



NÁRODNÁ BANKA SLOVENSKA  
EUROSYSTEM



# MEDIUM-TERM FORECAST

Q4  
2010

Published by:  
© Národná banka Slovenska

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Approved by the NBS Bank Board  
on 7 December 2010.

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ISSN 1338-1474 (online)



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# 1 SUMMARY

The medium-term forecast of Národná banka Slovenska (NBS) has been updated to take into account new technical assumptions for the external environment, the effect of the Slovak Government's planned measures for improving the performance of public finances, and the latest developments in real economy indicators.

This current medium-term forecast (MTF-2010Q4) was produced on the basis of moderately more adverse assumptions for external demand towards the end of the medium-term horizon as well as estimates of higher external prices and lower oil prices (expressed in euro).

Since proposed government measures had still not been reviewed as at the cut-off date of this forecast, it is assumed that the impact of fiscal consolidation measures will be the same as projected in the previous forecast (with the general government deficit to be reduced by €1.7 billion in 2011).

In the third quarter of 2010, GDP continued to grow in quarter-on-quarter terms, but its level was slightly lower than projected, according to the flash estimate published by the Statistical Office of the Slovak Republic.<sup>1</sup> The main driver of this development was a higher rise in imports, which dampened the contribution of net exports to GDP growth. The fourth quarter of 2010 is expected to see a further quarterly increase in GDP growth. As for the individual components of GDP, household consumption is assumed to record only a moderate increase in 2010, owing to a decline in consumer confidence and the persistently high unemployment rate. With the rise in disposable income bringing about only a modest increase in household consumption, the savings ratio is set to climb. Among the components of domestic demand, general government final consumption is expected to make the largest contribution to GDP growth. Gross fixed capital formation is assumed to continue its decline from the previous year, albeit at a slower pace. Consequently, the total contribution of domestic demand to GDP growth is projected to be only slightly positive. There should, however, be a positive effect from the rebuilding of inventories,

following the substantial destocking recorded in the previous year. As external demand continues to pick up, it should gradually be reflected in an improved export performance and, given the current import intensity, in a rise in this year's imports. Net exports are therefore expected to be one of the main components that make a positive contribution to GDP growth in 2010. The gradual recovery of economic growth is expected to result in the labour market situation improving towards the end of the year. As for price developments, the last months of 2010 have been marked by stagnation. Looking ahead, the price level is assumed to come under upward pressure mostly from food prices.

In the medium-term horizon, the economic situation is expected to be affected mainly by the consolidation measures currently under the Government's consideration. These are assumed to cause a slowdown in GDP growth in 2011 by dampening the contribution of domestic demand. The projected increase in external demand should in subsequent years feed through to growth in exports and, eventually, in imports too. Net exports are expected to contribute positively to GDP throughout the projection horizon. The labour market situation should improve in the medium-term, although in 2011 it is assumed to be negatively affected by reductions in the public sector workforce brought about by consolidation measures. As for inflation, it is expected to accelerate mainly in 2011, amid increasing economic activity and rises in excise taxes and value-added tax.

GDP growth in 2010 is expected to be slightly slower than projected in the previous forecast, owing to a lower contribution of net exports. For 2011, the GDP growth forecast remains unchanged, while for 2012 it is marginally lower due to the expected development of external demand. The inflation rate in 2010 is assumed to rise at a slightly slower pace than previously projected, given lower than expected inflation in prices of food products, energy, and services. The forecast for price developments in subsequent years remains largely unchanged from MTF-2010Q3.

<sup>1</sup> The current GDP forecast is based on data from the SO SR's flash estimate for the third quarter of 2010, which also includes the publication of a revised time series for GDP and employment. However, data on GDP structure and the revisions of individual components of GDP were not available as at the cut-off date of this forecast.



The risks to this medium-term forecast for GDP are the same as were stated in the previous forecast. The main risk continues to be the expected impact of the Government's consolidation measures. One of the upside risks to GDP growth is the substitution of reductions in government investments with private funds and/or with funds drawn from EU structural funds; another is the possible implementation of infrastructure projects. The downside risks include the possibility that the decline in household disposable income is more strongly reflected in lower final consumption, and also that additional consolidation measures, not envisaged in this forecast, are undertaken in the medium term. The risks to the projection for GDP growth remain predominantly on the upside (especially in 2011).

The factors determining the medium-term inflation forecast for 2011 do not include any substantial risks, according to risk assessment results. Among the downside risks to the 2011 inflation forecast are a negative output gap, stagnating domestic demand, and commodity prices not being transmitted to food consumer prices to such a significant extent. The upside risks to the forecast for consumer prices in 2011 include a stronger recovery of the labour market, a sharper rise in commodity prices, and exchange rate developments.

