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EUROSYSTEM



MEDIUM-TERM FORECAST

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1 SUMMARY

The December edition of the Medium-Term Forecast of Národná banka Slovenska (MTF-2011Q4) is based on revisions to the technical assumptions for the external environment and on the latest information from real economy indicators. It was produced using revised quarterly national accounts data¹ and taking into account estimates of higher oil prices, lower external prices and slower growth in external demand.

According to the flash estimate of the Slovak Statistical Office (SO SR), Slovakia's GDP growth² in the third quarter of 2011 was slightly higher than projected in the previous NBS Medium-Term Forecast published in September (MTF-2011Q3). The main cause of this positive development was probably the higher contribution of net exports, and this view is supported by the available monthly statistics. However, GDP for the year as a whole is expected to be somewhat more moderate, owing to the dampening effect of lower external demand towards the year-end along with low domestic demand. The upturn in the labour market continued to be slightly stronger than projected, mainly due to an increase in employment in the industry sector.

Economic growth in 2011 is expected to be lower than in 2010, reflecting the slower rise in external demand and the continuing decline in domestic consumption demand. Even though Slovakia's trading partners are reporting slower GDP growth, the country's main driver of growth will continue to be net exports, with their positive contribution being largely attributable to the low level of imports. Although the improvement in the labour market situation is being reflected in household income, the persisting uncertainty about the future situation is expected to ensure that the household saving rate remains high. As a result, the downward trend in household consumption is assumed to continue in the near-term horizon. General government consumption is also expected to make a negative contribution to economic growth, as public spending cuts are implemented. The only component of domestic demand that is projected to support growth in 2012 is fixed investment. As economic growth slows towards the year-end,

employment growth is expected to decelerate, too, although the full-year change in employment should reflect mainly the positive developments in previous quarters. Prices are assumed to stabilise gradually, after rising sharply at the beginning of the year when the annual rate of change in prices of goods and services increased.

In 2012, the slowdown in economic growth is expected to continue, chiefly on account of the projected moderation in the economy's export performance amid lower external demand. In 2013, however, external demand is expected to follow a slowly increasing path, and growth should rebound to a moderately higher level. The positive contribution of net exports is expected to diminish in the medium-term horizon, as household consumption picks up and puts upward pressure on the amount of imports. The lower contribution of net exports should be offset by a higher contribution of domestic demand, reflecting not just the effect of stronger final consumption, but also the rise in investments in line with economic growth. Slower economic growth in the medium-term horizon is expected to be reflected in labour market indicators, and alongside the fading of the effects of indirect tax cuts in 2011, it should also lead to a lowering of inflation.

GDP growth for the whole projection horizon has been revised down from the previous forecast. As a result of the projected deceleration in external demand, export performance is expected to decline most markedly in 2012. The situation in the domestic side of the economy is likewise assumed to be more negative, amid lower household consumption and more moderate investment growth. As the GDP growth forecast has been revised down from MTF-2011Q3, the situation in the labour market is expected to be more difficult than previously envisaged and inflation is assumed to be lower over the projection horizon.

The risks to the GDP forecast continue to be on the downside over the projection horizon. The most significant risk is that the debt crisis in Europe escalates and results in a more pronoun-

¹ The revision of the time series and its impact on the forecast is described in Box 2: Revision of the national accounts.

² The current GDP forecast is based on data from the SO SR's flash estimate for the third quarter of 2011, which includes published data on GDP and employment. Data on the structure and individual components of GDP were not available as at the cut-off date of this forecast.



ced slowdown or decline in external demand.³ Another downside risk is the implementation of further consolidation measures in the medium-term horizon.

The risks to the inflation forecast for 2012 are balanced, while for 2013 they are more on the upside. The implementation of necessary fiscal consolidation measures in certain euro area countries, but also in Slovakia, represents an upside

risk, since any increase in indirect taxes or administered prices that exceeds current projections could push up inflation. The risk of higher inflation in 2012 may, however, be mitigated by lower than expected external demand or a more marked deterioration in the labour market situation. A risk specific to 2012 is a possible further rise in heat prices as from January, owing to a lower than expected increase in heat prices during the course of 2011.

³ The risk of lower external demand is looked at more closely in Box 1: Scenario of a further slowdown in external demand growth.



2 TECHNICAL ASSUMPTIONS AND THE INTERNATIONAL ENVIRONMENT

The NBS Medium-Term Forecast follows the technical assumptions and international environment projections set out in the Eurosystem's December forecast (Eurosystem Staff Macroeconomic Projections for the Euro Area).⁴

The technical assumptions about interest rates and commodity prices are based on market expectations, with a cut-off date of 17 November 2011. The average level of short-term interest rates is expected to reach 1.4% for 2011, 1.2% for 2012, and 1.4% for 2013. The market expectations for euro area ten-year nominal government bond yields imply an average level of 4.4% in 2011, 5.3% in 2012 and 5.6% in 2013. Reflecting the path of forward market interest rates and the gradual pass-through of changes in market rates to lending rates, both short-term and long-term bank lending rates are expected to gradually increase further over the entire projection horizon. Credit supply conditions are expected to weigh negatively on activity. As regards commodity prices, the price of a barrel of Brent crude oil is assumed to average USD 111.5 in 2011, USD 109.4 in 2012 and USD 104.0 in 2013. The prices of non-energy commodities in US dollars are assumed to rise by 17.8% in 2011, to fall by 7.3% in 2012 and to increase by 4.3% in 2013. The bilateral EUR/USD exchange rate is assumed to remain unchanged over the projection horizon at the average level prevailing in the two-week period ending on the cut-off date. This implies an exchange rate of EUR/USD 1.40 in 2011 and

EUR/USD 1.36 in 2012 and 2013, and an effective exchange rate of the euro that, on average, remains unchanged in 2011 and decreases by 0.9% in 2012.

