

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 third quarter of 2019 by 1.3% year on year (compared with 2.2% in the second quarter) and by 0.4% quarter on quarter. The main driver of growth was domestic demand. The slowdown was due to the negative contribution of net exports. Exports suffered a year-on-year decline, which was, however, more modest than in the previous quarter. Investment experienced a revival, in particular investment by non-financial corporations.

The annual rate of employment growth slowed in the third quarter of 2019, to 1% (from 1.4% at the end of the previous quarter). Employment growth weakened in manufacturing, trade and services. Despite a slowdown, the average wage growth remained strong (7.7%) in the third quarter of this year (compared with 9.7% in the second quarter), owing to wage increases in the public sector.

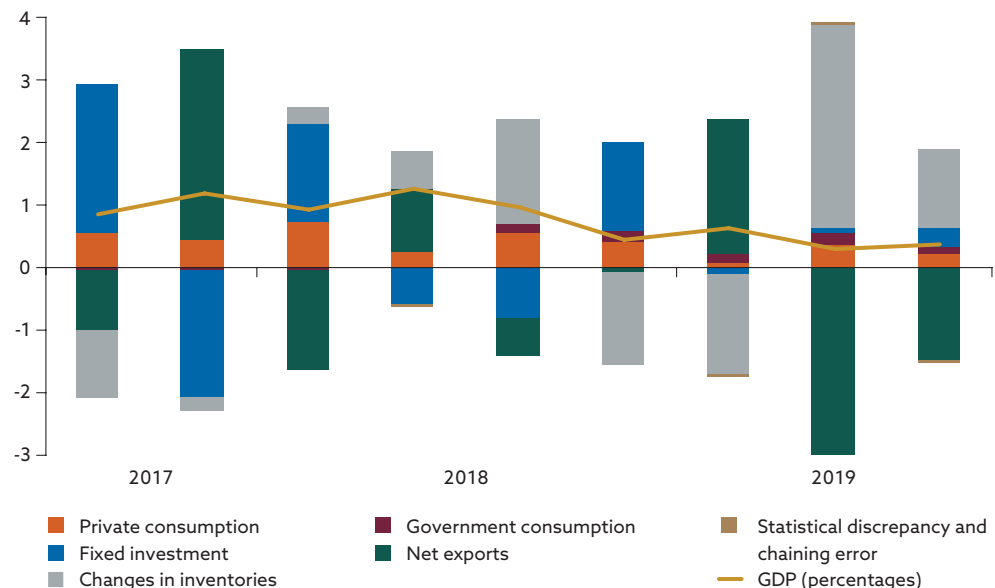
Inflation accelerated in the third quarter of this year to 3.0% (from 2.6% in the second quarter), owing mainly to a rise in food and services prices.

2 Gross domestic product

The Slovak economy expanded in the third quarter of 2019 by 1.3% year on year, representing a slowdown caused mainly by a deterioration in foreign trade as in the previous quarter. The exports of goods and services continued to decline, while imports experienced accelerating growth. Thus, net exports again made a negative contribution to economic growth. On the side of domestic demand, both private and government consumption grew at a slower pace over the period under review. Fixed investment experienced a revival in that period.

Chart 1

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

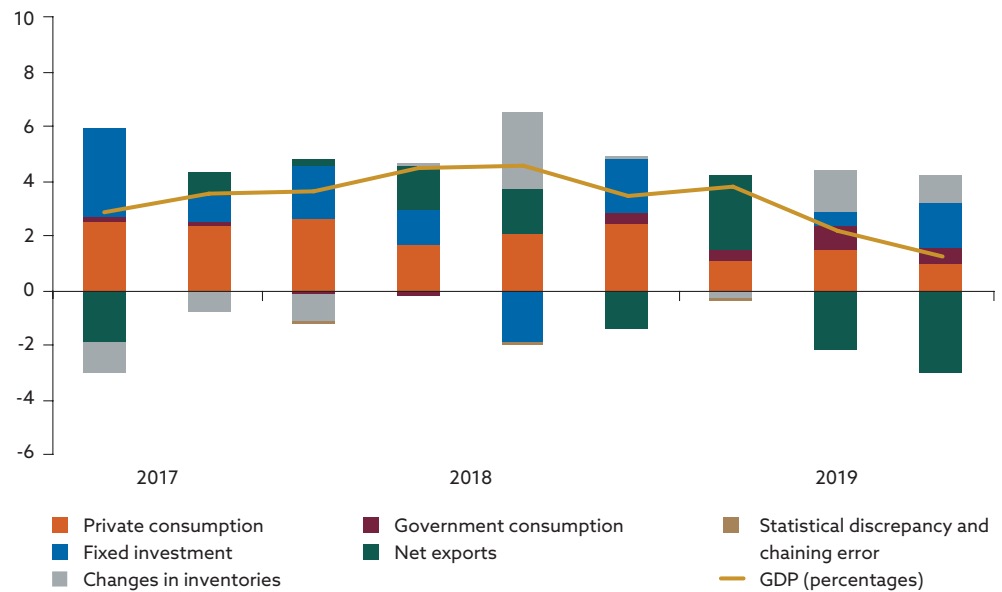


Sources: SO SR, and NBS calculations.

In quarter-on-quarter terms, Slovakia's GDP increased in the period under review by 0.4% (after seasonal adjustment), owing to the positive contributions of domestic demand and inventories. Exports and imports also increased on a quarter-on-quarter basis. A slowdown was recorded in the growth rate of private and government consumption. As regards the components of domestic demand, investment grew at a faster pace, so domestic demand made a positive contribution to GDP growth. The positive contribution of changes in inventories was partly offset by the negative contribution of net exports.

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)

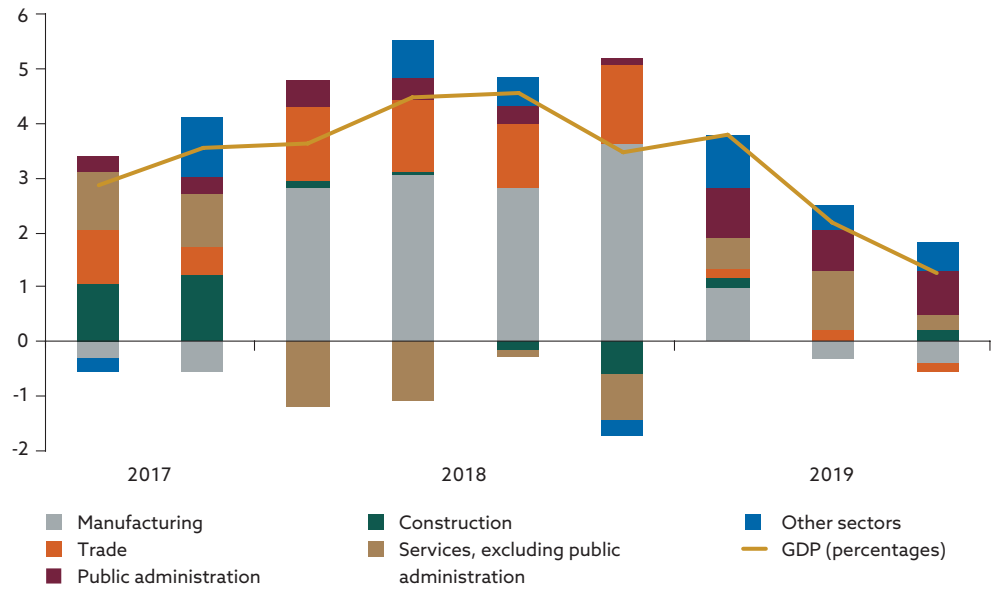
	2018					2019		
	Q1	Q2	Q3	Q4	Year	Q1	Q2	Q3
Gross domestic product	0.9	1.2	1.0	0.5	4.0	0.6	0.3	0.4
Final consumption of households and non-profit institutions	1.4	0.5	1.0	0.7	3.9	0.2	0.7	0.4
Final consumption of general government	-0.1	-0.1	0.7	1.1	0.2	0.9	1.1	0.6
Gross fixed capital formation	7.6	-2.6	-3.9	7.1	3.7	-0.6	0.3	1.4
Exports of goods and services	-1.1	4.2	-0.2	2.1	5.4	2.5	-5.1	0.5
Imports of goods and services	0.6	3.3	0.4	2.3	5.0	0.3	-1.5	2.2

Source: SO SR.