The upside risks to the 2012 forecast have, however, increased. If these risks materialised, the inflation rate at the end of the projection horizon would increase as a result of import price movements, higher energy prices, and the recovery of the labour market and domestic demand.



## 2 TECHNICAL ASSUMPTIONS AND THE INTERNATIONAL ENVIRONMENT

The technical assumptions for the medium-term forecast as well as developments in the international economy were taken from the Eurosystem Staff Macroeconomic Projections for the Euro Area published in December 2010.<sup>2</sup>

The technical assumptions about interest rates and both energy and non-energy commodity prices are based on market expectations, with a cut-off date of 11 November 2010. The average level of short-term interest rates is expected to be 0.8% for 2010, 1.4% for 2011 and 1.7% for 2012. The market expectations for euro area ten-year nominal government bond yields imply an average level of 3.5% in 2010, increasing to 4.0% in 2011 and 4.3% in 2012. The baseline projection takes into account the recent further normalisation of financing conditions and assumes that bank lending rate spreads vis-à-vis the above-mentioned interest rates will remain broadly stable overall. Credit supply conditions are assumed to ease gradually over the projection horizon. As regards commodities, oil prices per barrel are assumed to average USD 79.5 in 2010, USD 88.6 in 2011, and USD 90.7 in 2012. The prices of non-energy commodities in US dollars are assumed to rise by 40.6% in 2010, followed by increases of 19.2% in 2011 and 2.3% in 2012. The bilateral EUR/USD exchange rate is assumed to remain unchanged over the projec-

tion horizon at the average level prevailing in the ten-working day period ending on the cut-off date. This implies a USD/EUR exchange rate of 1.34 in 2010 and 1.39 in 2011 and 2012, and an effective exchange rate of the euro that, on average, depreciates by 5.9% in 2010 before appreciating by 0.8% in 2011.

Compared with the September projections, the December projections assume that oil prices will be higher and that non-energy commodity prices will rise more sharply in both 2010 and 2011.

The global recovery is ongoing but decelerating temporarily, as the previously supportive contributions from inventories and the fiscal stimulus packages are coming to an end. Looking ahead, however, global economic growth is expected to strengthen gradually over the projection horizon. Emerging markets remain the main driver of global economic growth over the projection horizon. At the same time, in major advanced economies growth is expected to be held back by weak labour markets. World real GDP outside the euro area is projected to increase by 5.3% in 2010, by 4.3% in 2011 and by 4.7% in 2012. Growth in the euro area's export markets is estimated to be 11.3% in 2010, 7.2% in 2011 and 7.2% in 2012.

**Table 1 Technical assumptions (annual percentage changes, unless otherwise indicated)**

	Published in	Projection		
		2010	2011	2012
Oil (USD/barrel)	September 2010	78.8	84.0	
	December 2010	79.5	88.6	90.7
Non-energy commodities	September 2010	39.1	11.0	
	December 2010	40.6	19.2	2.3
USD/EUR exchange rate	September 2010	1.32	1.31	
	December 2010	1.34	1.39	1.39

Source: ECB.

<sup>2</sup> More detailed information about the ECB projection is available at [www.ecb.int](http://www.ecb.int).



### 3 MEDIUM-TERM FORECAST FOR THE EURO AREA

Following stronger growth in the second quarter of 2010, real GDP grew by 0.4% in the third quarter. Net exports contributed to growth, while domestic demand also increased, albeit at more subdued rates than in the previous quarter. In the last quarter of 2010, growth is expected to remain weaker than during the first half of the year, as the supportive impact of fiscal stimuli, the inventory cycle and the rebound in trade is diminishing. Looking ahead, economic activity is projected to continue its recovery, led by exports, with domestic demand gradually gathering pace. Private consumption growth is expected to firm gradually over the projection horizon, supported by the projected improvement in employment and increase in related incomes. In addition, the household saving ratio is projected to decline as confidence improves. The unemployment rate is expected first to stabilise, before declining in 2012. Private investment demand is also projected to rise moderately. In line with the ongoing implementation of fiscal consolidation packages, government investment is assumed to be relatively weak. Both exports and imports

are expected to grow more slowly than in 2010. Overall, net trade is projected to make a positive, but diminishing, contribution to GDP growth. Potential GDP growth is assumed to rise slightly, while the output gap is expected to narrow.

With regard to real GDP growth, the projection range for 2010 has narrowed somewhat and shifted towards the upper end of the range given in the September 2010 projections, while the range for 2011 is slightly narrower.