Compared with the projections published in September, oil prices are revised up in the December forecast, while the weaker exchange rate of the euro against the dollar should be reflected in a higher rise in oil prices in euro terms; by contrast, prices of non-energy commodities are expected to increase more moderately in 2011, to decline in 2012, and to rise in 2013.

The momentum of global growth weakened in the course of 2011. In the second half of the year the positive impetus from the unwinding of supply chain disruptions in the aftermath of the natural disasters in Japan was thwarted by renewed global financial market tensions, largely driven by the intensification of the sovereign debt crisis in the euro area. This eroded consumer and business confidence worldwide. Looking ahead, a gradual recovery is expected, although headwinds, such as the continued need to repair balance sheets and the weakness in housing and labour markets, imply a prolonged period of sluggish growth, particularly in advanced economies. In emerging economies, growth is continuing at a rather strong pace, but is expected to lose momentum, owing to earlier policy tightening aimed at mitigating financial imbalances and price pressures, as well as expected

Table 1 Technical assumptions

	Published in	Projection for			
		2010	2011	2012	2013
Oil (USD/barrel)	September 2011	–	110.1	106.5	–
	December 2011	79.6	111.5	109.4	104.0
Non-energy commodities (annual percentage changes)	September 2011	–	19.6	-0.8	–
	December 2011	37.1	17.8	-7.3	4.3
USD/EUR exchange rate	September 2011	–	1.42	1.43	–
	December 2011	1.33	1.40	1.36	1.36

Source: ECB.

⁴ Further information about the Eurosystem projections is available at www.ecb.int.



weaker foreign demand and adverse spillovers from the global financial turbulence. World real GDP growth outside the euro area is projected to decrease to 4.1% in 2011 and 3.9% in 2012 before increasing to 4.5% in 2013. The projected pace of

growth in 2012 has therefore been revised down from the previous forecast. Growth in euro area foreign demand is estimated to decline, to 6.4% in 2011 and to 4.8% in 2012, before increasing to 6.9% in 2013.



3 MEDIUM-TERM FORECAST FOR THE EURO AREA

Euro area real GDP grew only moderately in the third quarter of 2011, rising by 0.2% in quarter-on-quarter terms, which is the same rate as recorded in the second quarter. The weak underlying growth momentum has increasingly reflected the impact of the sovereign debt crisis in the euro area and the associated tightening of the fiscal stance in some euro area countries. On the domestic side, the adverse impact of increased uncertainty related to intensified tensions in financial markets in the euro area resulted in a substantial deterioration in business and consumer confidence, a sharp decline in equity prices and a worsening of financing conditions for households and non-financial corporations. As foreign demand also turned weaker in 2011, external factors are not expected to offset the adverse impact of these domestic factors in the near term. Looking ahead, assuming that the financial crisis does not intensify further, real GDP growth is expected to pick up during the course of 2012 and to improve somewhat further in 2013. The recovery is expected to be supported by a strengthening in global growth, and a decline

in energy and food price inflation supporting real incomes, as well as the favourable impact on domestic demand of the low interest rates and of the measures to restore the functioning of the financial system. Compared with the ECB staff macroeconomic projections published in September, there is a narrowing of the range of the real GDP growth projection for 2011 and a significant downward revision of the range for 2012.

Driven by past hikes in commodity prices and, to some extent, by increases in indirect taxes, the overall euro area HICP inflation rate is projected to remain above 2% in the first quarter of 2012. Thereafter, it is expected to moderate considerably. This pattern largely reflects a sharply decreasing contribution from energy prices, as a result of the fading-out of the impact of past increases in oil prices and the assumed gradual decline in crude oil prices over the projection horizon. Food price inflation is expected to moderate from mid-2012, once the pressures currently in the pipeline have passed through. Finally, HICP inflation excluding food

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

	Published in	Actual figures	Prediction for		
		2010	2011	2012	2013
HICP	September 2011	–	2.5 – 2.7	1.2 – 2.2	–
	December 2011	1.6	2.6 – 2.8	1.5 – 2.5	0.8 – 2.2
Real GDP	September 2011	–	1.4 – 1.8	0.4 – 2.2	–
	December 2011	1.8	1.5 – 1.7	-0.4 – 1.0	0.3 – 2.3
Private consumption	September 2011	–	0.3 – 0.7	0.0 – 1.6	–
	December 2011	0.8	0.3 – 0.5	-0.4 – 0.6	0.0 – 1.8
Government consumption	September 2011	–	-0.2 – 0.8	-0.7 – 0.5	–
	December 2011	0.5	-0.3 – 0.5	-0.5 – 0.7	-0.3 – 1.3
Gross fixed capital formation	September 2011	–	2.2 – 3.6	0.8 – 5.4	–
	December 2011	-0.6	1.6 – 2.4	-1.6 – 1.8	-0.5 – 4.3
Exports (goods and services)	September 2011	–	5.6 – 8.4	2.3 – 9.7	–
	December 2011	10.8	5.4 – 7.2	0.3 – 6.1	2.1 – 8.9
Imports (goods and services)	September 2011	–	4.7 – 7.3	2.0 – 9.2	–
	December 2011	9.2	4.0 – 5.4	-0.5 – 5.1	1.7 – 8.1