On the production side, the slowdown in economic growth was fuelled mostly by a downturn in manufacturing production and trade. The contribution of services decreased considerably. This trend was partially offset by developments in public administration and in other sectors.

Chart 3

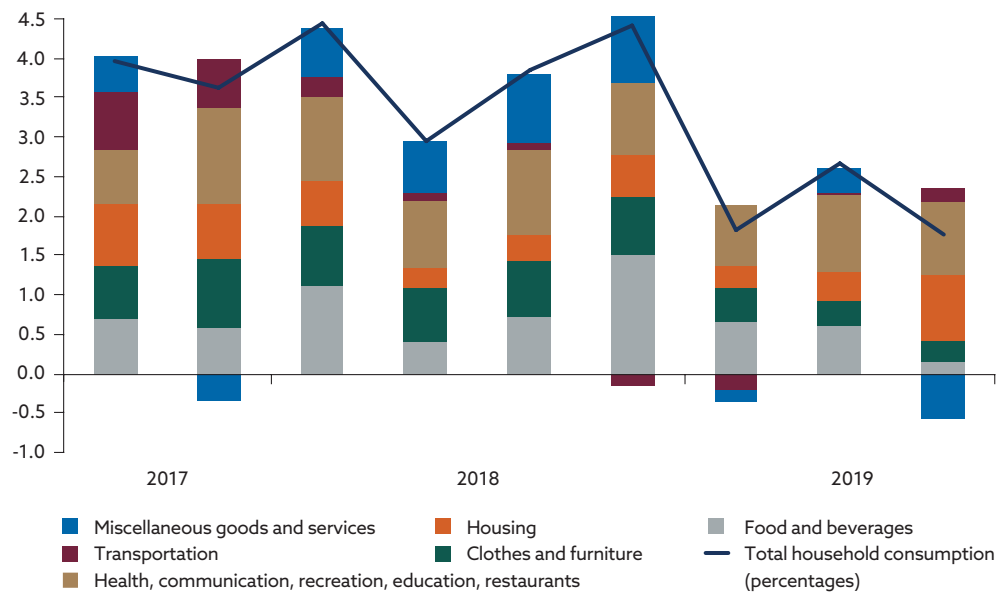
GDP – production-side contributions of sectors to annual percentage changes (percentage points; constant prices; non-seasonally adjusted)



Sources: SO SR, and NBS calculations.

Chart 4

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



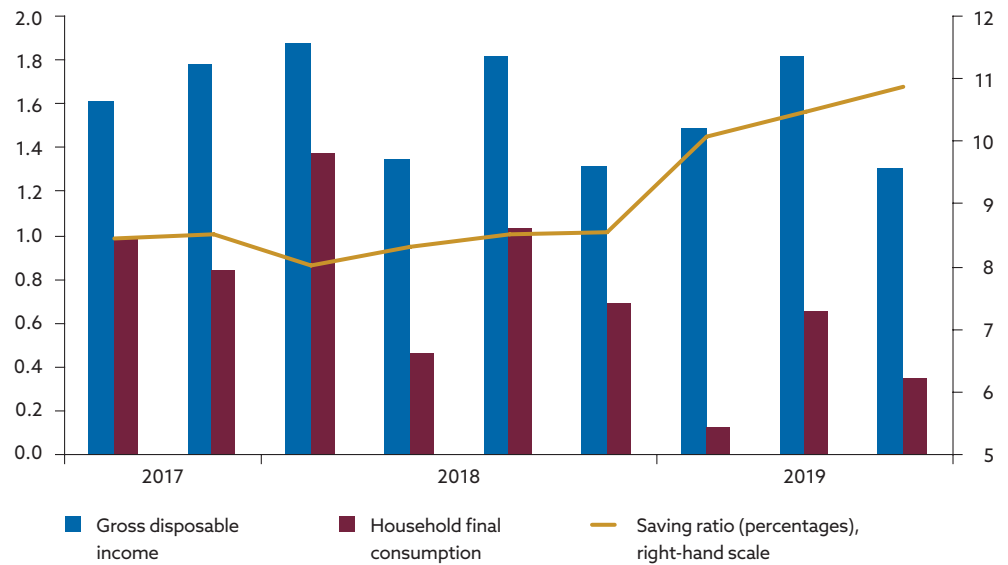
Sources: SO SR, and NBS calculations.

The annual rate of household final consumption growth slowed to 1.9% at the end of the third quarter, from 2.7% at the end of the second quarter. The labour market experienced a downturn, which was manifested in weaker growth in the disposable income of households (particularly in employee compensation). Broken down by component, the slowdown in consump-

tion growth was caused mainly by lower spending on miscellaneous goods and services. Spending on hotels and restaurants, housing, education and health care continued to grow, year on year. The growth in households' disposable income still enabled higher consumption in the period under review, but households continued to give preference to saving over increased consumption, owing probably to uncertainty regarding the future economic situation. As a result, the saving ratio increased still further, to almost 11%.

Chart 5

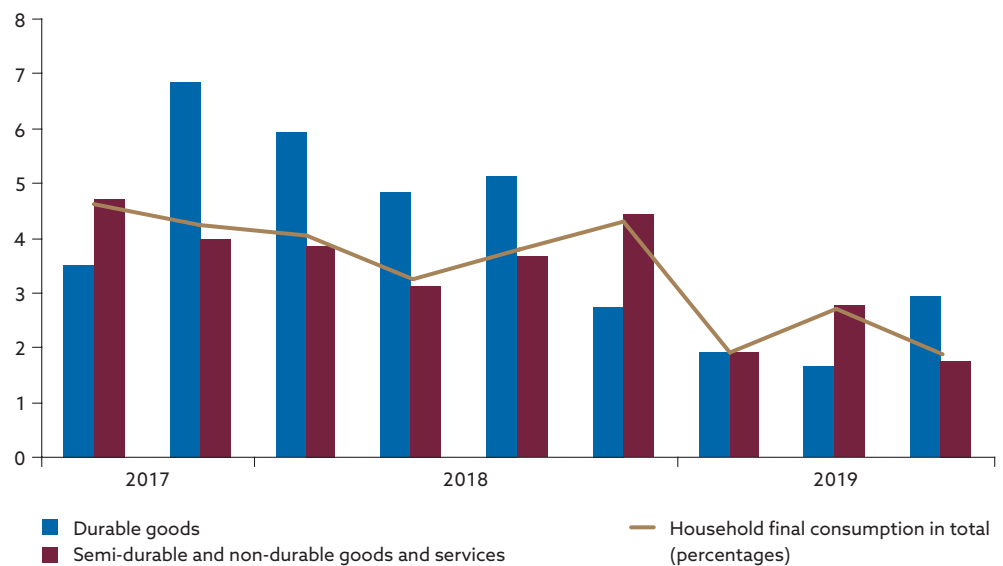
Gross disposable income and consumption of households (quarter-on-quarter percentage changes; constant prices)



Sources: SO SR, and NBS calculations.

