



“Better Policies” Series

# **SLOVAK REPUBLIC**

FOSTERING AN INCLUSIVE  
JOB-RICH RECOVERY

**APRIL 2013**



Better Policies

# **Slovak Republic: Fostering an Inclusive Job-rich Recovery**

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ISBN 978-92-64-20163-7 (PDF)

Series: Better Policies

ISSN 2308-1392 (online)

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# FOREWORD

The Slovak Republic is one of the most dynamic economies in the euro area. The country has continued to converge rapidly towards the living standards of advanced OECD economies.

However, the road ahead is full of challenges. The fiscal room gained in the run-up to euro accession evaporated during the euro area debt crisis and public debt has increased considerably since 2009. Slovakia still faces a large productivity gap and comparatively low labour utilisation, with one of the weakest employment developments in the OECD area. While income inequality remains low in Slovakia, regional disparities are large and high long-term unemployment combined with low labour mobility may increase them further. These challenges need to be addressed.

To achieve balanced, fair and sustainable growth, the Slovak Republic should continue on its path of reform.

First, fiscal consolidation needs to continue in a way which supports the still fragile recovery and protects spending on growth-enhancing and social policies. This implies further improving the fiscal framework.

Second, Slovakia needs new domestic drivers of growth. The country needs to upgrade and diversify its participation in global value chains. This implies investing in human capital and skills, improving the business environment and the quality of institutions and government, as well as strengthening its innovation performance.

A third key challenge for Slovakia is to address the especially high youth and long-term unemployment rates. This requires substantial reforms of activation policies and of the education system. Increasing the quality of education would tackle inequalities at their root and at the same time significantly boost human capital, and therefore productivity and growth.

The OECD stands ready to be a partner in the formulation and implementation of an agenda for inclusive jobs-rich recovery in Slovakia – and to advance *“better policies for better lives.”*



Angel Gurría  
OECD Secretary-General

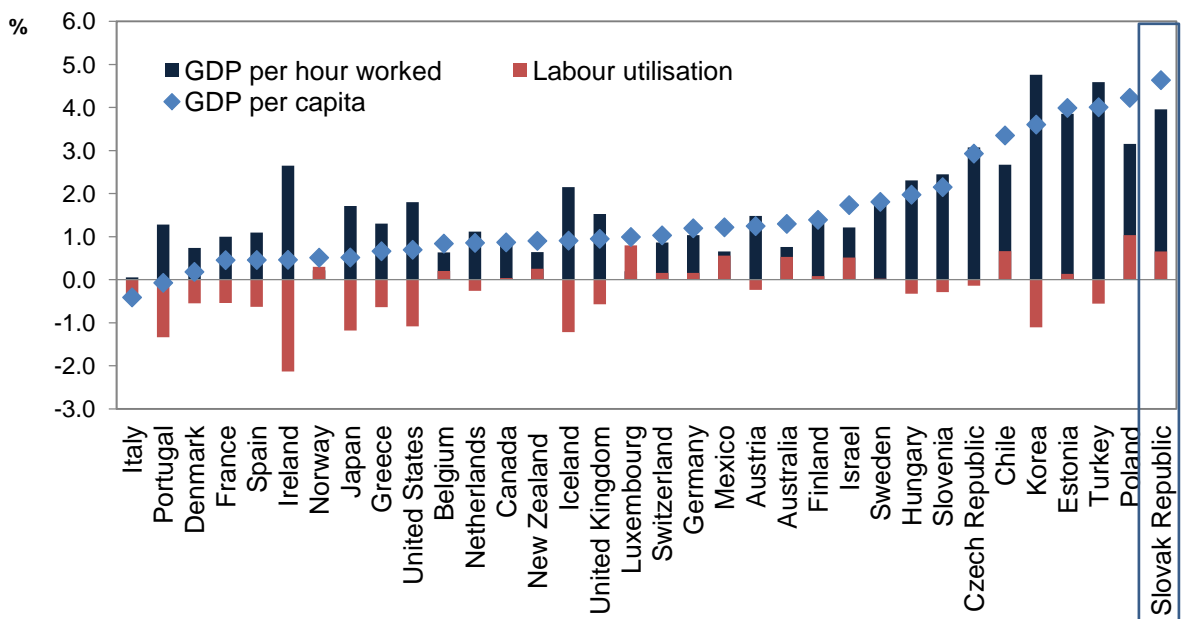
# 1. KEY CHALLENGES FOR INCLUSIVE, ROBUST AND SUSTAINABLE GROWTH

The Slovak economy is one of the most dynamic economies in the euro area. Over the past decade, it has continued to converge towards the living standards of advanced OECD economies at a fast pace. The country also recovered strongly from the global economic crisis and weathered well the financial crisis that affected its main European trading partners.

