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MEDIUM-TERM FORECAST

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1 Summary

Slovakia's economic growth remained stable, at 1.0%, in the last quarter of 2015. The growth was driven mainly by increasing domestic demand (boosted by the absorption of EU funds) and by steady growth in private consumption. Despite a slowdown in foreign demand, the export performance of the Slovak economy improved towards the end of 2015. With its economy experiencing balanced growth, Slovakia reported net job creation and employment growth of 0.4% in the fourth quarter of 2015.

These favourable trends are expected to continue in 2016. Annual GDP growth is projected to slow slightly in 2016, to 3.2%, with domestic demand making a smaller contribution owing to a sizeable decrease in government investment. There should, however, be a gradual increase in private investment demand and private consumption. The economy's growth is expected to accelerate to 3.3% in 2017 and 4.2% in 2018, thanks partly to new investment in the car industry. The GDP growth projections are unchanged from the previous forecast.

The labour market situation is expected to remain favourable. Employment growth is projected to be slightly lower in 2016 than in 2015, with firms being more inclined to increase hours worked than to recruit. Since there is a risk that labour market shortages could increase, the labour market participation rate is expected to rise. Nominal wage growth is projected to increase moderately, but owing to the impact of rising inflation, real wage growth should decrease.

In the light of current developments and technical assumptions, the inflation forecast over the projection horizon has been revised markedly. After falling in 2015, the price level is now expected to decrease further in 2016 (by 0.2%), reflecting low energy prices and surprisingly subdued trends in prices of food and services. The annual inflation rate is forecast to return to positive territory over the rest of the projection period, up to 1.3% in 2017 and 1.9% in 2018. These years should see increases in the prices of demand-led goods and services and in food prices. Energy prices, on the other hand, are expected to continue making a negative contribution to headline inflation.

The real GDP growth outlook is subject to the downside risk of lower foreign demand growth. In particular, if China's economic slowdown is more rapid than expected, it could, via energy prices, prolong the non-inflationary environment.

Table 1 GDP and inflation projections (annual percentage changes)

	MTF-2016Q1			Difference vis-à-vis MTF-2015Q4U		
	2016	2017	2018	2016	2017	2018
GDP	3.2	3.3	4.2	0.0	0.0	---
HICP	-0.2	1.3	1.9	-0.6	-0.5	---
Net inflation excluding automotive fuel	1.0	1.6	2.4	-0.5	-0.7	---

Sources: SO SR and NBS.
Note: Net inflation excluding automotive fuel refers to the HICP inflation rate excluding food, energy and administered prices. This rate is better than the headline HICP rate at reflecting domestic prices.

2 Current developments in the external environment and in Slovakia

Euro area GDP growth remained unchanged in the fourth quarter of 2015

The euro area's quarter-on-quarter GDP growth rate was 0.3 % in the fourth quarter of 2015, the same as in the previous quarter. Among the larger national economies in the euro area, the highest growth rates were reported by Spain (0.8%), Germany (0.3%), France (0.3%) and the Netherlands (0.3%). At the same time, both the Greek and Estonian economies grew in the fourth quarter after contracting in the previous quarter. Leading indicators are at present sending out less favourable signals, and do not as yet point to a pick-up in economic growth. The annual HICP inflation rate in February was -0.2% (after registering 0.3% in January). Energy price inflation became markedly more negative, while both the food and services components posted lower positive rates.

The Slovak economy is maintaining solid growth[1]

Slovakia's economy maintained stable growth of 1.0% in the fourth quarter of 2015. The growth was driven mainly by the domestic economy, which was boosted by the elevated absorption of outstanding EU funds available from the previous programming period. Private consumption continued to increase steadily, supported by the favourable labour market situation. Export growth also picked up notably towards the year-end.

Labour market developments were in line with projections. There was net job creation, and employment increased by 0.4%. The unemployment rate declined significantly below 11%. Nominal wage growth was strong and, together with falling prices, had an upward impact on households' real disposable income and also their savings.

Consumer prices continued to decline in the last quarter of 2015. This was largely attributable to falling oil prices that translated almost immediately into reductions in automotive fuel prices. In addition, food prices fell further. Prices of consumption goods and services increased marginally, but not enough to counterbalance the impact of decreases in other components.

1 *For further details, see the "Report on the Slovak Economy – March 2016"*

3 Technical assumptions of the forecast [2]

3.1 COMMODITIES AND THE EXCHANGE RATE

The exchange rate[3] of the euro against the US dollar remained almost unchanged between the cut-off dates for the previous forecast (early January) and this forecast, as it appreciated by 0.7%.

The recent slump in **oil prices** was factored into the assumptions of January's update of the December 2015 Medium-Term Forecast (MTF-2015-Q4U). The assumptions for the oil price in euro are revised up slightly in this MTF-2016Q1 forecast, by 4% in 2016 and by 0.5% in 2017). Based on the path implied by futures markets, the price of a barrel Brent crude oil is assumed to be USD 38.9 in 2016, USD 44.7 in 2017, and USD 47.1 in 2018.

