Report on the Slovak Economy

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Abbreviations

CPI	consumer price index
ČNB	Česká národní banka
EA	euro area
ECB	European Central Bank
EC	European Commission
EMEs	emerging market economies
EONIA	euro overnight index average
ESA 2010	European System of Accounts 2010
ESI	Economic Sentiment Indicator (European Commission)
EU	European Union
EUR	euro
EURIBOR	euro interbank offered rate
Eurostat	statistical office of the European Union
FDI	foreign direct investment
GDP	gross domestic product
GNDI	gross national disposable income
GNI	gross national income
HICP	Harmonised Index of Consumer Prices
IMF	International Monetary Fund
MFI	monetary financial institutions
MF SR	Ministry of Finance of the Slovak Republic
MMF	money market fund
MNB	Magyar Nemzeti Bank
MTF	NBS's Medium-Term Forecast (published on a quarterly basis)
NACE	Statistical Classification of Economic Activities in the European Community (Rev. 2)
NARKS	National Association of Real Estate Offices of Slovakia
NBP	Narodowy Bank Polski
NBS	Národná banka Slovenska
NEER	nominal effective exchange rate
NFC	non-financial corporation
NPISHs	non-profit institutions serving households
OECD	Organisation for Economic Co-operation and Development
p.a.	per annum
p.p.	percentage point
PMI	Purchasing Managers' Index
REER	real effective exchange rate
SASS	Slovenská asociácia správcovských spoločností – Slovak Association of Asset Management Companies

SME	small and medium-sized enterprise
SO SR	Statistical Office of the Slovak Republic
ULC	unit labour costs
ÚPSVR	Ústredie práce, sociálnych vecí a rodiny – Central Office of Labour, Social Affairs and Family
ÚRSO	Úrad pre reguláciu sieťových odvetví – Regulatory Office for Network Industries
USD	US dollar
VAT	value-added tax

Symbols used in the tables
. – Data are not yet available.
- – Data do not exist / data are not applicable.
(p) – Preliminary data

1 Summary

The Slovak economy grew in the second quarter of 2019 by 2.0% year on year (compared with 3.7% in the first quarter) and by 0.5% quarter on quarter. The main driver of growth was consumption, in particular the build-up of inventories (including statistical discrepancy). A negative trend was observed in net exports, accompanied by a slight decline in investment.

The annual rate of employment growth slowed to 1.4% in the second quarter of this year, from 1.8% in the first quarter. This slowdown was largely attributable to a fall in employment in trade. The average wage in the economy rose in the quarter under review by 9.7% (compared with 7.1% in the previous quarter), mainly as a result of accelerating wage growth in services and, in particular, in the public sector.

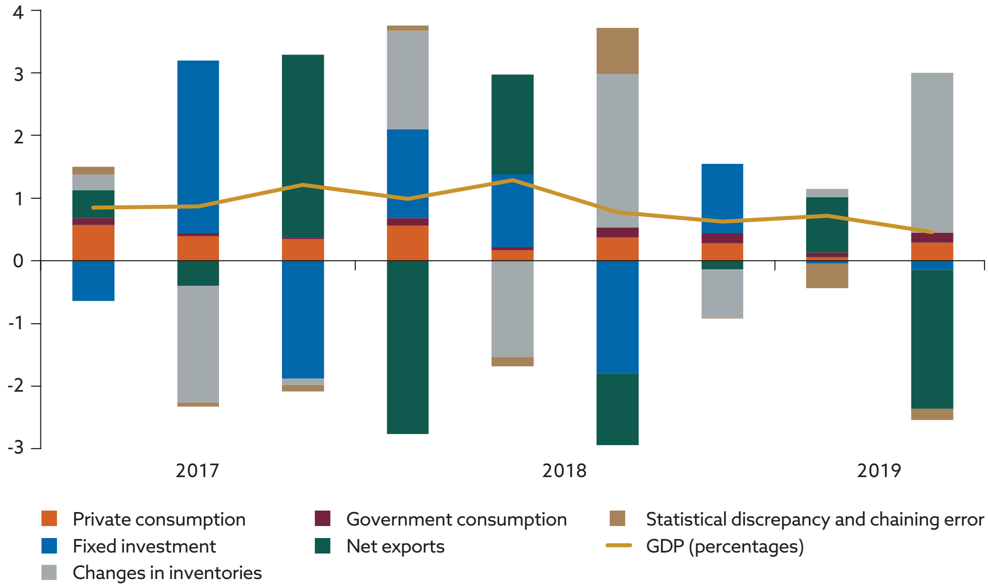
Inflation accelerated in the second quarter of 2019 to 2.6% (from 2.4% in the first quarter), owing mainly to a rise in food prices.

2 Gross domestic product

The Slovak economy expanded in the second quarter of 2019 by 2.0% year on year, representing a marked slowdown caused mainly by a deterioration in foreign trade. After growing considerably in the first quarter, the exports of goods and services suffered a decline in the second quarter. The rate of import growth slowed, too, but to a lesser extent, so net exports made a negative contribution to economic growth. On the side of domestic demand, however, both private and government consumption grew at an accelerating pace over the quarter under review. Fixed investment fell somewhat in that period.

Chart 1

GDP and its components (quarter-on-quarter percentage changes; percentage point contributions; constant prices)

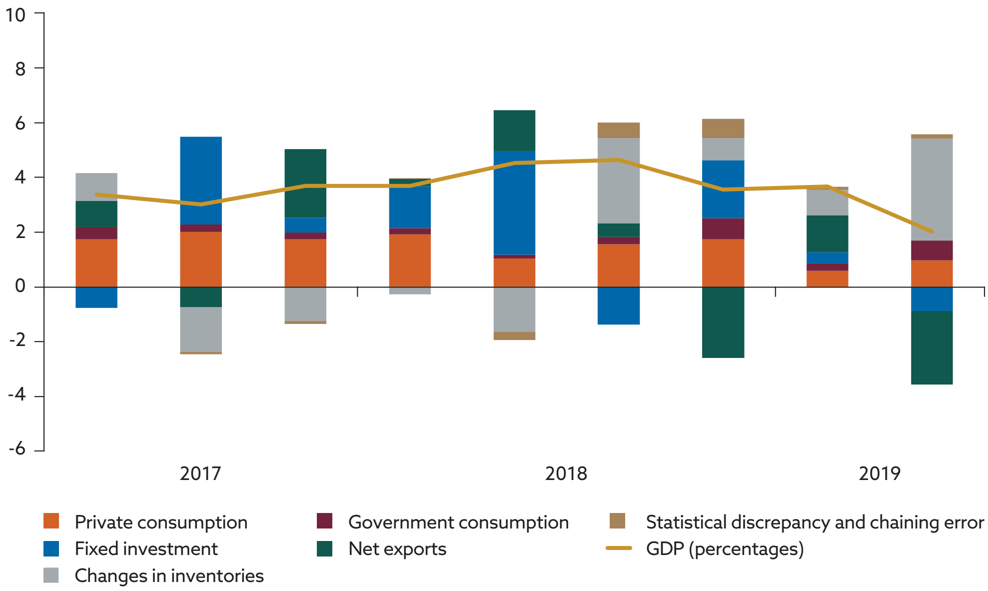


Sources: SO SR, and NBS calculations.

In quarter-on-quarter terms, Slovakia's GDP increased in the period under review by 0.5% (after seasonal adjustment), owing to the effects of changes in domestic demand and, in particular, in the volume of inventories. This was the smallest quarter-on-quarter increase recorded since the second quarter of 2013. It reflected the consequences of cooling of the global economy, coupled surprisingly with slowdown in domestic demand. In response to the resulting uncertainty, investment demand continued to decline in the period under review. Although the favourable situation in the labour market had enabled households to spend more on consumption, they maintained a cautious attitude to spending during that period and thus consumer demand growth was slower than expected. Thus, the saving rate reached its highest level since 2000. Besides the changes in inventories, the only driver of economic growth was public consumption.

Chart 2

GDP and its components (annual percentage changes; percentage point contributions; constant prices; non-seasonally adjusted)



Sources: SO SR, and NBS calculations.