Overall, growth in GDP per capita was the highest in the OECD in 2001-2011, supported especially by strong productivity growth (Figure 1). The income gap relative to the upper half of OECD countries narrowed from over 60% in the early 2000s to close to 40%.

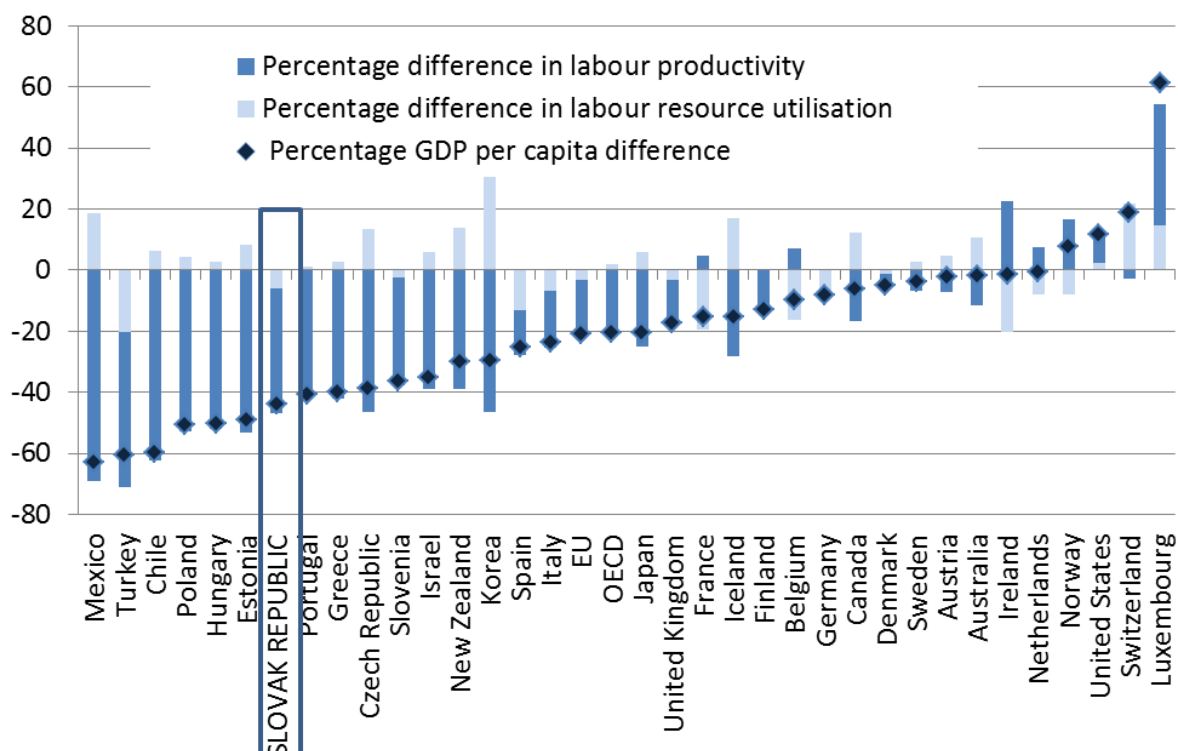
The remaining gap reflects a still large productivity shortfall and lower labour utilisation (Figure 2). The employment rate is the sixth lowest in the OECD at just 59.5% against 64.8 % on average in the OECD, and unemployment is high. Going forward, Slovakia needs economic growth underpinned by strong productivity gains while making the labour market more inclusive and offering opportunities for all Slovak residents.

**Figure 1. GDP per capita growth and its components, 2001-2011**



Source: OECD Productivity Database OECD, Annual National Accounts Database

**Figure 2. Difference in GDP per capita with the upper half of OECD countries, 2011**



Notes: Compared to the simple average of the 17 OECD countries with highest GDP per capita in 2011, based on 2011 purchasing power parities (PPPs). The sum of the percentage difference in labour resource utilisation and labour productivity do not add up exactly to the GDP per capita difference since the decomposition is multiplicative. Labour resource utilisation is measured as the total number of hours worked per capita. Labour productivity is measured as GDP per hour worked.

Source: OECD Going for growth (2013).

## Fiscal consolidation remains a priority but needs to proceed in a way that is least harmful to growth and social cohesion

Ensuring fiscal sustainability requires strong fiscal consolidation, and much has been done already. It should also be achieved in a way that supports the still-fragile recovery and protects spending on growth-enhancing and social policies.

