it led to a reduction in the deficit of trade and to a more balanced relationship between domestic demand and domestic supply. The relationship between the individual components of GDP was improved mainly by restricting domestic demand, which subsequently affected the level of domestic as well as foreign supply. The fall in domestic demand caused its share in aggregate demand to decrease to 58.8%. The share of domestic supply (created by GDP) in aggregate supply reached 58.5% and was 1.1 percentage points higher than in the previous year.

Aggregate Supply

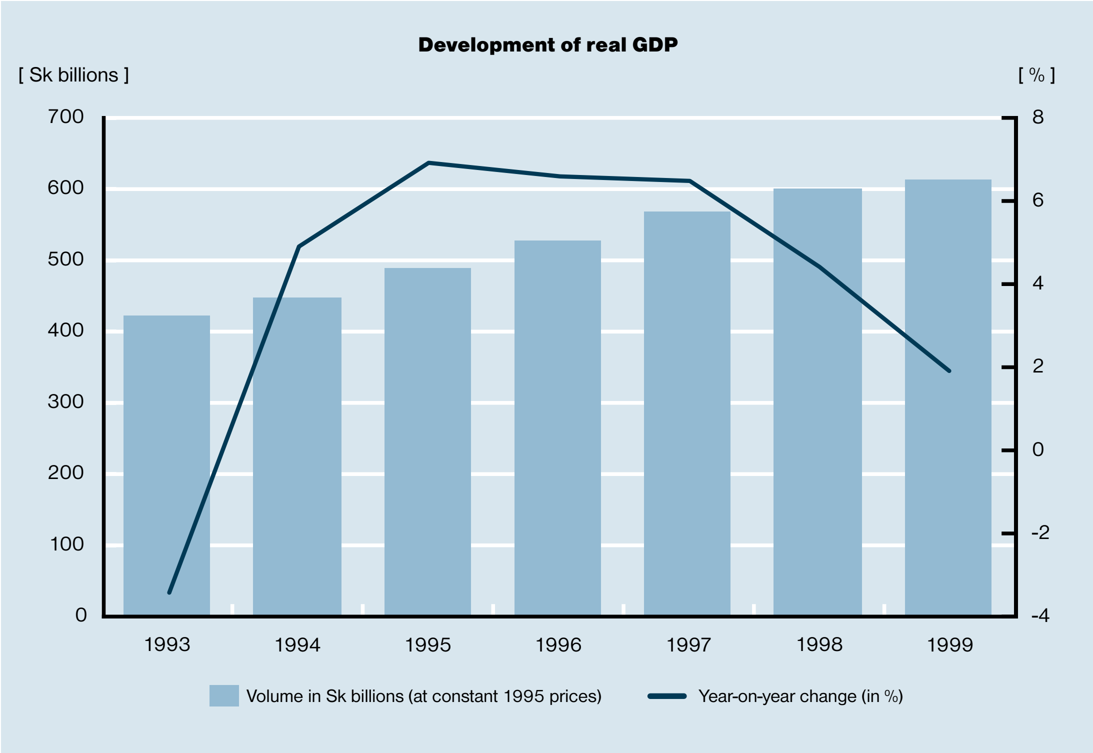
Substantial influence on GDP creation was exerted by the added value, which increased in real terms by 2.1% in 1999, while gross production fell by 1.0% and intermediary consumption by 2.9%.

The data in the table indicate that the appreciation of material, labour, and capital inputs in the production of goods and services improved in 1999. This is documented by the

Development of aggregate demand and supply

	Sk billions 1/			Share in %		
	1997	1998	1999	1997	1998	1999
Aggregate supply	1,002.2	1,067.8	1,068.3	100.0	100.0	100.0
Domestic supply (GDP)	586.8	612.7	624.5	58.6	57.4	58.5
Foreign supply (imports of goods and services)	415.4	455.1	443.8	41.4	42.6	41.5
Aggregate demand	1,002.2	1,067.8	1,068.3	100.0	100.0	100.0
Domestic demand	631.2	656.9	628.6	63.0	61.5	58.8
Foreign demand (exports of goods and services)	371.0	410.9	439.7	37.0	38.5	41.2

1/ Constant 1995 prices



share of intermediary consumption in gross production, which reached 60.4% at constant prices (compared with 61.6% in 1998). The largest share of intermediary consumption in gross output was recorded in the sectors of market products (agriculture, industry, construction), which can be attributed to the modest number of sophisticated products in industrial production.

The creation of added value by sector underwent numerous changes in 1999, due to the development of domestic as well as foreign demand. A significantly accelerated increase in added value was recorded only in industry, due mainly to a dynamic growth in electricity, gas, and water supply, and in mining and quarrying. Agriculture also recorded an increase in the creation of added value. In market services, added value increased at a slower rate than in 1998, due to slower growth in GDP. The sharpest fall in added value took place in the construction sector (30.4%) as a result of a marked decline in demand for construction work. The creation of added value also fell behind in non-market services.

Agriculture

Agriculture contributed 88.9% to the creation of added value in the sector of agriculture and fishery. In 1999, added value was created in

Creation of gross domestic product (Sk billions, constant 1995 prices)

	1997	1998	1999	Index 1998/97	Index 1999/98
Gross output	1,458.9	1,511.5	1,496.2	103.6	99.0
Intermediate consumption	904.8	931.4	904.1	102.9	97.1
Added value	554.1	580.1	592.1	104.7	102.1
Other 1/	32.7	32.6	32.4	99.9	99.3
GDP	586.8	612.7	624.5	104.4	101.9

1/ Value added tax, tax on imports, imputed production of banking services

Breakdown of gross domestic product by sector (Sk billions, const. 1995 prices)

	1997	1998	1999	Index 1998/97	Index 1999/98
GDP	586.8	612.7	624.5	104.4	101.9
Agriculture	28.8	28.5	30.4	99.1	106.6
Industry	171.0	172.5	186.1	100.9	107.9
of which: Manufacturing	143.1	149.9	153.5	104.8	102.4
Construction	27.3	25.3	17.6	92.6	69.6
Market services	252.4	275.6	280.8	109.2	101.9
of which: Trade	126.7	133.5	133.1	105.4	99.6
Transport	33.8	36.6	35.9	108.4	98.0
Non-market services	74.6	78.2	77.0	104.8	98.5
Other 1/	32.7	32.6	32.4	99.9	99.3

1/ Value added tax, tax on imports, imputed production of banking services

agriculture in the amount of Sk 27.1 billion, representing a year-on-year increase of 5.1% at constant prices. The share of agriculture in the creation of GDP remained virtually unchanged (4.3%).

Proceeds from the sale of agricultural products increased at constant prices by 2.0%. This was due primarily to an increase of 11.8% in proceeds from plant produce. Proceeds from the sale of animal products fell by 2.5% compared with the figure for the previous year. In terms of volume, sales of oil-seed crops increased by 58.2%. Sales of other commodities recorded only a slight increase, while the sale of potatoes fell year-on-year by 16.1%.

Crops of cereals (except maize), oil-plants, and vegetables recorded a marked year-on-year decline in 1999. The sharpest fall took place in the production of wheat, barley, and potatoes. The decline in crops was due to the use of smaller crop areas, the extremely wet weather, floods, saturation of the soil at sowing-time, the reduced quality of seeds, and to the limited use of industrial fertilisers and chemical protection. A year-on-year decline was also recorded in the production and sale of all types of animal products, with the exception of poultry. However, the decline in animal production recorded a certain slowdown in 1999, compared with the previous year.

According to preliminary data, the agricultural sector suffered a loss of roughly Sk 2 billion in 1999, with more than 40% of the agricultural organisations ending the year with a loss. On a year-on-year basis, the financial performance of the sector deteriorated by more than Sk 650 million. The persistently unfavourable economic position of agricultural companies was due to several factors. One of these factors was the increased cost of sowing resulting from the extremely unfavourable weather conditions. Over the last ten years, the budgetary performance of agricultural companies has been negatively affected by the continued ‘opening of the gap’ between input and output prices to the detriment of the sector, which drains, according to the estimates of the Ministry of Agriculture, Sk 1.3 to 1.5 billion from the sector every year. In comparison with 1998, the prices of agricultural products fell by an average of 1.8%, while input prices continued to rise.

The unfavourable weather conditions and the lack of financial resources led to lower output in all important plants and continued decrease in the number of farm animals, which negatively effected the proceeds and financial results of companies.

The balance of foreign trade in agricultural products used for food processing resulted in a deficit of Sk 15.2 billion, which was roughly at the level of the previous year. Of this volume, the so-called essential commodities (according to preliminary data from the Ministry of Industry of the SR) accounted for 41%, i.e. Sk 6.25 billion. The following goods had a considerable share in the imports of essential commodities: dairy products, alcoholic beverages, fruit from the Mediterranean zone, as well as traditional Slovak goods such as cabbage, vegetables, and potatoes. The imports of beef and live pigs significantly exceeded their exports (as in 1998). The best results were recorded in the exports of cheese, oil-plants, and malt.

Industry

Industrial production in 1999, expressed in terms of the index of industrial production, was 3.4% lower than in 1998. The development of this index was most affected by a marked fall in the first quarter (8.0%), which was gradually eliminated, and the growth in industrial production was restored as early as the 4th quarter (1.0%).

The index of industrial production is based on the statistics of industrial production and is an index of physical volume. Its calculation is based on changes in the volumes of selected products and on a two-stage weight system. The index expresses a change in industrial production in a certain month in relation to the average month of a base year. The base period of the index of industrial production for 1999 is the average month in 1998.

The decline in industrial production during 1999 was due to a fall in output in manufacturing (5.3%), while the output of mining, quarrying, and electricity, gas, and water supply increased. In manufacturing, the sharpest decline was recorded in the manufacture of rubber and plastic products, wood-working, and in the metal-working industry. Production exceeded the level of 1998 only in paper manufacturing industry, including printing and publishing, tanning and leather industry, and in the manufacture of transport equipment. A slight increase in output was also recorded in the processing of foods, beverages, and tobacco.

The situation in industry may also be evaluated on the basis of receipts from industrial activity. Receipts from industrial activity, unlike industrial production, increased during the whole year. In 1999, it grew year-on-year by an average of 4.2%, due primarily to an increase in receipts from the supply of electricity, gas, and water (11.5%). Increased receipts were also recorded in manufacturing (3.8%), due to growth in receipts from the leather industry and the wood-working industry.

Construction

The trend of decline in construction, which started in September 1998, continued in 1999 with a moderate slowdown in the rate of decline at the end of the year. In terms of volume, the output of the construction sector reached only 82% of the figure for the previous year, as a result of a fall in the volume of new construction projects, reconstruction, modernisation, and a downturn in domestic and foreign production. A survey in the construction sector has revealed that the main barriers to growth in production were the difficulty in obtaining bank loans, their high cost, and the low demand for construction work.

The decline in construction output had an unfavourable effect on the development of added value in the sector. The creation of added value in construction has been on the decline since 1997; in 1999, the level of added value fell at constant prices by almost a third on a year-on-year basis. Subsequently, the share of the sector in GDP decreased from 4.1% in 1998 to 2.8% in 1999.

Services

The share of services in GDP creation recorded, for the first time since 1995, a year-on-year decrease (0.5% points). Market services reached an actual year-on-year increase of 1.9% in added value and the volume of added value in non-market services fell year-on-year by 1.5% at constant prices. Despite a slight fall, the largest share in GDP creation was maintained by the retail trade.

Receipts from retail sales increased by 5.4% at constant prices. The rate of growth was 2.8 points slower than in 1998. The slowdown in the dynamics of growth took place during the second half of the year after the introduction of government measures. Marked increases were recorded in proceeds from the sale of motor vehicles, fuels, pharmaceuticals, and cosmetics. The increase in proceeds from the sale of fuels was to a considerable extent influenced by the rise in fuel prices. A year-on-year decrease in receipts (roughly 3%) was recorded in retail trade in foodstuffs, which was due to a fall in real wages and employment. The reduced purchasing power of households was documented by a dynamic year-on-year growth in proceeds from the sale of second-hand goods.

Receipts from hotel services and tourism were 10% higher (at current prices) than in 1998. A marked fall in receipts (almost 20%) was recorded in hotels and restaurants.

Transport organisations reported a year-on-year increase of 8.4% in receipts (at current prices). Receipts from freight transport grew by 7.4% compared with 1998 and represented more than 75% of total income. An increase in receipts was recorded mainly in road freight transport. The downturn in economic performance was reflected in the continued year-on-year decline in the volume of transported goods (by more than 11%). Despite the persistent decrease in the number of passengers (3.5%), income from passenger transport grew by 12.1%, due mainly to an increase in fares.

In postal and telecommunications services, receipts increased by 15.2% (at current prices) in comparison with 1998. More than 85% of total receipts came from telecommunications services. The increase in number of telephone and mobile phones continued (by 9.1% and 34.1% respectively). In postal services, the most dynamic growth was recorded in Express Mail Service and in banking services at the Postal Bank.

Receipts from other market services (at constant prices) remained virtually unchanged in 1999. The most dynamic year-on-year growth in receipts took place in services specialising in the lease of machines, cars, and equipment; software consulting; inspection and security services, and business consulting. In comparison with the previous year, a marked fall was recorded in architects' services, computerised data processing, geological surveying, and other services.

Wages and labour productivity

According to data from the Statistical Office of the SR, the average nominal monthly wage of employees in the Slovak economy reached Sk 10,728 in 1999, representing a year-on-year increase of 7.2%, which was spread evenly over the four quarters.

The dynamics of nominal wages slowed by 2.4 percentage points compared with 1998. Smaller increases were recorded in all sectors of the economy except hotels and restaurants; construction saw a fall in nominal wages. The lowest increases in average nominal wages took place in sectors financed or subsidised from the State budget - health service (0.1%) and education (2.6%). Wages in public administration, defence, and compulsory social insurance increased by 5.2%. In the business

Development of real wages **(index: same period of last year = 100)**

	1997				1998				1999			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Average monthly nominal wage	114.9	114.5	113.2	110.8	110.8	110.4	108.8	108.4	107.2	107.4	107.3	107.3
Average monthly real wage	108.4	107.7	106.8	104.3	103.3	102.8	102.4	102.4	100.3	100.5	94.0	94.1

sector, the lowest increase was recorded in banking and insurance (3.5%).

The level of real wages in the Slovak economy as a whole fell by 3.1% (for the first time since 1993). The fall in real wages in 1999 was caused by a slowdown in the rate of growth in nominal wages coupled with faster increase in average consumer prices, the dynamics of which accelerated year-on-year by 3.9 percentage points.

A positive development was the growth in labour productivity in relation to real GDP. Labour productivity per employee increased year-on-year by 4.2%, while the dynamics of growth slowed by 0.7 percentage points. On the one hand, the development of labour productivity was influenced by the slower dynamics of growth in real GDP, and on the other hand by the accelerated fall in employment (from 0.4% in 1998 to 2.2% in 1999).

The growth in labour productivity, accompanied by a fall in real wages, led to an increase in excess of growth in labour productivity over rise in real wages, from 2.2 percentage points in 1998 to 7.3 percentage points in 1999. This was most apparent in the 4th quarter, when labour productivity increased by 5.4% and real wages fell by 5.9%.

The fall in employment at a time of growth in GDP signified reduction in overemployment. This fact was positively reflected in the improved budgetary performance of organisations and created conditions for an increase in the competitiveness of the Slovak economy. On the other hand, the sharp fall in employment and the inadequate promotion of job creation led to an increase in the rate of unemployment.

Employment and Unemployment

The labour market in the SR was, as in 1998, characterised by a fall in demand for labour. This led to a marked fall in employment and a high rate of unemployment. In 1999, the average number of employees in the Slovak economy was 1,988.2 thousand, i.e. almost 44 thousand (2.2%) less than a year earlier.

The fall in employment culminated in the 4th quarter, when it fell year-on-year by 2.9%, i.e. 58.6 thousand persons (the sharpest fall since the 1st quarter of 1994).

The fall in employment was caused by a decrease in the number of jobs in most sectors. The greatest fall in employment was recorded in agriculture (14.0%) and construction

Development of labour productivity, wages and employment in the national economy

		Index (same period of last year = 100)						
		1993	1994	1995	1996	1997	1998	1999
Labour productivity in GDP per employee	curr. p.	111.7	121.5	114.8	110.5	113.3	110.2	111.0
	con.p.1/	96.3	106.8	104.6	105.7	106.3	104.9	104.2
Average monthly wage per employee	nom.	118.4	117.0	114.3	113.3	113.1	109.6	107.2
	real	96.4	103.2	104.0	107.1	106.6	102.7	96.9
Total number of employees		99.9	98.2	102.2	100.8	100.2	99.6	97.8

1/ Constant prices: average of 1995 = 100

(9.5%). In the key production sectors of the economy (industry, construction, and agriculture), the number of employees decreased by as many as 54.8 thousand. On the other hand, only 17.5 thousand new jobs were created (predominantly in trade, maintenance, and hotel and restaurant services).

The fall in employment was reflected in the rate of unemployment. At the end of December, the absolute number of registered unemployed (according to the National Labour Office) reached 535.2 thousand, i.e. 25% more than in the same period a year earlier. The rate of unemployment, calculated from the disposable number of registered unemployed, stood at 19.2% at the end of 1999.

On average, the number of registered unemployed increased year-on-year by 105.7 thousand in 1999. The steepest increase was recorded in July and August, when the number of unemployed exceeded 500 thousand.

Unemployment rates continued to show big differences by region. The difference between the highest (Rimavská Sobota - 37.4%) and the lowest rate of unemployment (Bratislava IV - 4.2%) was more than 33 percentage points in December. The number of districts with unemployment above 20%, increased from 25 in 1998 to 39 in 1999. In 10 districts, the rate of unemployment exceeded 30%.

Problems with restructuring in the microsphere led to failure to create a sufficient number of new jobs. As a result, the number of vacancies decreased from 11,167 in January to 5,709 in December. Thus, the average number of unemployed per vacancy increased from 41 to 94 in the Slovak economy. However, regions with the highest unemployment rates produced much worse results.