3.2 FOREIGN DEMAND

The recovery in euro area activity is expected to continue, albeit with somewhat less momentum than previously projected. The slower pace reflects weakening global growth and a strengthening of the effective exchange rate of the euro. Nevertheless, growth will be supported by the ECB's accommodative monetary policy stance and by domestic demand, which will be influenced by a one-year prolongation of the non-inflationary environment. In time, the global recovery should contribute to a gradual pick-up in investment. Domestic demand will also benefit from some fiscal easing, partly related to the influx of refugees (particularly in Germany). Private consumption expenditure is projected to benefit strongly from low energy prices in 2016. Nominal disposable income should rise over the projection horizon, supported by steady growth in employment and rising growth in nominal compensation per employee, while other personal income is also expected to contribute positively. Private consumption should be supported by low financing costs and moderately rising household net worth, both reinforced by the ECB's recent monetary policy package. Residential investment in the euro area is projected to gain momentum, albeit from a very low level. Business investment is expected to show a subdued recovery. Extra-euro area exports should benefit from the lagged effects of the past depreciation of the euro and from a recovery in euro area foreign demand (albeit somewhat lower than previously envisaged). As actual GDP growth is expected to exceed the rate of potential output, the output gap is expected to narrow steadily over the projection horizon. Overall, euro area GDP growth is projected to slow from 1.5% in 2015 to 1.4 % in 2016, before accelerating to 1.7% in 2017 and 1.8% in 2018. Compared with the ECB's projections published in December, the growth forecasts for 2016 and 2017 have been revised up by, respectively, 0.3 and 0.2 percentage point.[4]

Slovakia's foreign demand growth has been revised down owing to mounting concerns about increasingly severe slowdowns in emerging market economies (China in particular) and their impact on the economies of Slovakia's main trading partners. The assumptions for Slovakia's foreign demand growth are 3.5% in 2016, rising to 4.5% in 2017 and 4.8% in 2018.

2 The technical assumptions of this Medium-Term Forecast are based on the "March 2016 ECB staff macroeconomic projections for the euro area", with a cut-off date of 15 February 2016. The assumptions for the EUR/USD exchange rate, Brent oil prices and Slovakia's foreign demand were updated as at 4 March 2016.

3 The bilateral EUR/USD exchange rate is assumed to remain unchanged over the projection horizon at the average level prevailing in the ten-working day period ending on the cut-off date.

4 According to the "March 2016 ECB staff macroeconomic projections for the euro area".

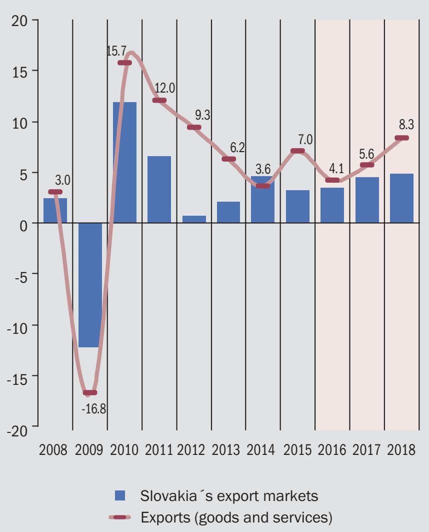
4 Macroeconomic forecast for Slovakia

4.1 ECONOMIC GROWTH

Slowdown in early 2016; car industry investment to have positive impact over medium term

The rapid increase in exports in the last quarter of 2015 and first quarter of 2016 has laid the basis for strong export growth in 2016. Given the impact of financial turbulence and worse than expected hard indicators for emerging market economies, the projection for Slovakia's export growth in the first half of 2016 has been revised down slightly. In subsequent years, exports are expected to increase in line with foreign demand, and there should be moderate acquisition of market share. The outlook for 2018 incorporates the impact of the gradual roll out of new production in the car industry, which is expected to add approximately 2.2 percentage point to export growth (and 0.7 percentage point to GDP growth).

Chart 1 Forecast for foreign demand and for Slovak exports of goods and services (annual percentage changes; constant prices)



Sources: SO SR, ECB and NBS calculations.

Investment will be dampened in 2016 by drop-off in EU funds, and then pick-up significantly over the rest of the projection horizon

After recording strong growth in 2015, investment demand is expected to remain flat in 2016. The drop-off in EU-funded public investment should be counterbalanced by an increase in private investment. Residential construction is expected to provide an additional impulse to investment, given that the number of flats under construction reached a four-year high in the second half of 2015 and that an increasing number of building permits were issued during the same period. Investment demand is expected to be supported by low interest rates and by favourable economic outlooks. New investment in the automotive industry should also begin to have an impact in 2016 and 2017, with investment demand growth touching 5%. The absorption of EU funds is projected to pick-up significantly again in 2018, with the absorption of outstanding EU funds in the second half of the new programming period.

Private consumption growth to increase over projection horizon

Private consumption growth is expected to increase this year, with one-off administrative factors[5] projected to contribute around 0.4 percentage point to the growth rate. The growth outlook for households' real disposable income in 2016 reflects expectations of a marginal drop in consumer prices. Consumers are expected to chan-

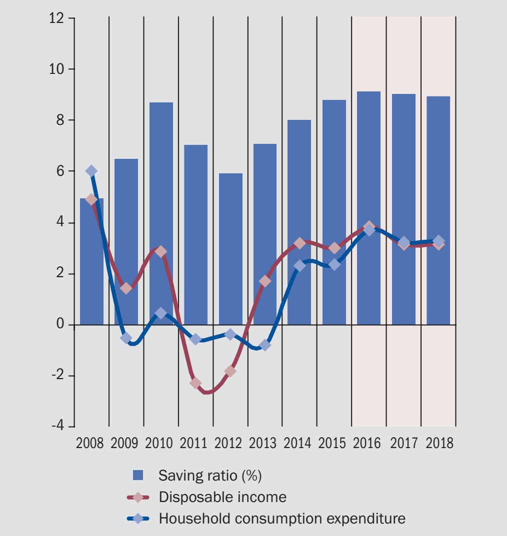
Table 2 Investment (annual percentage changes)

	2015	2016	2017	2018
Gross fixed capital formation in total	14.0	0.2	5.0	5.5
– private sector	5.2	8.9	6.8	5.1
– public sector	55.3	-27.7	-3.7	7.3

Sources: SO SR and NBS calculations.