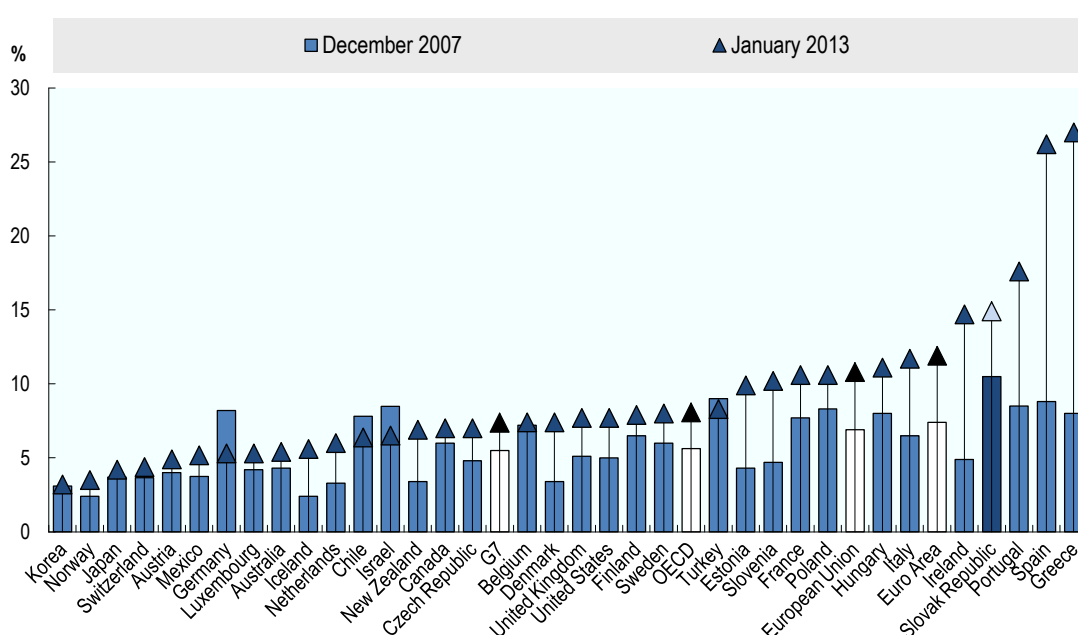
As argued in the *2012 OECD Economic Survey on the Slovak Republic* achieving fiscal sustainability will require a long-term effort that needs to be underpinned by further strengthening of the fiscal framework. This framework should in particular ensure a careful prioritisation of spending and cost efficiency (Chapter 2). It is also important for the Slovak Republic to enhance the absorption of EU funds, which took longer than in other central and eastern European countries. Moreover, tax collection could be made more efficient, and the burden of social security contribution for low income earners should be reduced, improving the incentives to create jobs for long-term unemployed.

In addition, reconciling fiscal consolidation with growth promotion measures in a more challenging global environment also requires increasing the capacity of the public administration to steer reforms (Chapter 3).

## Poor labour market outcomes contrast with growth performance

The Slovak labour market has been hard hit by the crisis: aggregate unemployment, youth unemployment and long-term unemployment are among the highest in the OECD (Figure 3, as well as Chapter 4 Figures 12 and 13). The subsequent export-driven recovery was strong but the labour market situation has deteriorated. Business efforts to regain competitiveness weigh on wage growth, and the resulting stagnation of purchasing power prevents a job-rich recovery of domestic demand. This dichotomy further aggravates the stress on public finances and social cohesion. It may also lead to increased inequality going forward.

**Figure 3. Unemployment rates December 2007-January 2013**



Notes:

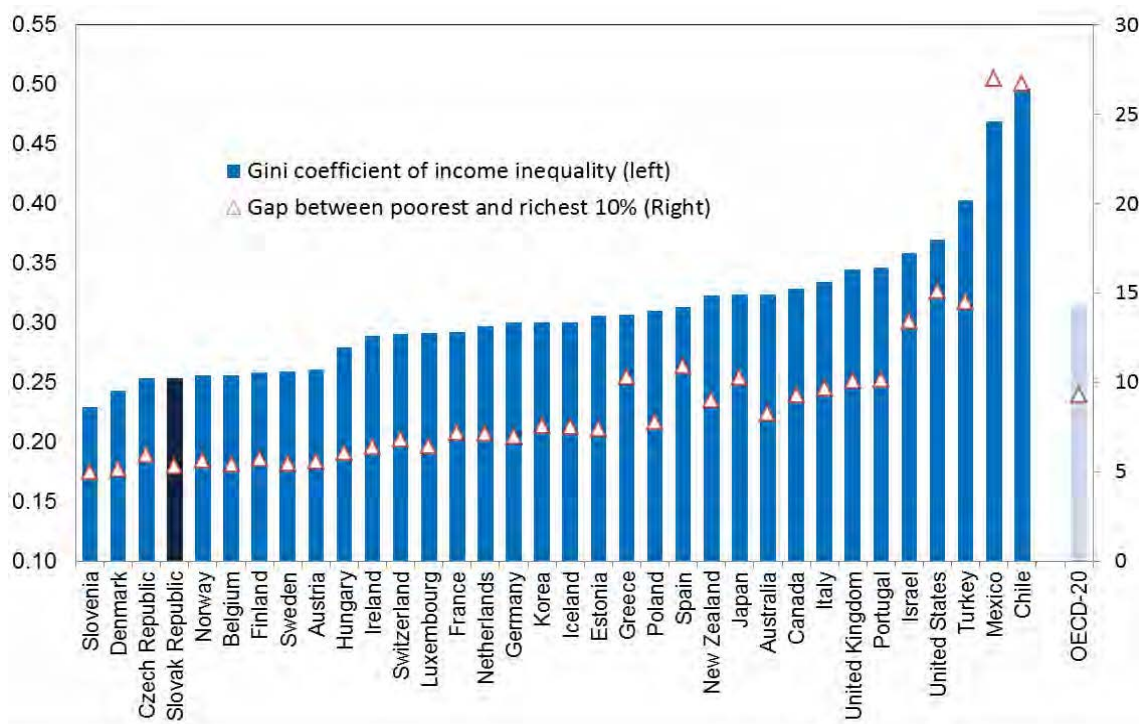
1. For Israel, the series has been chained to take into account the break series in 2012.
2. November 2012 for Greece, Turkey and the United Kingdom; December 2012 for Chile, Estonia, Hungary and Norway; February 2013 for Canada and the United States; 2012 Q3 for Switzerland; and 2012 Q4 for New Zealand.