In 1999, the negative development in employment was influenced by the following factors:

- a record fall in employment in connection with the fall in over-employment, the liquidation of ineffective entrepreneurial entities, and the unsatisfactory state of undercapitalised and unconsolidated companies;
- inadequate promotion of job creation;
- demographic development leading to an accelerated increase in the number of economically active persons on the labour market (the 70's generation);
- the applied system of social insurance and unemployment benefits, which fails to motivate people enough to become officially employed, instead of doing 'black work'.

The fall in employment and the steep increase in the number of unemployed were reflected in the expenditures of the National Labour Office.

According to preliminary data from the National Labour Office, expenditure on unemployment benefits for registered unemployed increased year-on-year by 35.9% (to Sk 5.3 billion) and transfers for health, sickness, and pension insurance for job applicants receiving unemployment benefits by 25.0% (to Sk 1.95 billion). On the other hand, expenditure on promoting job creation fell, due to a shortage of resources, by 79.2% (to Sk 0.47 billion) and accounted for only 6.1% of total spending.

In connection with the growth and structure of unemployment, which was dominated by long-term unemployment, a steep increase was also recorded in social benefits and assistance, which increased year-on-year by 39.1% and reached Sk 15.67 billion.

With its size, structure (increase in long-term unemployment among the unskilled), territorial concentration, and effect on the expenditure side of the State budget, unemployment has become a serious economic and social problem in the SR in recent years.

Aggregate Demand

A substantial change in the development of aggregate demand in 1999, was the fact that its growth was due exclusively to the export of goods and services.

Net Exports

In 1999, the export of goods and services was a crucial factor, stimulating the Slovak economy. Its growth (7.0% at constant prices) was connected, among other factors, with the relatively favourable development of foreign demand in the European Union and the Czech Republic, which are among our main trading partners. In the structure of commodity exports, there was a certain shift towards commodities with higher added values – machines, instruments, electrical appliances, sound and video recording equipment, vehicles, aircraft, boats, transport equipment, and mineral products.

The imports of goods and services fell year-on-year by 2.5% at constant prices, due to the slack domestic demand for consumer goods and investments, which was multiplied by the introduction of a surcharge on imports in June 1999. The fall in the volume of exports took place mostly in vehicles, aeroplanes, vessels, transport equipment, base metals and articles of base metals.

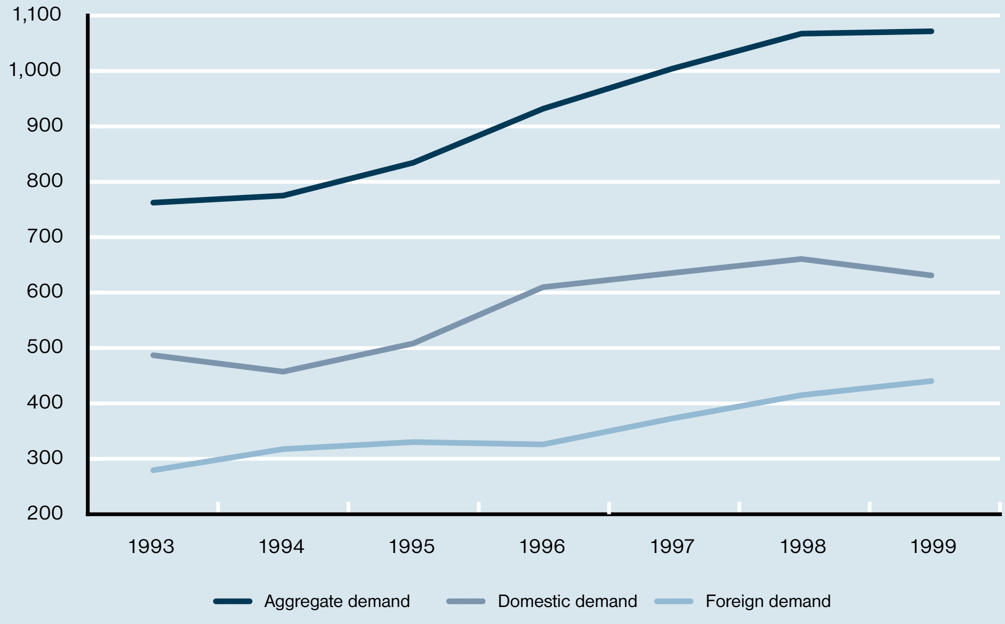
The growth in exports and fall in imports led to a marked reduction in the deficit of trade in goods and services. Compared with the previous year, the size of the deficit diminished by Sk 40.1 billion, to Sk -4.1 billion at constant prices, which represented -0.7% of GDP.

Domestic Demand

After a long period of growth, domestic demand recorded a year-on-year decline of 4.3% at constant prices (for the first time since 1994). It started to fall at the beginning of the year and continued with a sharper downturn during the second half. The structure of

Development of demand during 1993-1999

(Sk billions, at constant 1995 prices)



domestic demand in the individual quarters indicates that its development was affected by several factors. The decline in domestic demand was due mainly to a sharp downturn in gross capital formation, with a steeper fall during the second half of the month. During this period, the final consumption of households also recorded a fall, which caused the rate of annual growth to slow considerably.

The downturn in gross fixed capital formation reached 18.2%. This led to a year-on-year slowdown of 8.1% points in the actual rate of fixed investment, to 32.9%. The rate of gross investment reached 31.2% at constant prices, but was lower than the rate of fixed investment due to a fall in the volume of stocks (Sk 10.6 billion). In relation to the level of domestic savings, the rate of investment achieved may be regarded as sustainable, reducing demands on the financing of investments from savings abroad.

The decline in investment demand was reflected in the volumes of investment in machinery and construction, which fell year-on-year by 11% and 16% respectively. In the category 'machinery and equipment', growth was recorded in the acquisition of transport vehicles, furniture and office equipment, small and other low-value tangible fixed assets. Investment in machines, instruments, and equipment showed an unfavourable tendency, falling in volume by almost 16%.

Structure of GDP in terms of utilisation (Sk billions, const. 1995 prices)

	1997	1998	1999	index 1998/97	index 1999/98
Gross domestic product	586.8	612.7	624.5	104.4	101.9
Domestic demand	631.2	656.9	628.6	104.1	95.7
of which: Final consumption in total	417.2	431.8	433.7	103.5	100.4
Households	287.1	301.3	302.7	104.9	100.5
Non-profit institutions serving households	2.4	2.6	2.7	108.3	103.8
Government	127.7	127.9	128.3	100.2	100.3
Gross capital formation	214.0	225.1	194.9	105.2	86.6
Gross fixed capital formation	226.4	251.2	205.5	111.0	81.8
Change in stocks	-12.4	-26.1	-10.6	-	-
Net exports	-44.4	-44.2	-4.1	-	-
Exports of goods and services	371.0	410.9	439.7	110.8	107.0
Imports of goods and services	415.4	455.1	443.8	109.6	97.5

Development of investments and savings (in %)

	1997	1998	1999
Constant 1995 prices			
Savings rate 1/	28.9	29.5	30.6
Rate of gross investment 2/	36.5	36.7	31.2
Rate of fixed investment 3/	38.6	41.0	32.9
Coverage of investments by savings 4/	79.3	80.4	97.9
Current prices			
Savings rate 1/	28.4	28.2	28.7
Rate of gross investment 2/	38.7	39.4	33.8
Rate of fixed investment 3/	38.6	40.8	33.0
Coverage of investments by savings 4/	73.3	71.7	84.9

1/ Share of gross domestic savings (GDP less final consumption in total) in GDP.
2/ Share of gross capital formation in GDP.
3/ Share of gross fixed capital formation in GDP.
4/ Share of gross domestic savings in gross investments.

With regard to the structure of investments by sector, the sharpest fall was recorded in the investment demand of non-financial organisations, which accounted for 66.1% (70.3% in 1998) of the total volume of investment. In non-financial organisations with 20 or more employees, investment fell in almost all sectors with the exception of manufacturing and trade. Investment in manufacturing increased only slightly (by 1.8%, at current prices), while significant growth was recorded in investment in the manufacture of transport equipment, electrical and optical equipment, other non-metal mineral products, and in the production of rubber and plastic goods.

The downturn in investment by non-financial organisations was linked with the complicated financial situation in the corporate sector and the worsened conditions for obtaining domestic and foreign loans. This fact was reflected mainly in the volume of investment in large companies (with 1,000 or more employees), which fell year-on-year by 29% at current prices, and in medium-sized companies (with 50 to 249 and 250 to 499 employees).

Investment demand in the government sector fell, according to data on investments, by 6.8% at current prices. This was due primarily to the restriction of government spending on infrastructure-related projects, which had been financed from foreign loans in previous years. A slight increase (roughly 3%) was recorded in investments in the financial sector, mainly in investment in buildings and premises. Investment in the household sector grew at the same rate.

The final consumption of government (expenditures on its operation and on public services) increased at constant prices by 0.3%. Due to the relatively small weight of the said increase in total expenditure, the final consumption of government was not a key factor in GDP growth.

Apart from investment demand, the fall in domestic demand reflected a reduction in growth of final household consumption, which reached 0.5% and was 2.9 percentage points lower than in 1998. During 1999, household consumption followed an uneven course of development. During the first half of the year, the level increased by 2.7%, and during the second half, it fell by 1.7%. This development was connected with the level of employment, but mainly with the measures adopted by the Government to bring about economic recovery, which led to a marked fall in real wages during the second half of the year.

The reduced dynamics of nominal wages, accelerated rate of inflation, marked fall in employment, and the record increase in unemployment were reflected in the development and structure of household income and expenditure.

According to preliminary data from the Slovak Statistical Office, the current income of households increased year-on-year by 7.9% and current expenditure by 2.5% in 1999.

In 1999, the rate of year-on-year growth in current income was only 0.2% points faster than a year earlier. However, the dynamics of the basic components of income changed. Only the development of gross operating surplus (mixed income from employment and business including profit in the case of tradesmen) showed a more favourable performance than a year earlier, with a year-on-year increase of 15.7%, compared with a fall of 6.3% in 1998. The other components of income grew at a slower rate than a year earlier.

In absolute terms, the current income of households increased year-on-year by Sk 45 billion (compared with Sk 41 billion in 1998). The structure of the income, however, remained virtually unchanged. While bonuses to employees accounted for almost 58% of the increase in current income in 1998, their share decreased to 25.8% in 1999. On the other hand, the share of gross operating surplus, which reduced the increase in current income by

15,4% in 1998, rose to almost 33% in 1999. The proportion of income from property and business (interest, dividends, income from rented land, etc.) to the increase from current income, decreased from 20.5% to 13.0% In relation to the rise in unemployment, the share of income from unemployment benefits and other social security benefits in the increase in current income, increased from 7.8% in 1998 to 13.1% in 1999.

Current expenditures of households (i.e. not intended for standard consumption, but for payments to other sectors) increased by 2.5% compared with 1998. In contrast with current income, the rate of growth in current expenditure was 10 percentage points slower in 1999 than a year earlier. The slowdown was reflected in all basic components of expenditures. The development was most affected by a slowdown in the rate growth in unrequited current transfers, from 8.3% to 2.5%, and accounted for 88.5% of current expenditures. Payments to employment funds, pension funds, and sickness insurance (almost 70% of unilateral current transfers) paid by employers, employees, and others, recorded a slowdown in the rate of growth from 7.8% to 1.1% (from Sk 7.3 billion in 1998 to Sk 1.0 billion in absolute terms). Similarly, income tax paid by natural persons to the State budget (almost 20% of unrequited current transfers) recorded a slowdown in dynamics from 14.5% to 3.5% (from Sk 3.8 billion to Sk 1.0 billion). The slowdown in the rates of growth in both items was directly connected with the slowdown in the growth in earnings.

Income and expenditure of households (at current prices)

	1997		1998		1999	
	Sk billions	Index: p.y. = 100	Sk billions	Index: p.y. = 100	Sk billions	Index: p.y. = 100
Compensation of employees	302.2	111.5	325.8	107.8	337.4	103.5
of which: Gross wages and salaries	233.2	112.3	252.4	108.2	263.3	104.3
Gross operating surplus	100.6	113.2	94.3	93.7	109.1	115.7
Incomes from property and business	22.9	107.5	31.3	136.9	37.2	118.9
Accident insurance transactions	4.5	100.0	6.7	150.4	7.2	107.5
Unrequited current transfers received	98.3	110.9	111.1	113.1	123.3	110.9
of which: Pensions	52.5	-	58.5	111.4	63.5	108.7
Sickness insurance benefits	22.7	-	24.8	109.1	24.6	99.4
Unemployment benefits	2.8	-	3.9	140.1	5.3	135.9
Other social security benefits	10.5	-	12.6	120.3	17.1	135.7
Social security payments in total	88.5	111.7	99.8	112.7	110.5	110.7
Current income in total	**528.3**	**111.4**	**569.2**	**107.7**	**614.2**	**107.9**
Income from property and business	4.3	78.2	5.0	117.2	4.6	91.2
Accident insurance transactions	6.7	117.5	12.9	191.8	13.9	107.2
Unrequited current transfers paid	132.9	110.7	144.0	108.3	147.6	102.5
of which: Personal income tax to SB	25.6	125.5	29.4	114.5	30.4	103.5
Contributions to funds 1/				107.8	101.3	101.1
Current expenses in total	144.0	109.0	162.0	112.5	166.1	102.5
Gross disposable income	**384.4**	**112.0**	**407.2**	**105.9**	**448.1**	**110.0**
Final household consumption	**322.3**	**112.7**	**360.1**	**111.7**	**395.4**	**109.8**
Gross savings of households	**62.1**	**108.9**	**47.1**	**75.9**	**52.7**	**111.7**
Rate of gross savings 2/	**16.16**	-	**11.57**	-	**11.76**	-

1/ Social contributions paid by employers, employees, self-employed and free-lance persons, non-residents and others.
2/ Gross savings rate = gross savings of households / gross disposable income.
Note: Gross savings of households include (apart from cash, deposits, securities, etc.) expenses for which households purchased investments from own resources, including investments for the development of businesses and for the purchase or construction of family houses.

Financial Reults of Organisations

A positive aspect of economic development in 1999, was the fact that the entrepreneurial sector achieved much better financial results than a year earlier. A marked improvement was recorded in the results of financial organisations, whose profit before tax increased from Sk 8.4 billion in 1998 to Sk 28.7 billion in 1999 and profitability reached 6.8% (compared with 2.3% in 1998). Favourable results were also recorded in non-financial organisations, which earned a total profit of Sk 47.1 billion (before tax), representing a year-on-year increase of Sk 25.5 billion.

The positive results of non-financial organisations were due mainly to an increase in profits in industry (more than 4 times), wholesale trade, retail trade, repair of motor vehicles, motorcycles, and consumer goods, real estate sector, leasing and business services, and research and development. The most serious losses were sustained in transport, warehousing, and postal and telecommunications services. Agriculture also continued to record a loss.

Positive financial results were also achieved in the processing industry, which consequently seased to be a loss-making sector. Organisations in the processing industry earned a total profit of Sk 6.4 billion in 1999, whereas a year earlier they had produced a loss of Sk 5.2 billion. Financial results improved in almost all sectors of the processing industry, except for the manufacture of machinery and equipment, production of coke, refined oil products, and nuclear fuels, and the wood-working industry. The best performers were organisations specialising in the manufacture of transport means - their profits increased almost six times in 1999 compared with the figure for the previous year.

2. BALANCE OF PAYMENTS

2.1. Current Account

In respect of external relations, the year 1999 saw a partial change in the trend set in 1996, which consisted in an abrupt increase in domestic demand, satisfied from imports. After three years, when the current account deficit exceeded 10% of GDP, the rate of growth in domestic demand, and in imports, was successfully reduced following the adoption of economic measures for stabilisation. As a result of an improvement in the imbalance of foreign trade in goods and services, the current account deficit diminished year-on-year by Sk 30.0 billion, i.e. 40%, and its share of GDP decreased by 4.6 percentage points (to 5.8%) compared with the figure for 1998.

In 1999, the balance of payments on current account resulted, according to preliminary statistical data, in a deficit of Sk 44.8 billion, in connection with the unfavourable balance of trade (Sk 45.7 billion). Apart from the trade deficit, another shortfall was recorded in the income balance (Sk 12.5 billion). The balances of services and current transfers remained positive in 1999: they generated together a surplus of Sk 13.4 billion.

In 1999, according to preliminary data from the Statistical Office of the SR, Slovakia exported goods in the total amount of Sk 442.3 billion, i.e. 11.8% more than in 1998. The volume of imports reached Sk 468.0 billion, representing a year-on-year increase of 1.6%. Compared with the same period in 1998, the deficit of trade diminished by Sk 37.2 billion in absolute terms, to Sk 45.7 billion in 1999. With regard to the marked year-on-year depreciation in the crown, the factor of exchange rate development should be remembered when evaluating the performance of foreign trade. The fall in exports expressed in dollar (5.0%) and imports (13.5%) indicates that the improvement in the trade balance was due primarily to a slowdown in the dynamics of imports.

The continued increase in the weight of trade in international business strengthened the orientation of foreign trade towards advanced countries. The share of Slovak exports to the EU in total exports increased to 59.5% and that of imports to 51.7%. In 1999, trade with EU countries underwent a significant year-on-year change, increasing from a deficit of Sk 20.7 billion to a surplus of Sk 9.1 billion. The change was due primarily to an improvement in the balance of trade with Germany, Italy, Austria, and France. Goods that substantially improved the balance included vehicles, clothes, and electrical machines and appliances.

The structure of Slovak exports, i.e. the increasing share of machines and transport means in total exports at the expense of exports intended for intermediary consumption, can be regarded as positive. The exports of machines and transport means increased year-on-year by 18%, i.e. Sk 25.6 billion, while imports grew in volume at a much slower rate in the category 'other commodities'. As a result, the share of goods in Category 7 - 'Machines and Transport Means' increased by 2.1 points, from 37.4% to 39.5%. The increase in the share of demanding markets and commodities with a higher degree of finish in total imports, indicates that export sectors underwent some structural changes. In this, a significant role was played by companies with foreign ownership interest, which provided assistance in increasing the quality of products and in their realisation on foreign markets. Companies with foreign capital participation continue to have potential for accelerating the pace of growth in Slovak exports. Further development of the trade balance will depend on whether joint ventures are joined by other domestic companies or not. The steepest increase was recorded in the category 'road vehicles' (Sk 9.4 billion), as in the previous year. Better results were also recorded in most sub-categories of machines and electrical equipment. Exports of electrical equipment, instruments, and appliances increased in volume by Sk 6.4 billion; machinery and equipment used in industry by Sk 4.3 billion; office equipment by Sk 2.8 billion; machines for specific industries by Sk 1.7 billion, etc.