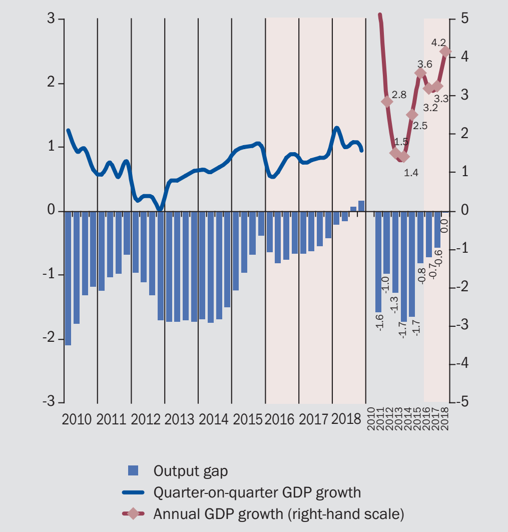
5 *An increase in the minimum wage, rebates on household gas bills, and a reduction in VAT on selected food products.*

Chart 2 Household income and consumption (annual percentage changes; constant prices) and the household saving ratio (%)



Sources: SO SR and NBS.

Chart 3 GDP growth and the output gap (%)



Sources: SO SR and NBS.

nel the bulk of their increased income into consumption and the lesser part into savings. Private consumption growth is projected to moderate in 2017 and 2018, as rebounding inflation dampens disposable income growth.

Slowdown in government expenditure growth

The growth in final consumption expenditure of general government is projected to fall over the projection horizon, owing to restrained growth in nominal expenditure as well as to a gradual increase in inflation.

Economic growth to increase over projection horizon

Even after factoring in slower global economic growth at the beginning of 2016, foreign demand for Slovak goods and services is projected to increase moderately in the medium term. Foreign demand growth should also be supported by the easing of the ECB's monetary policy at the beginning of March. **Slovakia's economic growth** is expected to be balanced and its rate **is projected to be 3.2% in 2016 and 3.3% in 2017 (both figures are unchanged from the MTF-2015Q4U forecast). GDP growth is assumed to accelerate to 4.2% in 2018,** owing to the launch of production at a new car plant (its impact on GDP growth being estimated at 0.7 percentage point). On the assumption that real GDP growth will be moderately higher than potential growth, the output gap is expected to close in 2018.

4.2 THE LABOUR MARKET

Labour market situation to remain favourable

Although economic growth will continue to support job creation, the rate of job growth is expected to be more moderate over the projection horizon than it was in the previous two years. Based on data for the first months of 2016, as well as on employers' expectations, the current upward trend is expected to continue in the short term. While accelerating activity growth is expected to boost demand for labour, it may also, in certain sectors, create labour shortages over the medium term. Firms may address such shortages by increasing hours worked per employee, employing older people, and by recruiting employees from abroad.

The unemployment rate is expected to fall gradually over the projection horizon, down to around 8.5% by the end of the period.

Table 3 Wages (annual percentage changes)

	2015	2016	2017	2018
Nominal labour productivity	1.2	2.0	4.1	5.1
Whole economy – nominal	2.9	3.3	3.7	3.8
Whole economy – real	3.2	3.4	2.3	1.8
Private sector – nominal	2.8	3.0	3.8	4.0
Private sector – real	3.1	3.1	2.5	2.0
Public administration, education and health care – nominal	3.3	4.7	3.1	3.3
Public administration, education and health care – real	3.7	4.8	1.8	1.3

Sources: SO SR and NBS calculations.
Note: Deflated by the CPI. The sector „Public administration, education and health care" corresponds to sections O, P and Q of the SK NACE Rev. 2 statistical classification of economic activities. Nominal average wage growth in the general government sector (ESA S.13) is projected to be 5.2% in 2016, 3.1% in 2017 and 3.3% in 2018.

Chart 4 Employment, hours worked (annual percentage changes), and the unemployment rate (%)

Zdroj: ŠÚ SR a NBS.

4.3 PRICE DEVELOPMENTS

Inflation not expected to approach 2% until the end of the projection horizon

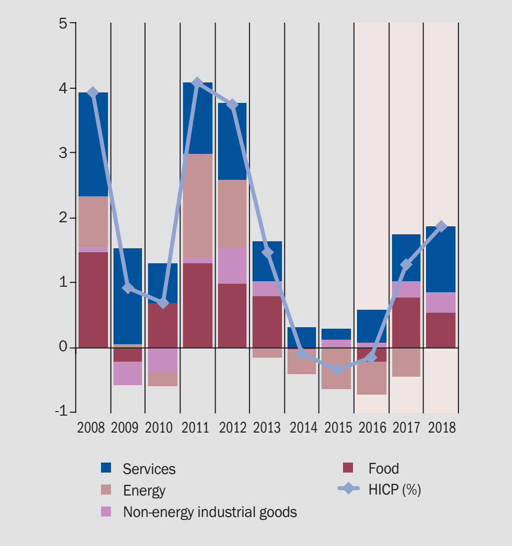
The price level is expected to continue falling in 2016 due to declines in prices of energy, food and imports and to lower services price inflation. This outlook is supported by figures for the first two months of 2016, with services inflation coming in lower than projected and food prices falling more markedly. Low wholesale prices of energy commodities and electricity have created scope for further reductions in consumer energy prices. As a result, administered prices of gas, heat and electricity are expected to be further reduced in January 2017. On the other hand, headline inflation is expected to come under upward pressure from import prices (for