Source: OECD calculations based on the OECD Short-Term Indicators Database.

Improving labour market outcomes requires broad-based reforms on the supply and demand side (Chapter 4). Endowing job seekers with employable skills will require substantial reforms of activation policies but also of the education system, which is not responding well to labour market needs. Improving education outcomes, particularly among children from lower social-economic backgrounds is also the best way to tackle inequalities at their root (Chapter 5). For instance, the recent OECD *Economic Survey of the Slovak Republic* highlighted that among the Roma population, which is already largely excluded from the labour market, only 32% of men and 24% of women have attained upper-secondary education.

While income inequalities are low compared to the OECD average (Figure 4), regional disparities are large. The recent increase in long-term unemployment in deprived regions and low labour mobility may deepen geographical inequalities. There is also a risk that the trend in poverty decline reverses.

**Figure 4. Income gap between rich and poor (2008 or latest year available)**



Notes: The Gini coefficient ranges from 0 (perfect equality) to 1 (perfect inequality).

Gaps between poorest and richest are the ratio of average income of the bottom 10% to average income of the top 10%. Income refers to disposable income adjusted for household size.

Source: OECD Income distribution and poverty.

## New domestic drivers of growth are needed

To stimulate job creation, it is also important to diversify the sources of economic growth. The Slovak economy remains very dependent on exports and foreign investments. It is overly specialised in assembly (notably of cars and consumer electronics) reflecting Slovakia's position in the downstream activities of Global Value Chains (GVC) (Box 1).

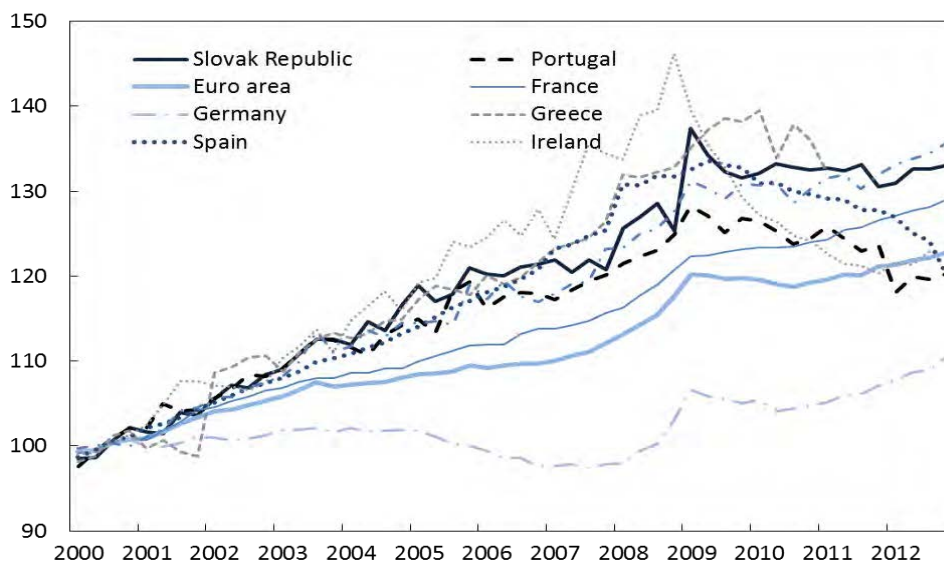
A strong inflow of FDI in export-oriented manufacturing, in particular in automotive sectors and consumer electronics, drove economic growth up to the crisis. Since then, the inflow of large, wage-cost sensitive and job-creating FDI projects has stopped and relative price competitiveness deteriorated somewhat: neighbouring countries experienced depreciations while Slovakia, as a member of the euro area, could not respond by adjusting its nominal exchange rate.