The revival of export was also reflected in category 8 - 'Industrial Products' (an increase of Sk 6.5 billion), which saw increased exports of clothes and shoes. The increase in the share of this group in total exports may be regarded as another contribution to the change in the structure of Slovak exports, from semi-finished products to goods with a higher added value.

As for imports, the year 1999 saw a visible slowdown in their dynamics, resulting in a year-on-year increase of 1.6%. The gradual decline in imports was due to a slowdown in the rate of growth in domestic demand, mainly for consumer goods and investment, and consequently for imports as well.

In Category 7 - 'Machinery and Transport Equipment', imports fell year-on-year by Sk 9 billion, due mainly to road vehicles and other transport means (railway wagons, aeroplanes, etc.). A slight year-on-year increase in imports was recorded in the category 'machinery and equipment' (0.9%). The share of machinery and mechanical equipment in total imports, remained at the level of 26%.

The year-on-year growth in imports in Category 3 - 'Mineral-Based Fuels' (Sk 10.3 billion) was due to increased imports of crude oil and natural gas, while the decisive role was played by the price of oil. The year-on-year increase in the sub-category 'crude oil, oil products, and related materials' (Sk 11.2 billion) was the result of a price increase, while imports in physical units recorded a slight fall. The given year-on-year comparison is, however, distorted to some extent by the development of oil imports in 1998, which was marked by low oil prices and increased imports in terms of volume. The growth in the import of natural gas (Sk 1.1 billion) was not caused by a price increase, as in the case of oil (the price of gas remained at the level of 1998). The growth in the import of natural gas was fully covered by increased revenues from the transit of gas across the territory of Slovakia.

The introduction of a surcharge on imports, coupled with an increase in regulated prices and tax rates, limited the purchasing power of households. The said measures were also responsible for the slower growth in domestic demand for foreign goods in Category 8 - 'Industrial Products' (books, toys, furniture, sports and travelling requisites, etc.).

In 1999, the balance of trade in services generated a surplus of Sk 6.2 billion, representing a year-on-year increase of Sk 5.5 billion. As in trade in goods, the improvement in the services balance was due primarily to a fall in imports of basic services-balance items. While payments for imports in Slovak crowns fell by 4.7% (in dollar by 18.9%), receipts from exports in crown increased by 2.1% (in dollar they fell by 13.1%).

Transport and foreign tourism, items affecting the positive balance of services, brought foreign exchange in the amount of Sk 18 billion, which represented an increase of Sk 6.1 billion compared with 1998.

In terms of volume, the largest item within transport services was the income from the transit of natural gas and oil from the Russian Federation (RF) to the Czech Republic and Western Europe. The volume of natural gas supplied from the RF in payment for the transit charges reached Sk 17.1 billion and its share in the total volume of gas imports increased to 92.6%. In 1999, transport (excluding the transit of natural gas and oil) resulted in a deficit of Sk 5.9 billion, i.e. Sk 0.5 billion higher than in 1998. In the structure of transport, there was a trend of gradual shift from railway freight service to other forms of transport, mainly road haulage. While railway traffic in 1998 accounted for 43% of the receipts, its share decreased to 36% in 1999. The same situation occurred on the side of payments, where the share of railway transport decreased from 52% to 41%. This change in the structure of transport is not in line with the economic policy of the European Union, which prefers railway transport as ecologically the most favourable form of transport.

Of the individual items of the services balance, the most spectacular improvement took place in tourism, where the balance surplus increased to Sk 5.0 billion, from Sk 0.5 billion in 1998.

The improvement in the area of net receipts from tourism was due primarily to a fall in expenses, when the number of Slovak citizens travelling abroad decreased significantly during the last few months of the year. Slovak citizens spent a total of Sk 14.1 billion on travel abroad, which represented a fall of 16% in Slovak crown and 28.5% in US dollar. Foreign exchange receipts from active tourism followed a different trend, due to a year-on-year change of 17.5% in the exchange rate of the crown against the dollar. When expressed in crowns, receipts increased by 10.7%; while in dollar, they fell by 5.8%. Despite a slight improvement in foreign exchange receipts, their share of GDP remained unchanged (when expressed in crowns), at the level of 2.4%.

Within the individual items of the services balance, the largest deficit was recorded in other services (Sk 11.8 billion, compared with Sk 11.2 billion in 1998), which include the entire spectrum of business and non-business services. Other services represented the only item where exports fell in crown terms as well. Receipts from the export of these services decreased by 4.8% (i.e. Sk 1.8 billion) due to a fall in the export of construction work abroad. In 1999, construction work joined the group of services where payments had exceeded receipts over the last few years. This group included business services (Sk 6 billion); legal, accounting, and consulting services (Sk 2.1 billion); financial services (Sk 1.3 billion); insurance (Sk 0.7 billion); computer engineering (Sk 0.6 billion), licensing (Sk 1.8 billion); and technical services (Sk 1.1 billion), etc., where the range and quality of services are not yet able to compete with services offered abroad. The fall in the export of these services (4.8%) and in import (2.4%) indicates that the part of material production that creates room for the expansion of services, remained unchanged. Experience from advanced countries indicates that the rapidly expanding sector of services supports economic growth and creates conditions for increased employment to a greater extent than other sectors.

Expansive borrowing from abroad in the last few years generated a gradual rise in the level of debt servicing, thereby causing a yearly increase in the income-balance deficit. In 1999, the deficit in the income balance increased year-on-year by Sk 7 billion, to Sk 12.5 billion. Income fell by more than Sk 4 billion, due to a decrease in the reserves of commercial banks, when their foreign exchange assets fell by nearly 60% in 1999. Payments were dominated by interest paid on borrowings from abroad, which reflects the inflow of long and short-term capital and indirectly the rise in the level of debt. Apart from interest payments in the corporate sector, recording an accelerated increase every year, the amount of interest payable on government bonds also increased in 1999. An important role in the increase in the income-balance deficit was played by a change in the exchange rate of the Slovak crown against foreign currencies, which made stronger demands on debt servicing in Slovak crowns (in 1999, the exchange rate of the SKK against USD depreciated by 17.5% and against EUR by 11.4% on a year-on-year basis).

With regard to the individual items of the current account, the most significant contribution to the foreign exchange economy of Slovakia was made by current transfers, which generated a surplus of Sk 7.2 billion. Transfers to the Slovak Republic from abroad were made predominantly as private transfers in the form of legacies, gifts, benefits pensions, etc.

2.2. Capital and Financial Account

The balance of payments on the capital and financial account resulted in a surplus of Sk 76.0 billion, i.e. US$ 1.8 billion.

An economic factor, which is generally regarded as a key indicator of the country's economic development, is foreign direct investment. Compared with other countries, Slovakia receives relatively little foreign investment.

During 1993-1998, foreign capital was, according to the IMF, invested in Poland, Hungary, Czech Republic, Slovakia, and Slovenia in a total amount of US$ 49.3 billion. Of this amount, 47% went to Poland, 28% to Hungary, 19% to the Czech Republic, 4% to Slovakia, and 2% to Slovenia.

The year 1999 saw a net inflow of foreign capital in the form of direct investment in the amount of Sk 28.9 billion, representing a year-on-year increase of 78.2%. Of this amount, Sk 15.6 billion came from the sale of the NBS's share in ČSOB, a.s. Prague, in the amount of Sk 17.1 billion, which caused a fall in the level of equity capital abroad. The sale of the above share, which had been held by the NBS since 1993 and which represented roughly 24% of ČSOB's total capital, took place in December 1999. Owing to the poor financial situation in the corporate sector, Slovak investors showed virtually no interest in investment abroad. The capital interests of Slovak investors abroad increase in volume by Sk 0.7 billion, mainly in industry, banking, and insurance.

Direct investment in the SR was low in 1999, despite the proclaimed policy of the Government to stimulate this form of investment. The increased inflow of capital during the last few months (mainly into the car industry) increased the volume of equity capital in banks and enterprises based in Slovakia by Sk 12.4 billion, which represented 82% of the level in 1998. Compared with 1998, the volume of other capital also fell (by 86%) within foreign direct investment (inflow of financial and commercial credits into enterprises with foreign capital participation). In 1999, the inflow of foreign capital to the Slovak economy in the form of direct investment totalled Sk 13.3 billion, which represented 62% of the level in 1998. Despite a reduction of 40% in the current account deficit, the ratio of foreign direct investment in Slovakia to the deficit in the current account increased by only 1 percentage point, to 29.7%, though the generally recognised, relatively safe limit is 50%. At the end of 1999, the net inflow of foreign capital in the form of direct investment reached 64.5% of the current account deficit.

The interest of foreign investors focused on industrial production (49%) and trade and business services (36%). One of the most successful sectors of industry, which attracted capital from abroad, was the manufacture of motor vehicles, which absorbed almost 50% of direct investment in industry. Another successful sector was the production of machines, metal structures and metal goods. Increased investment activity was also recorded in the sector of trade and business services as in previous years, which confirms the persistence of interest in the trade network. A disadvantage of this is that investment in the network of shops has no significant multiplier effect, creates fewer jobs, and fails to attract sophisticated technology.

Portfolio investment reached a level of Sk 26.9 billion, i.e. US$ 624.4 million, in 1999. On the asset side, portfolio investment was affected by the sale of foreign debt securities from the portfolios of commercial banks, in the amount of Sk 9.5 billion. Debt securities are part of the asset portfolios of commercial banks and are used for the financing of foreign exchange needs in the commercial sector.

With regard to portfolio investment, the net inflow of capital into Slovakia in the form of equity capital and debt securities, amounted to Sk 17.4 billion. A substantial part of this amount related to government and central bank bonds, while receipts came primarily from the issue of Eurobonds by the Government on foreign markets and the sale of government bonds issued in Slovak currency. On the other hand, payments included redemption of NBS bonds issued in 1993.

The increase of capital inflow in the form of portfolio investment in 1999 was to a great extent affected by the acquisition of funds for the needs of the Government. Slovak companies, in general, were slow to take advantage of the opportunity of obtaining foreign capital through the capital market: portfolio investment by the corporate sector increased by Sk 3.4 billion. This amount was made up of increases in the capital participation of foreign investors in the SR (up to 10%) and of the sale of bonds and bills of exchange in Slovak crown to foreign investors (to roughly the same extent).

In 1999, the Government and the NBS borrowed funds in two ways. The first was through an issue of Eurobonds (Sk 22.6 billion) and was recorded in the balance of payments under portfolio investment. The second was a loan from the European Investment Bank and a loan for the State Road Fund in the total amount of Sk 8.3 billion - recorded as other long-term investments. The net inflow of long-term funds (drawing less repayment) into the government sector (including the NBS) reached Sk 14.5 billion.

Concerning other long-term capital, the sharpest decline took place in the net inflow of funds into the corporate sector (financial and commercial credits). With drawings amounting to Sk 38.0 billion and repayments totalling Sk 24.4 billion, the volume of net inflow reached Sk 13.6 billion, which represented 51% of the level in 1998.

The increased drawing of long-term financial credits in the corporate sector during the last quarter, caused inflow in 1999 (Sk 35.4 billion) to reach the level of 1998. The structure of inflow by sector was again dominated by the production and distribution of electricity, gas, and water (35%) and by transport and telecommunications (30%). In industry, the inflow of financial capital into coke production, oil refining, and metal working continued to increase in 1999. A substantial increase was recorded in the repayment of financial loans in the amount of Sk 20.8 billion, representing almost a twofold increase compared with 1998.

The increased drawing of long-term financial credits, which started in 1995, makes ever greater demands on debt servicing every year. In 1999, the situation was complicated by the exchange rate risk arising from fluctuations in USD and DEM and from fluctuations in the exchange rate of the Sk against foreign currencies, which increased the costs of these credits to a significant extent. The change in the exchange rate of the Slovak crown against the US dollar and the euro substantially increased loan repayments in Sk. The volume of loan repayments reached Sk 20.8 billion, which represented a year-on-year increase of 75.4%.

Short-term capital, which showed marked volatility during the year, resulted in a surplus of Sk 3.9 billion in 1999. In the structure of short-term capital, the most significant change was recorded in the short-term capital of commercial banks.

In view of the revocation of the NBS decree regulating the foreign exchange positions of banks and branches of foreign banks for monetary purposes, commercial banks reduced their short-term claims during February to May, by deducting the artificially increased volume of foreign exchange in an amount of more than Sk 80 billion. These operations were reflected on both the liability side (reduction in liabilities) and the asset side (fall in the reserves of commercial banks). While short-term liabilities remained virtually unchanged during the following months, the fall in short-term assets began to slow step-by-step as the inflow of corporate capital increased. The increased deficit in the current account in December and the sale of foreign exchange to the NBS caused another fall in the short-term assets of commercial banks abroad. From January to December 1999, short-term assets declined by Sk 73 billion, while short-term liabilities fell by Sk 70 billion. Short-term capital in the corporate sector reached Sk 0.9 billion, due to growth in both export claims (Sk 7.1 billion) and import liabilities (Sk 8.0 billion).

2.3. Development of Foreign Exchange Reserves

At the end of 1999, the foreign exchange reserves of the NBS reached US$ 3,425.2 million, representing an increase of US$ 501.9 million compared with the figure for the end of December 1998. Over the course of the year, the total foreign exchange reserves of the NBS were influenced by numerous factors. A key factor that positively influenced revenues was government borrowing from foreign financial institutions and proceeds from the sale of ČSOB shares from the portfolio of the NBS. The expenditure side was determined by debt service payments effected by the Government and the NBS. During the year under review, the level of foreign exchange reserves was also affected by the development of cross rates between fully convertible currencies on world financial markets. The positive balance of revenues and expenditures (US$ 713.6 million) was partly offset by negative exchange rate differentials (US$ -211.7 million), which resulted from the weakening of other fully convertible currencies (especially the euro) against the US dollar on international financial markets.

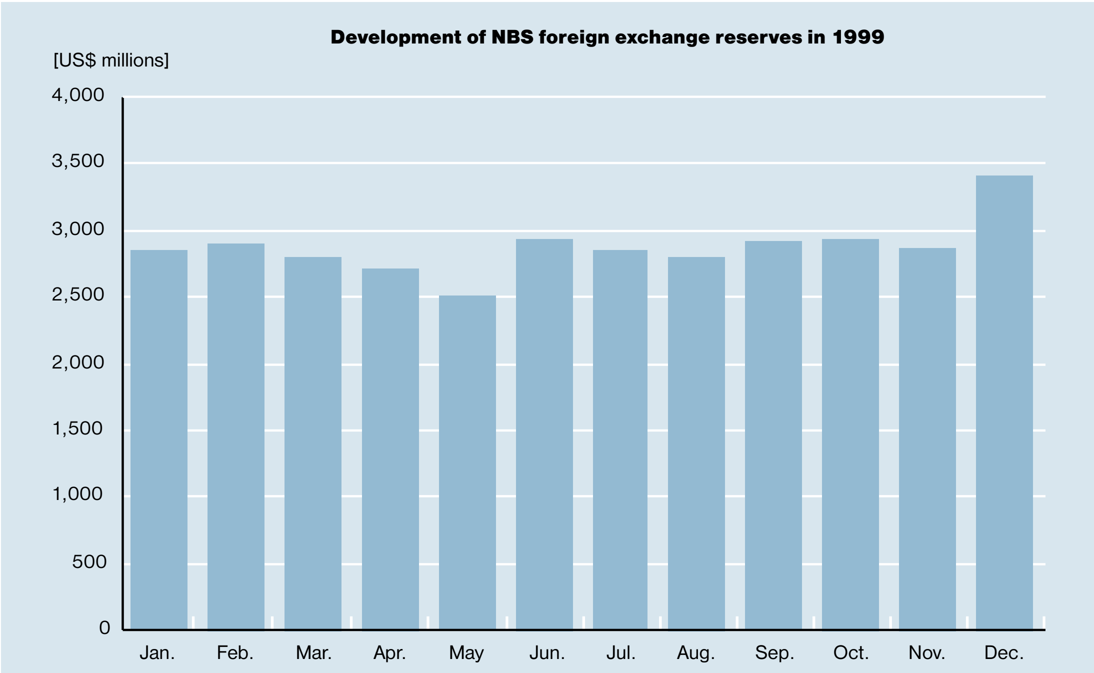
The revenue side of foreign exchange reserves was determined by the following factors:
- the drawing of government loans from foreign financial institutions in the amount of US$ 700.2 million (47% of the total revenue);
- proceeds from the sale of ČSOB shares held by the NBS, in the amount of US$ 407.0 million;

- income from deposits and securities in the amount of US$ 125.1 million;
- positive balance of central bank interventions in the interbank foreign exchange market, amounting to US$ 114.7 million;
- central bank borrowings from the European Investment Bank in the amount of US$ 17.0 million;
- other receipts of the NBS in the amount of US$ 110.8 million.

The expenditure side of foreign exchange reserves was affected by:
- debt service payments by the NBS in the amount of US$ 328.5 million (43% of total expenditure), with repayments of principal on bond issues by the NBS amounting to Sk 207.3 million;
- debt service payments by the Government in the amount of US$ 220.4 million, of which US$ 75.2 million was used for the repayment of interest on Eurobonds issued by the Government in 1998;
- other expenditures of the NBS totalling US$ 212.3 million, incurred mostly in connection with the realisation of cross-border payments for NBS clients (US$ 166.7 million).

At the end of 1999, the foreign exchange reserves of the NBS covered 3.1 times the volume of average monthly imports of goods and services to Slovakia in 1999, which represented an increase in coverage by nearly a whole month (0.8) in comparison with the previous year. The increase was due partly to a rise in the level of foreign exchange reserves during the year, and partly (roughly to the same extent) to a decline in the volume of average monthly imports of goods and services (13.8% in US$) compared with the previous year.