Table 1 GDP by expenditure (percentage changes compared with the previous period; constant prices)

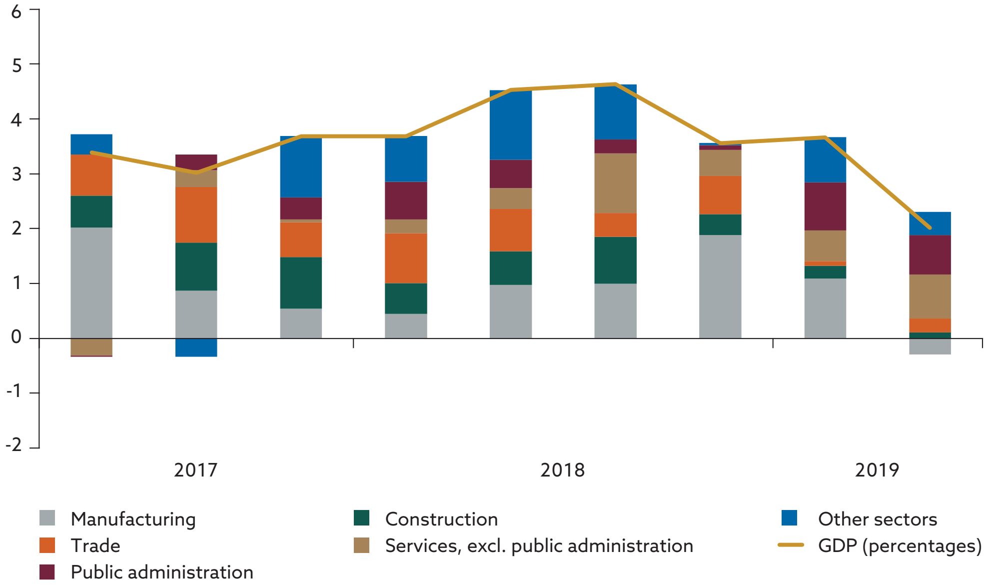
	2018					2019	
	Q1	Q2	Q3	Q4	Year	Q1	Q2
Gross domestic product	1.0	1.3	0.8	0.6	**4.1**	0.7	0.5
Final consumption of households and non-profit institutions serving households	1.1	0.3	0.7	0.5	**3.0**	0.1	0.6
Final consumption of general government	0.7	0.2	0.9	0.9	**1.9**	0.4	0.9
Gross fixed capital formation	6.7	5.2	-7.7	5.2	**6.8**	-0.2	-0.7
Exports of goods and services	-1.7	4.0	0.3	1.9	**4.8**	0.6	-4.6
Imports of goods and services	1.1	2.6	1.6	2.2	**5.3**	-0.2	-2.6

Source: SO SR.

On the production side, the slowdown in economic growth was fuelled mostly by a downturn in manufacturing production. At the same time, value added formation also moderated in construction and in other sectors. This slowdown was partly offset by developments in public administration, and mainly by value added growth in trade and services.

Chart 3

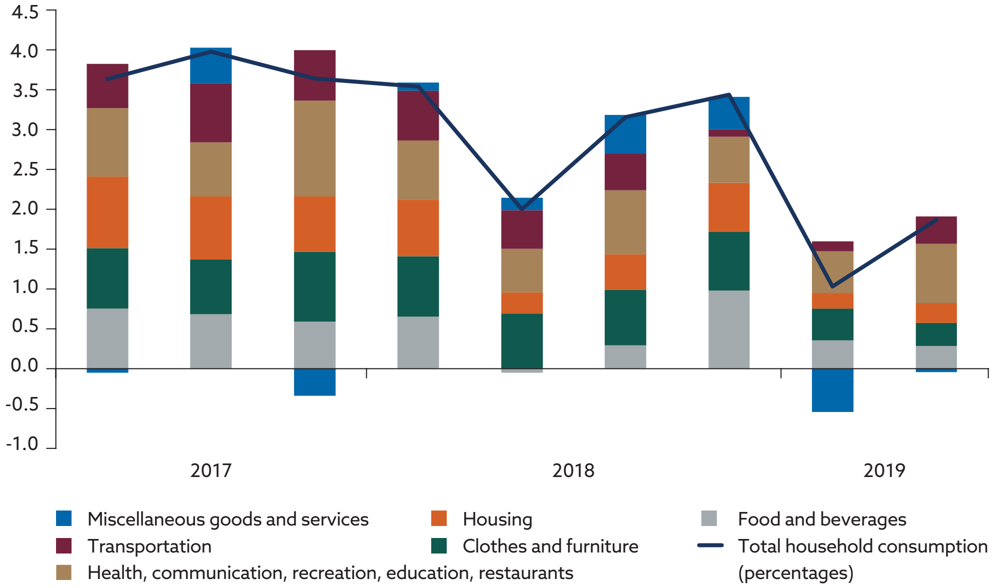
GDP – production-side contributions of sectors to annual percentage changes (percentage points; constant prices; non-seasonally adjusted)



Sources: SO SR, and NBS calculations.

Chart 4

Private consumption of households – contributions to annual percentage changes (percentage points; constant prices; non-seasonally adjusted)

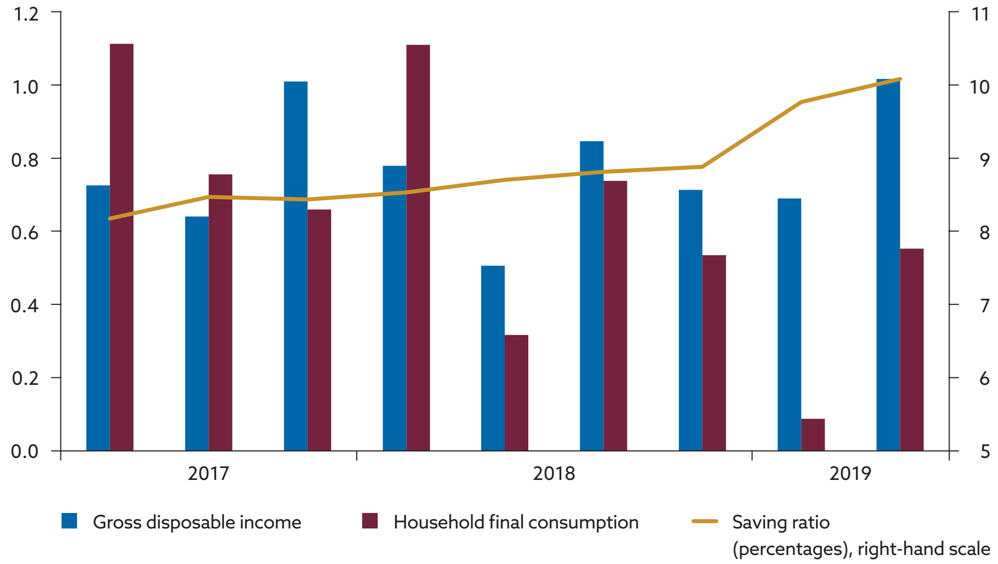


Sources: SO SR, and NBS calculations.

The growth in household final consumption accelerated in the period under review to 1.9% year on year, as a result of continued growth in household income. The favourable trend in the labour market was still reflected in the growing disposable income of households. This growth was supported by a marked increase in the compensation of employees. Within the structure of consumption, expenditure on hotels and restaurants contributed most significantly to the accelerating growth in consumption (owing partly to the introduction of vouchers for domestic holidays). Households also spent more on transportation. A modest increase was also recorded in housing expenses. At the same time, the growth in household spending on food, clothes and footwear continued to slow. After a slowdown in the previous quarter, household expenditure on non-durable and semi-durable goods and services increased again in the period under review. The growth rate of spending on durable goods remained unchanged. The growth in households' disposable income had created conditions for higher consumption, but households continued to give preference to saving over increased consumption. As a result, the saving ratio increased still further.

Chart 5

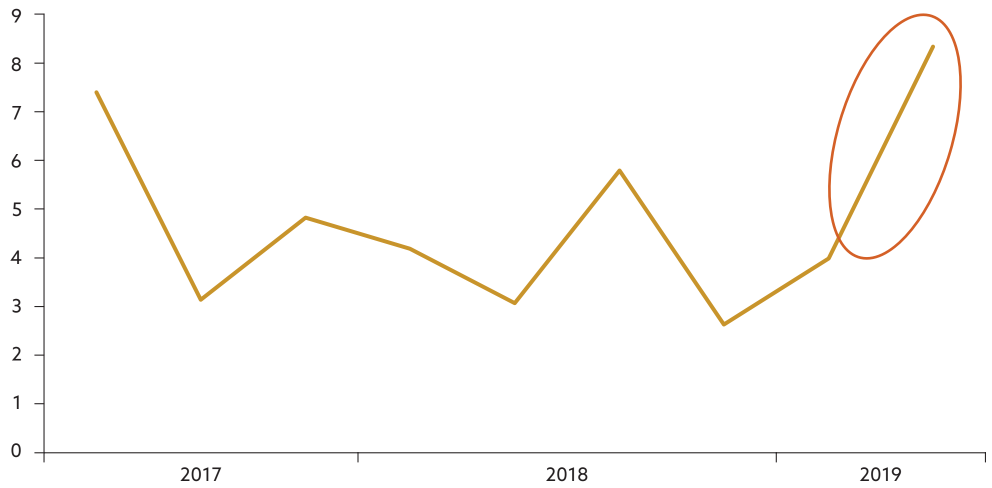
Gross disposable income and consumption of households (quarter-on-quarter percentage changes; constant prices)



Sources: SO SR, and NBS calculations.