Chart 6

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



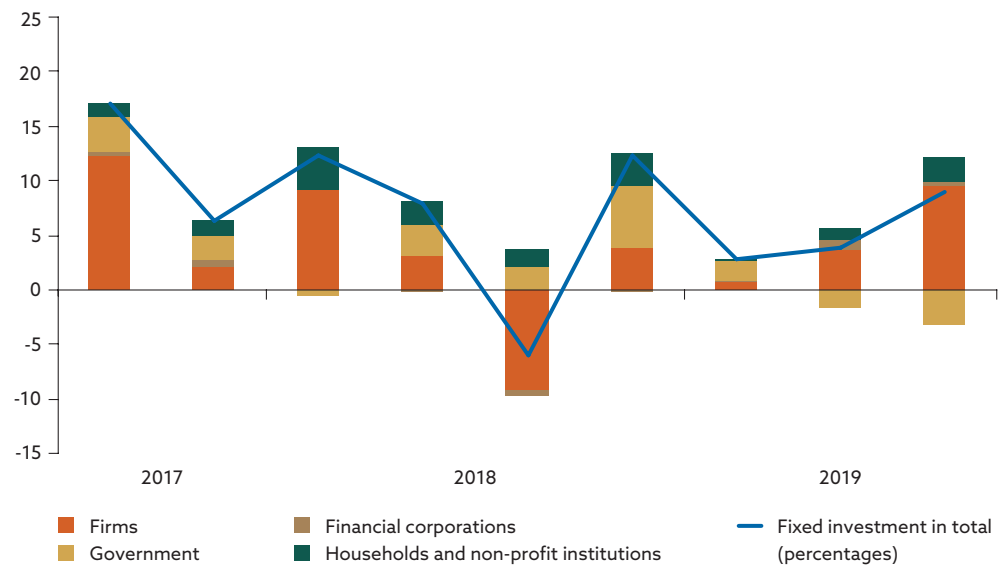
Sources: SO SR, and NBS calculations.

General government consumption grew in the third quarter by 3.7%, representing a slowdown compared with its growth in the previous quarter. The steep increase in employee compensation continued, while expenditure on intermediate consumption remained stagnant.

Fixed investment growth accelerated year on year by 7.8%, mainly as a result of an upturn in investment activity in the non-financial and household sectors. After accelerating considerably in the private sector, investment was affected to some extent by the base effect of curbed investment activity from last year and by the completion of projects launched in the past. Broken down by industry, dynamic investment growth was recorded in the oil refining, wood-processing, furniture, textile and leather industries. Year-on-year growth in investment was, after several quarters of decline, recorded in the automotive industry, too. Strong growth was also recorded in investment in machinery and equipment. Investment in intellectual property products (eKasa online cash registers) and transport equipment accelerated, too. A downturn in investment activity was recorded in the government sector.

Chart 7

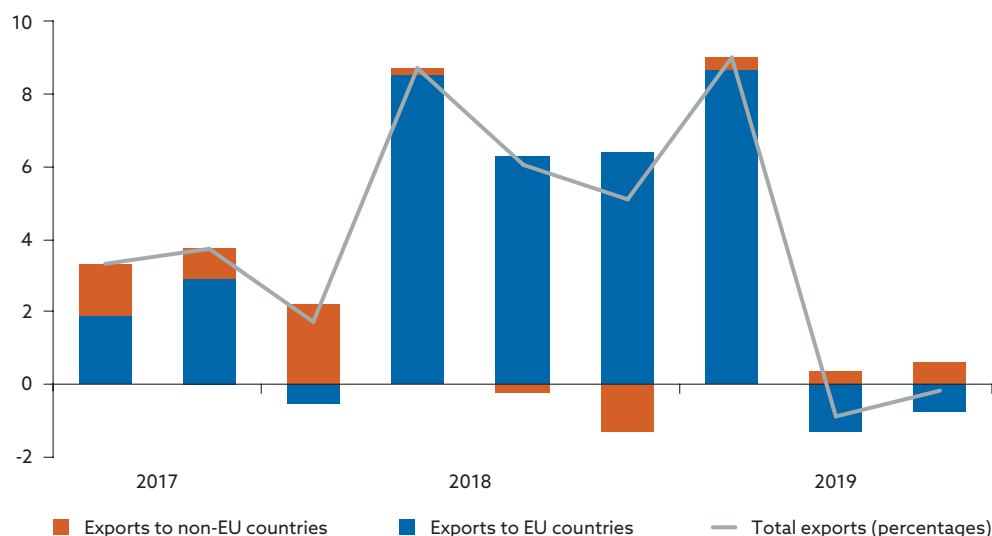
Investment – sectoral contributions to annual percentage changes (percentage points; current prices; non-seasonally adjusted)



Sources: SO SR, and NBS calculations.

Chart 8

Structure of exports by destination (annual percentage changes; percentage point contributions; constant prices; non-seasonally adjusted)



Sources: SO SR, and NBS calculations.

Net exports again made a negative contribution to economic growth in the third quarter, as a result of a year-on-year decline in exports (though this decline was not as sharp as in the previous quarter), accompanied by an acceleration in imports year on year. Broken down by country, exports to euro area countries (Germany, Italy and Belgium) continued to decline. With exports declining, the imports of goods and services grew in volume, at an accelerating pace. Imports from EU countries (France) grew at a steady pace, while imports from non-EU countries stagnated. Import growth is probably associated with the expected pickup in car production in connection with the launch of new car models, stockpiling in markets due to Brexit-related uncertainty, gas imports (uncertainty surrounding the Russian gas transit via Ukraine) and with the forthcoming Christmas season. Export and import volumes (in the entire reporting period, not only in the third quarter) were also affected by a major benchmark revision (see Box 1).

Box 1

Revision of export and import data in the national accounts

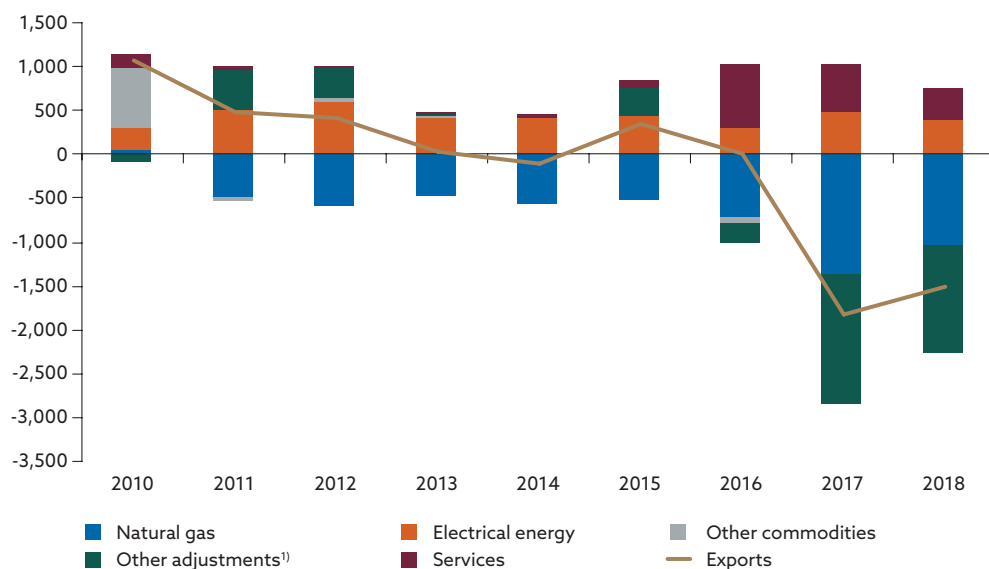
The Statistical Office of the Slovak Republic (SO SR) has carried out a major benchmark revision of the annual and quarterly national accounts for the period 1995–2017, including a preliminary revision of the annual account for 2018. The purpose of the revision was to incorporate information from updated data sources and refinements to the methodology used to compile specific national account indicators. One of the items that have been adjusted to a greater extent are data on foreign trade.