The foreign exchange reserves of commercial banks may be defined as short-term foreign exchange assets of commercial banks vis-à-vis non-residents. At the end of 1998, the volume of such assets stood at US$ 3,034.5 million. On 31 December 1999, commercial banks held foreign exchange reserves in the total amount of US$ 962.2 million, representing a year-on-year decline of US$ 2,072.3 million. The total volume of foreign exchange reserves in the banking sector including the NBS, stood at US$ 5,957.8 million at the beginning of January, and at US$ 4,387.4 million at the end of December.



2.4. External Debt of the Slovak Republic

At 31 December 1999, the total gross external debt of the Slovak Republic amounted to US$ 10.518 billion. At the same date, the official debt of the Government and the NBS stood at US$ 2.547 billion. The level of debt in the commercial sector, i.e. commercial banks and entrepreneurial entities (including foreign debt liabilities towards non-residents), reached US$ 7.699 billion at the end of December. The indebtedness of municipalities (bonds issued by the municipality of Bratislava) amounted to US$ 64 million and the level of debt owed by government agencies stood at US$ 208 million.

With regard to the structure of Slovakia's gross external debt, total gross medium and long-term foreign liabilities accounted for US$ 7.812 billion. At the end of December, the volume of short-term liabilities totalled US$ 2.706 billion. The share of the total gross external debt per capita reached US$ 1,952. The proportion of total short-term debt to the country's total gross external debt came to 25.73%.

The marked fall in the level of short-term foreign debt owed by commercial banks was affected by the cancellation of the foreign exchange positions of domestic banks and branches of foreign banks for monetary purposes.

The net external debt of the SR - expressed as the difference between gross foreign debt, i.e. US$ 10.5 billion (liabilities of the Government and the NBS, liabilities of commercial banks and the corporate sector – except investment), and foreign assets, i.e. US$ 6.1 billion (foreign exchange reserves of the NBS, foreign assets of commercial banks and the corporate sector – except investment), reached US$ 4.4 billion at 31 December 1999. At the beginning of 1999, the volume of net external debt stood at US$ 4.2 billion, so it increased by only US$ 0.2 billion over the course of the year, while the highest increase in net external debt was recorded in the corporate sector (US$ 0.3 billion).

2.5. Licensing Activity of the NBS

In 1999, the National Bank of Slovakia, acting as a foreign exchange authority in accordance with the relevant provisions of the Foreign Exchange Act, issued:
- foreign exchange permits: 337 permits and 74 supplements;
- foreign exchange licences: 93 licences and 19 supplements.

Foreign Exchange Permits

Investment abroad

In 1999, the NBS issued 40 foreign exchange permits and 1 supplement, of which 37 permits

Foreign liabilities in the commercial sector (US$ millions)

	31.12.1997	31.12.1998	31.12.1999
Foreign liabilities in the commercial sector in total	8,021.5	9,391.3	7,698.4
Commercial banks	2,905.5	2,665.6	680.4
Entrepreneurial entities	5,116.0	6,725.7	7,018.0
Medium and long-term foreign liabilities in total	3,917.4	4,786.7	4,998.3
Commercial banks	680.2	602.4	345.4
Entrepreneurial entities	3,237.2	4,184.3	4,652.9
Short-term liabilities in total	4,104.1	4,604.6	2,700.1
Commercial banks	2,225.3	2,063.2	335.0
Entrepreneurial entities	1,878.8	2,541.4	2,365.1

Structure of investment by country

Country	Number of licences and supplements	Investments (in Sk millions)
Ukraine	15	249.1
Czech Republic	2	135.0
Bulgaria	3	25.4
Uzbekistan	1	9.9
Rumania	3	8.9
Cyprus	5	7.0
Russian Federation	6	6.7
People's Republic of China	1	5.1
Croatia	3	1.1
Byelorussia	1	0.8
Slovenia	1	0.2
Total	41	449.2

Note: Direct investment in OECD countries has been liberalised.

and 1 supplement were for direct investment abroad (except OECD countries) in the amount of Sk 314.0 million and 3 permits for portfolio investment in the amount of Sk 135.2 million.

Of the total number of permits issued for investment abroad, 35 foreign exchange permits and 1 supplement were for investment in the form of cash deposits in the amount of Sk 64.7 million, and 5 permits for investment in securities (shares) in the amount of Sk 384.5 million.

Acceptance of financial credits from abroad

In 1999, the NBS granted 97 foreign exchange permits and 13 supplements relating to borrowing from abroad, of which 60 permits were for the acceptance of financial credits totalling Sk 9,639.9 million and 35 permits for the repayment of credits received in the amount of Sk 874.6 million. Two foreign exchange permits remained unused. At the same time, exceptions to the transfer requirement were allowed in 3 cases in the total amount of Sk 209.0 million.

With regard to structure by term, credits with a maturity of up to one year represented 80.0% (Sk 7,712.8 million), up to two years 19.8% (Sk 1,905.1 million), and those maturing in up to three years accounted for 0.2% (Sk 22.0 million).

Of the total number of loans approved, 30 were provided by non-bank entities (Sk 1,370.0 million) and 30 by foreign banks (Sk 8,269.9 million). A total of 25 loans (Sk 925.8 million) were backed by bank guarantees and 3 loans (Sk 4,706.0 million) by government guarantees.

The largest volumes of loans (including international loans) were provided by entities based in the Czech Republic (Sk 2,834.1 million); Great Britain (Sk 2,274.0 million); Cyprus (Sk 1,740.6 million); Germany (Sk 726.1 million); the Netherlands (Sk 655.7 million); Austria (Sk 646.1 million); and in France (Sk 604.1 million).

The majority of loans (97.3%, i.e. Sk 9,382.8 million) was provided for the coverage of operating expenses, the remaining amount (2.7%, i.e. Sk 257.1 million) was earmarked for the financing of investments.

Estimated drawing and repayment of loans approved in 1999, with a maturity of up to 3 years (Sk millions)

	1999	2000	2001
Drawing	9,012.8	627.1	0.0
Repayment	1,200.8	8,034.8	404.3
Balance	7,812.0	-7,407.7	-404.3

Structure of credits by sector

Sector	Number of licenc.	Vol. in Sk millions
Transport, tourism, telecommun.	3	4,706.0
Industrial production	29	3,979.5
Trade, public catering, hotel services	18	715.8
Building and construction	4	78.6
Other	6	160.0
Total	60	9,639.9

The acceptance of loans with a maturity of three or more years and credits from OECD countries for the purchase of goods and services from abroad, has been liberalised.

Covering the obligations of non-residents by residents

To secure the obligations of subsidiary or dealer companies abroad, the NBS issued 44 foreign exchange permits and 2 supplements to domestic entities, in the total amount of Sk 8,959.8 million.

Provision of financial credits to non-residents

In 1999, 4 foreign exchange permits were issued for the provision of financial credits abroad, in the amount of Sk 62.6 million.

The granting of loans to OECD countries with a maturity of five or more years and loans to OECD countries for payments for exported goods and services, have been liberalised.

Trading in foreign securities

For the sale and purchase of foreign securities, the NBS issued 25 foreign exchange permits totalling Sk 27.2 million. Of this amount, 4 foreign exchange permits were for the sale of foreign securities, in the amount of Sk 8.4 million; 20 permits for the purchase of securities in the amount of Sk 18.8 million; and 1 permit for the sale and purchase of foreign securities.

Two foreign exchange permits were issued for the acceptance of foreign securities as payment for financial liabilities via-à-vis abroad, and 4 permits and 1 supplement for the placement of foreign securities on the domestic market.

The purchase and sale of foreign securities and government bonds issued in OECD countries, have been liberalised.

Trading in foreign exchange assets

One foreign exchange permit was issued for trading in foreign exchange assets - sale of assets (gold coins) in foreign currency.

Trading in financial derivatives

The NBS issued 60 foreign exchange permits and 28 supplements for the conclusion of option contracts for the purchase of foreign securities (employee shares), and 1 permit and 2 supplements for trading in financial derivatives, in connection with the repayment of loans received in foreign currency.

Opening foreign-currency accounts at foreign banks

The NBS issued 51 foreign exchange permits and 26 supplements for the purpose of covering necessary expenses incurred in connection with construction, assembly, or repair work abroad, in a total amount of Sk 1,638.7 million (estimated in the contracts). One foreign exchange permit and one supplement were issued for securing operations conducted in connection with trade in financial derivatives. In addition, the NBS issued

4 foreign exchange permits for the opening of foreign-currency accounts at foreign banks in connection with the acceptance of loans from non-residents; 2 permits for the purchase and sale of foreign securities; and 1 permit exempting the holder from the transfer requirement in connection with the purchase of securities.

Foreign Exchange Licences

The NBS issued 85 foreign exchange licences and 19 supplements for trading in foreign currencies and traveller's cheques (non-bank exchange offices); 6 licences for transactions in foreign securities; and 2 licences for trading in financial derivatives.

3. THE PUBLIC SECTOR

Budgetary Performance

Since the draft budget for 1999 had not been submitted to the National Council of the Slovak Republic by 31 December 1998, the budgetary performance of the State was managed according to a provisional budget during the first quarter of 1999. According to regulations governing budgetary relations at the time of a provisional budget, the ceiling on government spending was Sk 46 billion, but actual budget expenditure was expected only in the amount of Sk 44.7 billion. With revenue projected in the amount of Sk 42 billion, the budget deficit was expected to reach Sk 2.7 billion at 31 March 1999.

At the end of March, the provisional budget resulted in a surplus of Sk 1.0 billion, with revenue totalling Sk 40.9 billion and expenditure Sk 39.9 billion, so that, in effect, the principles and limits laid down in the regulations governing the budgetary performance of the State at the time of a provisional budget were complied with during the 1st quarter of 1999.

Act No. 63/1999 Z.z. on the State Budget for 1999 was passed on 26 March, with effect from 1 April 1999. In the new budget, total revenue was set at Sk 179.9 billion, total expenditure at Sk 194.9 billion, and the size of the deficit at Sk 15.0 billion.

Since budget revenues lagged behind as early as the second quarter and as a result of their non-fulfilment the budget deficit increased to Sk 8.7 billion at the end of May, it was evident that without the adoption of effective economic measures by the Government, the budget deficit would have well exceeded the budgeted figure. The realisation of government objectives with a view to stabilising the economy proved too slow and the problems in the economic area continued to deepen. As a result, the Government approved, on 31 May, a strategy for the acceleration of reforms aimed at achieving key macroeconomic goals in 1999, which comprised savings in the social area, cuts in spending in public administration, and measures for the restoration of financial discipline, reduction in expenses and mobilisation of public finance revenues.

The economic measures included the reintroduction of the 7% import surcharge with effect from 1 June 1999; an increase in indirect tax rates with effect from 1 July 1999; taxes on hydrocarbon fuels and lubricants; excise duties on tobacco and tobacco goods; and an increase in the lower rate of value added tax (from 6 to 10%). This step proved effective and the decline in revenues gradually diminished.

At the end of 1999, actual budget revenue reached Sk 216.7 billion, expenditure Sk 231.5 billion, and the size of the deficit remained below the budgeted level (Sk 14.8 billion).

The revenue and expenditure sides of the budget were both significantly affected (to the same extent) by the sale of the NBS's stake in

Československá obchodná banka (ČSOB), by extraordinary transfers made by the National Bank of Slovakia in connection with the cancellation of provisions for redistribution loans, which were intended for bank restructuring, and by grants and transfers (Sk 12.6 billion), which were not entered into the accounts and represented a source for the financing of extrabudgetary needs (mainly for infrastructural projects through the State Road Fund). After being adjusted for these effects, budget revenue amounted to Sk 179.9 billion (budget fulfilment to 100%) and expenditure totalled Sk 194.7 billion (fulfilment to 99.9%).

The most significant contribution to the growth in budget revenues was made by the import surcharge, which was not taken into account in the original budget, and increased revenues by Sk 8.4 billion. The volume of value-added tax revenue reached Sk 58.9 billion (Sk 3.7 billion more than in 1998), exceeding the budgeted figure by almost Sk 1 billion. Revenue from excise duties (Sk 25.2 billion) also exceeded the budgeted figure by Sk 1 billion. In excise-duty collection, the year 1999 proved successful: revenue was Sk 2.1 billion higher than in 1998.

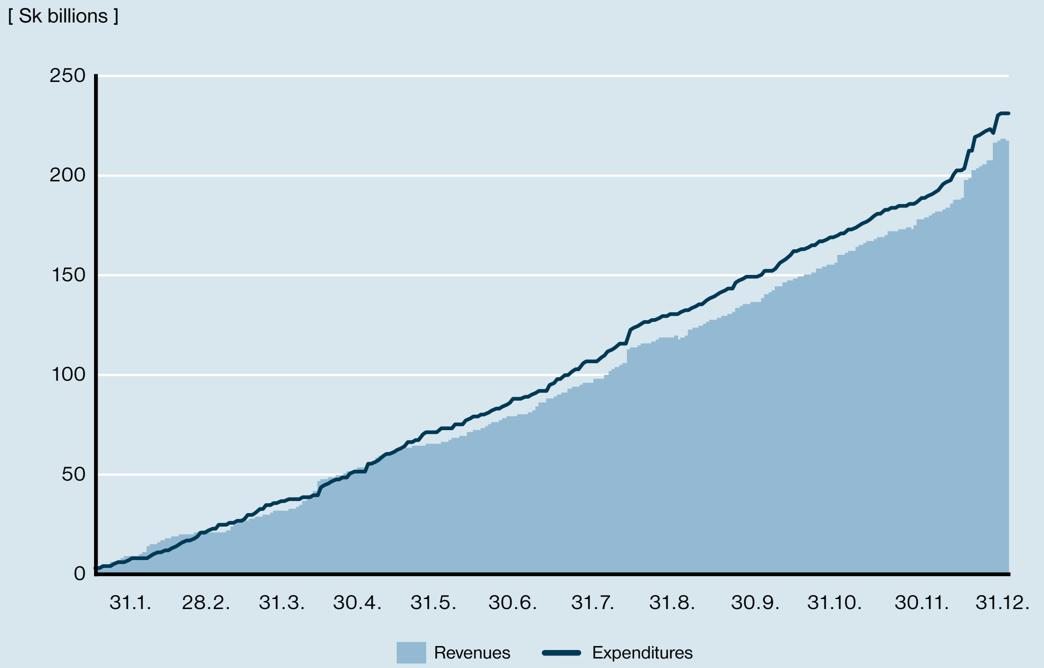
In the area of income taxes, however, the budgeted revenues were not fulfilled, especially the revenue from corporate income tax. Compared with the budgeted Sk 27.3 billion, corporate income tax was collected in the amount of roughly Sk 22 billion, i.e. Sk 2.6 billion less than in 1998. Revenue from personal income tax also recorded a fall (Sk 1.2 billion), but its contribution to the State budget was Sk 1.0 billion higher than a year earlier. The shortfall in personal-income tax revenue was a result of the slower pace of economic growth and higher rate of unemployment than were originally expected.

In comparison with the previous years, the budgetary discipline improved. Another positive result was that the size of the budget deficit remained below the budgeted figure.

Relationship Between the NBS and the State Budget

In 1999, the relationship between the National Bank of Slovakia and the Ministry of Finance of the SR was regulated by a directive passed by

Development of budget revenues and expenditures in 1999



the Board of the NBS on 22 February 1999, on the basis of which new interest rates were approved for the individual assets of the State, with effect from 1 January 1999 to 31 December 1999.

The interest rates approved were based on the valid discount rate of the NBS. The rate for the balance of the summary memorandum account of the State, kept with the NBS, was set at 7.8% and that for Treasury bills purchased for the portfolio of the NBS (so-called technical issues) at 11.8% for all.

During the year under review, the National Bank of Slovakia transferred a total of Sk 42.15 billion, of which Sk 27.20 billion to the State budget and Sk 14.95 billion to State financial assets. The funds were obtained from the cancellation of provisions at the NBS (Sk 17.8 billion), the sale of Slovakia's stake in ČSOB (Sk 15.65 billion), and from the operations of the NBS (Sk 8.7 billion, of which Sk 3.0 billion was the remaining profit transferred to the State budget in accordance with Act No. 63/1999 Z.z. on the State Budget for 1999, and Sk 5.7 billion was intended for increasing the capital of IRB).

Development of State Financial Assets and Liabilities

State financial assets maintained in the form of deposits at the NBS amounted to Sk 15.6 billion at the end of 1999. Over the course of the year, a marked change was recorded in the area of assets which increased by Sk 13.1 billion compared with the figure at the beginning of January (Sk 2.5 billion).

During the first half of the year, State financial assets fell by Sk 2.1 billion. Assets in this amount were used for the repayment of principal on SAL loans from the World Bank, the Export-Import Bank of Japan, a government loan provided by Russia (for the Nuclear Power Plant at Mochovce), and a loan provided by the government of Austria to the former CSFR for the support of the country's balance of payments. As a result of such payments, the balances on numerous accounts of State financial assets amounted to zero at the end of June. Another marked change occurred in the last month of 1999. In order to put to use the earnings of the National Bank of Slovakia from special one-off financial transactions in the long-term financial resources of the State, the National Council of the SR passed a law (Act No. 348/1999), which amends and augments the provisions of Act No. 303/1995 Z.z. on budgetary rules, and those of Act No. 566/1992 Zb. on the National Bank of Slovakia with subsequent amendments. In accordance with the said amendment, the remaining profit of the NBS is to be transferred to the State budget or, if the Government so decides, to the account of State financial assets. During December, part of the remaining profit of the NBS (Sk 14.95 billion) was transferred to the account of State financial assets. Part of these funds (Sk 850 million) was used, on the basis of a government decision, for the payment of Slovak Railways' liabilities to the Social Insurance Company. State financial liabilities amounted to zero throughout the year.

State Funds

At the end of 1999, the overall position of State funds was that of a debtor, in the amount of Sk 23.9 billion. This position was in large part due to domestic and foreign credit facilities, totalling Sk 27.7 billion. The dominant part of these credits (96.6%) was granted to the State Road Fund, for the financing of motorway construction. Excluding credit resources, State funds had Sk 3.8 billion at their disposal for the financing of their activities.