Owing mainly to oil and food price rises, overall HICP inflation is projected to stay close to 2% until early 2011. Thereafter, while imported inflation moderates, domestic price pressures are expected to increase somewhat, reflecting the gradual improvement in activity. The growth rate of the HICP excluding food and energy is projected to increase gradually over the entire projection horizon, reflecting the slowly increasing growth of unit labour costs in the context of improving labour market conditions. Profit margins are projected to continue to widen over the

**Table 2: Projections of selected euro area indicators (average annual percentage changes)**

	Published in	2009	2010	2011	2012
		Actual figures	Prediction for the period		
HICP	September 2010		1.5 – 1.7	1.2 – 2.2	
	December 2010	0,3	1.5 – 1.7	1.3 – 2.3	0.7 – 2.3
Real GDP	September 2010		1.4 – 1.8	0.5 – 2.3	
	December 2010	-4,1	1.6 – 1.8	0.7 – 2.1	0.6 – 2.8
Private consumption	September 2010		0.0 – 0.4	-0.1 – 1.5	
	December 2010	-1,1	0.6 – 0.8	0.4 – 1.4	0.5 – 2.3
Government consumption	September 2010		0.3 – 1.3	-0.1 – 1.1	
	December 2010	2,4	0.5 – 1.3	-0.8 – 0.6	-0.4 – 1.0
Gross fixed capital formation	September 2010		-2.3 – -0.7	-1.6 – 3.0	
	December 2010	-11,3	-1.4 – -0.6	-0.5 – 3.1	0.1 – 5.3
Exports (goods and services)	September 2010		7.4 – 10.0	2.9 – 9.3	
	December 2010	-13,1	9.9 – 11.7	3.7 – 8.7	2.5 – 8.7
Imports (goods and services)	September 2010		5.8 – 8.2	1.6 – 7.8	
	December 2010	-11,8	8.2 – 9.8	2.6 – 7.6	2.3 – 8.1

Source: ECB.



projection, having fallen steeply during the recession. Indirect taxes are also assumed to make a positive contribution to HICP inflation over the projection horizon.

With regard to HICP inflation, the projection range for 2010 is unchanged in comparison with the September projections, while the range for 2011 is marginally higher.



## 4 MEDIUM-TERM FORECAST FOR SLOVAKIA

The revised NBS medium-term forecast takes into account (in addition to the mentioned technical assumptions) new developments in real economy indicators and the effect of the Slovak Government's planned measures for improving the performance of public finances.

As in MTF-2010Q3, NBS took into consideration the proposed package of government measures aimed at reducing the 2011 general government deficit by €1.7 billion. Since the general government budget had not been approved before the preparation of MTF-2010Q4, it may be assumed that if the fiscal measures ultimately adopted differ in form from those incorporated in this forecast, the next forecast may have to revise the projections for macroeconomic development in the medium-term horizon.

### 4.1 THE REAL ECONOMY

#### CURRENT ACCOUNT

In the balance of payments **current account**, the **trade balance** for the third quarter of 2010 was worse than projected in MTF-2010Q3, since imports rose more strongly than expected. The import figures probably reflected higher restocking, particularly the increased imports of semi-finished goods. Since the upsurge in imports reported in the third quarter is largely ascribed to stocking up, import levels are not expected to rise in the months to come. Nevertheless, they have substantially undermined the trade balance for the whole of 2010. In 2011 and 2012, nominal imports are expected to rise slightly as a result of changes in prices (worsened terms of trade), and therefore the current medium-term forecast for the trade balance is less favourable than the previous forecast.

As stated in MTF-2010Q3, exports and imports are expected to return to growth in the years 2010 to 2012, after declining by around 20% in 2009 in year-on-year terms (taking into account expected external demand and the latest developments).

The main **risk** to the trade balance forecast is the future development of external demand, as well as the timing of individual infrastructure projects. Another risk is if import intensity develops differently than expected, which could result in higher imports.

Forecasts for **other current account components** have remained unchanged in the light of current developments.

In line with the previous forecast, the **current account** deficit to GDP ratio between 2010 and 2012 is expected to improve also in year-on-year terms, mainly because of steady growth in external demand.

#### LABOUR MARKET

The forecast for employment in 2010 remains unchanged from MTF-2010Q3, given that the Slovak Statistical Office's flash estimate for employment in the third quarter was in line with NBS expectations, and also taking into account current trends in monthly indicators. The medium-term forecasts for labour market indicators are also unchanged, still taking into account the same assumptions for reductions in the public sector workforce. As regards **wages**, the monthly statistics for selected sectors indicate that wage levels are in line with the expectations of MTF-2010Q3. Since the basic macroeconomic indicators for the medium-term horizon are substantially unchanged, the forecasts for compensation per employee also remain the same.