Chart 6

Private spending by households on hotels and restaurants (annual percentage changes; constant prices; non-seasonally adjusted)



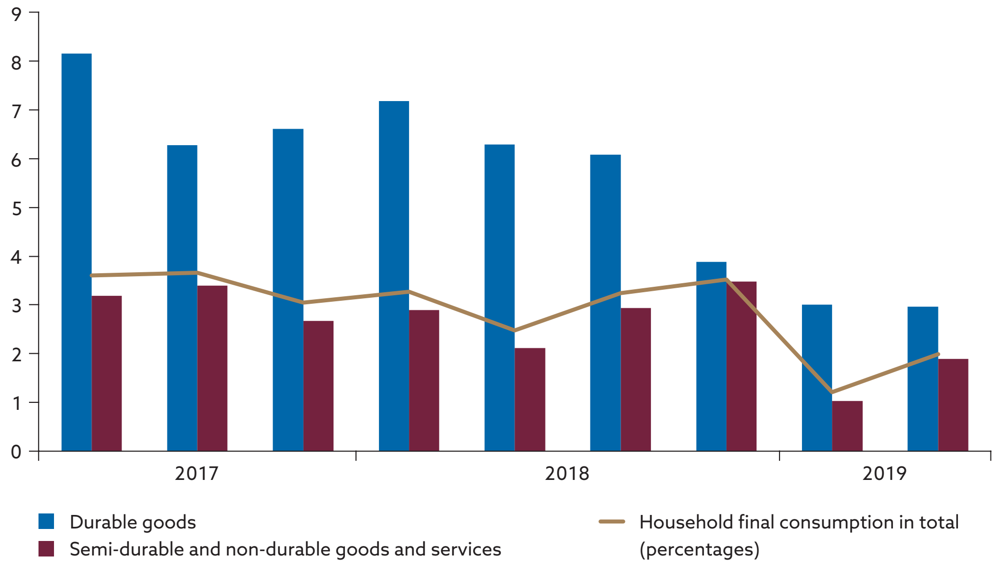
Sources: SO SR, and NBS calculations.

General government consumption rose by 4.2%, representing the steepest rise recorded since 2015. This rise occurred because the marked increase in employee compensation was only partly offset by a year-on-year decrease in expenditure on goods and services.

Fixed investment declined in the period under review by 3.8% year on year, owing to a downturn in investment activity in the non-financial sector accompanied by a moderation in government investment. Investment was probably curbed by the impact of uncertainty related to the unfavourable trend in foreign demand. In the non-financial sector, which contributed most to the slowdown in fixed investment growth, investment was also affected to some extent by the base effect of intense investment activity in the same period a year earlier (in the automotive industry). A rise in investment was recorded in the wood-processing and paper industry and in oil refineries. In terms of assets, investment in residential buildings, information technologies and telecommunications increased, too. The drawdown of resources from EU funds took place broadly in line with expectations. Capital transfers outside the public sector increased slightly and were used mostly for environmental projects. The funds were used predominantly for the investment projects of water supply and wastewater treatment companies.

Chart 7

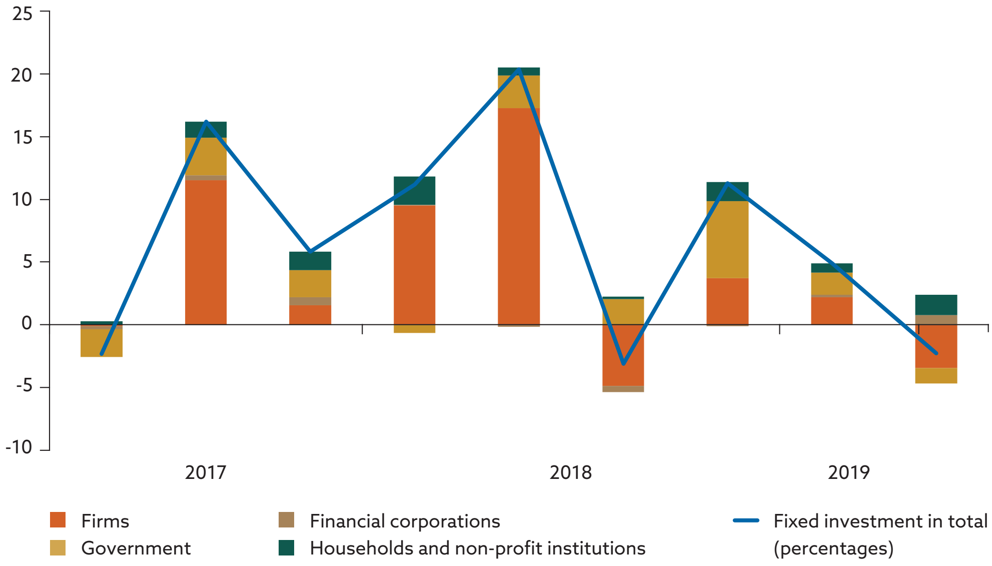
Household consumption broken down by durability of goods consumed (annual percentage changes; constant prices; non-seasonally adjusted)



Sources: SO SR, and NBS calculations.

Chart 8

Investment – sectoral contributions to annual percentage changes (percentage points; current prices; non-seasonally adjusted)



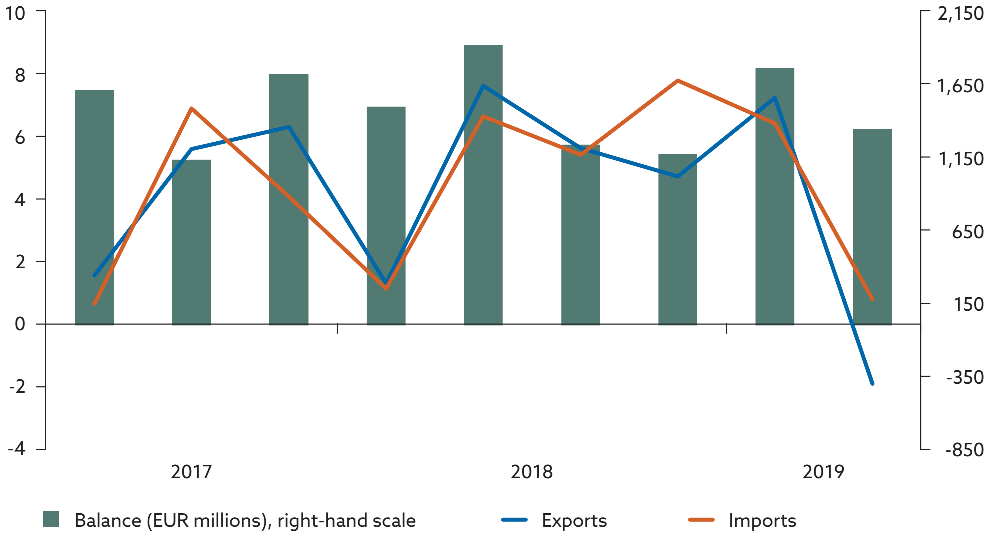
Sources: SO SR, and NBS calculations.

Net exports made a negative contribution to economic growth in the second quarter of this year. Broken down by country, exports to euro area countries recorded a marked slowdown, while exports to non-euro area EU countries fell into decline in year-on-year terms. The monthly data indicate that declines were recorded mainly in exports to the United Kingdom, Sweden and the Czech Republic. Somewhat slower growth was also recorded in exports to Poland. These developments reflected the impact of Brexit uncertainty and the fall in auto part exports via global value chains.

Looking at GDP at current prices as calculated using the income approach, it is evident that the slower economic growth in the second quarter was caused mainly by slower growth in entrepreneurial income (gross profits and mixed income) and, to a lesser extent, by slower growth in tax revenues on products and imports. Income from work remained strong and its contribution to annual GDP growth increased slightly.

Chart 9

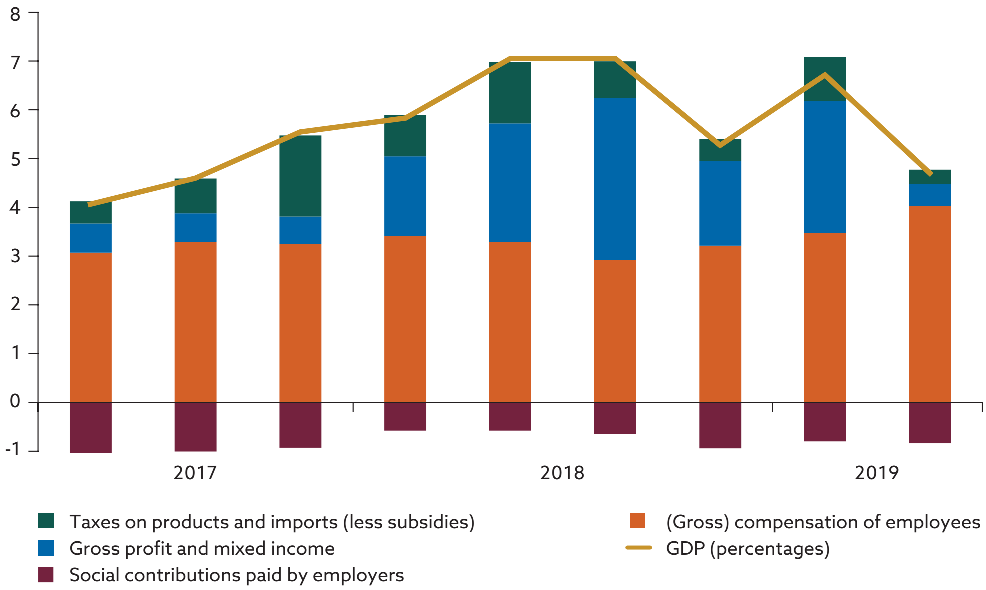
Exports and imports of goods and services (annual percentage changes, constant prices; non-seasonally adjusted)



Sources: SO SR, and NBS calculations.