In the final analysis, the benchmark revision of exports and imports is linked to adjustments in the regulation of the economic activities of non-residents registered in the Slovak Republic for VAT purposes, and of illegal activities such as smuggling and drug trafficking. Illegal activities

have been adjusted for both imports and exports of services. In cross-border trade, changes have been made in the amounts of transactions, in particular in natural gas and electrical energy.

Chart A

Revision of exports; volume changes after and before revision (current prices; EUR millions)

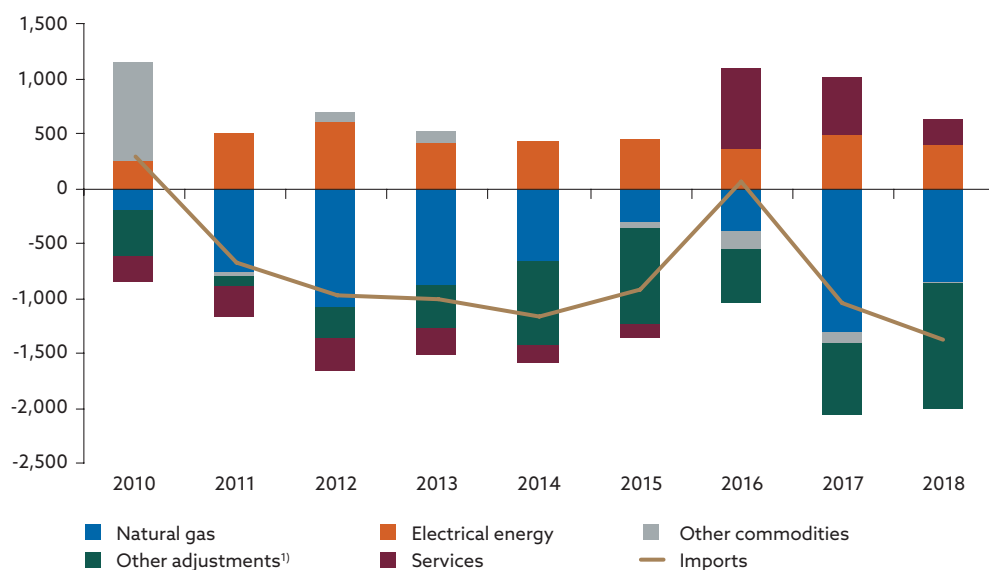


Sources: SO SR, and NBS calculations.

1) Other adjustments - mainly adjustments to the regulation of economic activities of the non-residents registered in Slovakia for VAT purposes and of illegal activities such as smuggling and drug trafficking, and other grossing-up factors.

Chart B

Revision of imports; volume changes after and before revision (current prices; EUR millions)



Sources: SO SR, and NBS calculations.

1) Other adjustments - mainly adjustments to the regulation of economic activities of the non-residents registered in Slovakia for VAT purposes and of illegal activities such as smuggling and drug trafficking, and other grossing-up factors.

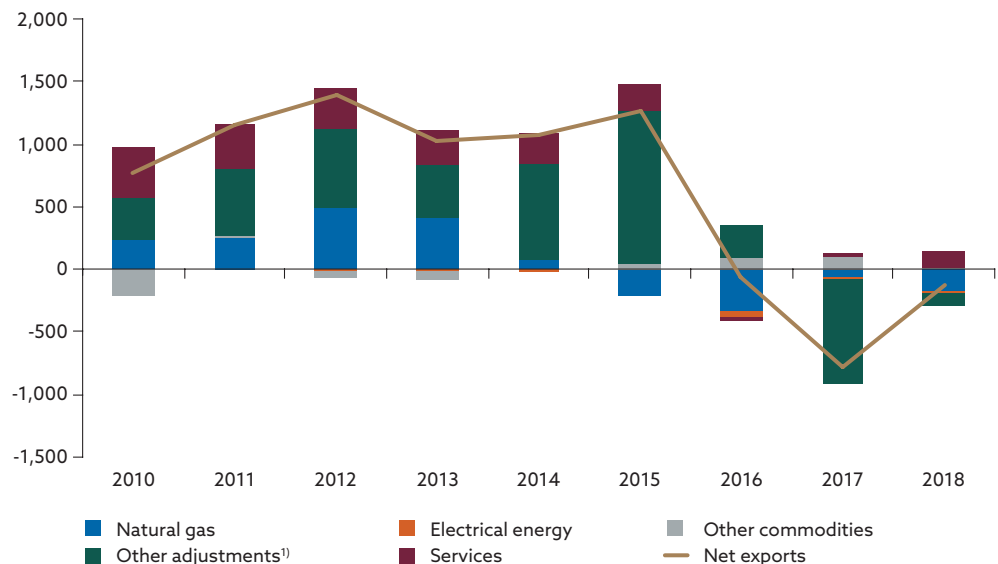
Cross-border natural gas trade through both channels has been reduced, owing to transition from accounting transactions to the recording of physical gas flows. As a result of this change, the volumes of trade decreased, mainly with the United Kingdom (UK). In 2017, the volume of Slovak exports amounted to €4.5 billion. Most estimates of the possible impact of Brexit on the Slovak economy are based on these data. The revised volume of exports is lower by one billion.

A change has also occurred in the recording of electrical energy. This change, however, has no impact on the balance of trade in this commodity.

As a result of all these adjustments, **the volume of net exports increased until 2015, remained unchanged in 2016, and then decreased in 2017 and 2018.**

Chart C

Revision of net exports; volume changes after and before revision (current prices; EUR millions)

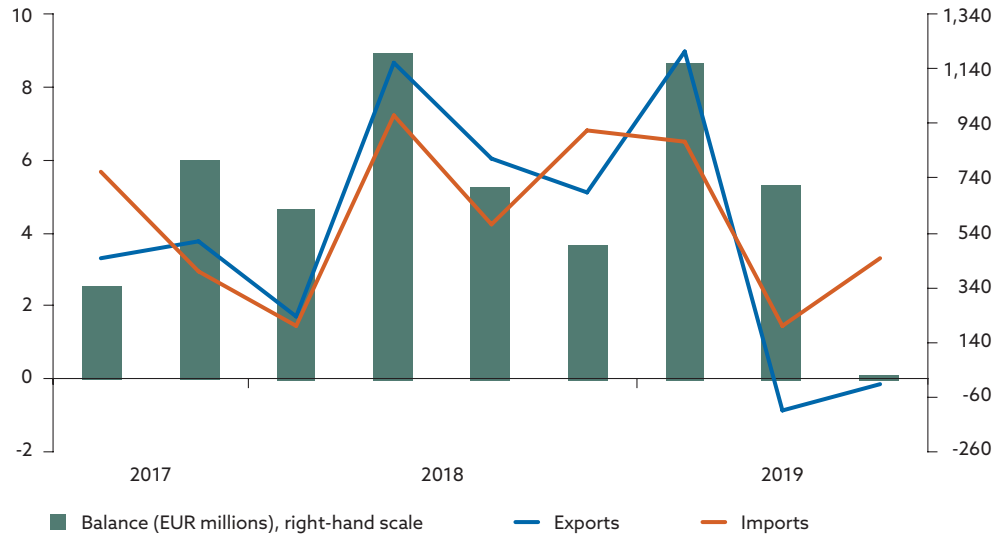


Sources: SO SR, and NBS calculations.