Table 4 Inflation components (annual percentage changes)

	Average 2004-2008 (pre-crisis period)	Average 2009-2014 (post-crisis period)	2014	2015	2016	2017	2018
HICP	4.1	1.8	-0.1	-0.3	-0.2	1.3	1.9
Food	3.6	2.5	-0.2	-0.1	-0.9	3.3	2.3
Non-energy industrial goods	0.2	0.1	0.0	0.4	0.3	0.9	1.0
Energy	8.3	2.0	-2.2	-3.9	-3.4	-3.0	0.1
Services	5.3	2.8	1.0	0.6	1.6	2.2	3.1
Net inflation excluding automotive fuel	1.8	0.9	0.5	0.9	1.0	1.6	2.4

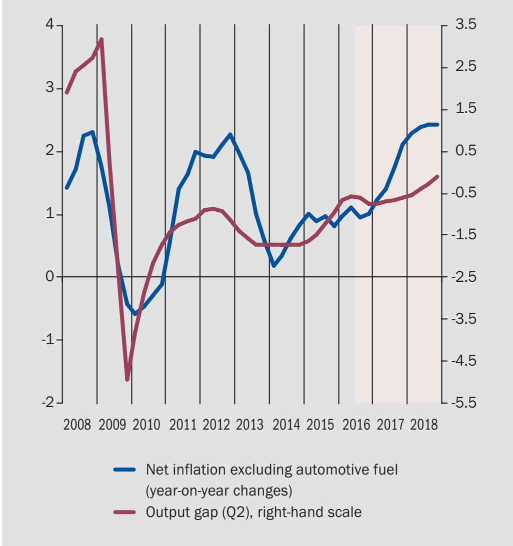
Sources: SO SR and NBS calculations.

Chart 5 Composition of annual inflation (p.p.)



Sources: SO SR and NBS.

Chart 6 Net inflation excluding automotive fuel and the output gap (%)



Sources: SO SR and NBS calculations.

example, an increase in euro area inflation) as well as from food prices. Services inflation is expected to increase amid rising consumer demand. The overall rate of inflation is therefore projected to increase to almost 2% by the end of the forecast period.

5 Fiscal outlook[6]

General government budget to benefit from impact of macroeconomic developments

Public finances are expected to benefit from the combination of projected macroeconomic trends and government measures. The general government deficit is forecast to narrow from -2.7% of GDP in 2015 to -1.1% of GDP in 2018. The steadily diminishing deficit reflects the continuance of economic growth and the resulting increase in budget revenues. In an environment of low and even negative interest rates, the accommodative monetary policy stance should support savings on interest costs. Another factor is the reduction of other expenditure, particularly in 2017 and 2018, as part of fiscal consolidation efforts. The overall government revenue and expenditure-to-GDP ratio is expected to have peaked in 2015, thanks to the impact of EU funds absorption, and should decrease in subsequent years.

The fiscal deficit projections in this forecast are higher than the deficit assumptions in the General Government Budget (GGB) for 2016–2018), since the GGB does not factor in specific deficit-reduction measures and the consequent risks of a substantial drop in intermediate consumption and capital expenditure. This forecast does not take into account the fiscal targets of the new government (i.e. the risk that the target year for achieving a balanced budget will be postponed until 2020).

Government revenue affected by lower nominal economic growth

Although the real economy continues to post solid growth, price developments are not as yet putting any significant upward pressure on tax revenues. But although tax revenue growth is not expected to be as strong in 2016 as it was in 2015, continuing growth in both the real economy and in employment is expected to support a further increase in tax revenues. VAT revenues are projected to drop in 2016 following the reduction in VAT on selected foodstuffs. Tax revenues should see a further negative impact in 2017 with the discontinuation of the special levy on regulated industries. Slower nominal wage growth is expected to be reflected in social and health contributions. Furthermore, a change in pension rates is scheduled for 2017, with the rate paid to the earnings-related first pillar being reduced and the rate paid to the mandatory, defined-contribution second pillar being correspondingly increased. The fiscal outlook does not take account of tax policy adjustments that may be made by the new government.

Government expenditure is benefiting from low inflation and an accommodative monetary policy stance

Primary government expenditure in 2015 is expected to have increased substantially in

Table 5 Fiscal assumptions of the medium-term forecast and the GGB for 2016–2018 (% of GDP)

	2014	2015	2016	2017	2018
General government budget balance	-2.8	-2.7	-2.6	-1.8	-1.1
General government debt	53.5	52.5	52.9	52.6	51.3
Total revenue	38.9	41.9	39.8	39.1	38.8
Total expenditure	41.6	44.6	42.4	40.9	39.9
Target deficit in the GGB for 2016-2018	-	-2.71	-1.9	-0.4	0.0
Fiscal gap (deficit projected by NBS – GGB target deficit for 2016-2018)	-	0.0	-0.7	-1.4	-1.1
Fiscal stimulus (- denotes expansion) 2)	-0.2	-0.3	-0.3	0.5	0.5
Fiscal stimulus including impact of relations with the EU (- denotes expansion)	-0.3	-3.2	2.7	0.5	0.2

Sources: MF SR and NBS calculations.
1) In the GGB for 2016-2018, the figure for 2015 is the expected deficit.
2) Change in the cyclically-adjusted primary balance.