In comparison with the beginning of the year, the volume of credits increased by Sk 4.1 billion. The largest balance (Sk 2.0 billion) was recorded on the account of the State Fund for the Liquidation of Nuclear Power Engineering

Facilities and Handling of Spent Fuel (as at 31 December 1999).

Internal Debt of the Government to the Banking Sector

At the end of 1999, the net internal debt of the Slovak Government vis-à-vis the banking sector stood at Sk 58.6 billion, representing a fall of Sk 19.3 billion since the beginning of the year. This marked fall took place during the last ten days of December, when the funds obtained from the sale of ČSOB were entered in the accounts (which positively affected the balance on the summary memorandum account of the State).

During the period under review, the level of the internal debt fluctuated from Sk 63.1 billion (July) to Sk 86.0 billion (May). The net position of the Government was affected by the following factors:

- the internal debt of the Government was positively affected by budgetary performance under the provisional budget during the first quarter, when government spending was restricted and the budget generated a surplus;
- in the second quarter, the budget deficit started to increase, from Sk 1.4 billion in April to Sk 8.7 billion in May, and closed the year at Sk 14.7 billion;
- the conversion of yields from the June issue of Eurobonds into crown equivalents, reduced the internal position of the Government; on the other hand, the volume of foreign debt recorded an increase, which was mirrored in the volume of net credit to the Government;
- during the year, the internal position of the Government vis-à-vis the banking sector was gradually reduced in relative terms. On the one hand, the current performance of the State budget deteriorated, on the other, the internal debt was financed with the help of non-bank entities, which are not included in the net internal debt of the State (government securities held by non-bank entities had the highest weight in July and August);
- at the end of the third quarter, the level of internal debt was again lower due to the drawing of foreign loans by the State Road Fund. This led to an increase in the level of external debt, while the crown equivalent of these loans reduced the internal debt of the State;
- in October and November, the level of internal debt rose again (by approximately Sk 5.0 billion), due to increases in the debt positions of State funds, accompanied by decreases in the balances of social security funds and deposits on the summary account of the State.

In November, the schedule of principal repayments on bonds for 1999 was fulfilled (Sk 64.0 billion was repaid in total), while the volume of new government bond issues (one and three-year bonds) reached Sk 61.2 billion. During 1999, the coverage of the budget deficit and repayments of principal on government bonds were successfully achieved through new issues, either in the form of Treasury bills (48 issues) or government bonds (38 issues in domestic currency, 1 issue of 5-year Eurobonds in the amount of EUR 500 million, the yield of the Ministry of Finance totalled Sk 22.2 billion).

National Property Fund

In 1999, as in 1998, the revenues of the National Property Fund were largely dependent on loans and receipts in the form of REPO deals.

The position of the National Property Fund vis-à-vis the banking sector was that of a debtor during the whole year, while it increased from Sk 0.15 billion at the beginning of January to Sk 1.22 billion at the end of December.

The number of bonds redeemed during the year totalled 21,501 pcs in comparison with 400,030 pcs in 1998 (when bonds were repaid in large amounts to citizens over 70 years of age and were also used by debtors of the National Property Funds for the repayment of their liabilities). Thus, 2,230,903 pcs of bonds remained in circulation, i.e. 67% of the issue.

4. MONETARY POLICY AND MONETARY DEVELOPMENT

Monetary development in 1999 was influenced by the economic policy of the Government. During the first half of the year, the negative trend in basic macroeconomic indicators continued, especially in the area of fiscal policy and foreign trade, due to the slow rate of economic reform. Although the 12-month rate of inflation remained stable, around 7%, the exchange rate of the crown reacted rather sensitively to signals from the real economy; its depreciation was due partly to a decrease in confidence among foreign investors, which was reflected in the unfavourable credit rating assigned to Slovakia. In May 1999, the Government of the SR approved a strategy for the acceleration of reforms. The measures adopted were designed to improve public finances and restrict domestic demand with a view to mitigating the effects of macroeconomic imbalances. Subsequently, the Government took the first steps towards restructuring the microsphere, by starting the process of recovery in large commercial banks and making preparations for the privatisation of state holdings. The measures adopted proved effective as they reduced both the fiscal deficit and the shortfall in the balance of payments. Exchange rate development also reflected the effects of the same measures. During the second half of 1999, the exchange rate of the crown showed a tendency to appreciate; its year-end value vis-à-vis the euro was stronger than at the beginning of the year. In accordance with the monetary programme, the NBS intervened in the foreign exchange market several times to prevent the Slovak crown from excessive volatility. In line with the monetary programme, the year-end rate of inflation reached 14.2%, as a result of administrative adjustments to regulated prices, while the other sectors excluding foods (net inflation) contributed 6.06 percentage points to overall inflation. Net inflation reached the lower limit of the interval set by the National Bank of Slovakia for 1999.

The monetary policy pursued by the NBS in 1999 was of a stabilisation nature. The goal was to eliminate secondary price infection in sectors with non-regulated prices, which was also supported by a reduction in domestic demand and real wages. The improvement in exchange rate development and the trade balance created room for a fall in interest rates. At the beginning of 1999, the NBS continued to pursue an active refinancing policy with the aim of lowering the level of interest rates on the interbank money market and, subsequently, the rates of interest for customers. The trend of fall in interest rates was interrupted in May. As a result of combined interventions in the foreign exchange and money markets, interest rates reached high levels temporarily. In June, the money market stabilised and interest rates followed a downward trend until October. At the end of the year, interest rates on deposits at up to 1-month notice rose, as commercial banks showed increased interest in financial resources for ensuring a smooth transition to the year 2000. In average terms, interest rates in December were 3.2 percentage points lower than a year earlier. Although there were no conditions for transition to qualitative control in 1999, the NBS, by cancelling foreign exchange positions of commercial banks and branches of foreign banks, stopped applying administrative instruments of monetary control. At the same time, the NBS reduced the ratio of required reserves from 9% to 8%. This, however, represented only a slight reduction in the total volume of required reserves since the basis for the creation of required reserves had been extended.

4.1. Monetary Development

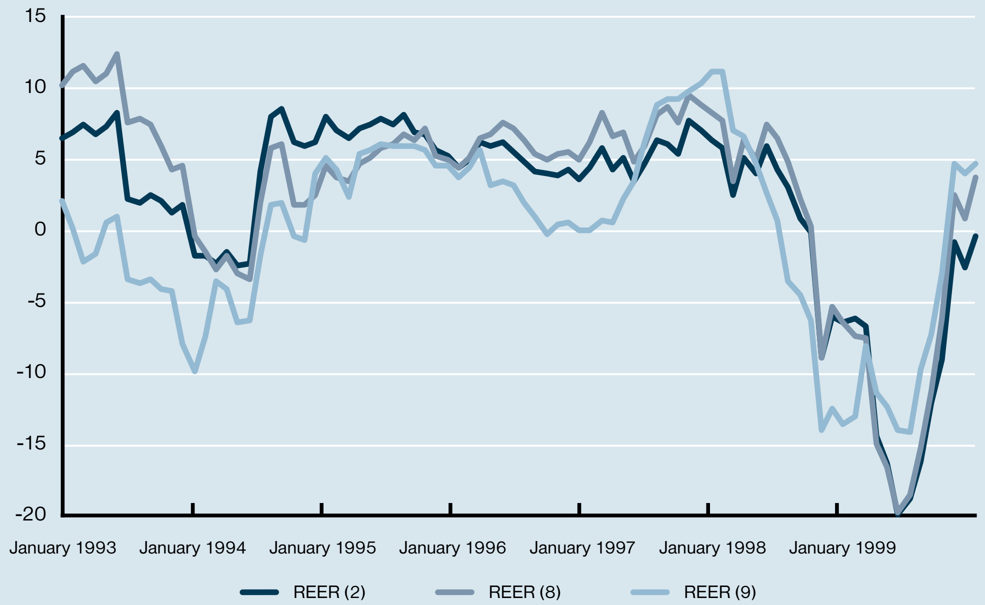
The temporary two-digit increase in prices was within the scope projected and accepted by the

National Bank of Slovakia in the Monetary Programme for 1999 as an inevitable step leading to the elimination of existing price deformations preventing domestic prices from approaching effectively the level of EU prices. According to the Revised Monetary Programme for 1999, the NBS was to maintain net inflation within 6.0 to 7.5 percentage points, in order to keep the inflation expectations at a stable level.

On 1 January 1999, the euro became a currency in its own right within the European Monetary Union, replacing the German mark as reference currency to which the exchange rate of the Slovak crown is pegged. The higher sensitivity of a floating exchange rate in comparison with a fixed rate, to signals of economic as well as non-economic nature, was mirrored in the exchange rate of the Slovak crown throughout the year. Until May, the exchange-rate value of the crown had shown a tendency to depreciate in response to the unstable course of macroeconomic development, which was also reflected in the unfavourable rating of Slovakia by international agencies. At the end of May, when the effects of the unfavourable factors culminated, the rate of depreciation in the crown's exchange rate had reached 9.75% since the beginning of the year. The rate of depreciation was moderated, in accordance with the Monetary Programme of the NBS for 1999, through central bank interventions in the foreign exchange market. In May, foreign exchange interventions were combined with operations on the money market, which led to a rise in interbank deposit rates due to the limitation of liquidity in the banking sector. The adoption of a strategy by the Government for the acceleration of reforms reversed the trend of exchange rate development and the Slovak crown began to appreciate. At the end of the year, the trend of appreciation accelerated after the SR had been invited to join the group of countries associated with the EU. Since the factors acting in support of appreciation in the exchange rate of the Sk were not of fundamental nature, the NBS intervened in the foreign exchange market to protect the crown from excessive appreciation. At the end of the year, the Slovak currency was 1.5% stronger than at the beginning of the year.

The steep increase in price levels, coupled with appreciation in the nominal exchange rate of

Real effective exchange rate (REER) of the Slovak crown
(based on CPI for 2, 8 and 9 trading partners) – year-on-year change in points



the crown against the euro, tended to reduce the price competitiveness of domestic production. The index of the real effective exchange rate (REER) is an indicator of change in the trade terms of domestic producers. Its appreciation indicates a decrease in the degree of competitiveness and depreciation is a sign of increase in the competitiveness of domestic products in comparison with foreign goods. The index of the real effective exchange rate, calculated on the basis of consumer prices and including the nine most important trading partners of Slovakia, appreciated by 11.8 percentage points in 1999.

When using a producer price index, the rate of appreciation in the real effective exchange rate was smaller, i.e. 4.5% (for nine trading partners), which is a more representative value with regard to the competitiveness of Slovak exporters. At the same time, the effect of appreciation in the real effective exchange rate on the trade balance was, in all probability, eliminated by other factors. The introduction of a surcharge on imports and measures for the restriction of domestic demand reduced the deficit of trade from Sk 80.8 billion in 1998 to Sk 45.7 billion in 1999. The balance of trade was also affected by a decrease in the current account deficit as a share of GDP, from 10.1% in 1998 to 5.8% in 1999. The government measures also eliminated the risk of unfavourable development in public finances.

In comparison with the revised monetary programme, the development of monetary aggregates followed a different course. As a result of a steeper than expected increase in net domestic assets, the dynamics of growth in the money supply accelerated.

The money supply, expressed in terms of the M2 aggregate (at fixed 1993 exchange rates), reached Sk 508.9 billion on 31 December 1999. The rate of growth in M2 accelerated year-on-year by 8.4 percentage points (to 10.9%), which was partly a result of its low value a year earlier. In absolute terms, the money supply increased by Sk 50.0 billion in 1999 compared with Sk 11.0 billion in 1998. The accelerated growth in M2 in 1999 had no inflationary effect as it was not large enough to fully offset the rise in consumer prices.

Domestic resources increased year-on-year by 10.3%, contributing 9.5 percentage points to growth in the money supply. Of net domestic assets, other items net made the most significant contribution to the growth in M2, in connection with the loss incurred in the banking sector. In 1999, net credit to the Government and the National Property Fund (NPF) recorded a marked improvement: the annual rate of growth reached 2.8% in December compared with 38.0% in the same period a year earlier. With respect to monetary policy, the volume of net credit to Government is to be assessed without taking into account one-off proceeds from the sale of NBS's stake in ČSOB in 1999, which distort the result. After adjusting the volume of net credit for proceeds from the sale of ČSOB, the dynamics of net credit to the Government (including NPF) would have reached 14.0% in December. This represents a much slower rate of growth than the figure projected in the revised monetary programme. Bank lending to households and enterprises remained within the range set in the monetary programme, with the year-end rate of growth reaching 4.0%, i.e. an absolute increase of Sk 15.1 billion in the volume of loans.

4.2. Structure of the Money Supply

During 1999, the M2 money supply (at fixed 1993 exchange rates) increased by Sk 50.0 billion, due to growth in both quasi-money (Sk 43.3 billion) and the M1 aggregate (Sk 6.6 billion). At the end of the year, the volume of the money supply reached Sk 508.9 billion.

The dynamics of year-on-year growth in the M2 aggregate gradually increased during the year, to 10.9% at the end of December (compared with 2.5% in 1998). On a year-on-year basis, quasi-money grew by 13.9% (compared with 10.6% in 1998) and the M1 aggregate by 4.5% (compared with a decline of 11.4% in 1998).

The volume of currency in circulation outside the banking sector increased year-on-year by Sk 7.7 billion (15.5%) and its development towards the end of the year was affected by the expectation of possible software problems in connection with transition to the year 2000 (Y2K). In December, the volume of currency issued grew by Sk 7.8 billion, compared with a fall of Sk 0.5 billion in 1998, and an increase of Sk 4.8 billion in 1997.

The volume of demand deposits remained virtually unchanged during 1999: it fell by only Sk 1.1 billion (1.0%) due primarily to decline in household deposits (Sk 1.1 billion). With regard to the relatively high level of interest rates on short-term deposits, the corporate and household sectors tried to minimise the balances of demand deposits and to transfer free resources to more profitable forms of deposit. This fact was reflected in the development of demand deposits virtually throughout the year, when they showed a tendency to fall during the first three quarters. During the individual months, the development of demand deposits was significantly affected by changes in corporate deposits. These were mostly seasonal changes connected with the discharge of liabilities vis-à-vis the State budget. Globally, however, corporate demand deposits recorded only a negligible change in volume (a fall of Sk 0.2 billion). Demand deposits in the insurance sector increased by Sk 0.2 billion.

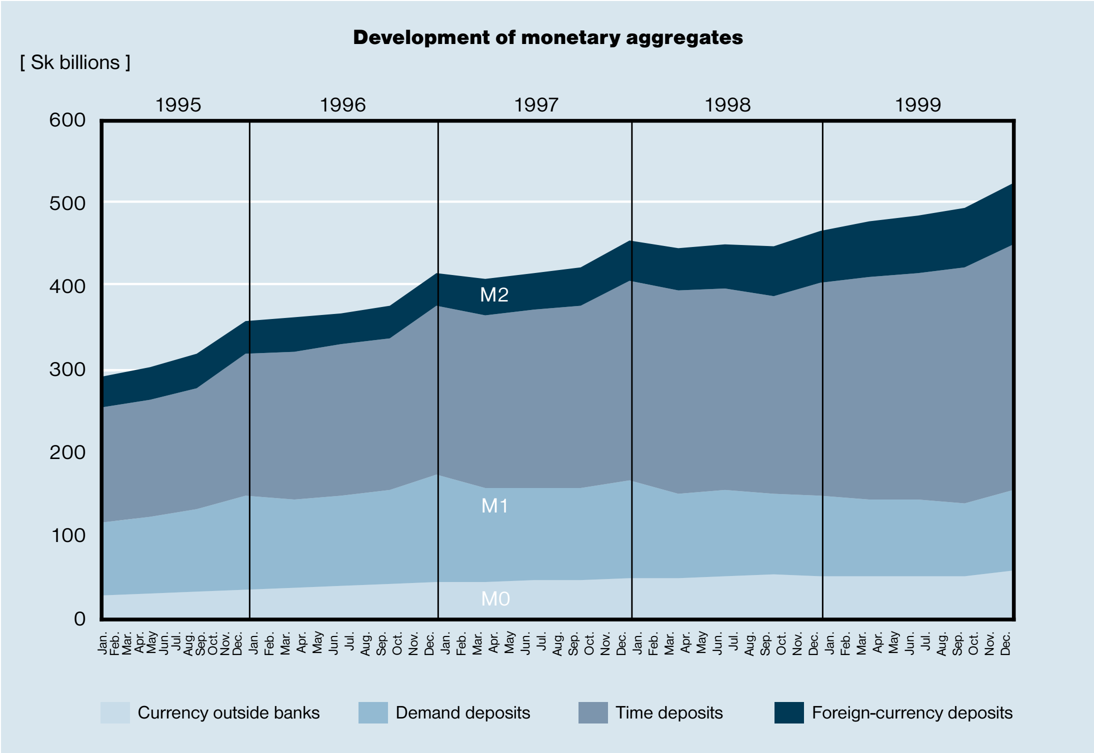
Time deposits represented the most dynamic component of the money supply, with an increase of Sk 39.8 billion (15.5%) during the year. The most rapid increase took place in household deposits (Sk 26.8 billion), though their annual growth dynamics slowed by 3 percentage points (to 12.7%) in comparison with 1998. The increase in time deposits took place mostly in deposits at up to one, three, and six-month notice. On the other hand, medium and short-term savings deposits declined in volume (passbooks). In comparison with 1998, time deposits in the corporate sector followed a completely different course of development in 1999: they increased in volume by Sk 9.6 billion (30.2%). In 1998, these deposits declined by almost Sk 10 billion. The increase took place in deposits with the same maturities as in the case of household deposits. In the corporate and household sectors, the structure of time deposits was affected significantly by the persistence of high interest rates on short-term deposits. In the insurance sector, time deposits increased in volume by Sk 3.4 billion.

Slovak-crown deposits (demand and time) increased in volume by Sk 38.7 billion (10.9%) during 1999. The increase was due primarily to growth in household deposits (Sk 25.7 billion). Corporate deposits grew by Sk 9.5 billion, which represented a change in their downward trend in comparsion with 1997 (Sk -6.6 billion) and 1998 (Sk -24.2 billion). The deposits of insurance companies increased by Sk 3.6 billion.