Chart 10

GDP – revenue-side contributions to annual percentage changes (percentage points; current prices; non-seasonally adjusted)



Sources: SO SR, and NBS calculations.

Box 1
Economic cooling as reflected in the key sectors

Manufacturing production in Slovakia had been growing, quarter on quarter, at a steadily accelerating pace for more than five years. The sector had maintained its position as a stable contributor to GDP growth up to the second quarter of 2019, when it suffered a decline (as the only sector monitored on the production-side of GDP). This decline was attributable to the cooling of the global economy, which, coupled with several one-off factors, pushed the country's key manufacturing segments into negative territory. An exception was the manufacture of motor vehicles (i.e. the most important sector in volume terms), which continued to grow in the second quarter, but at a much slower pace than at the beginning of the year.

The potential for growth in car production and exports would be gradually exploited even if the car manufacturing risks remained unmaterialised, because last year's base was extremely high, but its impulses have faded away this year. The manufacturing sector's concentration on car production, however, strengthened in the period when the risks accumulated and became global. In the first quarter of 2019 the Slovak car industry's production and exports managed to profit from the mounting global risks, due to stockpiling in markets threatened by trade barriers and by Brexit-related uncertainty. With a few exceptions, the effects of stockpiling wore off during the second quarter. After two highly successful quarters at the turn of 2018/2019, the American and British markets ceased to support the exports of cars in the second quarter of 2019, when motor vehicle manufacturing was also hit hard by the cooling German economy.

The suppliers of car manufacturers, i.e. producers of machines, metal products and electrical equipment, were also affected by the economic cooling and recorded a fall in their revenues in the quarter under review. The production and exports of base metals had been exposed to the negative trends seen throughout Europe since the middle of last year (falling demand for steel, growing imports to European markets, rising prices for emission quotas, increasing domestic cost factors, especially wage factors, etc.).

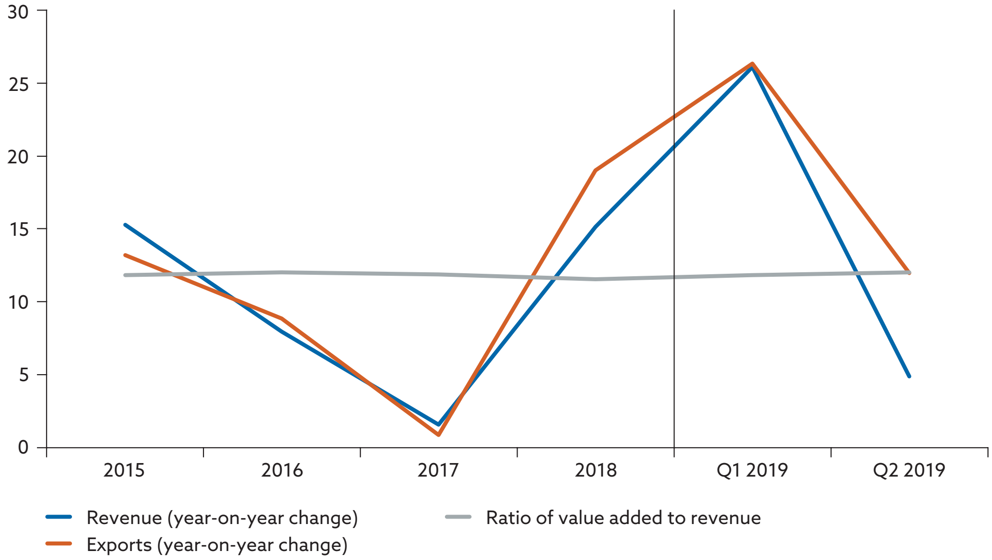
The relatively stable growth in machine industry production and exports turned into decline in the second quarter of 2019. A considerable part of this decline was attributable to machine industry production aimed at supplying the car industry via the Central European automotive supply chain. Shutdowns of production facilities in the machine industry gave rise to concerns, because they interrupted the stable growth in production and exports, as well as the relatively strong value added growth from revenues, recorded by firms with more than 20 employees.

The combined production of two commodities, i.e. electronic and electrical equipment, had long been pushed down by the transfer of manufacturers of electronic equipment within the central European region. The exports of electronic equipment grew even during the period of falling revenues (2015–2017), mainly as a result of re-exports without any significant positive effect on the Slovak economy. By contrast, the production and exports of electrical equipment was performing well, except in the second quarter of 2019. (The imports of electrical machines, instruments and equipment, computers, electronic and optical devices intensified in that period. The increased demand for imports was probably fuelled by the investment needs of firms and sporting events of international importance).

The technological shutdowns in the petrochemical industry planned for the second quarter of 2019 were of one-off nature; they led to planned shutdowns in the production and exports of refined oil products.

Chart A

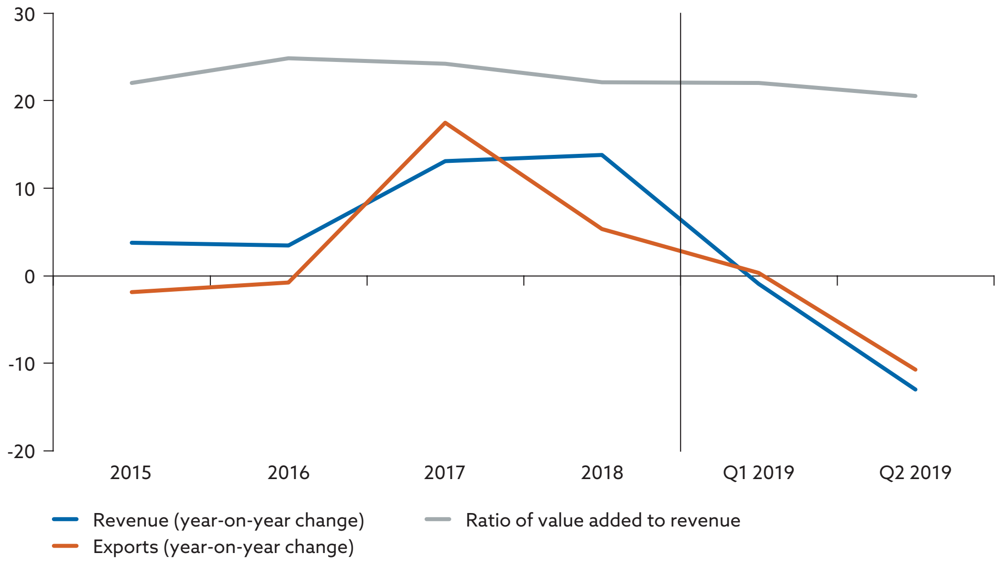
Manufacture of motor vehicles (%)



Sources: SO SR, and NBS calculations.