6 *The analytical premise for the production of the MTF-2016Q1 forecast.*

year- year-on-year terms, thanks to the absorption of EU structural funds and the related co-financing. Primary expenditure is also expected to have been negatively affected by financial corrections to EU funds[7]. On the other hand, subsidies are assumed to have declined and other current transfers to have increased more moderately, reflecting mainly lower contributions to the EU budget. Primary expenditure in 2016 is expected to fall year-on-year owing to the drop-off in EU funds, the impact of which will be partly offset by second social package measures, increases in public sector salaries, and the expected purchase of land for the establishment of a new Jaguar Land Rover car plant in Slovakia. Primary expenditure is projected to fall further in 2017 and 2018, reflecting restrained growth in government consumption in the post-election period and the fact that social expenditure growth will be modest owing to the low inflation environment and falling unemployment.

The cost of servicing the public debt is expected to continue falling over the projection horizon due to the impact of monetary policy easing, with some new bond issues being offered at negative yields.

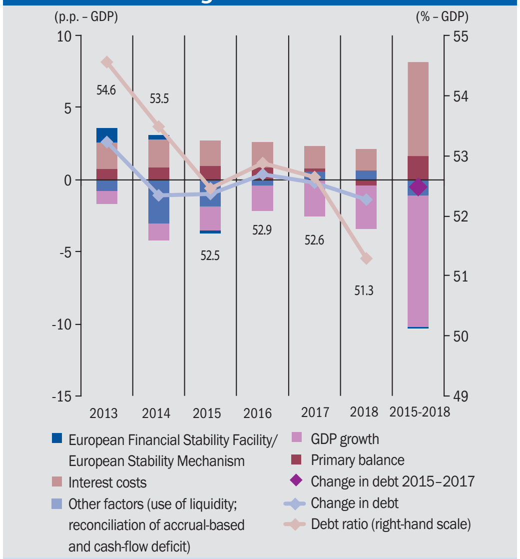
Impact on aggregate demand

Public finances are projected to have an expansionary impact on economic growth in 2016 and a restrictive impact over the rest of the projection horizon. Taking the impact of EU funds absorption into account, however, the overall impact of public finances is expected to be restrictive, and in 2016 that impact should be entirely attributable to the slow absorption of EU funds under the new programming period.

Government debt not expected to begin falling until 2017

The general government debt is assumed to have fallen in 2015 to 52.5% of GDP, owing mainly to privatisation revenues and to the windfall provided by a temporary opening of second pension pillar (allowing people to withdraw from what is usually a mandatory private scheme and transfer their pension contributions to the state-run first pillar). Decreasing prices had a downward effect on the debt ratio denominator – nominal GDP growth, and this is the main reason that the debt is projected to increase in 2016, to 52.9% of GDP. The debt is not expected to begin falling again until 2017, and as the general government deficit improves, it should continue falling in 2018, down to 51.3%.

Chart 7 Assumptions for gross general government debt and for factors contributing to its rate of change



Sources: SO SR and NBS calculations.

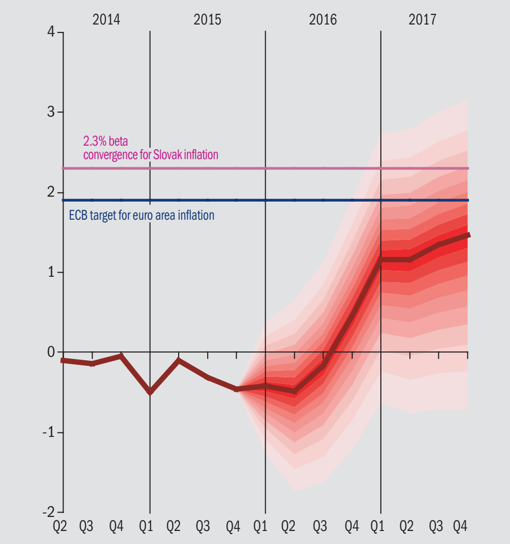
7 *The corrections to EU funds are assumed to amount to 0.3% of GDP. This relates to projects that are not expected to be refunded from the EU under the 2007-2013 programming period because they involved infringements of EU funding rules.*

6 Risks to the forecast

The risks to the outlook for the real economy over the medium term are on the downside. The main risk is that foreign demand growth may be weaker than expected owing to slower GDP growth in China and other emerging market economies.

The risks to the medium-term inflation projections are downward. If the negative scenario for the real economy materialises, inflation may be lower than expected owing to lower imported inflation.

Chart 8 HICP inflation forecast (%)



Sources: SO SR and NBS.

Table 6 Risks to the forecast

	2016	2017	2018
GDP	Balanced	↓ Foreign demand	↓ Foreign demand
Inflation	Balanced	↓ Imported inflation	↓ Imported inflation

Source: NBS.