**Employment** levels will be affected by growth in economic activity; the labour market is expected to recover gradually, but will experience a partial correction in 2011 owing to the effect of fiscal consolidation measures in the public sector. The forecast assumes that cuts in public sector expenditure will be achieved equally (50:50) through redundancies and wage reductions. In the medium-term horizon, the number of employed persons is projected to increase in comparison with the levels recorded during the crisis, albeit at a slower pace than the recovery

of economic performance. This is expected to result in higher labour productivity growth and, to a lesser extent, in rising compensation per employee. The dynamics of these indicators are also assumed to reflect, on one hand, the expected reduction in the public-sector salary bill and and, on the other hand, an increase in payroll contributions.

The level of **unemployment** is expected to respond only gradually to the economy's improving performance, since its decline will be dampened by an increase in the number of people in the productive age group (especially in 2011, projected on the basis of demographic trends), despite the expected rise in the number of employed. The unemployment figures are also expected to be adversely affected by cuts in the public sector workforce in 2011. In the medium-term horizon, the unemployment rate is assumed to fall by approximately 0.5 of a percentage point from where it stands at present.

The risks to the forecast for labour market indicators are mostly on the downside, in that the labour market situation may improve owing to

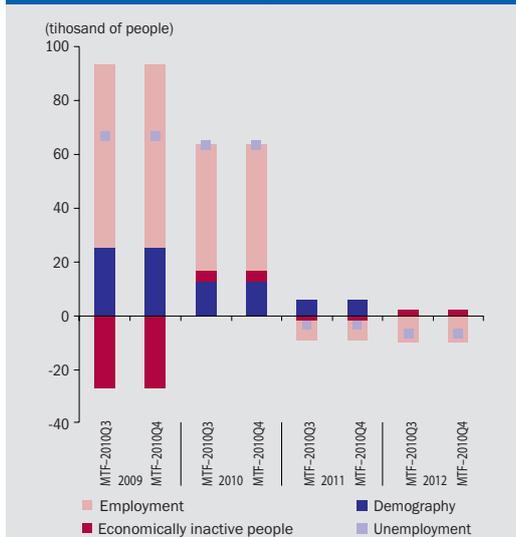
stronger economic growth as well as to the implementation method and impact of fiscal consolidation measures. Developments in employment and wages will depend on the extent to which public expenditure is trimmed through reducing the workforce and wages. The adverse risks include the way in which business entities cope with rising labour costs. It is possible that lower corporate profits (with the price of labour pushed up by higher payroll contributions and with profit margins absorbing part of the increase in VAT) may feed through to lower employment or to downward pressure on wage settlements and variable wage components, which in turn would lead to slower growth in compensation per employee. The unemployment rate will also depend on the age structure of the public sector workers who are laid off, since the release of those who are already at retirement age will not put upward pressure on unemployment.

## GDP

**GDP** for the third quarter of 2010 and its growth in year-on-year terms were slightly lower than projected in NBS's September forecast, according to the SO SR flash estimate (taking into account a revision of the GDP time series). Real GDP growth for the whole of the year has therefore slowed marginally, largely owing to the lower contribution of net exports. The GDP growth forecast for 2011 remains unchanged from MTF-2010Q3, while the forecast for 2012 has been revised down slightly amid the expectation of slower growth in global demand and, consequently, a more gradual increase in Slovak exports. As for the structure of GDP, the changes in comparison with the previous forecast are negligible.

The slowdown in GDP growth in the third quarter of 2010 was caused by a lower contribution of net exports, which in turn stemmed mainly from higher imports, according to the monthly foreign trade figures. The third-quarter upsurge in imports is expected to show up to some extent in higher inventories and could represent future consumption, investments, or exports. Looking at the structure of GDP, private consumption is expected to continue stagnating in 2010, while general government consumption will probably rise. Gross fixed capital formation is assumed to decline this year. Positive contributions to GDP at constant prices in 2010 are expected from net

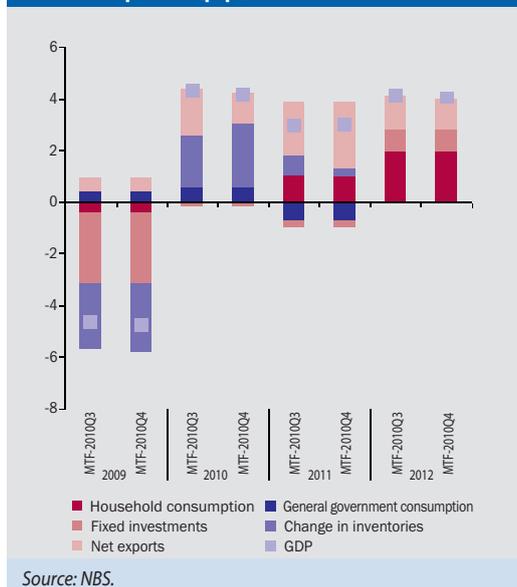
**Chart 1 Contributions of labour market indicators to unemployment**



Source: SO SR and NBS calculations.