Foreign-currency deposits recorded an increase of Sk 3.5 billion (6.4%) in 1999, but their annual growth dynamics slowed considerably in comparison with 1998 (Sk 13.3 billion; 31.9%). This change was connected with the declaration of the Government and the NBS about the restoration of macroeconomic stability in the Slovak Republic, and was supported by the adoption of economic measures. The adoption of economic measures led to increased confidence among economic entities in the Slovak currency and the stability of the crown exchange rate.

4.3. Bank Lending

Bank lending in Sk and foreign currency to the entrepreneurial sector, households, central and local authorities for extrabudgetary purposes, by commercial banks and the NBS, was uneven



over the course of 1999. The month-on-month change in total credit ranged from Sk -2.1 billion to Sk 4.8 billion. The highest increases in bank loans were recorded in March, April, and August (an average of Sk 3.7 billion per month). In July 1999, the total volume of loans fell by Sk 2.1 billion. This development reflected the basic problems of the economy: external and internal imbalances, liquidity problems of commercial banks, and the situation on the interbank money market. From the beginning of the year, bank lending increased by a total of Sk 12.3 billion, of which crown loans accounted for Sk 9.9 billion and foreign-currency loans Sk 2.4 billion. At the end of the year, the total volume of bank loans reached Sk 410.7 billion, of which crown loans accounted for Sk 350.2 billion and loans in foreign currency Sk 60.5 billion.

The development of bank lending followed different trends over the course of the year. During the first six months, crown loans increased by 1.4% and loans in foreign currency by 18.1%. During the second half of the year, crown loans increased by 1.4%, while foreign-currency loans fell in volume by 11.8%. Bank lending was influenced by the availability of loans, the exchange rate of the crown, and by the level of interest rates.

A characteristic feature of bank lending was that, despite the slow growth in crown loans, their volume increased in the household sector by Sk 9.4 billion (due mainly to loans granted by home savings banks) and in the corporate sector (non-financial organisations) by Sk 6.3 billion, while in the entrepreneurial sector they fell in volume by Sk 5.2 billion. In the financial sector, the volume of crown loans increased by Sk 1.9 billion. At the end of the year, however, the financial sector accounted for only 3.1% of total crown credit.

The structure of crown loans by sector changed during the year as follows: loans in the public sector increased by 15.3 points (to 29.7%) and in the household sector by 2.5 points (to 10.3%), while those in the private sector fell by 18.1 points (to 50.3%).

During the period under review, the structure of loans by term saw a decrease in the share of short-term loans in total credit (by 7.1 points, to

36.5%) and in that of long-term loans (by 6.0 points, to 28.5%), while the share of medium-term loans increased (by 13.1 points, to 35.0%), as a result of loan portfolio restructuring at the three largest banks in December 1999, which distorts the comparability of the above figures with the initial level to a certain extent.

During the year, the structure of crown loans by sector changed as a result of restructuring and their inclusion in the category 'other loans', while the share of loans in industrial production decreased from 34.2% to 24.4%; loans in trade, repair of consumer goods and motor vehicles, hotels and restaurants from 22.1% to 16.8%; and the percentage of loans in other sectors (except banking) also decreased to a lesser extent. The largest share of the total volume of crown loans was taken up by industrial production and trade.

Of the total volume of credit granted in 1999 (Sk 527.5 billion, including loans reclassified in connection with the restructuring of loan portfolios of banks), loans to the entrepreneurial sector accounted for 92.3%. They were, however, mostly short-term loans with a maturity of up to 3 months. The household sector absorbed 3.4% of the total volume of new loans.

With regard to the structure of new loans by purpose, operating loans accounted for 58.0% and overdraft facilities 15.3%. Loans granted for development programmes represented only 2.4% of the total volume of credit extended during the given period, which was associated with their structure by term. Short-term loans with a maturity of up to 1 year accounted for 82.1% of the volume of new loans. In terms of volume, a significant role was played by 1-day loans. Another significant item was represented by credits extended for the coverage of non-performing loans, which reduced the actual volume of loans available for the financing of specific development projects. At the end of the year, loan portfolio restructuring was in process at three banks, which distorts the structure of loans by term and purpose to a certain extent.

4.4. Interest Rate Development

In 1999, primary interest rates were influenced by the unfavourable course of economic development during the first six months on the one hand, and by the restoration of macroeconomic stability in the following period on the other. In addition, primary interest rates were affected by changes in the volume of new loans (from Sk 31.8 billion to Sk 52.2 billion per month – excluding loans reclassified within the scope of restructuring), while the biggest changes were recorded in the volume of very-short-term loans with a maturity of up to 1 month and interest rates around 20%. The situation on the capital market did not allow bank lending to be replaced by other sources of finance. In setting their interest rates, commercial banks took into account their economic situation, the quality of their loan portfolios, and other factors.

During the period under review, the development of interest rates on new loans can be characterised as relative stable with a temporary moderate fall in March and April, followed by a sharp decline during the second half of the year, when interest rates fluctuated between 15 and 17%. This development was affected by changes in the level of liquidity in the banking sector and by depreciation in the exchange rate of the crown during the first half of the year. Of crown deposits, marked fluctuations were recorded in interest rates on very-short-term deposits with a maturity of up to 3 months, which reacted very sensitively to changes in bank liquidity. During the second half of the year, their level fell due to an adequate amount of liquidity in the banking sector.

Compared with December 1998, the average interest rate on the total volume of loans recorded a marked change (a fall of 2.17 points, to 14.0%, which was to a certain extent due to the reclassification of loans provided to Slovenská konsolidačná, a.s., at a rate of 10.3%, within the scope of restructuring). The rate was also affected by other factors, such as the structure of loans by term and purpose and the structure of customers. The average lending rate for short-term loans fell by 2.63 points (to 18.45%); for medium-term loans by 3.57 points (to 12.64%); and the rates for long-term loans rose by 0.50 points (to 10.86%), while they continued to be influenced by loans granted in the past at fixed and low interest rates.

Over the course of 1999, commercial banks maintained the rates of interest they had announced, particularly on short-term loans, at roughly the same level. Compared with December 1998, the actual price of new loans fell by 6.07 points, to 12.55% (due to the transfer of Sk 61.7 billion at a rate of 10.3%), while the lowest level was recorded in December (12.55%). With regard to the dominance of short-term loans (82.1%), the average annual rate of interest on these loans (17.45%) affected the level of average interest rate on the total volume of new loans. Interest rates on new short-term loans followed the variations in interest rates on the interbank money market. The level of interest rates on short-term loans fell by 2.51 points, to 16.4%. Compared with December 1998, lending rates for medium and long-term loans fell to 10.36% (by 3.84 points) and to 14.21% (by 0.71 points) respectively. With regard to the small volume of these loans, the average lending rate was to a large extent exposed to random structural changes, depending on the purpose of the given loans, with different interest rates (loans to employees).

Over the course of the year, the development of average interest rates on loans by purpose was characterised by marked fluctuations, mainly in lending rates for operating loans (from 14.29% to 19.68%); current-account loans (from 16.71% to 23.90%); and for development loans (from 15.70% to 20.43%). Average interest rates on consumer loans to households fluctuated between 12.05% and 16.31%.

With regard to the rate of inflation, real interest rates on new short-term loans fluctuated from 1.4% in October to 13.16% in May. After taking the prices of industrial producers into account, the above rates ranged from 8.70% in December to 18.43% in January, as a result of marked fluctuations in interest rates, industrial producer prices, and in the rate of inflation.

In 1999, the development of interest rates on crown deposits was affected by inflation only to a limited extent, it rather reflected a need for liquid resources, which were cheaper than interbank money market resources despite the high level of interest rates. In an effort to obtain such resources, commercial banks raised their interest rates, which led to a rise in the average level of deposit rates in the first half of the year. During the second half, interest rate levels showed a tendency to fall.

The average interest rate on total deposits fluctuated around 10% (up to 11.0%) and reached 9.85% at the end of December, while interest rates on demand deposits were basically stable (3.8%). Interest rates on time deposits fluctuated from 12.0 to 13.5%, while marked variations were recorded in time deposits at 7-day to 3-month notice. Deposits with a maturity of 7 days to 3 months attracted interest at an average rate of 12 to 18%, whereas other time deposits earned interest at 10.6 to 17.5%. The low rate of interest on deposits at over 5-year notice (4.0 to 4.5%) was attributable to deposits at home savings banks, which accounted for 92.6% of the total volume of long-term deposits.

In 1999, real interest rates on one-year deposits remained within the range of –2.37% to 5.80%. The increase in the annual rate of inflation (from 5.6% in December 1998 to 14.2% at the end of 1999) and in the average interest rate on one-year deposits (from 12.01 to 12.30%) led to a fall in the level of real interest rates (by 8.31 points). During the second half of the year, real interest rates fluctuated between –1.18% and –2.37%.

4.5. Implementation of Monetary Policy

The monetary policy pursued by the National Bank of Slovakia in 1999 focused on the control of liquidity in the banking sector through regulating the level of excess reserves of banks.

In the area of exchange rates, interventions in the foreign exchange market were used mostly for the prevention of excessive exchange rate volatility, with a view to influencing the liquidity of commercial banks, the level of which was subsequently adjusted through central bank operations on the interbank money market.

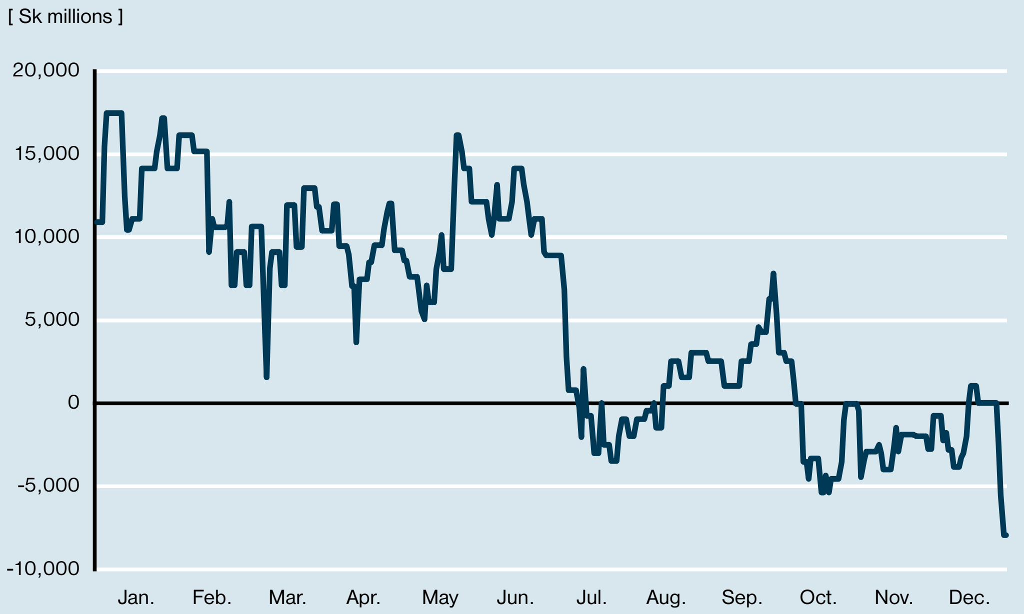
In 1999, especially in its second half, after the exchange rate of the crown had stabilised, the NBS also paid attention to the stabilisation and subsequent lowering of interest rates on the interbank money market. The NBS realised its goals in this area in the form of open market operations through which it supplied liquidity into the banking sector and thus created conditions for the smooth fulfilment of reserve requirements. During the first half of 1999, the NBS supplied refinancing into the banking sector in the average amount of Sk 11.4 billion.

The issuing policy of the Ministry of Finance of the SR, designed to reduce the costs of domestic debt servicing, in an environment marked by increased repayments on government securities (Sk 110.6 billion in 1999), led to the utilisation of resources through technical issues of Treasury bills for the portfolio of the NBS.

The unfavourable trend in budgetary performance; the servicing of the domestic debt from the resources of domestic banks; the uneven distribution of liquidity over the banking sector, and the exchange rate development prevented the price of money from falling, to a significant extent during the first half of 1999.

The foreign exchange market experienced some turbulence, which also contributed to the rise in the level of interbank deposit rates. The two markets stabilised towards the end of May, following the adoption of economic measures by the Government.

Balance of central bank interventions in 1999



This created more favourable conditions for the conduct of monetary policy. The exchange rate of the crown started to appreciate owing to the renewal of confidence among foreign as well as domestic investors and the inflow of foreign exchange from abroad.

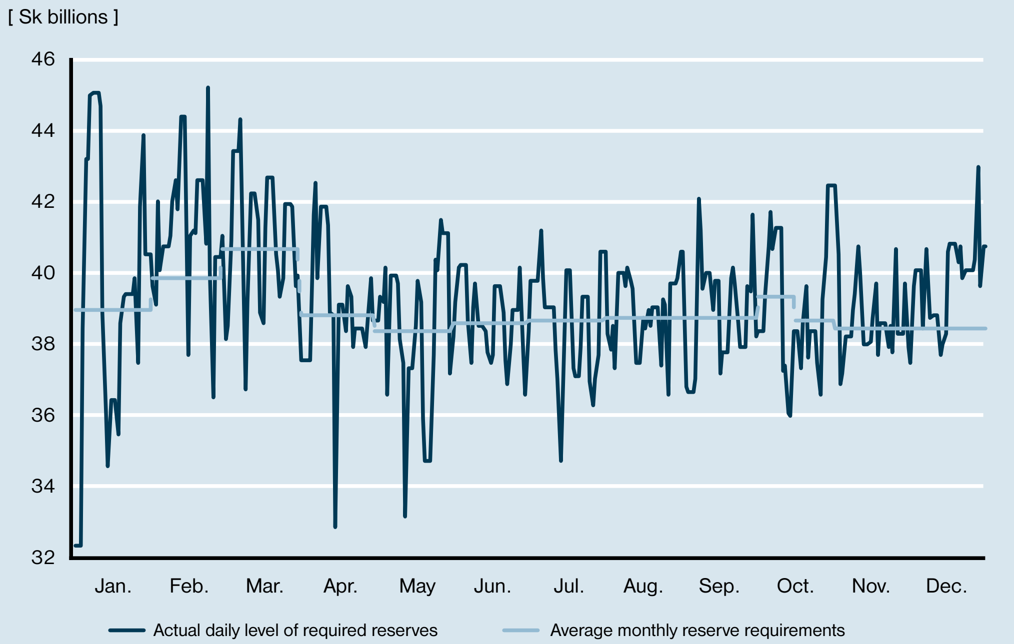
The inflow of funds from issues of Eurobonds, used for the coverage of domestic debt service payments, enabled the National Bank of Slovakia to reduce the volume of refinancing. The average volume of refinancing granted to the banking sector fell from Sk 11.8 billion in June to Sk 1.1 billion in July. In October, the position of the National Bank of Slovakia vis-à-vis the banking sector changed from refinancing to sterilisation, which continued until the end of the year.

The inflow of foreign resources and improvement in macroeconomic indicators were accompanied by a fall in interest rates on the interbank money market as well as in yields on government securities (the fall in the level of yields was due partly to a change in the method applied by the Ministry of Finance in setting the conditions of sale at auction – limits on volume and rate).

The implementation of monetary policy was affected substantially in December 1999, when liquidity in the banking sector was replenished by funds transferred from the profit of the NBS to the State budget, for the restructuring of commercial banks. Another major pro-liquidity factor was the income from NBS operations on the foreign exchange market, conducted to prevent the exchange rate of the Slovak crown from excessive appreciation.

Since the level of demand for cash increased in connection with the fear of problems with the transition of computer systems to the year 2000, the volume of currency in circulation expanded in December, reducing the level of liquidity in the banking sector. The National Bank of Slovakia responded to the liquidity situation in the banking sector by conducting open market operations, through which the temporary rise in the level of interest rates on the interbank market, linked with the effect of this specific factor, was overcome. In connection with the expected increase in cash withdrawals towards the end of the calendar year, the NBS prepared a special refinancing facility for commercial banks, which was drawn in the amount of Sk 1.8 billion.

Fulfilment of reserve requirements in the banking sector in 1999



Required reserves (in Sk billion and %)

	Required reserves		Fulfilment in 1st period		Fulfilment in 2nd period	
	Set	Actual	Average	% fulfilment	Average	% fulfilment
January	38.95	39.40	39.51	101.46	39.29	100.89
February	39.88	41.27	41.40	103.81	41.13	103.13
March	40.67	40.94	41.06	100.97	40.83	100.40
April	38.81	39.02	39.27	101.18	38.77	99.90
May	38.36	38.42	38.38	100.04	38.45	100.22
June	38.58	38.72	38.98	101.04	38.46	99.68
July	38.64	38.64	38.71	100.17	38.57	99.80
August	38.71	38.96	38.94	100.60	38.97	100.68
September	38.77	38.91	39.04	100.68	38.78	100.02
October 1/	39.35	39.11	39.09	99.35	-	-
October 1/	38.67	39.11	-	-	39.13	101.19
November	38.43	38.75	38.87	101.15	38.63	100.51
December	38.48	39.81	39.03	101.42	40.53	105.32

1/ In October, reserve requirements for the second period were subsequently adjusted.

In 1999, the fulfilment of reserve requirements in the banking sector followed a relatively balanced course. An exception was February, when the actual amount of required reserves exceeded the set level by more than 3% in both periods, and the second period in December, when the actual reserves of banks exceeded the set level by more than 5% on average.

Excess reserves in the individual periods ranged from Sk 3.0 billion to Sk 2.5 billion.

4.6. Instruments of Monetary Policy

1. Interest rate policy

- From 13 January 1996:
  discount rate = 8.8%.

2. Reserve requirements

With effect from 1 April 1999, the basis for the calculation of minimum required reserves for commercial banks was extended, making domestic and foreign primary resources of banks equal. The basis was extended so that the foreign exchange and crown liabilities of commercial banks includes non-residents, but the ratio of required reserves was reduced from 9% to 8%, while the ratio for home savings banks remained unchanged (3%). Required reserves attracted interest at the rate of 1.5%.