Source: ECB.



and energy is projected to increase only slightly, reflecting relatively weak domestic demand and contained labour costs. Increases in administered prices and indirect taxes are expected to contribute substantially to HICP inflation in 2011 and 2012, reflecting ongoing fiscal consolidation. The impact in 2013 is expected to be smaller. The annual growth rate of compensation per employee is expected to slow in the first half of 2012, largely reflecting the impact of one-off payments in the first half of 2011. The annual growth rate of compensation per employee is expected to pick up in the second half of 2012 and to stabilise thereafter. This pattern reflects the impact of offsetting factors. On the one hand, upward pressures would stem from past increases in consumer price inflation. On

the other hand, the general slowdown in economic activity and the persistently weak labour market conditions are expected to exert downward pressure on wages. The growth rate of unit labour costs is expected to increase somewhat in 2012 and to ease subsequently. This profile reflects a cyclical drop in productivity growth in 2012 and a subsequent increase in 2013. The growth of profit margins is expected to remain low throughout 2011 and 2012, on the back of subdued aggregate demand and accelerating unit labour costs. In 2013 profit margins are expected to recover as activity picks up.

Compared with the September projections, the projection ranges for 2011 and 2012 have been revised slightly upwards.



4 MEDIUM-TERM FORECAST FOR SLOVAKIA

The December Medium-Term Forecast is based on revised quarterly national accounts data and on the same technical assumptions that the ECB uses in its projections.⁵ The revision of the time series did not significantly affect the forecast for the real economy, although it did have a marked effect on the forecast for labour market indicators in 2011. As regards assumptions about the external environment, the main revision in the current forecast is lower growth in external demand, particularly in the short-term horizon. This translates into a deceleration of Slovakia's economic growth over the projection horizon, but particularly in 2012.

4.1 THE REAL ECONOMY

CURRENT ACCOUNT

In the balance of payments current account for the third quarter of 2011, exports and imports continued to increase, although their rates of growth were lower than in the first half of the year. With external demand expected to carry on rising, albeit more slowly than in 2011, exports and imports can be assumed to continue growing – with trade balance surpluses – in the periods ahead. Despite lower exports, the trade balance for the full year is expected to be better than projected in the previous forecast, mainly due to lower imports of semi-finished goods, which may reflect a response from exporters to persisting negative sentiment. Since this effect is not assumed to continue in the near-term, the main influence on the trade balance is expected to be a relatively marked slowdown in external demand (the difference in comparison with MTF-2011Q3 being 4.2 percentage points over the projection horizon), which alongside domestic demand developments in 2012 should result in the trade balance remaining almost unchanged. The projected trade balance for 2013 has been revised down from the previous forecast.

The main risk to the trade balance forecast is a further slowdown in external demand; an indicator of such development could be lower-than-projected imports of semi-finished goods in the

third quarter of 2011, provided that this reflects firms' preparations for lower demand in the future.

With the latest figures for the services balance showing both receipts and expenditure to be moderately lower than expected, it may be assumed that the balance will remain unchanged in the next period. Decelerated drawing on EU funds affected the estimate for the current transfers balance in 2011; the assumptions for the level of drawing in the following years remained unchanged.

In line with the previous forecast, the current account to GDP ratio in the years 2011 to 2013 is expected to improve in year-on-year terms. In comparison with MTF-2011Q3, the ratio is assumed to develop in the same way as the trade balance.

LABOUR MARKET

According to the SO SR's flash estimate, employment growth in the third quarter of 2011 was moderately higher than projected and reflected faster economic growth. Employment developments at the sectoral level can only be evaluated from monthly indicators, which suggest that employment growth was driven mainly by a rising number of workers in the industry sector.⁶ The labour market in other sectors under review also showed a gradual improvement during 2011. Towards the end of the year, however, the labour market is expected to decline or stagnate, chiefly due to the projected slowdown in economic growth. For the whole of 2011, the annual rate of growth in the number of employed people is assumed to be moderately higher than projected in MTF-2011Q3, owing to the slightly better than expected employment figures in the second and third quarters of the year.

In the medium-term horizon, the number of employed people is expected to rebound moderately, but since the GDP growth outlook has been revised down from the previous forecast, this upturn is assumed to be smaller than previously projected.

The unemployment rate is expected to stagnate until the end of 2011, and then gradually to

⁵ ECB Staff Macroeconomic Projections for the Euro Area, September 2011. Further details about the ECB projections are available at www.ecb.int

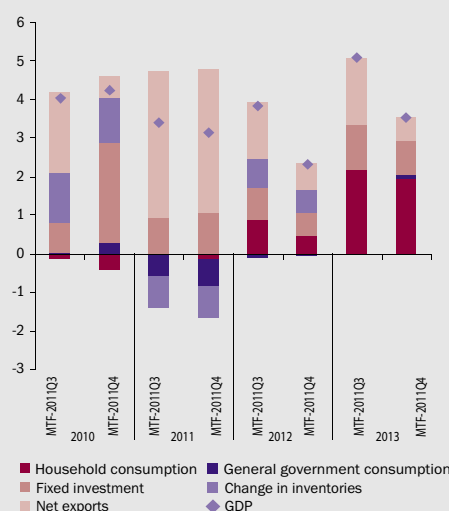
⁶ Detailed data on employment developments were not available as at the cut-off date for this forecast.

decline in the medium-term horizon. With the recovery in the labour market expected to be slower than projected in the previous forecast, the decline in the unemployment rate in the medium-term horizon has been revised down.