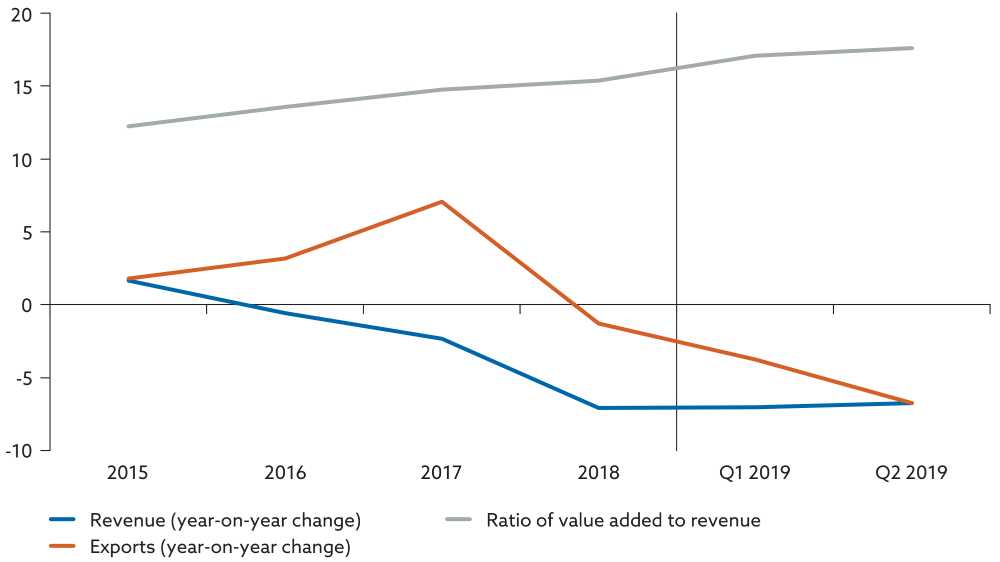
Chart B

Manufacture of base metals and metal products (%)



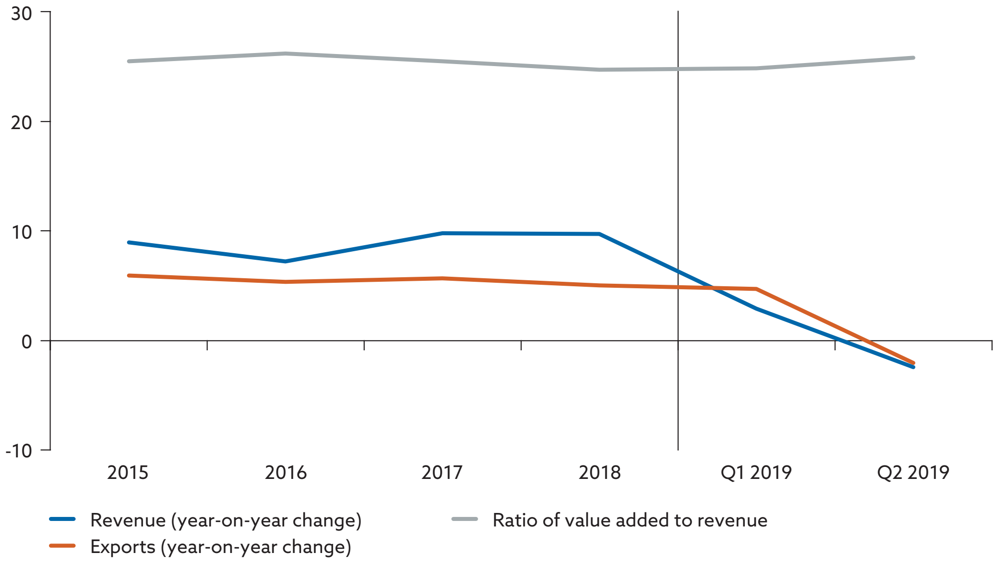
Sources: SO SR, and NBS calculations.

Chart C
Manufacture of electronic and electrical equipment (%)



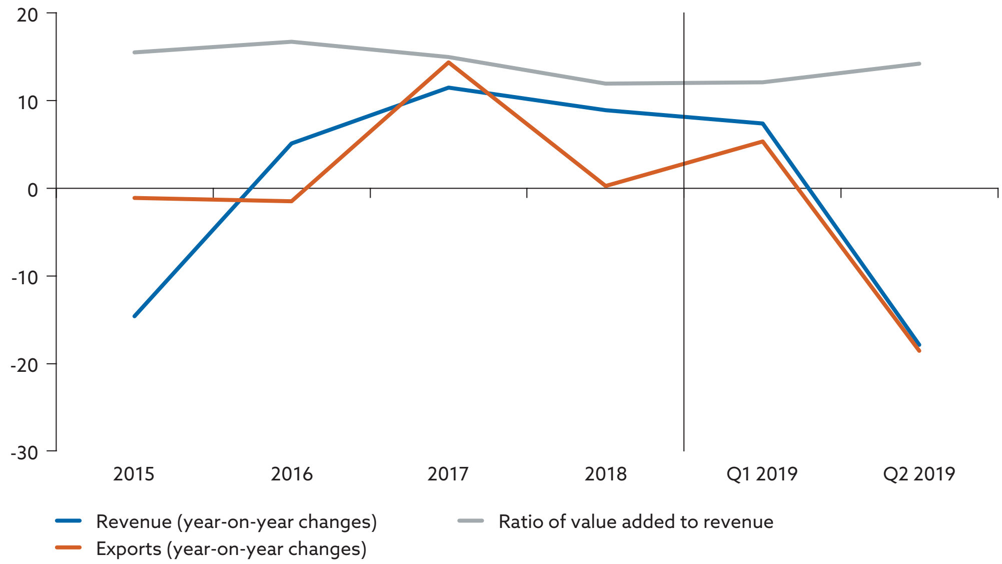
Sources: SO SR, and NBS calculations.

Chart D
Manufacture of machinery and equipment (%)



Sources: SO SR, and NBS calculations.

Chart E
Manufacture of petroleum and chemical products (%)



Sources: SO SR, and NBS calculations.

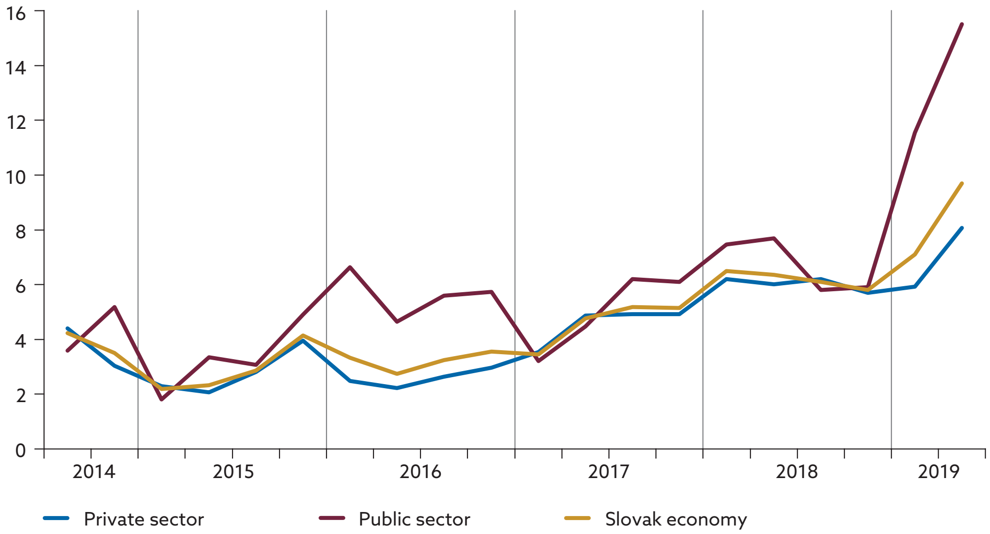
3 The labour market

3.1 Wages and labour productivity

The average wage in the Slovak economy rose considerably in the second quarter of 2019. Its growth rate accelerated by 2.6 percentage points compared with the previous quarter, to 9.7%. This development was a result of strong wage growth in the public sector. The two-digit annual rate of wage growth in the public sector since the beginning of the year (11.5% in the first quarter and 15.5% in the second quarter) was caused by an increase in the contractual wages of employees working in public and state services. Wage growth in the second quarter was also driven by increases in bonuses and other wage components (thirteenth salary). The accelerating wage growth was also fuelled by the private sector, especially by services, marked by relatively dynamic wage growth for a longer period. Wage growth in the second quarter was also stimulated by a rise in extra pays (since May 2019). On the other hand, wage growth in industry and construction slowed in year-on-year terms. In these sectors, the higher costs of extra pays were probably offset by the lower bonuses paid by smaller firms and entrepreneurs in particular. In addition, the number of hours worked in industry decreased for a second successive quarter.

Chart 11

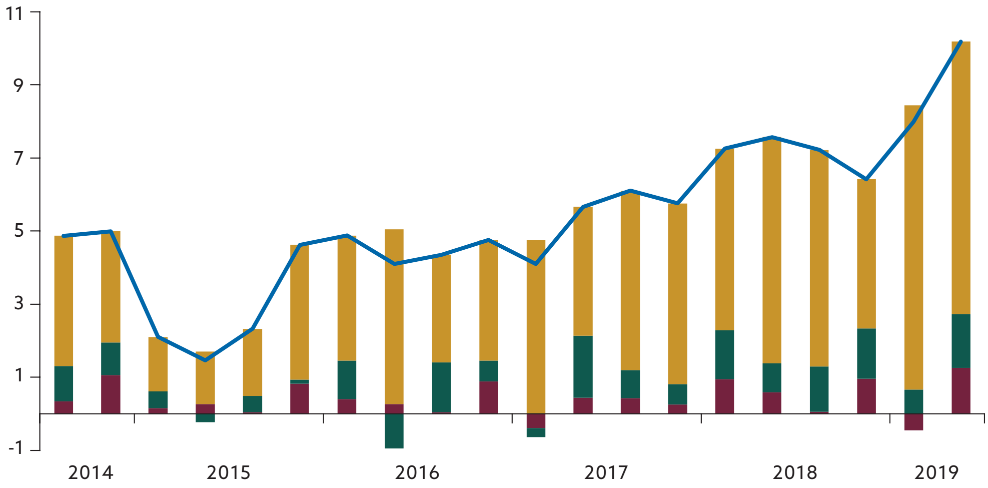
Wage levels in the public and private sectors and in the overall economy (annual percentage changes)



Sources: SO SR, and NBS calculations.
Note: The data for the public sector were calculated on the basis of developments in the categories O, P and Q of the NACE classification.