Recent performance has proven the ability of the Slovak industrial exporting sector to regain international competitiveness by increasing productivity growth and achieving wage moderation. This has helped stabilise unit labour cost for the whole economy over the past two years despite some increase in unit labour costs in the



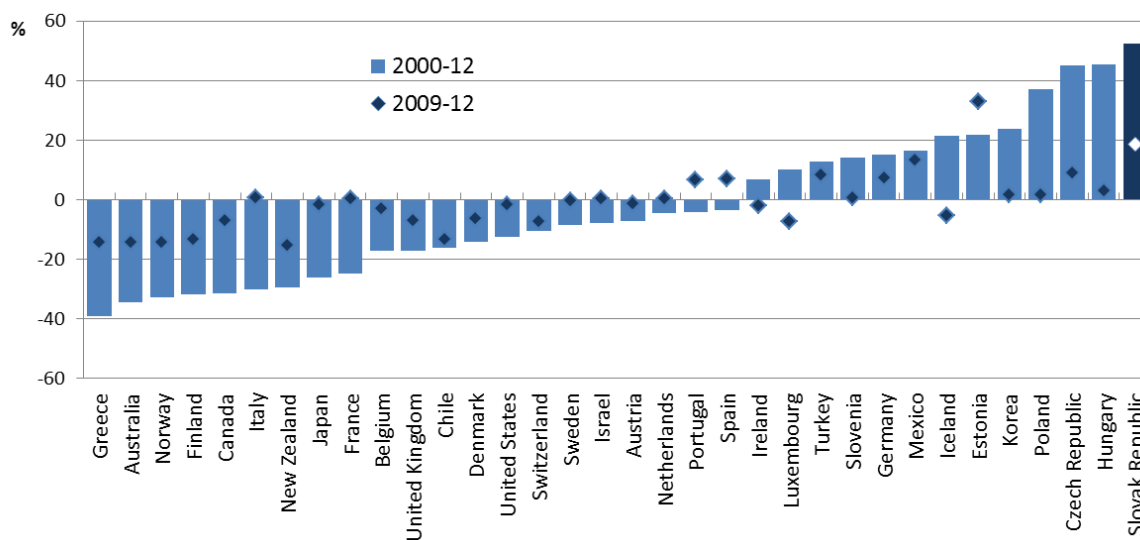
non-export oriented sectors including services (Figure 5). The country has continued gaining international market share at a fast pace, and recorded one of the strongest gains in the OECD before the crisis but also since 2009 (Figure 6).

**Figure 5. Unit labour costs- Total economy (2000 = 100)**



Source: OECD Early Estimates of Quarterly ULC Indicators.

**Figure 6. Export performance: Cumulated gains or losses in market share**



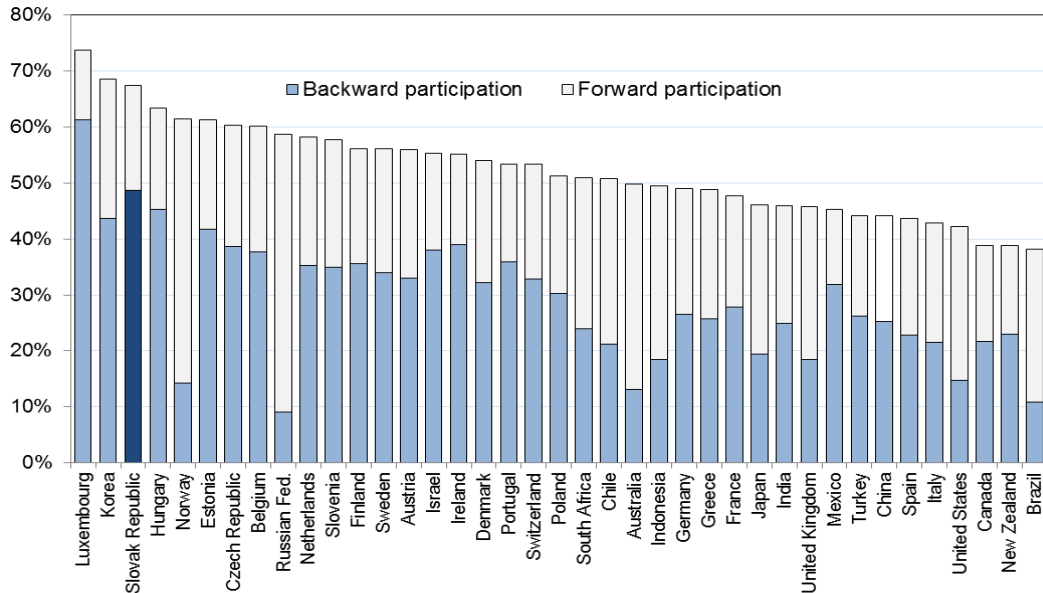
Notes: Export performance measures the relative gain and losses of world market share of a given country. If a country's exports are growing faster (slower) than the weighted average demand from its partners, it is gaining (losing) market share.