The composition of GDP growth at current prices as calculated using the income approach indicates that the slower economic growth in the period under review was caused mainly by lower income from work and lower tax revenues on products and imports. Entrepreneurial income (gross profits and mixed income) maintained its growth dynamics from the previous quarter and its contribution to year-on-year GDP growth remained stable.

Chart 9

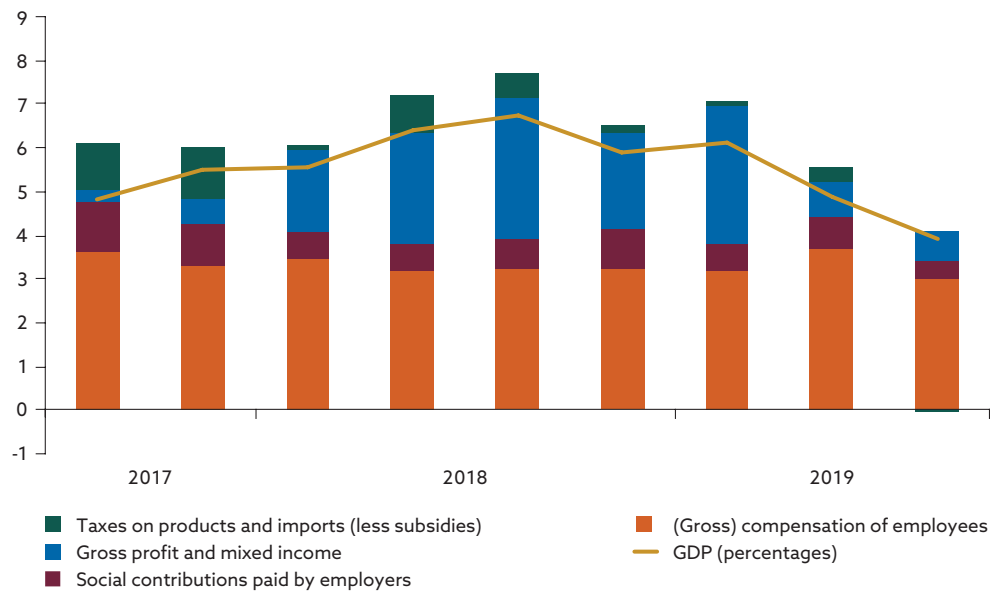
Exports and imports of goods and services (annual percentage changes; constant prices; non-seasonally adjusted)



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.

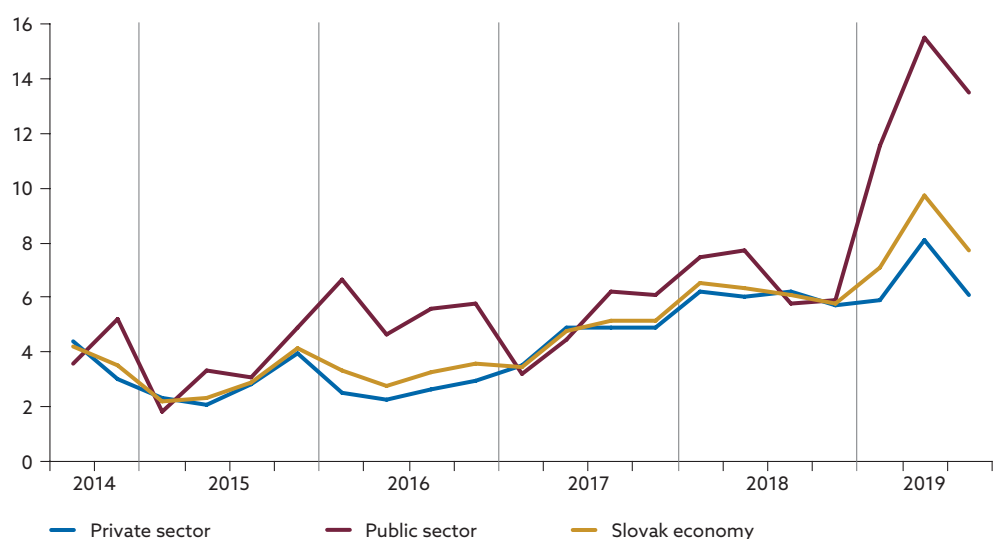
3 The labour market

3.1 Wages and labour productivity

Despite a slowdown, the average wage continued growing relatively dynamically in the third quarter of 2019. Its dynamics weakened by two percentage points quarter on quarter, but remained fairly strong (7.7%). This development was supported by strong wage growth in the public sector (13.5%). The two-digit annual rate of wage growth in this sector since the beginning of the year was caused by an increase in the contractual wages of employees working in public and state services. Wage growth in the private sector slowed in the period under review. This slowdown took place mostly in manufacturing, but certain subsectors of services also recorded slower wage growth. By contrast, accelerated wage growth was recorded in construction and wages in trade continued growing at a pace of more than 7%. As a result of weaker demand in the labour market, the tension has eased and pressure for wage growth has weakened gradually in the recent period. Moreover, firms faced rising labour costs this year, so they tried to keep the variable wage components down. Bonus payments in the private and public sectors showed weaker dynamics in the period under review. Wage growth was strengthened in the second quarter to the detriment of the next quarter by the payment of 13th salaries (exempt from income tax and health insurance contributions) in June in the amount of roughly 1% of the volume of wages in the economy.

Chart 11

Wage developments in the main sectors of the economy (annual percentage changes)

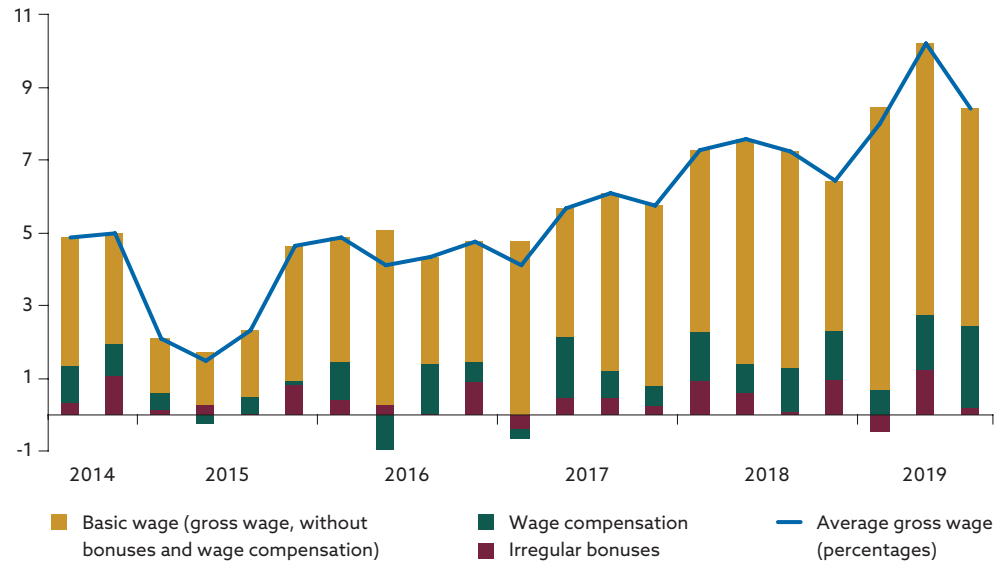


Sources: SO SR, and NBS calculations.

