NÁRODNÁ BANKA SLOVENSKA


# Annual Report
2003

## Contents

**Foreword**

Macroeconomic and monetary developments in the Slovak Republic in 2003 were affected by the implementation of measures, which were directly or indirectly connected with the forthcoming entry of Slovakia into the European Union. These measures included the elimination of price distortions through adjustments to regulated prices, changes in indirect taxes, and the initiation of consolidation in public finances.

Price developments were determined first and foremost by a marked increase in regulated prices and excise duties, which led to an acceleration in the 12-month inflation rate, from 3.4% in December 2002 to 9.3% in December 2003. Administrative adjustments were responsible for more than 75% of the rise in consumer prices. Due to the absence of demand-based pressures, however, the profound impact of cost factors on price levels produced no marked secondary effects, which is documented by the relatively low level of core inflation (3.0%). In addition to a fall in effective demand, the price increase was also dampened by an appreciation in the exchange rate of the Slovak koruna, especially against the US dollar, but vis-à-vis the euro as well.

The increase in household spending on goods and services with regulated prices, accompanied by a fall in real wages, resulted in a drop in final household consumption. This, coupled with the effect of continuing decline in investment demand, led to a fall in domestic demand. Despite this development, the Slovak economy showed relatively dynamic growth (4.2%), which was, in contrast with the previous year, stimulated exclusively by foreign demand. As a result of export efficiency surpassing import intensity the balance of net exports at constant prices in 2003 improved significantly.

In the balance of payments, the current account deficit as a share of GDP diminished from 8.1% in 2002 to 0.9% in 2003. This development was due primarily to a favourable trend in the trade balance, mainly the dynamic growth in exports, achieved despite a downturn in economic activity in the countries of our most important trading partners. The increase in Slovakia's export efficiency was closely connected with the foreign direct investments made in previous years, with the most dynamic growth in exports being recorded in the automobile industry.

A factor stabilising the Slovak economy in 2003 was the launch of the process of consolidation in public finances, causing the ratio of the public sector deficit to GDP to drop to 3.6%, from 5.7% in 2002. This, together with the preparation of further reforms in health services, the pension system, social security, and tax systems, helped improve the image of Slovakia, which is documented by an increase in the country's credit rating and its growing popularity among foreign investors.

Under conditions of renewed price deregulation and increased indirect tax rates, the objective of the monetary policy of the NBS in 2003 was to prevent, through monetary policy instruments, the aforementioned administrative measures from exerting profound secondary effects. The impact of administrative measures on the level of effective demand in the household sector and the marked excess of growth in labour productivity over growth in real wages, however, hindered the effect of demand-based pressures on prices and imports. The stagnation of private consumption, coupled with a fall in investment demand, led to a decline in domestic demand. In view of the absence of demand-based pressures in the economy and the attempt to maintain the positive trends of development in the Slovak economy (including its balanced growth), the Bank Board of the NBS decided to lower its key interest rates in September and December, equally by 0.25 of a percentage point.

To bring its monetary-policy tools into harmony with those applied by the ECB, the NBS reduced the ratio of required reserves to 3% with effect from 1 January 2003, and with effect from 1 January 2004 to 2%, which corresponds to the reserve ratio used in the euro area.

In 2003, the situation in the banking sector stabilised, due to the results of banks achieved in 2002, when, among other things, the productivity of assets increased, competition on the market for bank products intensified, and the prudential rules and regulations were obeyed. In this area, a qualitative change was made in the calculation of the adequacy of own resources, with the coming into effect of the decree concerning the adequacy of own resources (on 1 January 2003), stipulating that market risks are to be taken into account as well, in addition to the credit risk.

The year 2003 also saw the coming into effect of numerous other decrees, amendments, laws and other regulations, which will certainly improve the work of banking supervision.

With effect from 1 January 2003, a significant change was effected in the interbank payment system of the Slovak Republic. The National Bank of Slovakia took over the operation of the payment system from the National Clearing Centre of Slovakia, and thus became the operator and clearing agent of the SIPS (Slovak Interbank Payment System).

The rationale behind this change was the attempt of the National Bank of Slovakia to increase the effectiveness and security of the payment system by adopting RTGS (Real Time Gross Settlement) based on the latest information technology. The system was put into operation on 1 April 2004. Another reason was the price policy based on the principle of full return on expenditures, which meant, in the final analysis, a substantial multiple reduction in transfer charges for the participants in the SIPS.

To accomplish the tasks in the area of currency circulation, the National Bank of Slovakia ensured the reprinting of banknotes in the nominal value of Sk 5,000 and the minting of coins in the nominal values of 50 haliers, 2 koruna, and 10 koruna. With regard to the low real value and high production

/ processing cost of coins of the two lowest nominal values, 10- and 20-halier coins were withdrawn from circulation and ceased to be used as legal tender with effect from 31 December 2003.

In addition to banknotes and coins, the National Bank of Slovakia issued four types of commemorative coins of precious metals, in order to mark the anniversaries of important personalities and events from Slovak history. Of special importance is a unique set of seven rectangular coins with motifs from the Slovak banknotes, issued to mark the 10th anniversary of the establishment of the National Bank of Slovakia and the birth of the Slovak currency. On this occasion, an exhibition was staged at the head office of the National Bank of Slovakia, where visitors could get acquainted with the history, preparation, and birth of the new Slovak currency.

The construction of branch offices was completed in 2003. The branch offices of the NBS are equipped with the latest technology for the safekeeping of money and the processing of banknotes and coins.

By joining the European Union on 1 May 2004, the Slovak Republic has become a member of the Economic and Monetary Union with the status of a member state with a derogation, i.e. a country which has not yet adopted the euro. In future, after creating conditions for entry into the monetary union in compliance with the convergence criteria, the Slovak Republic is supposed to join the euro area. The adoption of the single European currency is expected to provide a basis for the completion of the process of integration, balanced growth in the Slovak economy, and accelerated convergence towards the more advanced part of the EU.

May 2004

Jusko

Marián Jusko
Governor

Members of the NBS Bank Board in 2003

First row, from left to right:
Elena Kohútiková, Deputy Governor
Marián Jusko, Governor
Ivan Šramko, Deputy Governor

Second row, from left to right:
Jozef Košnár, Professor at the University of Economy in Bratislava
Karol Mrva, Chief Executive Director, Trade and Foreign Exchange Division
Ján Mathes, Chief Executive Director, Currency Division