Chart 12

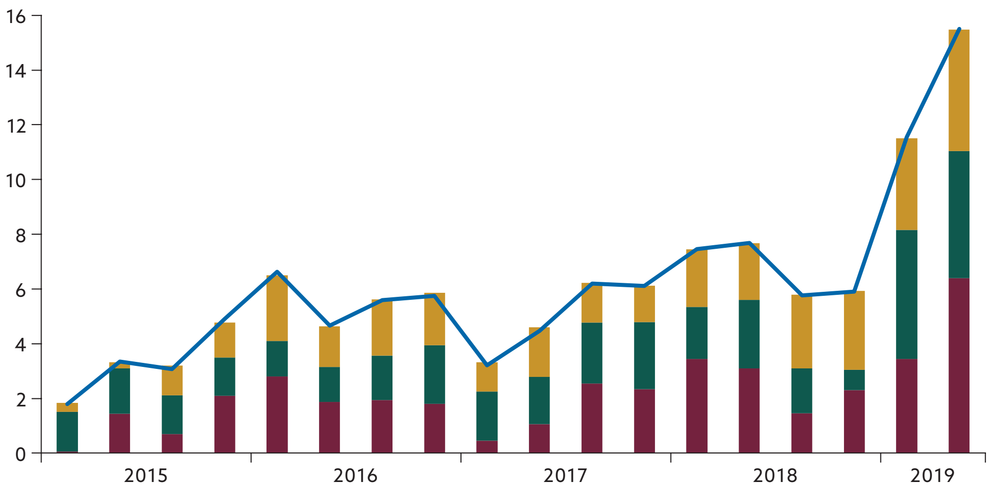
Average wage components (annual percentage changes; percentage point contributions)



Sources: SO SR, and NBS calculations.
Note: The data for organisations with 20+ employees include organisations in the public and financial sectors, irrespective of the number of employees.

Chart 13

Wage developments in the public sector (annual percentage changes; percentage point contributions)



Sources: SO SR, and NBS calculations.

Compensation per employee, i.e. gross wages and other employee-related expenses, rose in the second quarter of this year by 8.4% year on year, representing an acceleration in comparison with the previous quarter (6.3%). This development was influenced by the same economic fundamentals as those determining the average wage. In the long-term, nominal wages grew at a faster pace than nominal labour productivity. As a result of a marked increase in the average wage, the gap between these indicators widened further in the quarter under review. Unit labour costs increased in that period by 8.1% year on year (after seasonal adjustment). In terms of wage growth, Slovakia still only lagged behind the V4 countries, i.e. Hungary and the Czech Republic, where wages had been rising more steeply over the last few quarters. The accelerating wage growth, however, is supposed to enable Slovakia to maintain its wage-based competitiveness in relation to the neighbouring countries.

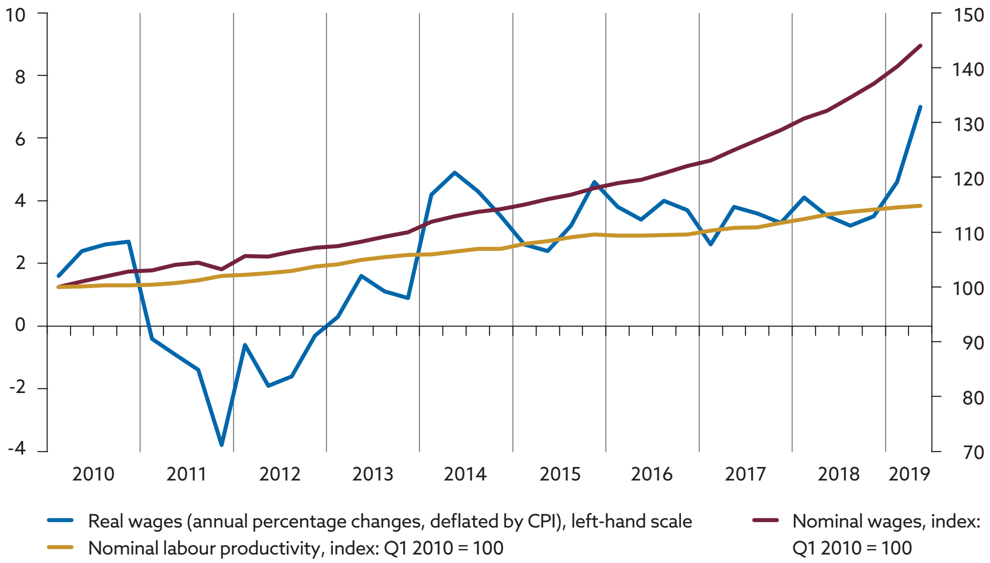
Table 2 Wages and labour productivity (annual percentage changes)

	2018					2019	
	Q1	Q2	Q3	Q4	Year	Q1	Q2
Average wage (headline)	6.5	6.4	6.1	5.8	**6.2**	7.1	9.7
Consumer price inflation	2.3	2.8	2.7	2.2	**2.5**	2.4	2.5
Average real wage (headline)	4.1	3.5	3.3	3.5	**3.6**	4.6	7.0
Average wage (ESA 2010)	6.2	6.2	5.5	4.9	**5.7**	6.4	8.8
Compensation per employee (ESA 2010)	5.4	5.6	5.3	5.5	**5.4**	6.3	8.4
Nominal labour productivity (ESA 2010)	3.5	4.8	5.0	3.5	**4.2**	4.8	3.2
Real labour productivity (ESA 2010)	1.4	2.3	2.7	1.8	**2.1**	1.8	0.6

Sources: SO SR, and NBS calculations.
Note: Average wages (headline) are based on data from SO SR statistical reports. Average real wages were calculated on the basis of CPI inflation. Labour productivity (ESA 2010) was calculated as the ratio of nominal GDP to employment as defined in the ESA 2010 methodology.

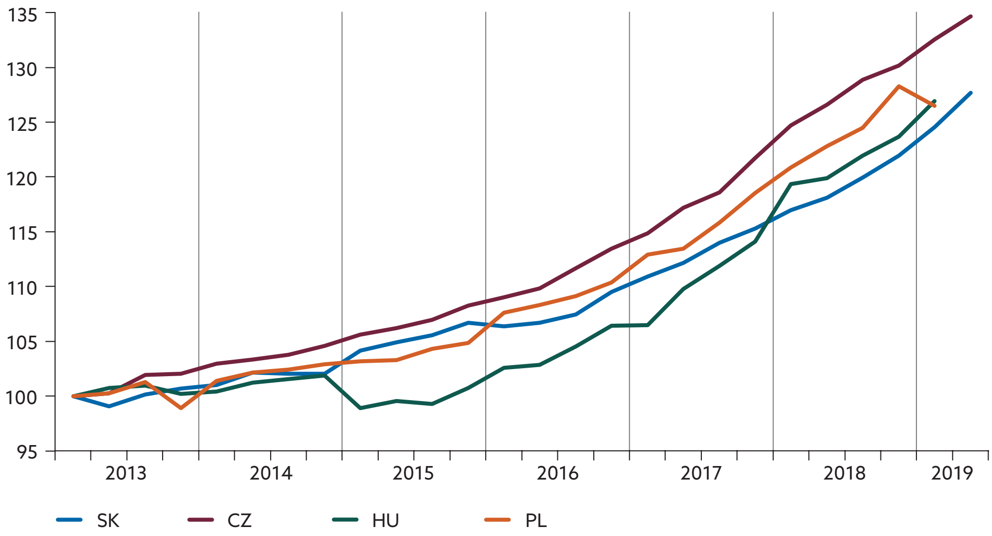
Chart 14

Wages and labour productivity (percentages; index)



Sources: SO SR, and NBS calculations.
Note: Wages are based on data from SO SR statistical reports. Nominal labour productivity was calculated from employment according to SO SR statistical reports. Base indices are based on seasonally adjusted data.

Chart 15
Unit labour costs in the V4 countries (index, Q1 2013 = 100)



Sources: Eurostat, and NBS calculations.