3. System of banking operations

The liquidity of commercial banks is influenced by the following operations:

a) Open market operations.

b) Bills-of-exchange operations - bills of exchange are rediscounted at the discount rate; this form of refinancing includes bills rediscounted in the support of agriculture.

c) Lombard loans – loans backed by the pledge of securities granted at Lombard rate. With effect from 1 January 1999, the Lombard loan was set at 5% above the level of funds of the same maturity on the interbank market. The NBS may grant Lombard loans for a period of 7 calendar days, 14 calendar days, and for one month.

d) Redistribution loans:
- Traditional - at a rate of 9.5%;
- Soft loans - at a rate of 7.5%.

4. Treasury bills

a) An operative instrument for financing the State budget deficit;

b) An instrument for managing the liquidity of commercial banks through:
- secondary sales and purchases;
- REPO operations (repurchase agreements).

5. NBS bills

- Instrument used by the central bank to influence the liquidity of commercial banks via the same trading system as for Treasury bills.

6. Exchange-rate and foreign-exchange policy

a) Floating exchange rate
With effect from 1 October 1998, the National Bank of Slovakia ceased to guarantee a fixed nominal exchange rate for the Slovak crown within a fluctuation band. The value of the Slovak crown is tied to a reference currency: on 1 January 1999, the euro (EUR) started to be used as reference currency in connection with the introduction of a single currency within the European Monetary Union. The exchange rate of the Sk now depends primarily on the development of supply and demand for the Slovak crown on the foreign exchange market. The National Bank of Slovakia may intervene against excessive volatility of the crown's exchange rate through foreign exchange transactions, i.e. purchases or sales of foreign exchange on the foreign exchange market.

b) Nominal exchange rate of the Slovak crown:
In relation to EUR, the nominal exchange rate of the Slovak crown (SKK) depreciated by 1.5% during 1999, to SKK 42.458/EUR at 31 December 1999. In relation to central parity, applied in a fixed exchange rate regime, the Slovak crown depreciated by 5.83% points, to 18.56%. This was due primarily to appreciation of the cross-currency rate of USD/EUR on the world markets. As a result, the Slovak crown weakened against the US dollar by 14.4% during the year, to SKK 42.266/USD.

c) Real effective exchange rate of the crown:
The real effective exchange rate of the Slovak crown, calculated on the basis of the producer price index, compared with Slovakia's eight trading partners having a significant share in the country's foreign trade turnover (USA, Great Britain, Austria, France, Germany, Italy, the Netherlands, and Switzerland), appreciated by 3.6 percentage points over the course of 1999; or, when compared with the country's nine trading partners (including the Czech Republic), it appreciated by 4.5 percentage points.

The real effective exchange rate of the Slovak crown, calculated on the basis of the consumer price index, compared with Slovakia’s eight trading partners, appreciated by 13.0 percentage points during 1999; or, when compared with the country's nine trading partners (including the Czech Republic), it appreciated by 11.8 percentage points.

d) Currency structure of receipts and payments in foreign exchange:
The turnover of foreign-exchange operations for payment items specified in groups 1 to 6 in convertible currencies reached Sk 813.6 billion in 1999. The average monthly turnover (Sk 67.8 billion) decreased by 1.5% year-on-year. The balance of foreign exchange receipts and payments resulted in a deficit of Sk 16.6 billion. The currency structure of the turnover was dominated by EUR (36.0%) and

USD (28.4%). The currencies of EMU and EU member states accounted for 24.4%, and those of countries for which the euro is a reference currency 10.8%. Together with EUR, these currencies represented 71.3% of the total volume. The percentage of non-European currencies was 0.3%, and together with USD accounted for 28.7% of the total turnover.

e) Foreign exchange positions of banks and branches of foreign banks for monetary purposes:
The ratio for the foreign exchange position for monetary purposes (FXPMP) was calculated as the proportion of foreign exchange assets of non-residents to the sum of non-resident banks' liabilities denominated in Slovak crowns and foreign exchange liabilities in total, less capital in foreign currency. The value of this ratio was first set at 0.65, and banks were required to achieve it by 31 December 1996.

Calculation of the foreign exchange position (FXPMP):

$$FXPMP = \frac{FXAN}{FXL + LNSk - C}$$

FXAN - Foreign exchange assets of non-residents;
FXL - Foreign exchange liabilities in total;
LNSk - Liabilities of non-residents in Slovak crowns;
C - Capital and non-paid-up capital in foreign currency.

Obligatory values of the FXPMP ratio:
As of 31 December 1996 - min. 0.65;
As of 31 March 1997 - min. 0.70;
As of 30 June 1997 - min. 0.80;

Penalties for non-fulfilment of the FXPMP ratio:
9% of the volume of the non-fulfilled ratio of FXPMP.

Period of monitoring the FXPMP ratio:
Before 10 July 1997, the FXPMP ratio had been calculated on the basis of average data from the 2nd and 3rd periods of the month N-2 and from the 1st ten-day period of the month N-1 of the Survey of Assets and Liabilities V(NBS) 6-36. With regard to the fact that banks, especially branches of foreign banks, circumvented the Decree by increasing FXAN and FXL vis-à-vis non-residents (FXLN) only at the end of the ten-day periods, the NBS issued a decree dated 16 July 1997 whereby FXPMP is monitored on a daily basis.

In connection with the abolition of the fixed exchange rate regime and the introduction of a floating rate for the Slovak crown in October 1998, the Decree on the Foreign Exchange Positions of Banks and Branches of Foreign Banks for Monetary Purposes was cancelled with effect from 26 March 1999.

4.7. Monetary Calendar

January

- The official currency of EU member states became the euro (EUR). With effect from 1 January 1999, DEM was replaced by EUR as reference currency for the exchange rate of the Slovak crown.
- The Government of the SR started the first phase of increase in regulated prices in 1999.

February

- The rating agency Standard & Poor's confirmed its long-term hard currency liability rating of the SR at the level of BB- and the short-term crown liability rating at BBB+. At the same time, the agency confirmed the negative outlook for Slovakia in both categories.
- The rating agency Moody's Investors Service changed the outlook for Slovakia from stable to negative. The country's long-term liability rating remained unchanged, at the level of Ba1.

March

- The Bank Board of the NBS decided to cancel the foreign exchange position of banks and branches of foreign banks for monetary purposes, with effect from 1 April 1999. The Bank also decided to extend the basis for the calculation of minimum required reserves and to lower the ratio of required reserves from 9% to 8%. The ratio for home savings banks remained unchanged (3%).

May

- Moody's Investors Service confirmed the existing rating of Slovakia with negative prospects.
- The Government of the SR approved a strategy for the acceleration of reforms, including measures for the elimination of macroeconomic imbalances.

June

- The rating agency Standard & Poor's confirmed the long-term hard currency liability rating of Slovakia at the level of BB+, with negative prospects.
- The National Council of the SR approved an amendment to the Act on the Protection of Bank Deposits.
- The Bank Board approved the Revised Monetary Programme of the NBS for 1999.
- The 7% import surcharge introduced by the Government entered into effect.

July

- The lower rate of value added tax was increased from 6% to 10%.
- The second phase of increase in regulated prices planned for 1999.

October

- The NBS placed Priemyselná banka, a.s. Košice under control of a conservator for liquidity problems, withholding payments to large customers, and failure to comply with the rules of banking business.
- The rating agency Moody's Investors Service improved the outlook for Slovakia from negative to stable.

November

- The Government of the SR approved a special guarantee for NBS redistribution loans in the amount of more than Sk 27 billion. This enabled the NBS to make an advance on the transfer of its remaining profits to the State budget.
- The rating agency Standard & Poor's improved the outlook for Slovakia from negative to stable.

December

- The Bank Board of the NBS approved the Monetary Programme for the Year 2000, with an outlook until 2003.
- At the Helsinki summit of the EU, Slovakia was invited to join the first group of associated countries.
- Priemyselná banka, a.s. (Industrial Bank) Košice was purchased by Slovenská sporiteľňa, a.s. which took over all commitments and liabilities of the bank.
- The NBS issued a decision on the revocation of the licence of AG Bank a.s. Nitra to operate as a bank.
- The Governor of the NBS signed a contract with KBC of Belgium and the European Bank for Reconstruction and Development for the sale of NBS's share in ČSOB, a.s. Prague.
- The NBS decided to terminate the conservatorship of Investičná a rozvojová banka, a.s. (Investment and Development Bank).

5. FINANCIAL MARKETS

5.1. Money Market

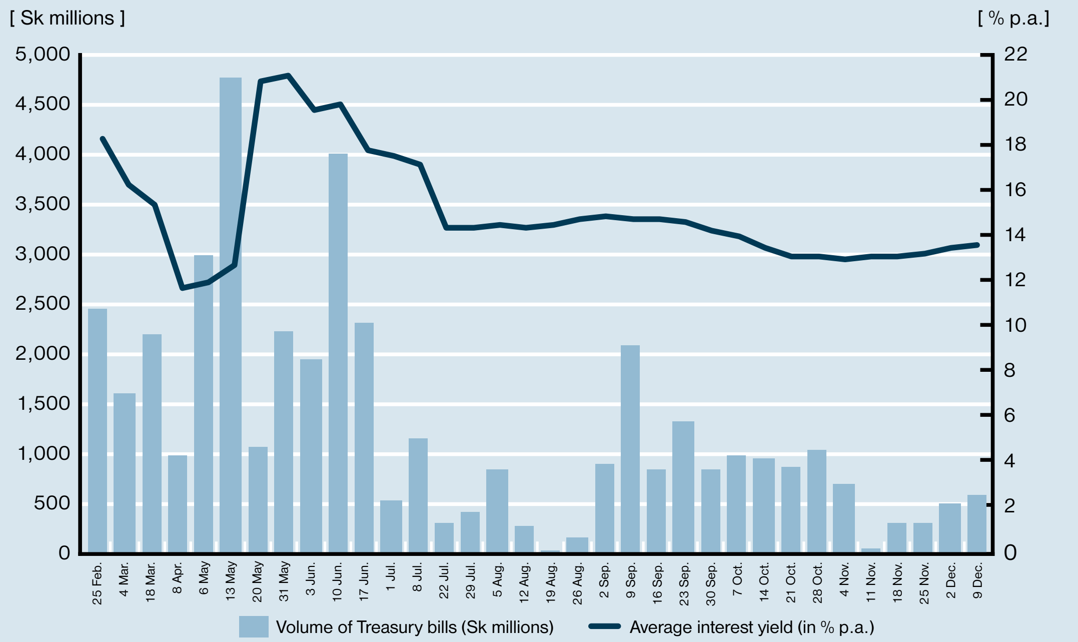
Primary Market for Treasury Bills

In 1999, Treasury bills were placed on the market in the total amount of Sk 80.229 billion. During that period, the schedule for the issue of government securities was published at regular quarterly intervals and a method was successfully introduced for the setting of maximum acceptable interest yields at auctions. The running deficit of the State budget was financed mostly from Treasury bills sold by auction and, to a lesser extent, from Treasury bills sold directly into the portfolio of the NBS. The Central Bank ceased to take part in deficit financing as late as April. A positive achievement in that period was the lower number of unsuccessful auctions.

In contrast with the previous year, issuing activity related to Treasury bills was concentrated in the first half of the year (80% of the Treasury bills was issued in this period). This was due mainly to the serious need for short-term resources during the first half of 1999. During this period, mostly short-term Treasury bills were issued, which had to be replaced with new bills after repayment. Issues for the portfolio of the NBS (all with a maturity of up to 7 days and with large-issue amounts) were floated exclusively in the first six months. During the second half of the year, Treasury bills were also issued with longer maturities (maturing in 2000).

Investors in Treasury bills were direct participants, i.e. domestic commercial banks, insurance companies, and dealers in securities, and indirect participants, i.e. other domestic legal entities registered in the Companies Register and foreign investors. The share of foreign investors in the primary purchase of Treasury bills at auction reached 14%, representing an increase of 100% compared with 1998. Their share in the holdings of Treasury bills was, however, much less, since they were selling these Treasury bills on the secondary market.

Volumes of Treasury-bill issues and average primary placement yields in 1999



In 1999, the Ministry of Finance managed to reduce the costs of Treasury-bill issues in comparison with 1998. This was due partly to the setting of the maximum interest yield that the issuer was willing to accept at the auctions, and the issue of Eurobonds which unburdened the domestic market. On the primary Treasury-bill market, the average interest rate achieved at auctions reached 15.91% p.a. (compared with 18.27% p.a. in 1998).

Secondary Market

The conduct of monetary policy continued to rely on quantitative control based on the same set of central bank instruments as a year earlier. The main instruments of the NBS were again REPO operations conducted in the form of auctions (REPO tenders). In contrast with the previous years, individual REPO deals were not conducted in 1999 and direct sale from own portfolio was only used in exceptional cases at the beginning of the year. In 1999, the NBS created room for drawing Lombard loans automatically, at variable interest rates, derived from BRIBOR rates with a 5% additional rate. In practice, this measure had no real effect on the development of liquidity and/or the money market.

The level of liquidity in the banking sector and its dependence on NBS resources, as well as the situation on the money market, varied considerably during 1999. During the first half of the year, the banking sector was permanently dependent on refinancing. In this period, 55 REPO tenders were conducted for refinancing purposes with a standard maturity of 14 days in most cases. The long-term dependence of the banking sector on refinancing necessitated the conduct of a refinancing tender once a month with a maturity of 28 days and thus contributed to stabilisation of the situation on the money market. In response to the actual situation on the money market, the NBS conducted refinancing tenders with non-standard maturities (1 to 7 days) and two sterilisation tenders for adjusting the volume of liquidity. Sterilisation activities performed in that period included direct sales of Treasury bills, previously purchased within so-called technical issues made by the Ministry of Finance of the SR.

The development and level of interest rates on the money market were not affected directly by the NBS, with regard to the quantitative conduct of monetary policy. Interest rates were influenced mainly by the issuing activities of the Ministry of Finance, and/or the direct reaction of the money and foreign exchange markets to the development of the domestic economy and foreign markets.

This can be explained by developments at the beginning of the year, when interest rates were stagnant despite the effort of the NBS to lower their actual levels. An adverse effect on the Bank's effort was caused by the assignment of a negative credit rating to Slovakia by Moody's Investors Service and interest rates rose slightly despite the high level of liquidity in the banking sector. Nor did the excess of resources, which led to over-fulfilment of reserve requirements, have a positive effect on the results of auctions held by the Ministry of Finance. During this period, interest rates on one to six-month deposits fluctuated from 17 to 18%. An impetus for a fall in deposit rates below 16% occurred in March as a response to the inflow of liquidity from the redemption of government securities and the expected absence of the Ministry of Finance as an issuer. By selling Treasury bills from its own portfolio, the NBS stopped the fall in short-term rates and fixed their lower limit at 10%. The persistent excess of liquidity, resulting from refinancing by the NBS, and the successful issuing strategy of the Ministry of Finance created room for a fall in deposit rates; at the end of April, the rate for 6-month deposits was close to 15%.

A turning point in the development of interbank deposit rates came in May, when the continued weakening of the Slovak crown, reflecting the persistent imbalance of the economy coupled with a certain degree of uncertainty arising from the run-up to presidential elections, led to a marked increase in interbank rates. In the interest of exchange-rate stability, the NBS considerably restricted the liquidity of the banking sector in connection with the sharp rise in the level of interbank deposit rates and the temporary suspension of the quoting of BRIBOR rates on 20 and 21 May. Interest yields on transactions reached 35 to 50%. After the introduction of government measures and the stabilisation of the exchange rate, refinancing was renewed by the NBS. This enabled banks to renew the quoting of BRIBOR rates (above 20%) to the full extent, in a relatively short time. In spite of this, developments on the money market in May confirmed their fragility.

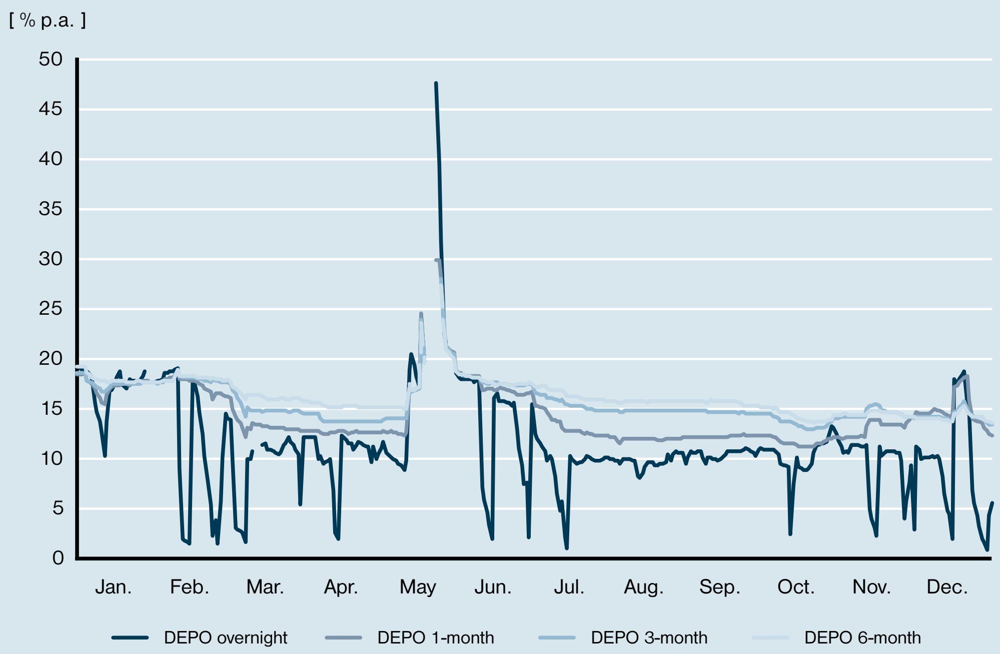
In June, all BRIBOR rates fell below the level of 18%. Their further fall, towards 17%, was due to the expected inflow of funds from an Eurobond issue and to intense refinancing by the NBS. The fall in deposit rates enabled the Ministry of Finance to reduce the level of interest yields at domestic auctions in government bonds.