Note: The contributions of individual labour market indicators are considered from the view of their effect on unemployment: for example, unemployment comes under upward pressure from a decline in employment, population growth (a higher number of people of productive age), and a decrease in the economically-inactive population.

**Chart 2 Contributions to GDP growth at constant prices (p.p.)**



exports and the post-crisis rebuilding of inventories in the economy, as well as from general government consumption.

In the medium-term horizon, the economic situation is expected to be affected mainly by the introduction of the Government's consolidation measures at the beginning of 2011 and the projected development of external demand. Domestic demand is assumed to continue stagnating in 2011 amid lower general government consumption, lower government investments, and a no more than moderate rise in private consumption. In 2012, GDP growth will be driven by net exports, private consumption, and fixed investments.

#### Domestic demand

After contracting in 2009, **household final consumption** is expected to stagnate in 2010. The current monthly indicators – falling or stagnating retail sales, ebbing consumer confidence and, in particular, the uncertainty among households about the future development of unemployment and about their financial situation – do not imply a substantial increase in private consumption this year. In the light of the current labour market situation, only slight growth in household disposable income can be expected and the savings ratio is assumed to remain at a

high level in the near term. In the medium-term horizon, labour productivity growth from previous years could feed through to higher wages, which, together with a gradual rise in employment, creates scope for an increase in real household consumer spending. Private consumption growth will be held back as real household income comes under downward pressure from the expansion of assessment bases for social and health contributions, the reduction of compensation in the general government sector, and the raising of indirect taxes. Since households, despite having lower disposable income, may be expected to implement part of their consumption plans, the forecast also assumes a decline in the currently high savings ratio.

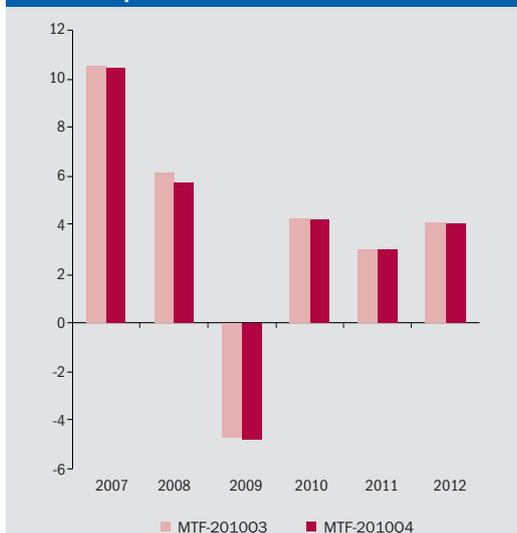
Investment activities slumped in 2009 owing to idle production capacity and uncertainty among firms about the future economic situation and about demand for products and services, as well as because of problems in financing investment activities. With these effects gradually waning, it is expected that the negative tendencies in **gross fixed capital formation** will lessen in 2010 and that private non-residential investments in 2011 will recover more strongly. Capital formation is also expected to be boosted by investment in infrastructure (2nd package of PPP projects, investments related to flood damage removal) and investment in the car industry, whose main impact on investment development will be felt in 2010. Owing to the base effect, the year-on-year growth in gross fixed capital formation will shrink in 2011. A further drag on investment activity in 2011 is the assumed reduction in general government investment as a result of fiscal consolidation measures.

In the current forecast, the change in inventories is expected to make a significant positive contribution to GDP growth in 2010, while its contribution in the medium-term horizon should be negligible.