Box 1

HOW SLOVAKIA MAY BE AFFECTED BY A 'HARD LANDING' SCENARIO FOR THE CHINESE ECONOMY

The persisting downside risks to the global growth outlook, stemming from concerns about future developments in China and other emerging market economies, are the starting point for modelling how the Slovak economy may be affected by a greater than expected economic slowdown – a 'hard landing' – in China. The technical assumptions of this scenario are based on the sensitivity analysis provided in the 'March 2016 ECB staff macroeconomic projections for the euro area'. The scenario includes three channels through which adverse developments in the external environment affect the domestic economy. The **lower demand channel** captures a hard landing in China in terms of its negative impact – via weakened demand for imports – on other emerging market economies. This assumption also has implications for advanced economies, to the extent that foreign demand is reduced. A decline in global demand will put downward pressure on commodity prices (especially oil), further undermining the position of oil-exporting countries (such as Russia).

This aspect of the scenario is captured by the **lower commodity prices channel**. Finally, the **exchange rate channel** describes the impact that the depreciation of local currencies in the affected region has on foreign trade and on developments in other countries. It is here assumed that depreciation-stimulated growth in emerging market economies (Russia and China) will stoke these economies' demand for imports and, albeit marginally, mitigate the negative impact of the overall slowdown in global demand.

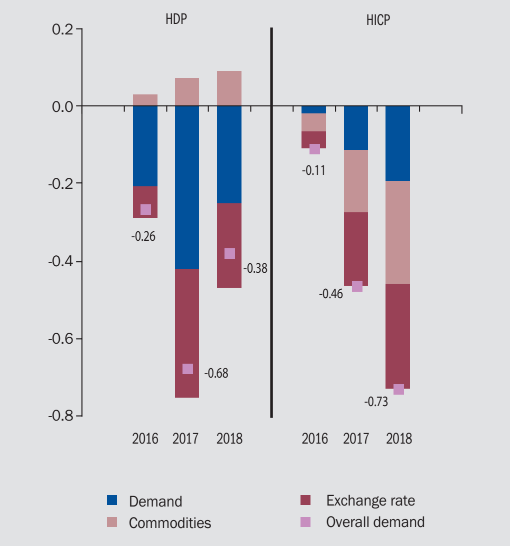
The scenario describes both the direct and indirect impact of adverse developments in the external models on the Slovak economy. The direct impact covers the repercussions stemming from Slovakia's direct trade links with countries of the affected region, while the indirect impact captures spillover effects resulting from the changed developments in Slovakia's business partners outside the affected region. The overall impact on the Slovak economy comprises the sum of the direct and indirect impacts.

Looking at the overall impact of a Chinese hard landing scenario on the Slovak economy, growth in foreign demand for Slovak exports is lower than the growth rate under the baseline scenario, by 0.4 percentage point in 2016, 0.8 percentage point in 2017 and 0.5 percentage point in 2018.

The adverse external developments of the stress scenario have a negative impact on both GDP growth and HICP inflation over the projection horizon. In the case of GDP, the demand channel causes the greatest shock owing to the significant openness of the Slovak economy, while the least significant factor is the growth-stimulating impact of lower commodity prices (via the positive income effect). GDP growth under the scenario is lower than this forecast's GDP growth projections, **by 0.3 percentage point in 2016, 0.7 percentage point in 2017 and 0.4 percentage point in 2018**.

As for HICP inflation under the stress scenario, all three transmission channels have a negative impact on its rate. The most pronounced

Chart A Impact on GP growth and HICP inflation (p.p.)



Sources: NBS calculations.

Table A Technical assumptions of the scenario

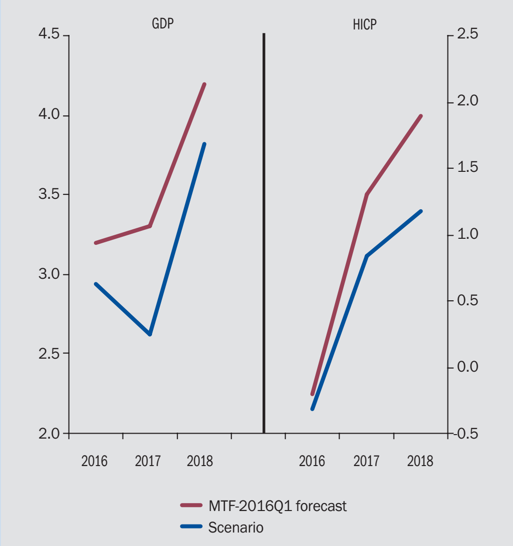
	2016	2017	2018
LOWER DEMAND CHANNEL			
Chinese domestic demand (p.p.)	-2.3	-4.7	-3.0
LOWER COMMODITY PRICES CHANNEL			
oil price (%)	-8.8	-26.0	-37.8
EXCHANGE RATE CHANNEL			
currency depreciation in emerging market economies (%)	-5.0	-10.0	-10.0
Slovakia's effective exchange rate (%)	0.6	1.5	1.5

Sources: NBS calculations.
Note: p.p. = deviation from growth under the baseline scenario, expressed in percentage points; % = deviation from the level under the baseline scenario, expressed as a percentage.

impact is that of the exchange rate channel, with euro appreciation having a marked downward effect on Slovakia's foreign trade and, consequently, a dampening effect on both economic activity and prices. In comparison with the forecast, HICP inflation under the scenario is lower **by 0.1 percentage point in 2016, 0.5 percentage point in 2017 and 0.7 percentage point in 2018**.

The scenario of a Chinese hard landing therefore represents a significant downward risk to the outlooks for both GDP and inflation over the projection horizon. Such an eventuality is not expected, however, to push Slovakia into recession.

Chart B Scenario for GDP growth and HICP inflatione (%)



Source: NBS calculations.