According to revised labour market indicators published by the SO SR, growth in compensation per employee in the first half of 2011 was far slower than projected in the previous forecast. There were two factors behind this decline, one of which was a base effect from 2010 as growth in employee compensation was revised up in all sectors of the economy. The other factor was a downward revision of the number of employed people in the first half of 2011. Together, these factors caused the annual rate of growth in employee compensation to decline by more than 2.0 percentage points in comparison with MTF-2011Q3 and were subsequently reflected in a slower rate of growth for the full year.

Although compensation per employee growth is expected to accelerate gradually in the medium term, the projected pace of this growth has been

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



Source: NBS.

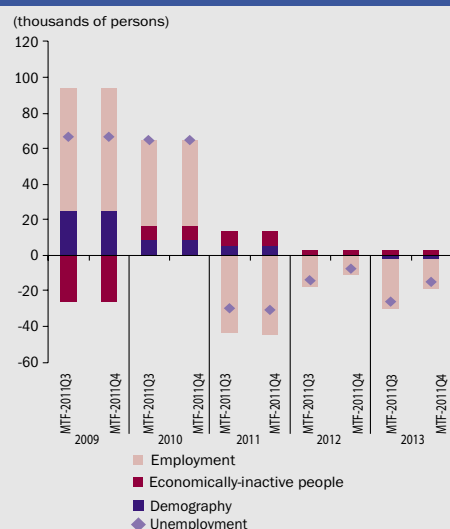
revised down. Amid a deceleration in economic growth, demand for labour will be lower.

The risks to the forecast for labour market indicators are predominantly on the downside. One of the downward risks to the employment forecast is that economic growth is slower than projected and therefore that not as many jobs are created. Another downward risk could be further consolidation measures in the form of public sector lay-offs.

GROSS DOMESTIC PRODUCT

According to the SO SR's flash estimate, GDP growth in the first half of 2011 was moderately faster than projected in the previous forecast. The monthly statistics imply that the main reason for the difference was a higher contribution of net exports, since the amount of imports is expected to have been lower due to the continuing decline in consumer demand and projected slowdown in exports. However, this upturn is not expected to continue in the periods ahead, given the dampening effect of external demand towards the end of the year. That situation, in conjunction with low domestic demand, should translate into more moderate GDP growth for 2011 as a whole. A similar trend is expected to continue next year, and then GDP growth should

Chart 1 Contributions of labour market indicators to unemployment changes



Source: SO SR; NBS calculations.

Note: The contributions of individual labour market indicators refer to their effect on the number of unemployed: for example, unemployment is reduced by a rise in employment, a drop in the number of people of productive age (demographics), and an increase in the economically-inactive population. In the medium-term horizon, the most significant factor in the unemployment rate is expected to be an increase in employment.



pick up somewhat in 2013, assuming that there is a similar trend in demand for Slovak output.

This forecast assumes that GDP growth for 2011 (at constant prices) will be 3.1% in 2011, 2.3% in 2012, and 3.5% in 2013. GDP growth for the whole projection horizon has been revised down from the previous forecast. Slower growth in the trading partners of Slovakia is expected to have a downward effect on the economy's performance, especially towards the end of this year and in 2012. Subsequently, however, the situation should gradually stabilise and external demand growth is therefore expected to start accelerating again. As output declines, investment growth is expected to decelerate, leading to a deterioration in labour market indicators. Given also that the propensity to save is assumed to exceed the propensity to consume, as this was the case in the past, the growth in domestic demand will be somewhat dampened.

Domestic demand

Household final consumption in 2011 is expected to continue declining moderately, as current developments indicate. Although the labour market situation has improved (with household income also rising moderately as a result), continuing uncertainty about the future situation has put downward pressure on consumption expenditure. The propensity to save is assumed to remain high in the following quarters, too. In the medium-term horizon, a gradual acceleration of economic growth and increase in labour productivity should result in a higher rise in household income. The income growth should in turn be reflected in increasing consumption expenditure and a modest decline in the higher saving rate.

Gross fixed capital formation is the only component of domestic demand that is projected to make a positive contribution to GDP growth in 2011. The projected growth in investment activity is predicated on accumulated profits (related to developments in industrial production) and relatively low real interest rates. Work on the completion of infrastructure projects, supported by a year-on-year rise in drawing on EU funds, is also assumed to contribute to investment growth. In the following year, however, the effect of uncertainty and lower economic activity is expected to act as a drag on firms' investment activity. This effect should only be temporary,

and gross fixed capital formation is projected to accelerate again in 2013.

As a result of the implementation of consolidation measures, general government consumption is assumed to make a negative contribution to economic growth in 2011. The forecast for 2012 takes into account further proposed austerity measures in regard to goods and services expenditure and operating expenditure, as well as wage freezes for public sector workers (except for teachers).

The current forecast expects change in inventories to make a slightly negative contribution to economic growth in 2011, as existing stocks are used in the production process. The partial replenishment of these stocks is assumed to contribute positively to GDP growth in 2012. In 2013, change in inventories is not expected to affect GDP growth.

The outlook for the positive contribution of domestic demand to GDP growth over the projection horizon has been revised down from the previous forecast. A slower increase is assumed for both private consumption and gross fixed capital formation.