#### Net exports

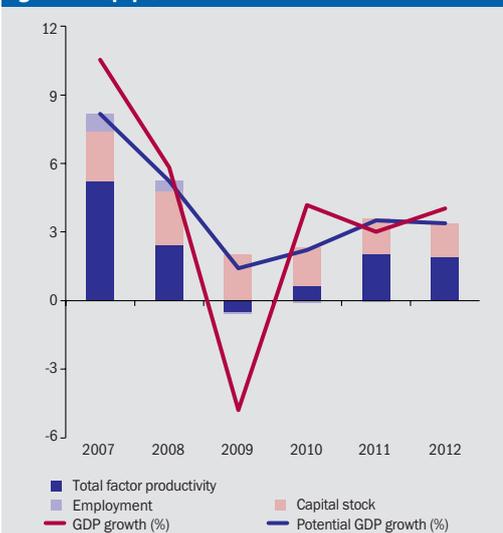
Based on monthly foreign trade statistics, import growth for 2010 is projected to be moderately stronger, therefore implying a decline in the positive contribution of net exports to GDP growth in comparison with the previous forecast. As in MTF-2010Q3, exports are assumed to continue rising in the medium-term horizon, although their pace of growth should decline slightly, es-

**Chart 3 Forecast for GDP growth at constant prices (%)**



Source: NBS.

**Chart 4 Contributions to potential GDP growth (p.p.)**



Source: NBS.

pecially in 2012, amid a slower increase in external demand. The slightly lower rise in exports will – through existing import intensity – eventually be reflected in a decline in imports, and therefore the impact of lower world demand on GDP growth is assumed to be only modest. Export performance in 2011 will receive a significant boost from the expansion of car industry production. At the same, the forecast for imports of goods and service incorporates the assumption that domestic demand will be dampened by fiscal consolidation measures.

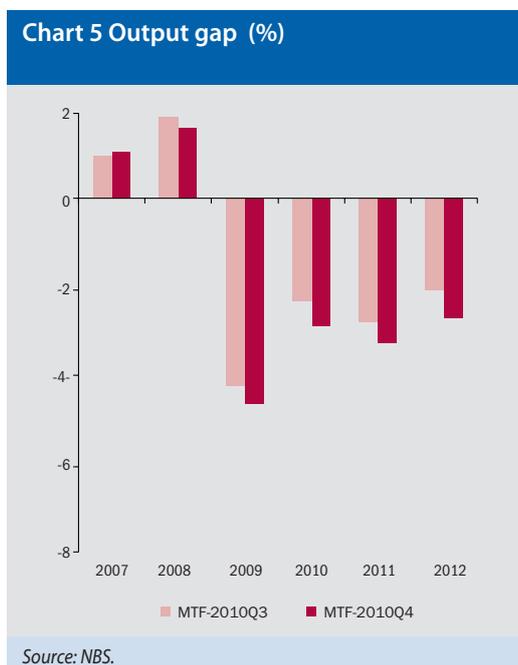
The main **risk** to the GDP forecast is the expected impact of consolidation measures and the possible introduction of additional measures. A downside risk to the growth forecast is that the decline in household disposable income has a more pronounced negative effect on final consumption in the event that savings are utilised to a lesser extent than expected. Another downward risk to disposable income growth could be if employers meet higher payroll contributions by reducing wage growth over the near term. One of the upside risks to GDP growth is the substitution of reductions in government investments with private funds and/or with funds drawn from EU structural funds; another is the possible implementation of infrastructure projects.

The **risks** to GDP growth (especially in 2011) therefore appear to be more on the upside.

#### POTENTIAL GDP AND THE OUTPUT GAP

The projection for potential GDP remains unchanged from that given in MTF-2010Q3. The potential growth of the Slovak economy in the medium-term horizon is gradually accelerating and it is expected to be driven mainly by rising total factor productivity (while the contribution of potential employment remains close to zero).

While the outlook for potential GDP remains the same, the output gap forecast has been revised from that given in MTF-2010Q3. This change is a direct consequence of the incorporation of the revised time series for real GDP, which was published together with the flash estimate for third-quarter GDP. As a result, around 0.5 of a percentage point was shaved off the unrevised real GDP figure for the first half of 2010, and thus the output gap forecasts for the years 2010-2012 have been widened by around half of a percentage point. Given that only the flash estimate of GDP (not including data on GDP structure) was available when this forecast was being prepared and that only overall GDP was revised, NBS reflected the extent of the revision in the output gap. How-



ever, based on an analysis of the revised structure of the historical GDP time series and the publication of detailed information about the economy's developments in the third quarter, the outlook for both potential and GDP and the output gap may be revised.

## 4.2 INFLATION

The year-on-year inflation rate since July 2010 has been at around 1%. As measured by the Harmonised Index of Consumer Prices (HICP), the inflation rate has been characterised by opposing developments among the basic components of the inflation structure. While the annual inflation of goods prices has come down slightly since August 2010, the year-on-year price inflation for services has recorded a modest rise. The inflation figure for goods prices includes a slowdown in annual food price inflation, as well as a slower year-on-year decline in prices of both non-energy industrial goods and energy.