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

Chart 12

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

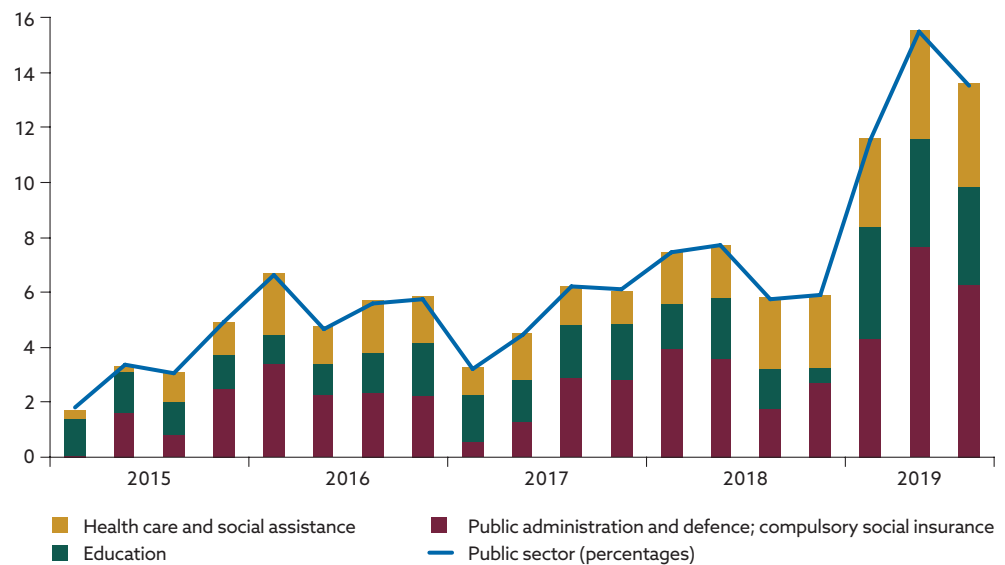


Sources: SO SR, and NBS calculations.

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

Chart 13

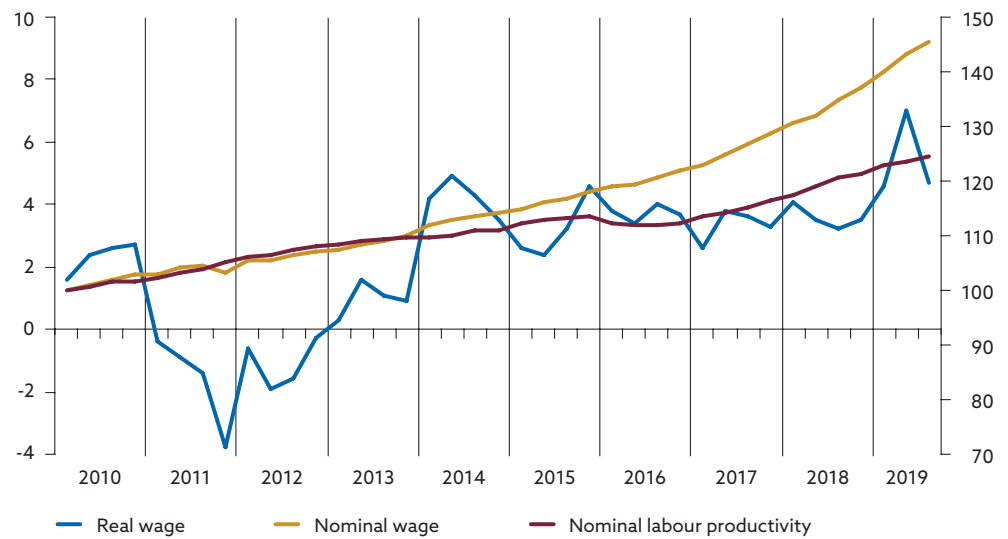
Wage developments in the public sector (annual percentage changes; percentage point contributions)



Sources: SO SR, and NBS calculations.

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.

Compensation per employee increased in the third quarter of this year by 6.1%, representing a slowdown in comparison with the previous quarter (from 8%). This development was influenced by the same fundamentals as those determining the average wage. With the slowdown in the rate of economic growth, labour productivity growth moderated, too, by 1.1 percentage points quarter on quarter.

Table 2 Wages and labour productivity (annual percentage changes)

	2018					2019		
	Q1	Q2	Q3	Q4	Year	Q1	Q2	Q3
Average wage (headline)	6.5	6.4	6.1	5.8	6.2	7.1	9.7	7.7
Consumer-price inflation	2.3	2.8	2.7	2.2	2.5	2.4	2.5	2.9
Average real wage (headline)	4.1	3.5	3.3	3.5	3.6	4.6	7.0	4.7
Average wage (ESA 2010)	6.4	6.4	5.6	5.0	5.9	6.1	8.5	7.0
Compensation per employee (ESA 2010)	5.7	5.6	5.4	5.6	5.6	5.7	8.0	6.1
Nominal labour productivity (ESA 2010)	3.4	4.5	4.9	3.5	4.1	4.9	3.4	2.3
Real labour productivity (ESA 2010)	1.4	2.3	2.6	1.7	2.0	2.0	0.7	0.2

Sources: SO SR, and NBS calculations.

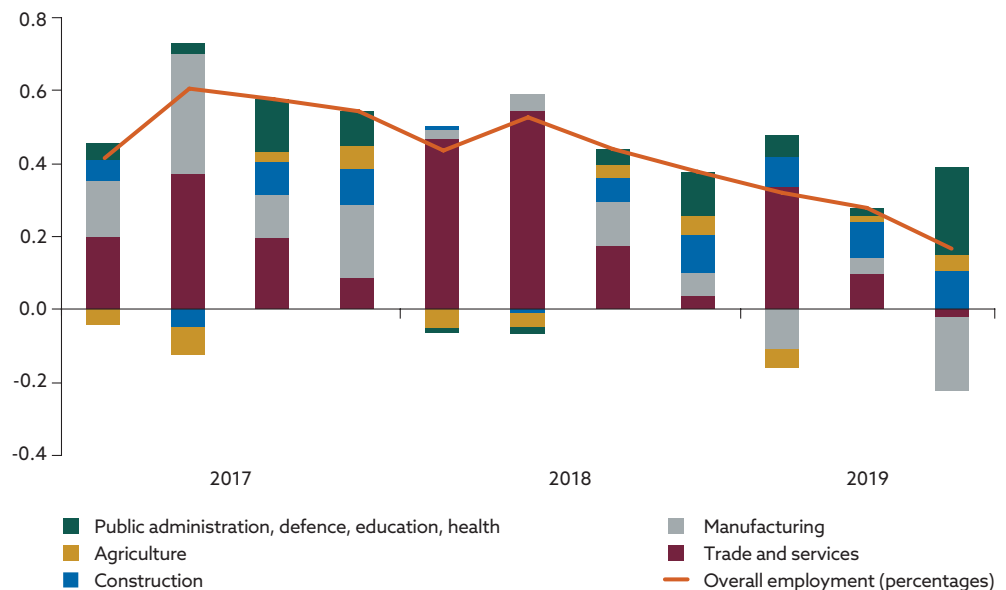
Note: Average wages (headline) are based on data from SO SR statistical reports. Average real wages were calculated on the basis of CPI inflation. Labour productivity (ESA 2010) was calculated as the ratio of nominal GDP to employment as defined in the ESA 2010 methodology.