Net exports

The latest monthly statistics for foreign trade show that the slackening of external demand is

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



Source: NBS.

beginning to have a moderating effect on the growth in the economy's export performance. This will feed through to the volume of imports, which are also expected to be affected in upcoming quarters by a continuing downturn in consumption and decelerating investment growth. As a consequence, net exports are assumed to be the main driver of economic growth in the near term. Looking ahead, the gradual recovery of domestic demand is expected to bring about growth in imports. In 2012, the moderation of external demand growth will have a downward effect on export growth, while at the same time imports increase; thus the positive contribution of foreign trade to economic growth will be lower. In the medium-term horizon, domestic demand growth is assumed to accelerate and

therefore its contribution to GDP growth is projected to rise at the expense of the contribution of net exports.

The positive contribution of net exports to GDP growth has been revised down from the previous forecast, owing to the expected slowdown in external demand in 2012.

The risks to the GDP forecast continue to be on the downside over the projection horizon. The most significant risk is that the debt crisis in Europe escalates and results in a more pronounced slowdown or decline in external demand. Another downside risk is the implementation of further consolidation measures in the medium-term horizon.

Box 1

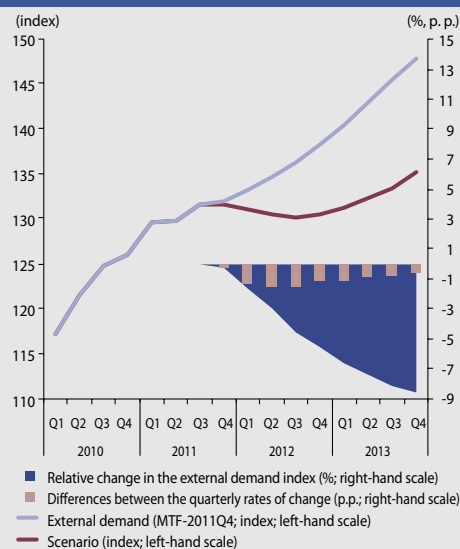
SCENARIO OF A FURTHER SLOWDOWN IN EXTERNAL DEMAND GROWTH

The external assumptions of this forecast are based on ECB assumptions that include a projection of external demand developments. The forecast assumes a slowdown in external demand growth in 2012, but financial market developments indicate a risk of its further slowdown or stagnation, which could substantially dampen domestic economic growth in 2012. The purpose of the scenario in this box is to estimate the impact of such development on the domestic economy.

Compared with this forecast (MTF-2011Q4), the scenario assumes that external demand for Slovak exports will decrease by an additional 8.5% (cumulative) before the end of 2013, specifically, that external demand will stagnate in 2012 and grow by 1.9% in the following year. In other words, external demand growth under the scenario is lower than projected in MTF-2011Q4 by 3.8 percentage points in 2012 and 4.4 points in 2013.

The pass-through of the lower growth rate in external demand to the export performance of the Slovak economy is expected to be immediate and to gradually exert a drag on GDP

Chart A External demand scenario



Source: NBS.

growth. Amid the constraints on external demand, all components of domestic demand are assumed to grow more slowly, and this will eventually feed through to consumer prices. In the case of households, the lower growth in disposable income is not expected to be fully



GDP (%)	2011	2012	2013
MTF-2011Q4	3.1	2.3	3.5
Scenario	3.0	0.5	1.3
Difference (p.p.)	-0.1	-1.8	-2.2

reflected in consumption, but to be to some extent compensated by the use of savings. Likewise, the slowdown in external demand is expected to see a lower decline in structural unemployment with repercussions for potential output.

HICP (%)	2011	2012	2013
MTF-2011Q4	4.0	2.8	1.9
Scenario	4.0	2.6	1.2
Difference (p.p.)	0.0	-0.2	-0.7

Overall, the downward effect of lower external demand on economic growth is put at -1.8 percentage point in 2012 and -2.2 percentage point in 2013, and its effect on the inflation rate is expected to be -0.2 percentage point in 2012 and -0.7 percentage point in 2013.

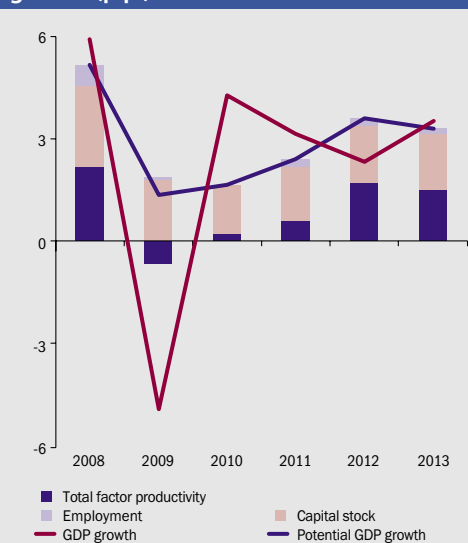
POTENTIAL GDP AND THE OUTPUT GAP

The potential growth output of the Slovak economy is expected to reach around 3% in 2012 and 2013, driven up mainly by an increase in capital stock and in total factor productivity. The contribution of employment to potential output growth is expected to be low, given demographic developments and a moderate decline in trend unemployment. In 2012, potential output is assumed to be boosted by the one-off effect of an expansion of production in the automotive industry. The forecast for potential output growth over the projection horizon has been revised down from the projection in MTF-2011Q3.

The weaker outlook for the global economy translates into lower investment activity and a slowdown in total factor productivity.