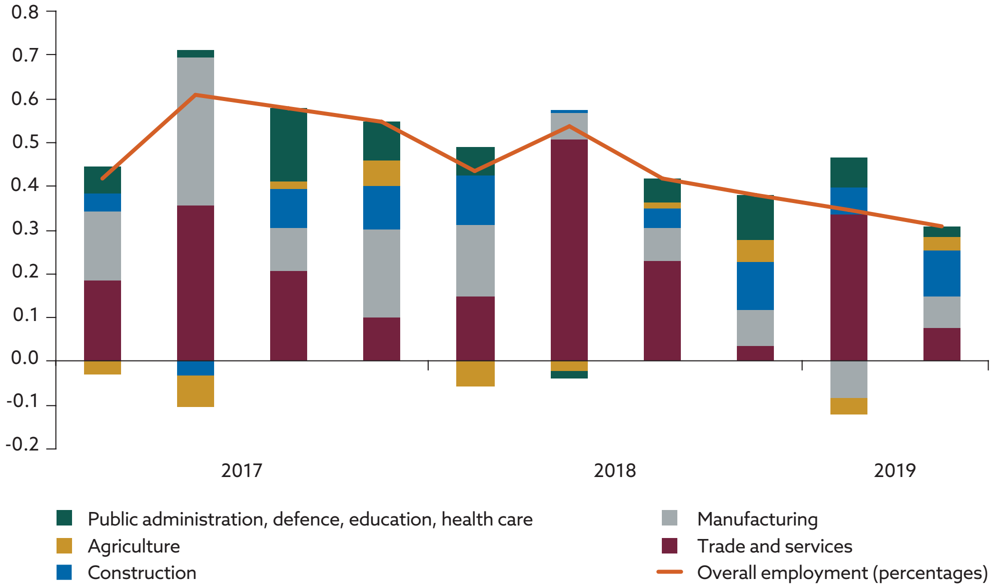
3.2 Employment and unemployment

The annual rate of employment growth slowed slightly in the second quarter of 2019, i.e. by 0.4 percentage point compared with the previous quarter, to 1.4%. The slowdown was caused mainly by employment in trade, which fell quarter on quarter for a second successive quarter. This was probably due to the shortened opening hours and reduced number of shifts worked (since the previous year). The wage costs of employers increased in the period under review, owing partly to legislative changes, hence they took steps to limit on the number of extra hours worked in trade, as well as in other sectors. Other sectors maintained stable employment growth quarter on quarter, with certain restrictions imposed on the number of hours worked. Relatively dynamic employment growth (4.7%) was recorded in the construction sector. In manufacturing, employment grew at the same pace as in the previous quarter (0.6%), but the cooling of activity in this sector is likely to affect employment, too. The most optimistic situation can be currently seen in the services sector, mainly in IT services and in services related to tourism.

In view of the slowdown in economic activity, employers are cautious in hiring new employees. This is also indicated by a moderate decrease in the number of job vacancies, mainly in manufacturing.

Chart 16

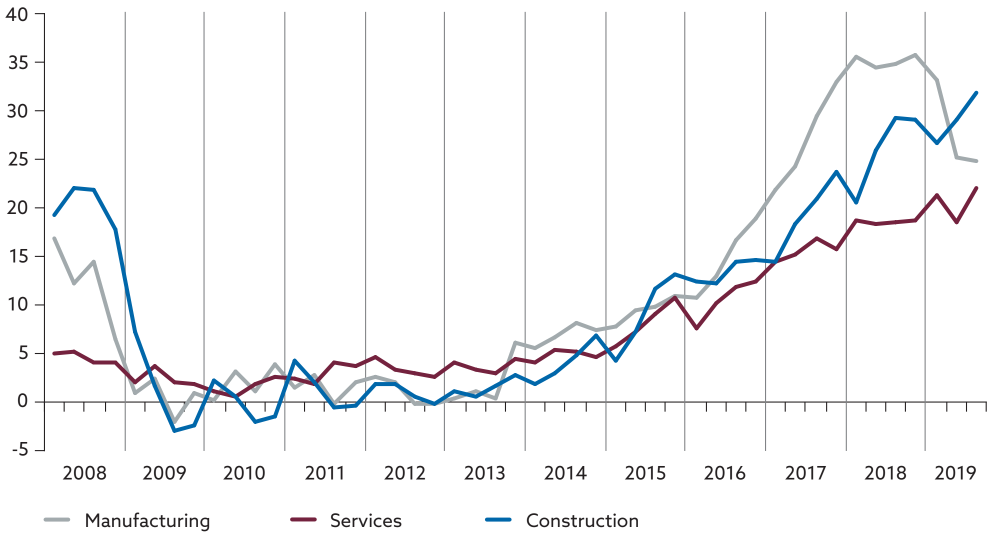
Employment – sectoral contributions to quarter-on-quarter percentage changes (percentage points)



Source: SO SR.

Chart 17

Perceived labour shortages broken down by sector (percentage of respondents)

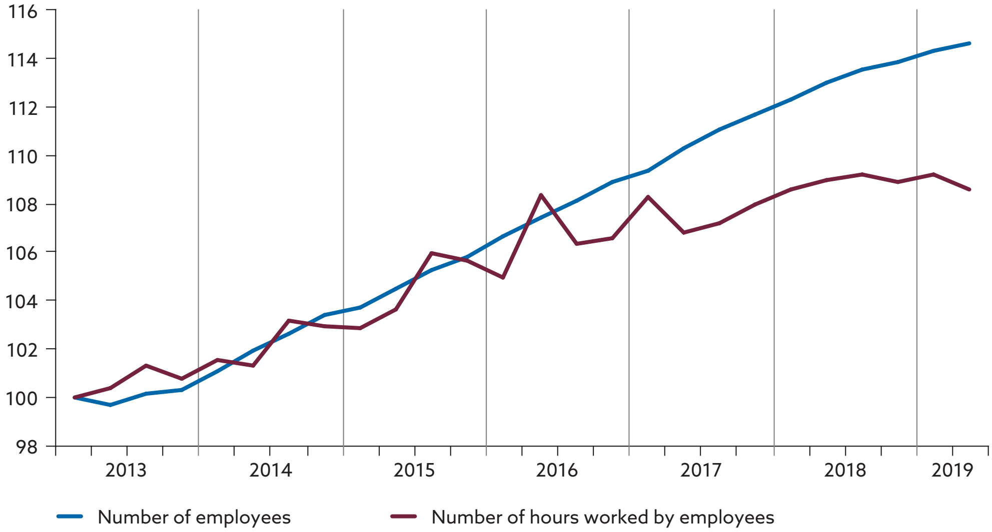


Sources: EC, and NBS calculations.
Note: The data on construction for Q3 2019 are average figures for July and August 2019.

The number of unemployed (according to the LFS methodology) was stagnant over the second quarter of this year. The seasonally adjusted number of unemployed fell by only slightly more than 800 persons, quarter on quarter. The unemployment rate thus reached 5.8% as in the previous quarter. The declining trend in the number of Slovak citizens working abroad stabilised, too, and remained broadly unchanged quarter on quarter. The growth in the number of foreigners working in Slovakia also moderated in the period under review.

Chart 18

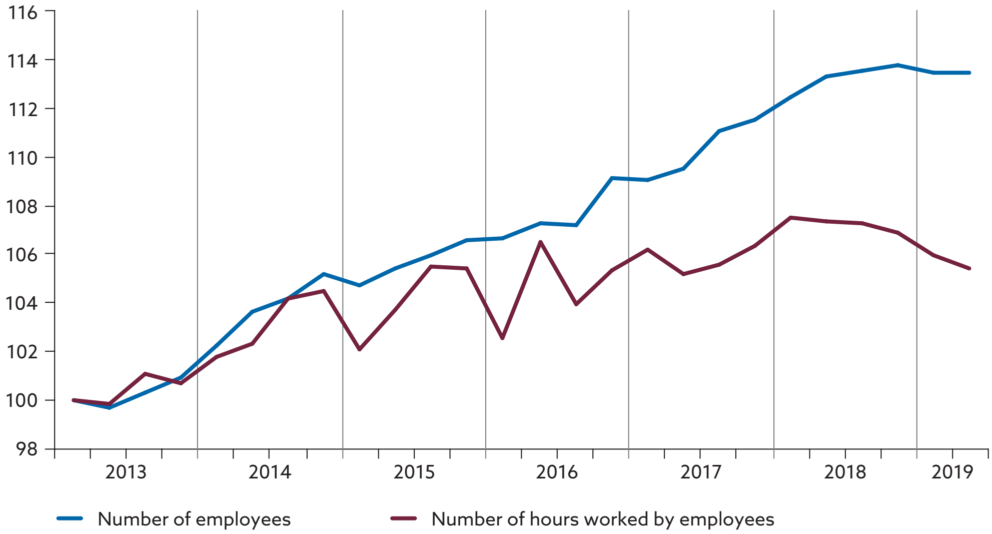
Employment growth and the number of hours worked in the economy (ESA methodology; index: Q1 2013 = 100)



Sources: SO SR, and NBS calculations.