Compared with the MTF-2010Q3 forecast, the actual inflation rate was on average lower in recent months, owing to the lower than expected price inflation for food, energy, and services. The deceleration of service price inflation continued

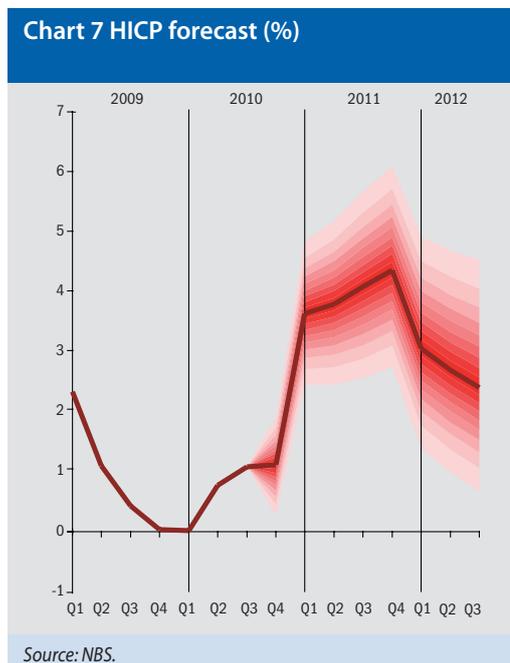
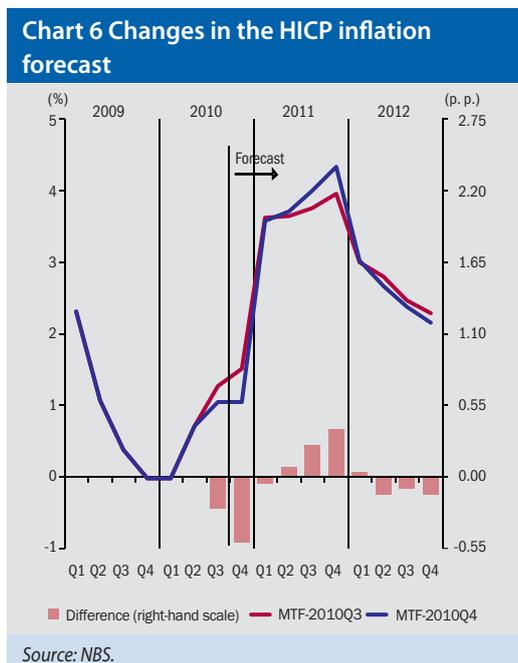
to be driven by stagnating demand and cautiousness among consumers, as confirmed also by developments in retail sales. With the actual inflation figures undershooting the projections given in MTF-2010Q3, the inflation rate at the end of 2010 will be lower.

This current forecast takes into account new assumptions regarding prices of energy and agricultural commodities, as well as the USD/EUR exchange rate. Compared with the previous forecast, MTF-2010Q4 envisages strengthening of the EUR/USD exchange rate and an acceleration of price inflation for certain key agricultural commodities in 2011. The forecast has reflected these assumptions by revising up the food price inflation figures for 2011 and 2012 from those given in MTF-2010Q3. The sharper rise in food prices is expected to lead indirectly to a slight rise in service price inflation. The increase in prices of industrial goods in 2011 is assumed to be lower than projected in the previous medium-term forecast. Like MTF-2010Q3, the December medium-term forecast assumes that excise taxes and VAT will increase and new fees will be introduced, thereby adding approximately 1 percentage point to the average expected inflation rate in 2011 and 0.1 of a percentage point in 2012. Therefore, neither the structure nor level of overall inflation are changed from MTF-2010Q3.

The upward revision of food price inflation from the projection given in the previous forecast is based on the stronger than forecasted rise in agricultural commodity prices (wheat, milk, slaughter pigs). The current forecast assumes that the transmission of agricultural price movements to consumer prices will occur at the same rate as in the past.

Although prices of **non-energy industrial goods** are expected to accelerate gradually in 2011, their level should remain relatively low owing to the projected strengthening of the EUR/USD exchange rate and the slower increase in prices of non-energy industrial goods in the euro area. The inflation of medicine prices slowed down considerably after the form of their regulation was changed in 2010, and this was taken into account for the whole of the projection horizon.

Prices of **services** continue to reflect the slowdown in economic activity in 2009, as well as the



low consumer demand recorded this year. Their accelerated increase in comparison with 2010 will be a result of higher taxes and food prices.