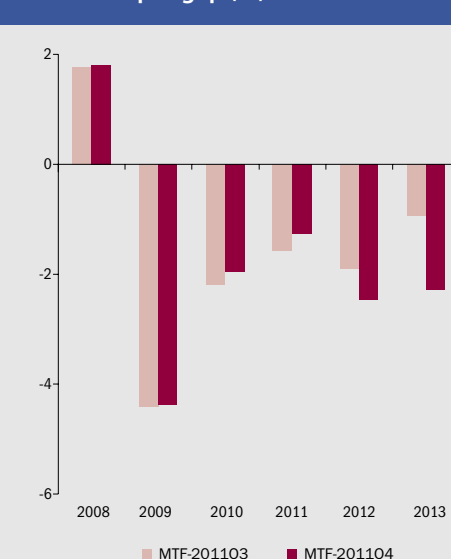
The outlook for the cyclical position of the economy reflects the revision of national accounts and the deceleration in both external and domestic demand. With GDP growth decelerating in 2012, it is assumed that the closing trend in the output gap will come to an end and that a negative output gap will reopen. The economy is not expected to reach equilibrium within the projection horizon, but GDP growth in 2013 should contribute moderately to a reduction in the negative output gap.

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



Source: NBS.

Chart 5 Output gap (%)



Source: NBS.

Box 2

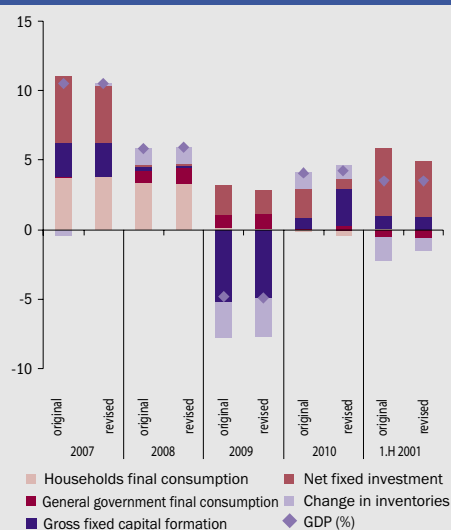
REVISION OF THE NATIONAL ACCOUNTS

This forecast (MTF-2011Q4) is based on the revised quarterly national accounts data that were published by the SO SR on 18 November 2011. The most substantial changes concerned the data for 2010, which were updated on the basis of firms' annual statements. As a consequence, GDP growth for 2010 was revised up by 0.2 percentage point, to 4.2%. This included a relatively marked increase in the contribution of domestic demand to GDP growth, partly at the expense of the contribution of net exports. As for consumption demand, there was a downward revision of household consumption, which, however, was more than compensated by a higher upward revision of government consumption. The general government final consumption figures were modified mainly on the basis of the updated data on employee compensation (which has been falling since 2006) and an increase in intermediate consumption. The largest revision, however, was in the fixed investment figures, which were raised substantially from the first quarter of 2010. As a result, the annual rate of change in fixed investment increased by 3.6 percentage point,

to 12.4%. A proportion of this investment was probably transferred from stocks of work in progress, resulting in a decline in stocks in 2010. As for changes at the structural level, investments of non-financial corporations in means of transport and intangible fixed assets increased. These changes in domestic demand were reflected also in higher imports of goods and services, which had a downward effect on the contribution of net exports to economic growth. In the first half of 2011, however, the different components of GDP did not undergo any significant revision and the adjustments that were made had a minimal effect on the forecast. The most marked changes were to the amounts of exports and imports, based on the regular monthly revisions to external trade.

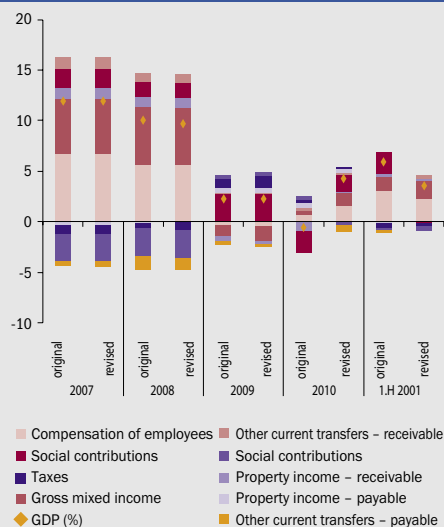
In the household account, both income and expenditure were revised up. Since the income figure increased by a larger margin, there was a rise in the overall disposable income of households in 2010. The largest revision on the income side was to the components social benefits and property income. The revision on the

Chart A GDP growth broken down by contributions of components (p.p.)



Source: SO SR.

Chart B Growth in household gross disposable income broken down by contributions (p.p.)

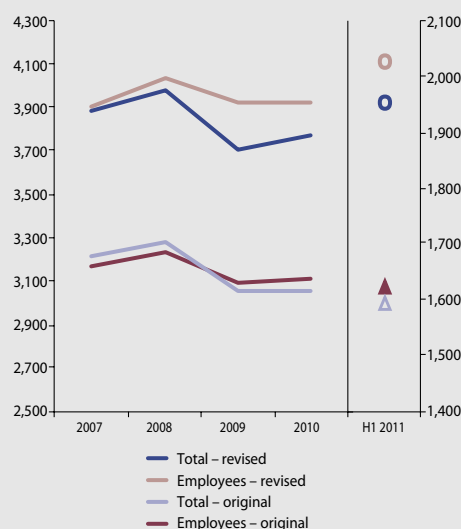


Source: SO SR.

expenditure side was distributed evenly between the different components. A combination of higher household disposable income and lower household consumption lead to an increase in household gross saving, and therefore the saving rate was revised⁷ to around 10% in the post-crisis period, at which level it remains in the near-term projection horizon. Data for the first half of 2011 were not revised up by as much as the data for 2010 were; this difference was reflected in the lower annual rate of growth in household disposable income, and it therefore affected the forecast for the whole of 2011.