Source: Economic Outlook 92 (November 2012) Database.

### Box 1. The Position of the Slovak Republic in Global Value Chains (GVCs)

The ability of countries to prosper depends heavily on their participation in the global economy, which is closely linked to their participation in GVCs. The Slovak Republic participates extensively in GVCs (Figure I) in sourcing a very high share of the intermediate inputs used for its exports from abroad. This strong position reflects the shift of European GVCs to the east over the past decades.

**Figure I. Global Value Chains participation, 2009**

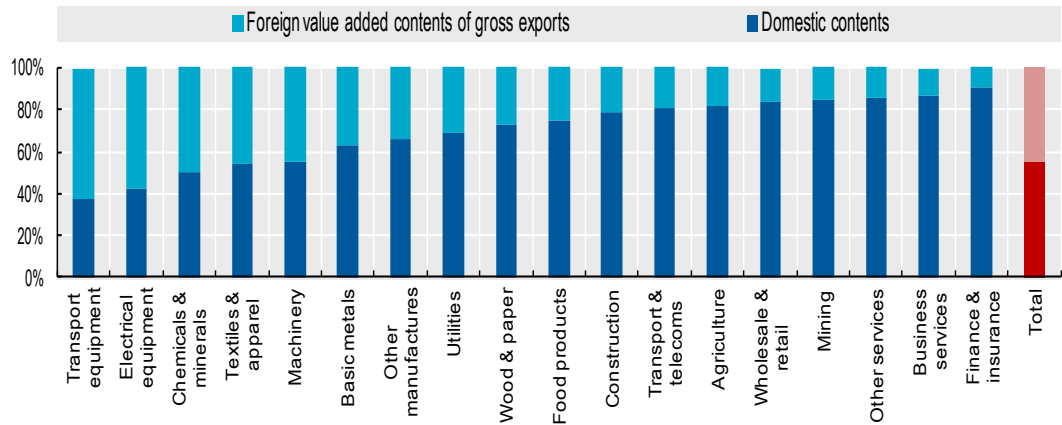


Source: OECD-WTO, Trade in Value Added database.

With a relatively high level of backward participation in GVCs (measured by the share of intermediate inputs used for exports abroad), combined with a relatively low level of forward participation (measured by the share of domestically produced inputs in third countries' exports), the Slovak Republic is mainly positioned in the downstream activities of GVCs, often involving the assembly or manufacturing of components and parts. This contributes to the relatively limited domestic value added created by exports: half of the value of exports is value added from abroad embodied in intermediates, compared to one quarter on average in the OECD. In important export sectors like transport equipment and electrical and optical equipment, the domestic value added is around 40% or below (Figure II).

Germany is the main source of foreign value added in output of the Slovak Republic (about 16% of the total) largely concentrated in semi-manufactured goods and intermediates (especially in the sectors of transport equipment and electrical and optical equipment). The Russian Federation is the second source of foreign value added output (9%) and this mainly involves embodied energy products.

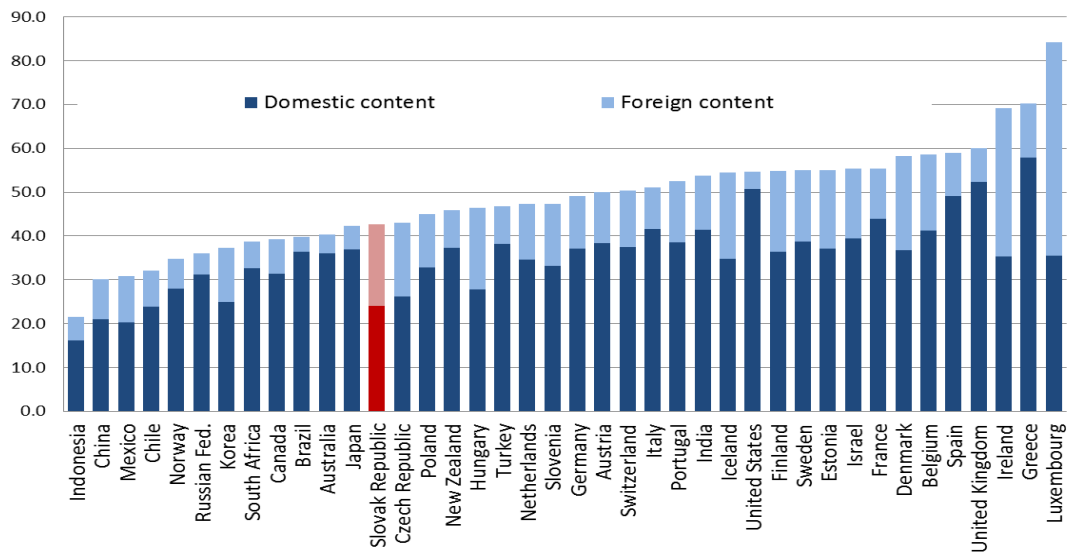
**Figure II. Slovak value added content of gross exports, by industry, 2009**



Source: OECD-WTO, Trade in Value Added database.