7 Comparison with the previous forecast

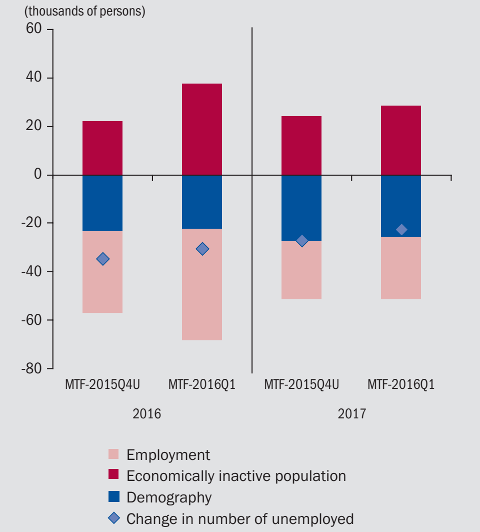
No change to Slovakia's economic growth outlook

Compared with the previous forecast – January's update of the December 2015 Medium-Term Forecast (MTF-2015Q4U) – **the projections for global GDP growth in 2016 and 2017 have been revised down** in this forecast (MTF-2016Q1) by a cumulative 0.8 percentage point. The projected acceleration in foreign demand growth has also been revised down, and the forecasts for export growth are correspondingly lower, particularly in 2017. This will not affect domestic demand, as **weaker inflation** is reflected in stronger real income growth and, consequently, **increasing private consumption**. Similarly, consumption expenditure growth is expected to be moderately higher.

Unchanged labour market outlook

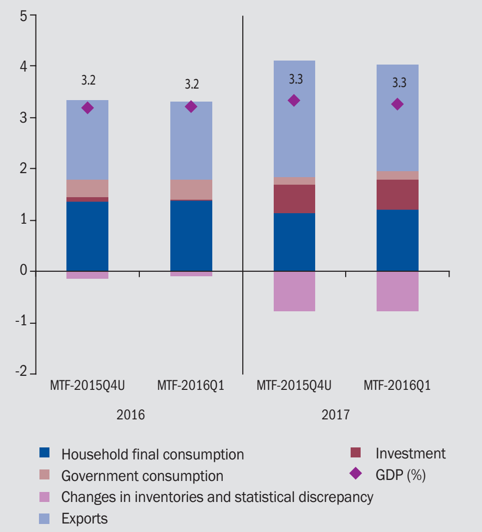
Since current developments in the labour market are fully in line with expectations, the labour market outlooks have not been significantly revised. The projected fall in the unemployment rate is now expected to be more moderate owing to an upward revision of the projected size of the working-age population. At the same time, the assumed inflow of foreign workers has been revised up. The nominal wage growth projections for 2016 and 2017 have been revised down due to the assumed pass-through of lower inflation.

Chart 10 Comparison of labour market indicators (contributions to unemployment)



Sources: SO SR and NBS.

Chart 9 Composition of GDP growth[8] (annual percentage changes; contributions in p.p.)



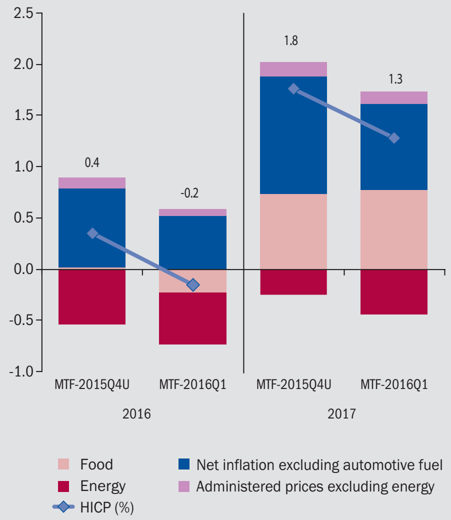
Sources: SO SR and NBS.
Note: The item "Changes in inventories and statistical discrepancy" includes uncategorised imports that remained after the calculation of import intensity.

Downward revision of inflation forecast over the projection horizon

The **inflation forecasts** for 2016 and 2017 **have been revised down**. Current developments imply significantly lower price growth this year, especially in the case of food and services prices. The technical assumption for import prices has also been reduced. The lower projection for inflation rate in 2017 reflects mainly the current subdued assumptions for prices in energy commodity markets. The outlook for net inflation excluding automotive fuel is revised down slightly.

8 *The composition of GDP growth is calculated as the contributions of components to GDP growth after deducting their import intensity. In this case the calculation uses the constant import intensity of the different GDP components (household final consumption – 30%, public consumption – 7%, investment – 50%, and exports – 62.5%). Remaining imports were included under changes in inventories and the statistical discrepancy.*

Chart 11 Comparison of inflation components (annual percentage changes; contributions in p.p.)



Sources: SO SR and NBS.

Public finance projections remain *largely unchanged*

Current estimates have had a favourable impact on the estimated performance of public finances, with tax revenues expected to have increased more than investment (adjusted for the neutral impact of EU funds). Further modest revisions for subsequent years reflect mainly revisions of the outlooks for investment and price indicators. The forecast does not take into account the new government's potential changes to fiscal targets.