3.2 Employment and unemployment

The annual rate of employment growth continued to slow in the third quarter of 2019, to 1%. A slowdown was also recorded in quarter-on-quarter terms (to 0.2%, from 0.3% in the second quarter). The cooling of global demand began to be reflected in manufacturing, which, after more than five years, recorded a year-on-year decline of 1% (as well as a quarter-on-quarter decline). While the previous quarters saw marked decreases in the number of hours worked in this sector, the third quarter witnessed a decrease in the number of employees, too. A deterioration was also recorded in employment in trade, which declined year-on-year for a second successive quarter. A certain slowdown was also recorded in services, but the sector's growth rate remained above the national average, owing to employment growth in the IT sector and accommodation services. The best performing sector in this respect was construction, where employment rose by more than 5%. Employment also followed a positive trend in the public sector, especially in health care and education.

Chart 15

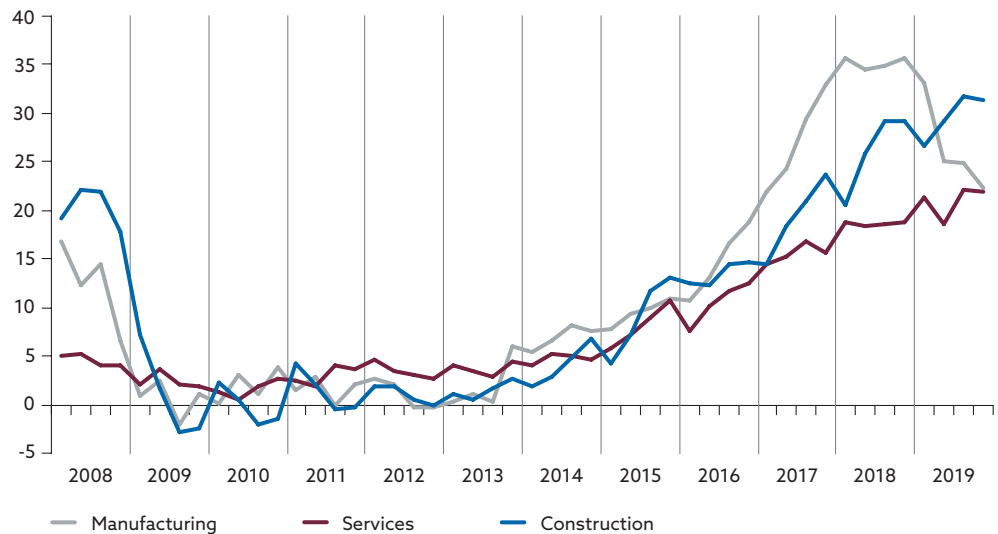
Employment – sectoral contributions to quarter-on-quarter percentage changes (percentage points)



Source: SO SR.

Chart 16

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



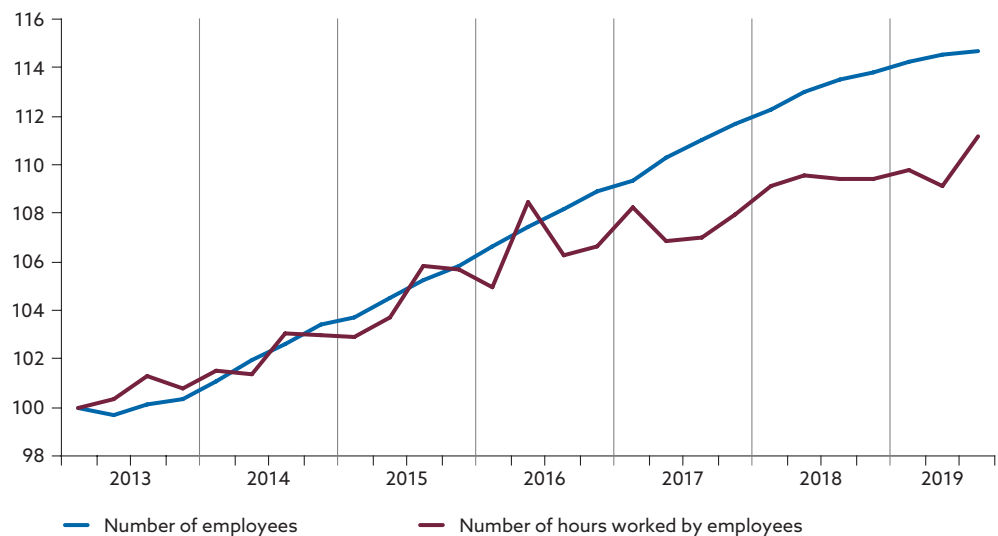
Sources: EC, and NBS calculations.

Note: The data on construction for Q3 2019 are average figures for October and November 2019.

The number of unemployed (according to the LFS methodology) remained broadly unchanged in the third quarter of this year. The seasonally adjusted number of unemployed dropped by 1,300 persons quarter on quarter. Thus, the unemployment rate reached 5.8% as in the previous quarter (or 5.9% without seasonal adjustment). The decreasing trend in the number of Slovak citizens working abroad came to a halt in the period under review. The number of foreigners working in Slovakia increased slightly. Labour market developments were also influenced by the rising labour market participation rate.

Chart 17

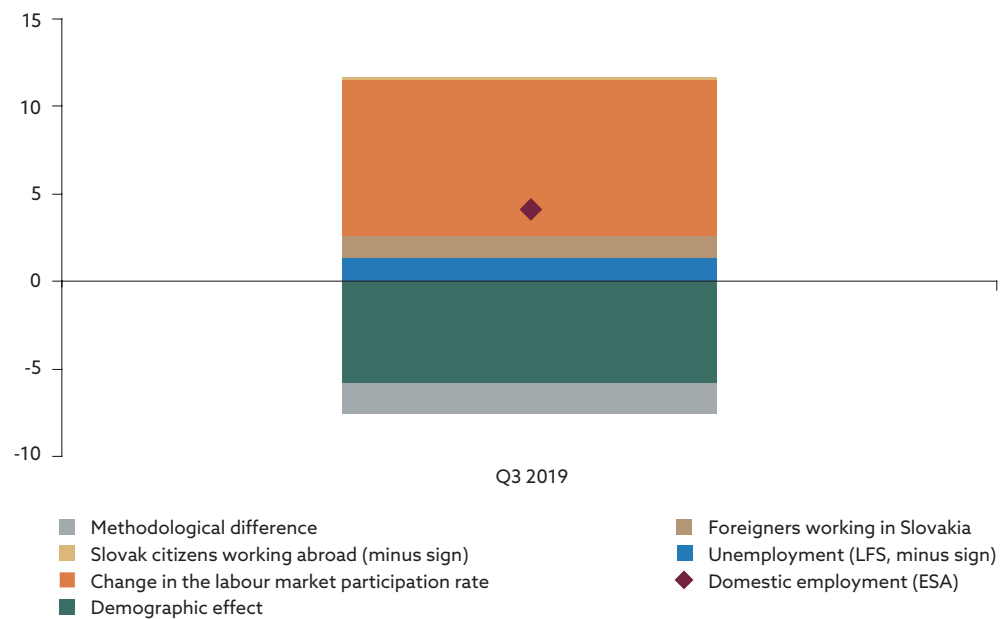
Employment growth and changes in the number of hours worked in the economy (ESA methodology; index: Q1 2013 = 100)



Sources: SO SR, and NBS calculations.