**Energy prices** are expected to rise more sharply in 2011 than in 2010, owing to the projected increase in prices of gas, electricity and heat, while the assumptions for inflation of these prices remain the same as in MTF-2010Q3.

The factors determining the inflation forecast for 2011 do not contain any substantial **risks**, according to risk assessment results. Compared with the previous forecast, the degree of **risk** inherent in these factors remains unchanged for 2011, and the crystallisation of these risks would put only moderate upward pressure on the inflation rate. Downside risks to the 2011 forecast include the approval process for fiscal consolidation measures (abstaining from the planned rise in the excise tax on beer will lower the contribution to inflation), a negative output gap, stagnating domestic demand, and commodity prices possibly not being transmitted to food consumer prices to such a significant extent. Among the upside risks to the forecast for consumer prices in 2011 are stronger improvements in the labour market, a sharper rise in commodity prices,

and exchange rate developments. The uncertainty is heightened by the situation regarding regulated prices, since this forecast was prepared before the publication of regulatory decrees for 2011 by the Regulatory Office for Network Industries.

The potential risks to the 2012 forecast have, however, increased. If these risks materialised, they would push up the inflation rate at the end of the projection horizon by approximately 0.2 of a percentage point. The upside risks include import prices, which may accelerate amid a stronger recovery of economic activity and an acceleration of energy price inflation (possibly related to a possible higher increase in regulated energy prices). The domestic causes of upward pressure on the price level include the risk of a stronger than forecasted recovery of the labour market and domestic demand.

(Footnotes)

1 The current GDP forecast is based on data from the SO SR's flash estimate for the third quarter of 2010, which also includes the publication of a revised time series for GDP and employment. However, data on GDP structure and the revisions of individual components of GDP were not available as at the cut-off date of this forecast.

**Table 3 Medium-term forecast (MTF-2010Q4) – main macroeconomic indicators**

	Actual data	Projection in MTF-2010Q4			Difference versus MTF-2010Q3		
	2009	2010	2011	2012	2010	2011	2012
<b>Prices (annual percentage changes)</b>							
HICP inflation (average)	0.9	0.7	3.9	2.6	-0.2	0.1	-0.0
CPI inflation (average)	1.6	0.9	3.8	2.6	-0.1	0.0	0.0
ULC <sup>1)</sup> (compensation per employee at current prices / labour productivity ESA 95 at constant prices)	7.1	-1.8	2.2	2.8	0.1	0.0	0.0
Labour productivity ESA 95 (GDP at constant prices / employment ESA 95)	-2.3	5.7	2.9	3.5	-0.2	-0.0	-0.2
Compensation per employee (current prices)	4.7	3.8	5.2	6.4	0.0	0.0	-0.1
<b>Economic activity (annual percentage change; unless otherwise indicated)</b>							
Real GDP	-4.8	4.2	3.0	4.0	-0.1	0.0	-0.1
Final consumption of households	-0.7	0.1	1.9	3.8	0.0	-0.1	0.0
Final consumption of general government	2.8	3.2	-3.9	0.1	0.0	-0.1	0.1
Gross fixed capital formation	-10.5	-0.4	-0.9	3.6	0.0	0.0	0.0
Exports of goods and services	-16.5	13.3	7.4	7.6	0.0	-0.1	-0.3
Imports of goods and services	-17.6	12.4	4.9	6.9	0.7	-0.7	-0.2
Gross real disposable income of households	-0.2	0.9	0.5	3.8	0.0	-0.6	0.0
Output gap (% of the potential output)	-4.6	-2.8	-3.3	-2.7	0.6	-0.6	-0.6
<b>Labour market (annual percentage change)</b>							
Employment, based on ESA 95	-2.5	-1.5	0.1	0.5	0.0	0.0	0.0
Unemployment rate, LFSS-based <sup>2)</sup> (%)	12.1	14.3	14.2	13.9	0.0	0.0	0.0
<b>Balance of payments</b>							
Economic openness (% of GDP)	139.8	156.1	159.3	163.1	0.7	-0.5	-0.6
Balance of trade (% of GDP)	1.9	0.8	2.1	2.7	-0.5	-0.2	-0.2
Balance of services (% of GDP)	-2.0	-1.6	-1.3	-1.1	0.0	0.0	0.0
Current account (% of GDP)	-3.2	-3.1	-1.3	-0.4	-0.5	-0.1	-0.2
Current and capital account (% of GDP)	-2.5	-1.6	0.5	1.5	-0.5	-0.2	-0.2

Source: NBS.

1) ULC – unit labour costs.

2) LFSS – Labour Force Sample Survey.