Table 7 Medium-Term Forecast (MTF-2016Q1) for key macroeconomic indicators

Indicator	Unit	Actual	MTF-2016Q1			Difference versus MTF-2015Q4 update		
		2015	2016	2017	2018	2016	2017	2018
Prices								
HICP inflation	annual percentage changes	-0.3	-0.2	1.3	1.9	-0.6	-0.5	---
CPI inflation	annual percentage changes	-0.3	-0.1	1.3	1.9	-0.5	-0.5	---
GDP deflator	annual percentage changes	-0.3	0.3	1.9	2.0	-0.6	-0.3	---
Economic activity								
Gross domestic product	annual percentage changes, constant prices	3.6	3.2	3.3	4.2	0.0	0.0	---
Final consumption of households	annual percentage changes, constant prices	2.4	3.7	3.3	3.3	0.1	0.3	---
Final consumption of general government	annual percentage changes, constant prices	3.4	2.3	1.0	1.0	0.3	0.1	---
Gross fixed capital formation	annual percentage changes, constant prices	14.0	0.2	5.0	5.5	-0.6	0.1	---
Exports of goods and services	annual percentage changes, constant prices	7.0	4.1	5.6	8.3	-0.1	-0.5	---
Imports of goods and services	annual percentage changes, constant prices	8.2	3.3	5.7	7.8	-0.4	-0.3	---
Net exports	EUR millions at constant prices	4,269	5,004	5,219	6,012	422	245	---
Output gap	% of potential output	-0.8	-0.7	-0.6	0.0	0.1	-0.1	---
Gross domestic product	EUR millions at current prices	78,071	80,815	85,024	90,330	-338	-696	---
Labour market								
Employment	thousands of persons, ESA 2010	2,267	2,299	2,324	2,349	0.9	1.8	---
Employment	annual percentage changes, ESA 2010	2.0	1.4	1.1	1.1	0.0	0.1	---
Number of unemployed	thousands of persons [1)]	314	284	261	240	3.5	8.1	---
Unemployment rate	%	11.5	10.3	9.5	8.7	0.1	0.2	---
Unemployment gap [2)]	p. p.	1.5	0.5	0.2	-0.3	-0.2	0.0	---
Labour productivity [3)]	annual percentage changes	1.6	1.8	2.2	3.1	0.0	-0.1	---
Nominal productivity [4)]	annual percentage changes	1.2	2.0	4.1	5.1	-0.6	-0.4	---
Nominal compensation per employee	annual percentage changes, ESA 2010	2.4	3.3	3.7	3.8	-0.3	-0.2	---
Nominal wages [5)]	annual percentage changes	2.9	3.3	3.7	3.8	-0.3	-0.2	---
Real wages [6)]	annual percentage changes	3.2	3.4	2.3	1.8	0.1	0.2	---
Households								
Disposable income	constant prices	3.0	3.8	3.1	3.1	0.1	0.1	---
Saving ratio	% of disposable income	8.8	9.1	9.0	8.9	0.6	0.5	---
General government sector [7)]								
General government balance [8)]	% of GDP	-2.7	-2.6	-1.8	-1.1	-0.1	-0.1	---
General debt	% of GDP	52.5	52.9	52.6	51.3	0.4	0.4	---
Total revenue	% of GDP	41.9	39.8	39.1	38.8	0.4	0.4	---
Total expenditure	% of GDP	44.6	42.4	40.9	39.9	0.5	0.5	---
Balance of payments								
Goods balance	% of GDP	2.4	3.1	2.8	3.2	0.4	0.4	---
Current account	% of GDP	-1.3	-0.8	-0.9	-0.1	0.6	0.5	---

Table 7 Medium-Term Forecast (MTF-2016Q1) for key macroeconomic indicators

Indicator	Unit	Actual	MTF-2016Q1			Difference versus MTF-2015Q4 update		
		2015	2016	2017	2018	2016	2017	2018
External environment and technical assumptions								
Foreign demand growth for Slovakia	annual percentage changes	3.3	3.5	4.5	4.8	-0.5	-0.3	---
Exchange rate (EUR/USD) 9)	level	1.11	1.10	1.10	1.10	0.7	0.7	---
Oil price in USD 9)	level	52.5	38.9	44.7	47.1	4.6	1.2	---
Oil price in USD	annual percentage changes	-46.9	-25.9	14.8	5.4	3.7	-3.9	---
Oil price in EUR	annual percentage changes	-36.4	-25.0	14.8	5.4	3.3	-3.9	---
Non-energy commodity prices in USD 9)	annual percentage changes	-19.9	-14.8	3.0	4.7	-9.6	-1.1	---
EURIBOR 3M 9)	% p. a.	0.0	-0.3	-0.3	-0.2	-0.1	-0.2	---
10-Y Slovak government bond yields	%	0.9	0.7	0.9	1.1	-0.2	-0.3	---

Sources: NBS, ECB and SO SR.
1) *Labour Force Survey.*
2) *Difference between the unemployment rate and NAIRU (non-accelerating inflation rate of unemployment). A positive value indicates that the unemployment rate is higher than the NAIRU.*
3) *GDP at constant prices. / employment – ESA 2010*
4) *Nominal GDP divided by persons in employment (according to SO SR quarterly statistical reporting).*
5) *Average monthly wages (according to SO SR statistical reporting).*
6) *Wages according to SO SR statistical reporting, deflated by CPI inflation.*
7) *S.13, fiscal outlook, actual data for 2014.*
8) *B9n - Net lending (+) / borrowing (-)*
9) *Changes vis-à-vis the previous forecast (in per cent).*

Time series of selected macroeconomic indicators can be found on the NBS website at
http://www.nbs.sk/_img/Documents/_Publikacie/PREDIK/2016/protected/P1Q-2016.xls