Chart 18

Employment – contributions of key 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 third quarter of 2019, to 3.0% (from 2.6% in the previous quarter), **owing to a rise in food and services prices.**

The continuing acceleration in food prices was caused by increases in the prices of meat, meat products and vegetables. Meat prices were strongly affected by the supply shock resulting from the spread of the African swine fever around the world. The year-on-year rise in processed food prices was also affected by the persisting dynamic growth in labour costs and extra pays. Food prices were thus affected by domestic and external factors. The rise in food prices contributed 1.1 percentage points to overall inflation, i.e. more than one-third of the annual inflation rate.

The year-on-year rise in services prices accelerated considerably, despite the expected reduction in the price of meals for primary school children in grade one to four in September 2019. The acceleration in services prices was caused by marked increases in air fares and administered prices. Administered prices reflected the rise in prices for postal services and bus fares. The rising food prices and wages caused, directly or indirectly, a rise in prices for meals in canteens and nursery schools. Services price inflation remained above 2% and was influenced most significantly by domestic factors in the form of cost impulses.

The rise in non-energy industrial goods prices remained stable, at 1.1%. This rise did not deviate significantly from the year-on-year increase in prices for non-energy industrial goods imported from euro area countries. The rate of increase in semi-durable goods prices (mainly those of ready-made clothes) accelerated somewhat in the third quarter of this year. By contrast, the rise in non-durable goods prices slowed slightly in that period, as a result of developments in the prices of pharmaceutical goods and products.

Table 3 Annual percentage changes in consumer-price inflation broken down by component

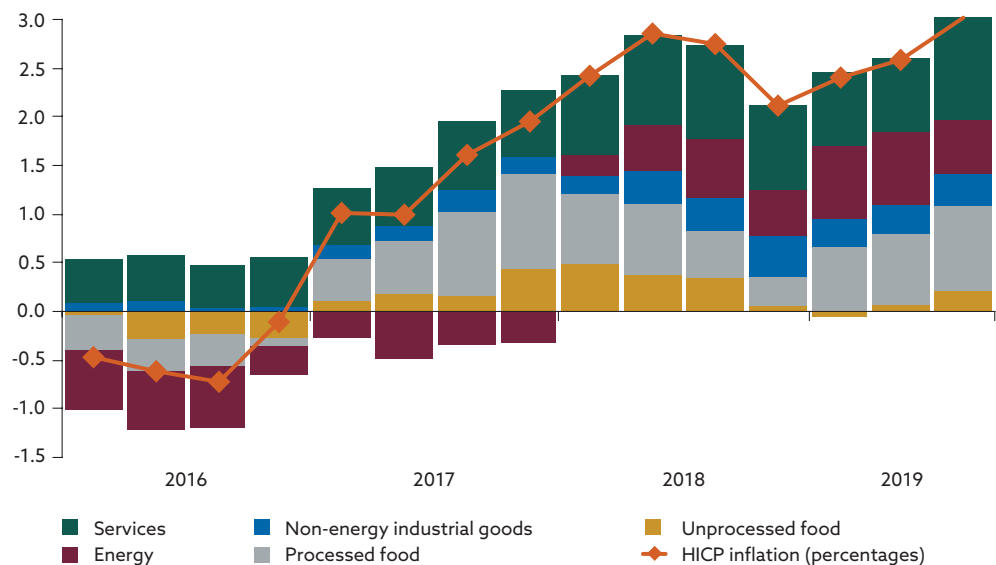
	2018					2019		
	Q1	Q2	Q3	Q4	Year	Q1	Q2	Q3
HICP inflation	2.4	2.9	2.7	2.1	2.5	2.4	2.6	3.0
Unprocessed food	11.0	8.8	7.1	0.4	6.8	-0.9	1.9	5.4
Processed food	3.4	3.4	2.3	1.5	2.7	3.3	3.5	4.3
Non-energy industrial goods	0.7	1.2	1.2	1.4	1.1	1.0	1.1	1.1
Energy	1.4	3.3	4.0	3.2	3.0	4.8	4.7	3.6
Services	2.6	2.9	3.1	2.7	2.8	2.4	2.4	3.3

Sources: SO SR, and NBS calculations.

The annual rate of increase in energy prices slowed in the third quarter. Their increase was dampened by the continuing year-on-year decline in Brent oil prices (in euros), which was reflected in fuel prices, too. The regulated prices of gas, electricity and heat showed stable but strong dynamics, owing to a marked one-off increase recorded at the beginning of 2019.

Chart 19

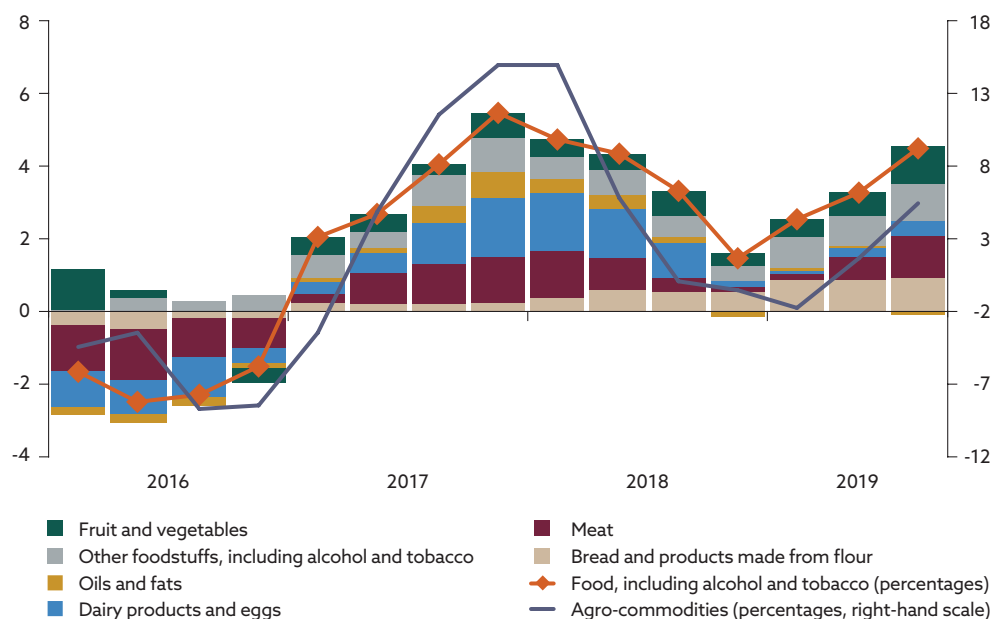
HICP inflation broken down by component (annual percentage changes; percentage point contributions)



Sources: SO SR, and NBS calculations.

Chart 20

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



Sources: SO SR, and NBS calculations.