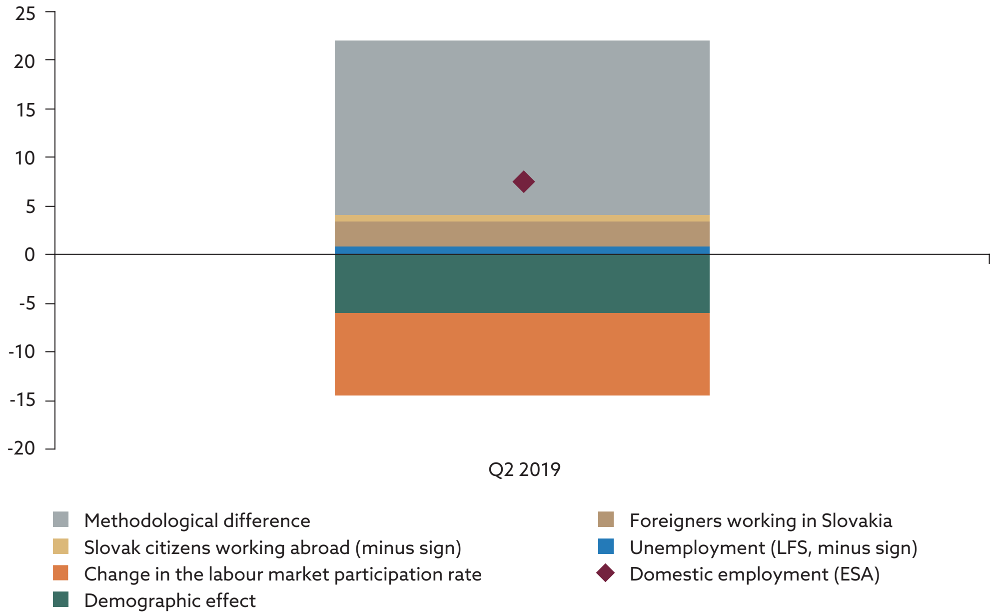
Chart 19

Employment growth and the number of hours worked in trade (ESA methodology, index: Q1 2013 = 100)



Sources: SO SR, and NBS calculations.

Chart 20
Employment – contributions of principal labour market variables to quarter-on-quarter changes (thousands of persons)



Sources: SO SR, and NBS calculations.
Note: The 'foreigners working in Slovakia' time series has not been seasonally adjusted owing to its short history. The seasonality observed in this time series, however, appears to be insignificant. The 'methodological difference' item includes the effect of residual differences between the LFS and ESA methodologies.

4 Price developments

Inflation accelerated in the second quarter of 2019, to 2.6% (from 2.4% in the previous quarter), **owing to an increase in food prices.**

Food prices increased mainly as a result of a rise in unprocessed food prices (meat and vegetable prices). Meat prices rose in response to growth in foreign demand in connection with the spread of African swine fewer around the world. The persisting dynamic growth in labour costs continued to contribute to the relatively steep year-on-year increase in processed food prices. This was reflected mainly in the rapidly rising prices of bakery products and products made from flour (since the beginning of 2019). Processed food inflation accelerated only slightly in comparison with the first quarter.

The annual rate of increase in energy prices reached almost 5% in the second quarter, too. This increase was dampened by the continuing moderate year-on-year decline in Brent oil prices (in euros), which reflected the persistent concerns about the tightening of customs barriers in the world.

Annual services inflation remained stable during the period under review, despite strong wage growth in the services sector. In all probability, effective demand for services in the middle-income group of households remained low. Cost impulses were thus dampened by the lower level of demand, compared with the services sector's available capacities.

Non-energy industrial goods prices increased at a somewhat faster pace in the second quarter of 2019. The slight acceleration was caused by a rise in prices for durable goods. Their year-on-year rise slowed in the first quarter as a result of a time shift in the price increase for used cars. In February 2019, used car prices recorded a temporary fall on a year-on-year basis. In the period from March to June, the rate of price increase stabilised. Thus, the rate of increase in durable goods prices accelerated in the second quarter.

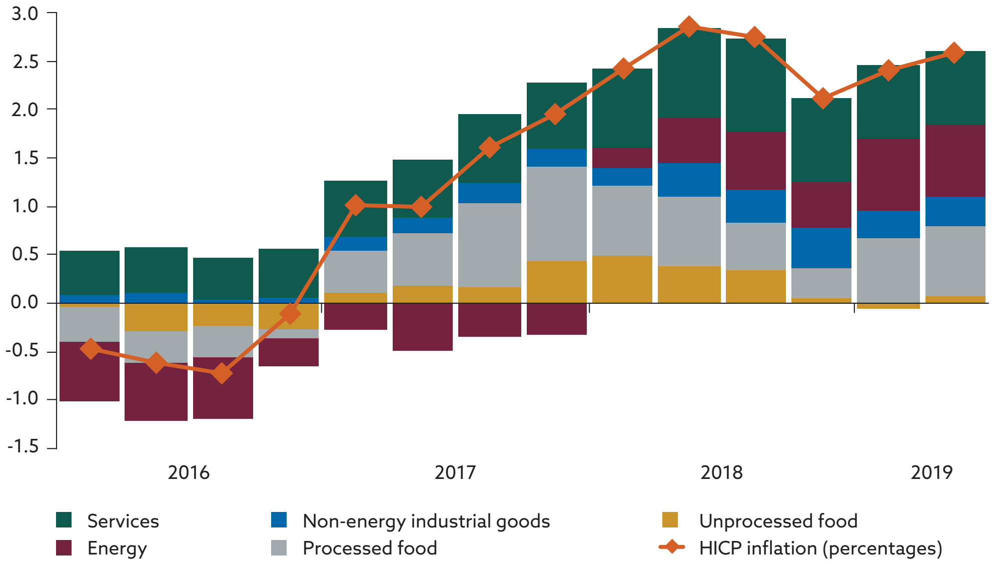
Table 3 Annual percentage changes in consumer price inflation by component

	2018					2019	
	Q1	Q2	Q3	Q4	Year	Q1	Q2
HICP inflation	2.4	2.9	2.7	2.1	**2.5**	2.4	2.6
Unprocessed food	11.0	8.8	7.1	0.4	**6.8**	-0.9	1.9
Processed food	3.4	3.4	2.3	1.5	**2.7**	3.3	3.5
Non-energy industrial goods	0.7	1.2	1.2	1.4	**1.1**	1.0	1.1
Energy	1.4	3.3	4.0	3.2	**3.0**	4.8	4.7
Services	2.6	2.9	3.1	2.7	**2.8**	2.4	2.4

Sources: SO SR, and NBS calculations.

Chart 21

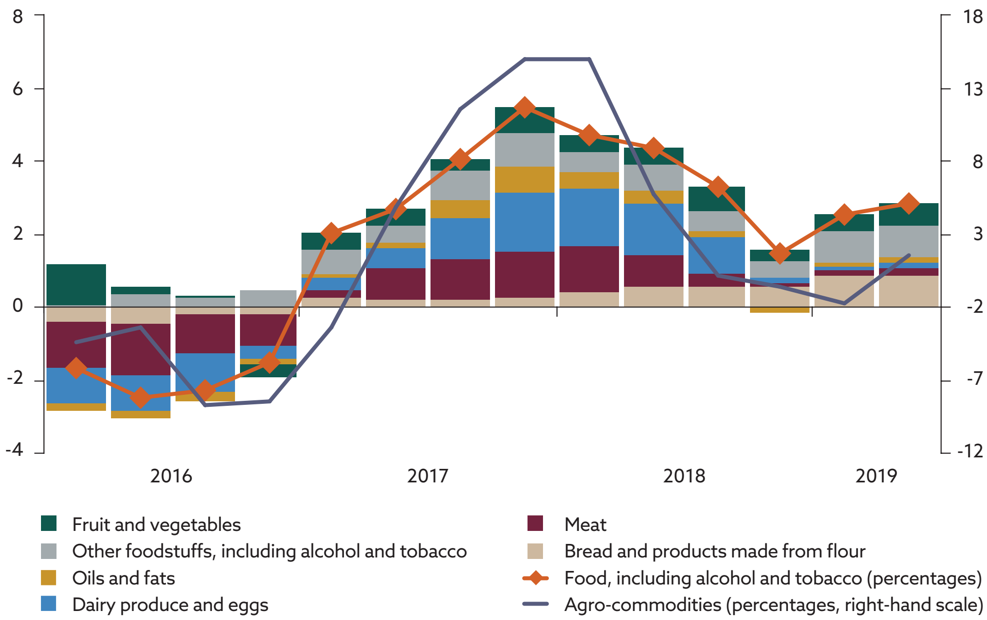
HICP inflation by component (annual percentage changes; percentage point contributions)



Sources: SO SR, and NBS calculations.

Chart 22

Food price inflation by component (annual percentage changes; percentage point contributions)



Sources: SO SR, and NBS calculations.