The most significant revision was made to the labour market indicators. It is worth noting that in contrast to the revision of GDP components, which was most pronounced in 2010, the revision of labour market indicators was substantial also in 2009. Overall employment and the number of hours worked were revised up over the projection horizon. The structure of employment also changed, as the number of employees was revised down while the number of self-employed increased. Based on the latest data, the overall amount of compensation paid in the economy in 2009 was revised down. Therefore, the impact of the economic crisis on compensation was

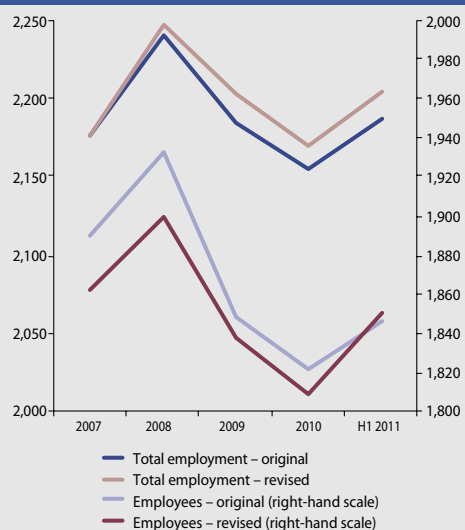
Chart D Number of hours worked (thousands of hours) (data for the first half of 2011 – right-hand scale)



Source: SO SR.

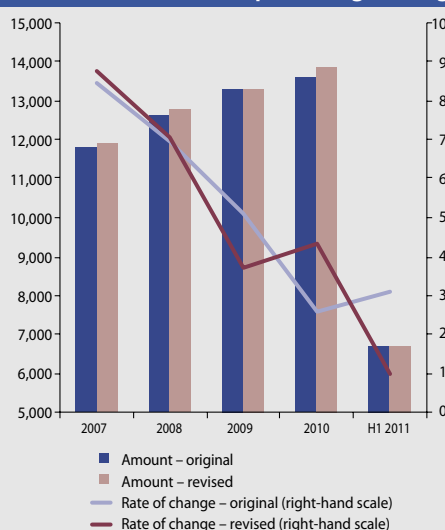
greater than originally assumed. By contrast, the amount of wages paid in 2010, during the post-crisis recovery, was revised up. This, alongside the lower number of employees has had a substantial downward effect on the annual rate of change in employee compensation in 2011.

Chart C Employment (thousands of persons)



Source: SO SR.

Chart E Compensation per employee (amount in EUR; annual percentage change)



Source: SO SR.

⁷ Household gross saving is the difference between household disposable income and final consumption of households and non-profit institutions serving households.

4.2 INFLATION

The annual rate of inflation accelerated from August 2011, owing to a higher rate of change in prices of goods and services. In the case of goods prices, the increase in prices of all the core components of inflation was quite marked. As for energy prices, the August increases in heat and gas prices were followed by further months of rising heat prices. The annual rate of change in non-energy industrial goods increased, largely due to rising prices of non-durable goods. Services prices, too, continued to record a moderately rising annual rate of change, which reflected higher increases in prices of transportation services and recreational and personal services. Food prices were pushed up by higher annual inflation in prices of unprocessed food. Looking at its recent development, the headline inflation rate may be described as cost-pushed, since demand-side factors had put only minor upward pressure on consumer prices.

The inflation rate until the end of 2011 is assumed to stagnate and gradually decelerate, owing mainly to the expected developments in heat prices (only a moderate increase). The trend in food prices towards the year-end should be influenced by this year's better harvest and fall in prices of agricultural commodities. Prices of services and non-energy industrial goods are assumed to rise gradually up to the end of 2011, due to the pass-through of cost impulses.

The inflation rate is expected to decelerate at the beginning of 2012, given the fading of the effects of indirect price rises and high prices of agricultural commodities and fuel. The hike in administered prices in January 2012 is expected to be lower than in the previous year. Food prices are also expected to contribute to the overall slowdown of inflation in 2012, reflecting the effect of this year's good harvest and fall in prices of agricultural commodities. Services prices are projected to accelerate moderately amid the secondary effects of rising energy prices.

In 2013, the year-on-year increase in consumer prices may further decelerate due to stagnation in administered energy prices, as well as to a slowdown in economic activity in 2012 (which by dampening consumer demand could have a downward effect on the annual rate of chan-

ge in prices of industrial goods and services in 2013). In this forecast, the average rate of consumer price inflation is expected to be 4.0% in 2011, 2.8% in 2012, and 1.9% in 2013.

Considering current inflation developments, the annual increase in the inflation rate in 2011 has been revised down from the previous forecast (MTF2011-Q3). The rise in administered prices of energy (heat) has been lower than projected in MTF2011-Q3, and since this trend is not expected to change before the year-end, the trajectory of the latest inflation forecast is lower. The projection for consumer price increases in 2013 has been revised down from the previous forecast, since there is assumed to be a lower rate of change in prices of non-energy industrial goods and prices of services, which are expected to reflect a slowdown in economic activity and lower rises in employee compensation and household consumption.