GVC activities in the Slovak Republic reflect its strong manufacturing orientation. Services account for 10% of Slovak exports in gross terms and about 40% in value added terms (Figure III); this is low compared to other EU countries, where the average is over 50%.

**Figure III. Services content of gross exports, by industry, 2009**



Source: OECD-WTO, Trade in Value Added database.

However, competitiveness gains in the industry have been achieved at the expense of employment. Export-oriented companies, under pressure to improve competitiveness, have invested to increase productivity and not to create jobs. As further efforts to support cost competitiveness will be necessary, labour market outcomes are expected to improve only slowly.

The Slovak Republic needs, therefore, to develop new drivers of growth, including a reconsideration of its position in GVCs. The involvement of the Slovak Republic in GVCs is highly concentrated, with strong involvement in a limited number of industries and a strong orientation towards Germany. There is a great potential for

diversification of the economy, which, however, needs an appropriate supply response, driven by skills and innovation. The Slovak economy can make more out of its privileged position in GVCs with the “globalisation giant” Germany by upgrading and diversifying its supply capacity. This could contribute to increasing the domestic value added created by exports.

Competitiveness in GVCs requires strengthening factors of production that are unlikely to cross national borders. This implies investment in human capital and skills (Chapter 5), high-quality infrastructure and innovation (Chapter 6) and encouragement of strong industry-university linkages and other forms of tacit knowledge. The quality of institutions and government (Chapter 3) are also important, long-term factors in firms’ decisions to invest and engage in value creation in the Slovak Republic. The business environment also needs to be improved, particularly by removing remaining barriers to entrepreneurship (notably, reduce further administrative burdens on corporations, increase competition in network industries and professional services, and eliminate corruption).

More generally, a better skilled labour force, better innovation performance and a stronger business environment are necessary for Slovakia to develop dynamic domestic drivers of growth.

## 2. STRENGTHENING THE FISCAL FRAMEWORK TO SUPPORT A MORE BALANCED AND FAIRER GROWTH

While it remains significantly below the OECD average, the debt to GDP ratio increased by 24 percentage points since 2008 to above 52% of GDP in 2012 (Maastricht definition). Slovakia remains under the Excessive Budget Deficit Procedure with a deficit at around 4.3% of GDP in 2012. The government is committed to reducing the deficit to below 3% in 2013 and has put together a credible consolidation programme for debt stabilisation.

However, improvements to the fiscal framework and tax system are needed to mitigate the impact of fiscal consolidation on growth, and support better growth in the medium-term.

### Improving the fiscal framework

The recently established fiscal rules have significantly improved the fiscal framework, including the establishment of a debt rule. While establishing a debt rule has several advantages (not least in terms of transparency) such a rule cannot substitute for a structural deficit rule and may lead to pro-cyclical fiscal action when debt is near the ceiling. As designed, the rule is intended to enforce continued consolidation during cyclical downturns and may not coincide with the structural budgetary objective.

The fiscal framework would be strengthened further by introducing enforceable spending ceilings, as planned. This would help make national fiscal rules consistent with Slovakia's new EU fiscal discipline requirements, and support a structural budgetary balance.

However, this introduction should be accompanied by reforms allowing a prioritisation of spending to support pro-growth policies, and ensuring that budget allocation is associated with programme monitoring and evaluation. Addressing these weaknesses is especially essential going forward to ensure more resources are directed towards growth-enhancing expenditure such as education, research and development and infrastructure, and that they are efficiently used.

In this respect it is also essential for Slovakia to make better use of EU structural funds. It is among the countries with the lowest rate of absorption of these funds, mainly as a result of a non-transparent selection process for projects, which limits stakeholders' access to these funding opportunities. The OECD can support the efforts of the country to take better advantage of the funds available.

Given the high share of procurement in total public spending (29% vs. 22% on average in the EU 27), raising the transparency and efficiency of public procurement is also essential to lowering their costs while ensuring service quality.