From the beginning of July to the middle of August, when the volume of crown liquidity in the banking sector grew to an absolute surplus due to an inflow of liquidity in the form of converted funds obtained from a Eurobond issue of the Ministry of Finance, the NBS put out REPO tenders for sterilisation purposes. Although this period was relatively short, interest rates fell below 16% at the beginning of August and then remained at this level until the next period.

From the middle of August to the beginning of October, the banking sector again became dependent on NBS refinancing, due mainly to the accumulation of funds in the accounts of the State budget. With regard to the expected short-term character of the situation, the length of tenders also became shorter; it did not exceed the time of 7-day maturity. During August and September, interest rates remained surprisingly stable; at the end of this period, they fell below 15%.

During the following period (until the end of the year), the position of the NBS vis-à-vis the banking sector gradually changed into that of sterilisation. Due to the persistent excess of

Development of interbank offered rates (BRIBOR) in 1999



liquidity, interest rates fell below the level of 14% at the end of the second period in October. The fall in interest rates was also supported by the State budget approved for the next year together with the cut in income tax rates. Another positive signal for the stabilisation of interest rates and the strengthening of the crown's exchange rate was the decision to invite the SR to start accession negotiations with the EU, taken at the Helsinki summit.

At the end of October and the beginning of November, interest rates followed a different trend as a result of concern about the expected effects on computer systems of transition to the year 2000. The most sensitive reaction was shown by rates maturing in 2000; their volatility increased as the end of the year approached. The situation stabilised as late as the last week of December, when the massive liquidity-surplus caused a general fall in interest levels.

5.2. Capital Market

Primary Market

In 1999, auctions in government bonds were held at regular weekly intervals in accordance with the issuing schedule. Of the total number of auctions (38), thirty-four were successful, i.e. 89.47% (compared with 82.5% in 1998).

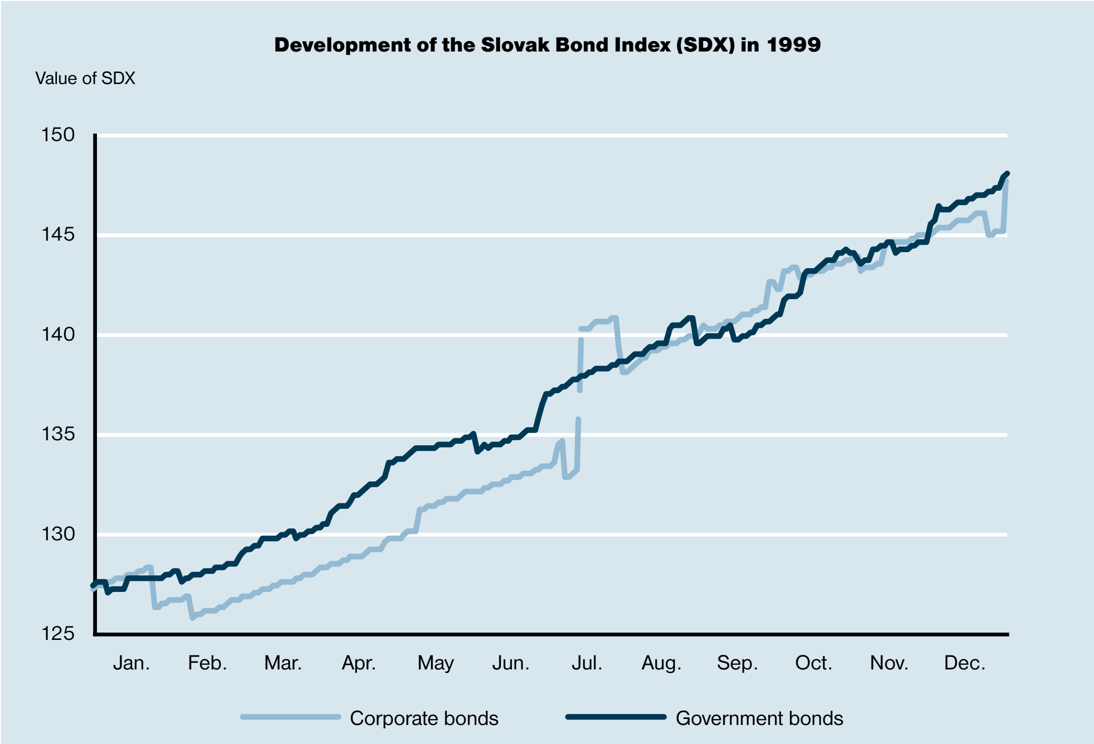
The year 1999 saw a change in the structure of bonds by maturity. In comparison with 1998, when 1-year bonds represented 77.1% of the total volume of government bonds issued, the maturities of bonds issued in 1999 were longer. Of the total volume of government bonds, 3-year bonds accounted for 14.3%, 2-year bonds 29.1%, and 1-year bonds only 56.6%. Total demand for bonds reached Sk 83.22 billion, demand accepted at the auctions was Sk 61.229 billion, which represented 73.6% of the total demand. In 1999, the volume of government bonds issued fell in absolute terms by Sk 5.758 billion compared with the figure for 1998. Total demand for government bonds also fell, by Sk 86.074 billion, due to a gradual reduction in the level of interest yields accepted at the auctions. The Ministry of Finance of the SR started setting limits on the prices and amounts of issues in an effort to lower the level of interest yields. The new method proved successful at government bond auctions. Interest yields accepted at the auctions fell continuously during the whole year, except the period that followed the depreciation of the crown in May. In 1999, the average yield to maturity on the primary market reached 16.994%, representing a marked fall (23.894%) in comparison with 1998. The lowering of yields at auctions was also supported by issues of bonds on foreign markets, which reduced the pressure on government debt financing on the domestic market.

In 1999, the primary market for government bonds underwent a marked qualitative change. The issuer succeeded in lowering the level of interest yields at auctions in government bonds and thus reducing the costs of debt servicing. At the same time, the issuer extended the maturities of these securities, which affected the length of maturity of the whole debt portfolio and created conditions for a further extension of maturities in future.

The total volume of publicly negotiable non-government bonds issued in 1999 reached Sk 1.65 billion, representing a fall of 25% (Sk 2.2 billion) compared with the same period in 1998. The trend of decline in the issue of non-government bonds started in 1996. The volume of non-government bonds issued fell mainly as a result of competition from government bonds.

Secondary Market

The total volume of trading on the secondary market reached, in 239 trading days, Sk 188.4 billion, representing a fall of 37% in



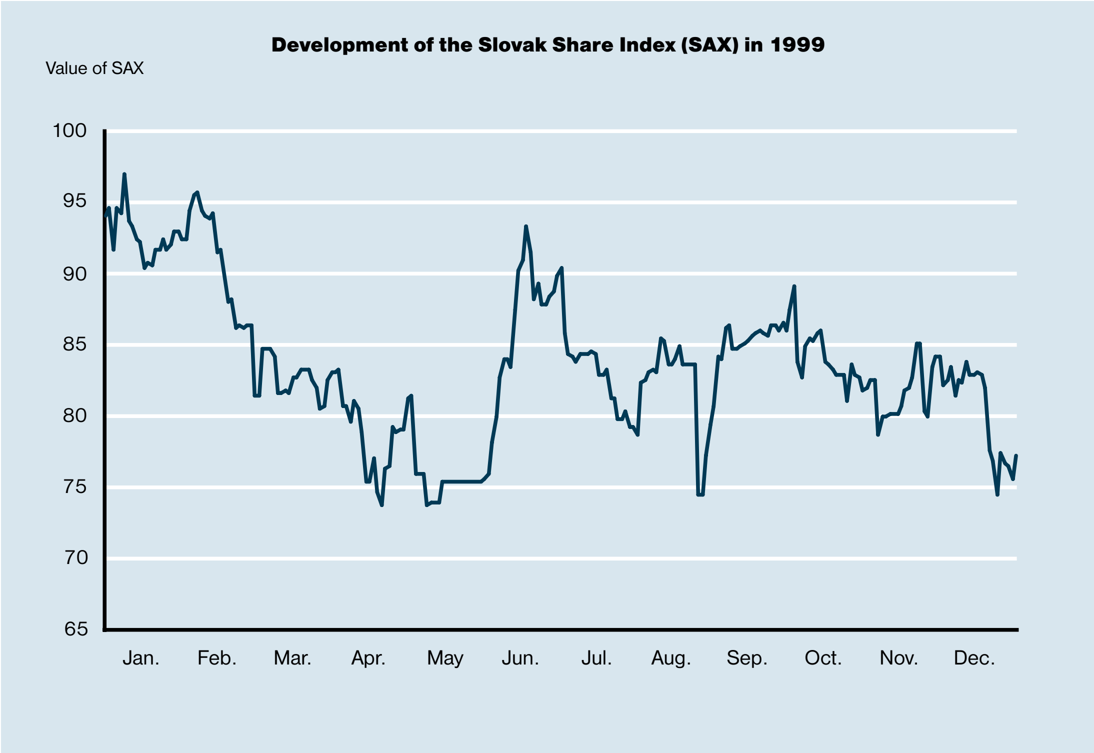
comparison with the previous year. Of the total volume of trading (Sk 188.4 billion), Sk 27.7 billion (14.7%) was in anonymous price-setting contracts and Sk 160.7 billion (85.3%) in direct transactions. In comparison with the previous year, the volume of price-setting transactions increased by 22.5%, reaching an all-time high in the history of the Bratislava Stock Exchange (BCPB). The increase in the volume of price-setting contracts was generated mostly by bond transactions.

Transactions in bonds represented a substantial part of trading on the BCPB floor. The volume of bond transactions totalled Sk 168.2 billion, of which price-setting transactions accounted for Sk 25.9 billion (an increase of 25.1% compared with 1998).

The increase in anonymous transactions in bonds on the BCPB in comparison with 1998 was the first condition for a gradual increase in the liquidity of transactions and the reporting function of prices, which is likely to increase the attractiveness of government bonds for investors. The new system of market makers for government bonds, which was introduced to BCPB at the end of October 1999, is also designed to strengthen the liquidity of the bond market.

The component of SDX (Slovak Bond Index) for bank and corporate bonds ended the last trading day of the year 1999 with an annual yield of 16.6%, at the level of 148.445% of the nominal value of its portfolio, offering an average yield of 15.98% to maturity and a duration of 1.4 years. At the end of the year, the average price of the government bond portfolio in the SDX base stood at 148.159%, while the average yield to maturity reached 15.24% and the period to redemption 0.8 years.

The total volume of trading in shares fell year-on-year by 45.7%, to Sk 20.2 billion, of which price-setting transactions accounted for Sk 1.8 billion, i.e. 8.9%. The value of SAX (Slovak Share Index) fluctuated below its initial level (100 points; as at 14 Sept. 1993) during the whole year. This was due to the low frequency of transactions, which caused the rates of individual base items to fluctuate. The index opened the first trading day of the year at the level of 94.00 points, and a few days later (on 14 January)



reached its yearly maximum (96.88 points) due to increases in the rates of Slovnaft and Slovakofarma shares. The index recorded an all-time low (73.62 points) on 7 May and closed the year at 77.07 points, with a loss of 18%.

During the period under review, the most significant year-on-year changes in the structure of government bonds held by domestic investors occurred in the share of other legal entities (an increase from 9.27% to 12.47%) and in that of commercial banks (an increase from 81.23% to 84.08%). The share of foreign investors remained virtually unchanged, at the year-end level of 1998. During the year, however, it fluctuated between 1.17% and 7.36%.

5.3. Foreign Exchange Market

Operations of NBS on the Foreign Exchange Market

With effect from 1 January 1999, the national currencies of the eleven EMU Member States were replaced by the single European currency (EUR). At the same time, the euro became a reference currency for the Slovak crown. The NBS declared in its monetary programme for 1999 that it would not prevent the exchange rate of the Sk from fluctuation and would intervene only in the presence of excessive volatility.

For the first time, the NBS entered the foreign exchange market in February, by purchasing EUR 103 million from domestic banks in individual transactions.

A month later (on 9 March), the NBS decided to intervene directly in support of the crown exchange rate, when it depreciated in relation to the euro from SKK 43.930 to SKK 44.800/EUR within an hour. The National Bank of Slovakia sold a total of EUR 20 million in support of the Slovak crown.

Due to the hesitant approach of the Government to economic reform and the slack budgetary discipline during the second quarter, the exchange rate of the crown continued to depreciate, to which the NBS responded by conducting further interventions in support of the crown. During this period, the exchange-rate

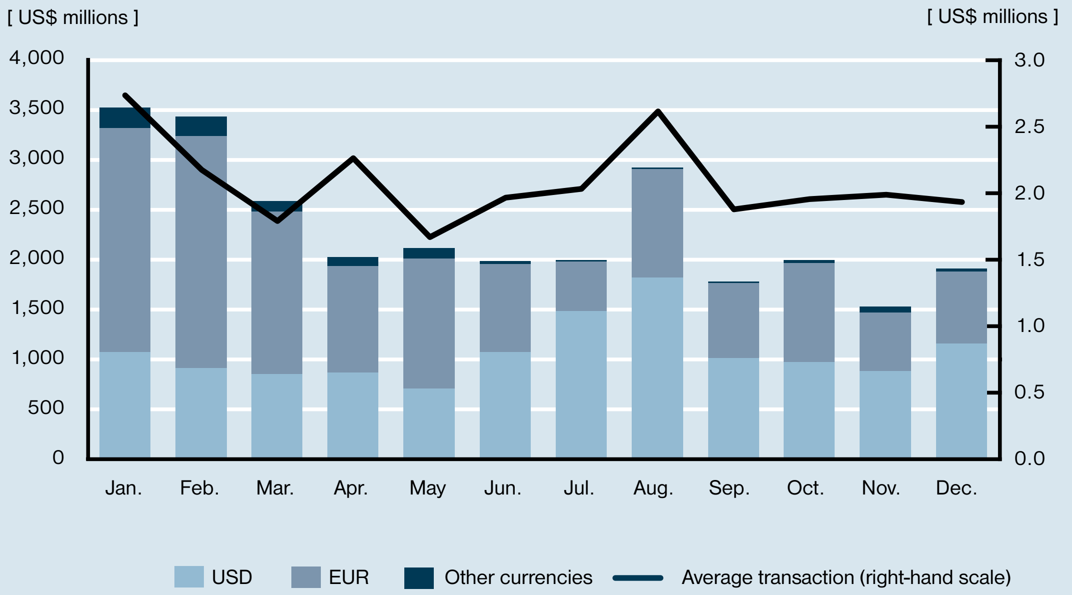
Basic characteristics of the Slovak foreign exchange market in 1999

	USD			EUR			Other currencies			Total		
	Volume (US$ mn)	(%)	Number of trans.	Volume (US$ mn)	(%)	Number of trans.	Volume (US$ mn)	(%)	Number of trans.	Volume (US$ mn)	(%)	Number of trans.
NBS	0.0	-	0	348.9	-	101				348.9	0.5	101
Transactions between Slovak banks (without foreign banks)	12,771.0	46.6	3,875	13,845.8	50.5	8,566	805.5	2.9	816	27,422.4	41.0	13,257
Interbank foreign exchange market: NBS + transactions between Slovak banks	12,771.0	46.0	3,875	14,194.7	51.1	8,667	805.5	2.9	816	27,771.3	41.5	13,358
Transactions between Slovak and foreign banks	25,095.6	64.2	7,682	13,769.3	35.2	4,494	217.7	0.6	259	39,082.6	58.5	12,435
Foreign exchange market in the SR - total	37,866.6	56.6	11,557	27,964.0	41.8	13,161	1,023.2	1.5	1,075	66,853.8	100.0	25,793

value of the crown weakened to SKK 48.200/EUR 1. The NBS sold a total of EUR 90 million in several interventions within a couple of days.

The clear statement made by the Government and the NBS about the restoration of economic stability led to a gradual growth in confidence in the Slovak currency among investors. This was followed by relatively frequent issues of bonds denominated in Slovak crowns by non-resident organisations. During the second half of the year, foreign banks and official institutions issued bonds with a maturity of 1 to 5 years in the total amount of Sk 12 billion. The exchange rate of the crown gradually appreciated during that period. In December, the trend of appreciation accelerated; hence the NBS had to intervene to prevent the Slovak crown from excessive appreciation. Over the course of December, the

Volumes of transactions on the domestic foreign exchange market in 1999 [1/]



1/ Excluding the NBS and foreign banks.

NBS purchased a total of EUR 114 million from commercial banks (of which EUR 72 million in individual transactions).

Interest in the Slovak crown was not an exception during that period; foreign investors also purchased Czech crowns and Polish zloty in expectation of positive economic and political development in the region.

During the year, the exchange rate of the Slovak crown appreciated in relation to the euro by 1.5%. The NBS concluded 101 transactions on the interbank market in the total amount of EUR 327 million, with a balance of EUR 107 million in favour of the NBS.

Interbank Foreign Exchange Market

In 1999, the volume of transactions between Slovak commercial banks totalled US$ 27,422.4 million, representing a decline of 8.2% compared with 1998. Trading between Slovak banks also declined in comparison with the beginning of the year. The number of transactions decreased to 13,257, from 14,508 in 1998. The average number of contracts was 108 per day, with an average amount of US$ 2.1 million per contract (compared with US$ 2.0 million in 1998). Most trading was conducted in EUR (50.5%), followed by USD (46.6%) and other currencies (2.9%).

Trading between Slovak and foreign banks maintained its dominant share of the country's foreign exchange market (58.5%, compared with 53.0% in 1998). The total volume of transactions amounted to US$ 39,082.6 million, representing a fall of 1.1% compared with 1998. Most trading was conducted in US$ (64.2%, compared with 86.2% in 1998), followed by EUR (35.2%, compared with 12.9% in 1998), and other currencies (0.6%). Although trading in US$ maintained its dominant position, its share decreased considerably as a result of the introduction of the single European currency (EUR).

Trading between Slovak and foreign banks resulted in a positive balance of US$ 59.3 million, representing a sharp fall in comparison with the previous year, when the balance reached US$ 388.9 billion. The fall was due to the fact that exchange rate losses became more difficult to predict after the introduction of a floating exchange rate for the Slovak crown.

Volumes of transactions between Slovak and foreign banks in 1999