The risks to the inflation forecast for 2012 are balanced, while for 2013 they are more on the upside. The implementation of necessary fiscal consolidation measures in certain euro area countries, but also in Slovakia, represents an upside risk, since any increase in indirect taxes or administered prices that exceeds current projections could lead to higher inflation. The risk of higher inflation in 2012 may, however, be mitigated by

Chart 6 Changes in the HICP inflation forecast

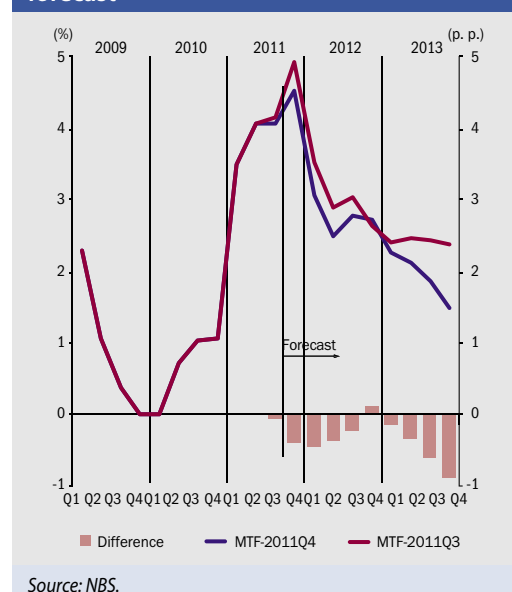
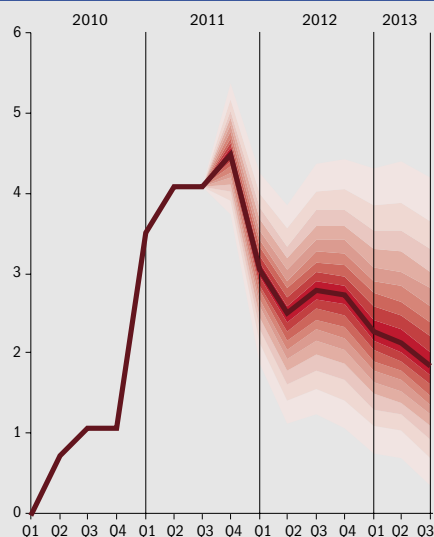




Chart 7 HICP inflation forecast (%)



Source: NBS.

lower than expected external demand or a more marked deterioration in the labour market situation.

A specific risk to the 2012 forecast is that heat prices are raised further in January, after increasing in 2011 by less than projected. It may happen that heating plant operators, which for various reasons did not apply for a higher increase in prices in 2011, will apply for a price hike in January 2012.



Table 3 Medium-term forecast (MTF-2011Q4) – main macroeconomic indicators

Indicator (y-o-y change in % unless otherwise indicated)	Actual data	Projection in MTF-2011Q4			Difference versus MTF-2011Q3		
	2010	2011	2012	2013	2011	2012	2013
Prices (annual percentage changes)							
HICP inflation (average)	0.7	4.0	2.8	1.9	-0.2	-0.2	-0.5
CPI inflation (average)	1.0	4.0	2.7	1.9	-0.1	-0.3	-0.5
ULC ¹⁾ (compensation per employee at current prices / labour productivity ESA 95 at constant prices)	-1.3	0.3	1.2	1.9	-2.6	-0.6	-0.1
Labour productivity ESA 95 (GDP at constant prices / employment ESA 95)	5.8	1.2	1.8	2.8	-0.4	-1.2	-1.0
Compensation per employee (current prices)	4.4	1.5	3.0	4.8	-3.1	-1.9	-1.1
Economic activity							
Real GDP	4.2	3.1	2.3	3.5	-0.3	-1.5	-1.6
Final consumption of households	-0.7	-0.3	0.8	3.8	-0.2	-0.9	-0.6
Final consumption of general government	1.5	-3.6	-0.5	0.5	-0.8	0.2	0.6
Gross fixed capital formation	12.4	4.6	2.6	3.7	0.4	-1.3	-1.5
Exports of goods and services	16.5	9.3	4.0	8.1	-2.1	-4.2	-1.2
Imports of goods and services	16.3	5.1	3.5	8.1	-2.9	-4.1	0.5
Gross real disposable income of households	3.2	-0.2	0.7	3.1	-1.5	-1.7	-1.2
Output gap (% of the potential output)	-2.0	-1.3	-2.5	-2.3	0.3	-0.6	-1.4
Labour market							
Employment, based on ESA 95	-1.5	1.9	0.5	0.7	0.1	-0.3	-0.5
Unemployment rate, LFSS-based ²⁾ (%)	14.4	13.2	12.9	12.3	0.0	0.3	0.6
Balance of payments							
Economic openness (% of GDP)	162.3	173.5	174.2	181.2	-3.8	-8.9	-8.0
Balance of trade (% of GDP)	0.2	2.2	2.5	2.5	0.5	-0.1	-0.3
Balance of services (% of GDP)	-1.1	-0.8	-0.8	-0.7	0.0	0.0	-0.1
Current account (% of GDP)	-3.5	-1.0	-0.4	-0.3	0.5	0.0	-0.3
Current and capital account (% of GDP)	-1.9	0.7	1.5	1.6	0.4	0.0	-0.2

Source: NBS.

1) ULC – unit labour costs.

2) LFSS – Labour Force Sample Survey.