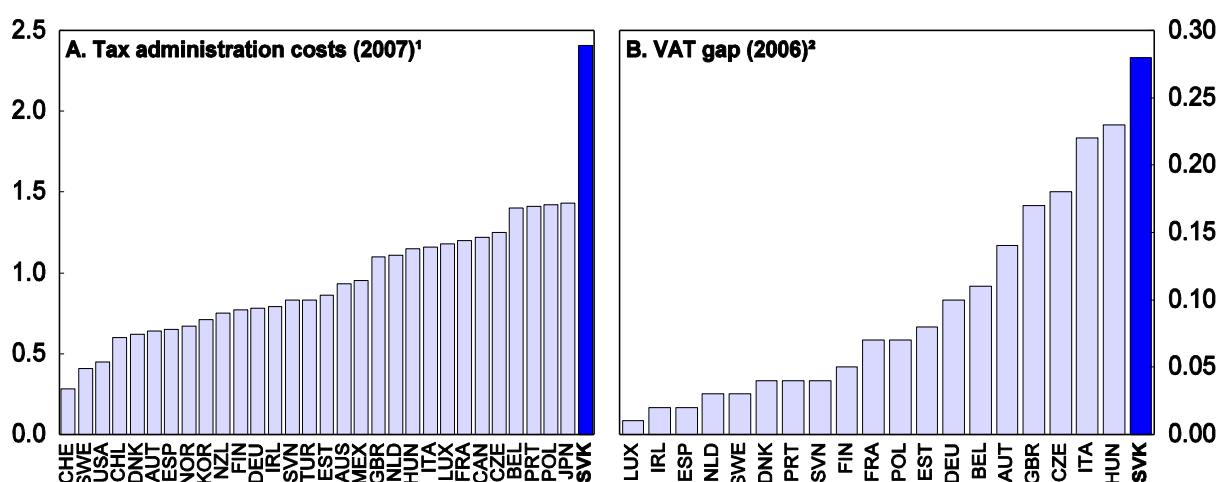
## Reforming the tax system

Tax revenues in Slovakia were equivalent to about 29% of GDP in 2011, lower than the OECD average (34%) and also lower than in other countries in the region. While there is room for higher taxation, fiscal consolidation efforts should focus on taxes that are less distortive and harmful to growth and jobs, and on improving tax administration.

Slovakia relies substantially more on social security contributions (SSCs) than other OECD countries. This likely contributes to the poor labour market outcomes (Chapter 4). Tax increases should involve the least distortive taxes, such as property and environmental taxes. In particular, the taxation of environmentally-harmful activities would not only contribute to fiscal consolidation but also support green growth. When the fiscal situation permits, it will be worth considering lowering labour taxes paid by employers, notably at lower wage levels, to encourage greater labour demand.

In addition, there is room to increase tax revenue through tax administration reforms, thereby increasing the efficiency of tax collection. The administrative cost of tax collection (annual administration costs given the total revenue collected) is the highest in the OECD (Figure 7, left panel). In addition, tax compliance is low. A case in point is the VAT, where the use of reduced VAT rates and exemptions is relatively limited, but where revenue is hampered by high levels of non-compliance and fraud (Figure 7, right panel).

**Figure 7. Efficiency of tax collection**



Notes:

1. Ratio of aggregate tax administration costs per 100 units of net revenue collection.
2. The VAT gap is defined as the difference between the accrued VAT receipts and the theoretical receipts, as a share of the latter.

Source: OECD, *Government at a Glance 2011 and Reckon (2009), Study to quantify and analyse the VAT gap in the EU25 Member States.*

## Key Policy Recommendations

- Strengthen the medium-term budgetary framework by introducing spending ceilings as planned, and adhere to them.
- Increase the scope for monitoring and evaluation of spending programmes and ensure that evaluation data informs policy decisions and resource allocations. Widen the use of performance elements in financing, contract renewals and compensation. Assess and, when needed, strengthen each ministry's capacity to assess the efficiency of policies. Establish a robust system of internal controls, and include appropriate performance and results information in annual budget documentation. Allocate more resources to ex-post audit and take into account evaluation outcomes in budget allocation.
- Provide an adequate degree of transparency throughout the entire public procurement cycle. Amend the Public Procurement Act to ensure that the tender achieving the best value for money is selected and that the competitive dialogue procedure can be used for complex projects. Systematically record problems with public procurement and implement a task force to provide recommendations on making procurement rules easier to apply without undermining their intentions of fighting corruption and increasing efficiency.
- Direct more resources towards growth-enhancing areas such as education, research and development, and infrastructure. Establish an effective framework for assessing and selecting infrastructure projects, using tools such as cost-benefit analysis.
- Raise the absorption of EU funds by reducing the administrative hurdles to the submission of projects.
- Reform the structure of taxation to make it less harmful to growth notably by increasing real estate and environmental taxes and, when possible, lowering labour taxes paid by employers at lower wage levels to encourage greater labour demand.
- Improve tax collection by implementing the transition towards an integrated tax collection system. Combat tax evasion by strengthening monitoring activities.

## 3. IMPROVING PUBLIC GOVERNANCE

In Slovakia, as in many OECD countries, there is growing awareness of the importance of strong and efficient public administration for the success of reforms. First, restoring public finances while fostering domestic drivers of growth and supporting employment requires significant improvements in the efficiency and effectiveness of public administration. Beyond the saving it can generate, a more efficient public administration is key to supporting the government's strategic agenda, and ultimately ensuring that it contributes to the growth and well-being of the country.

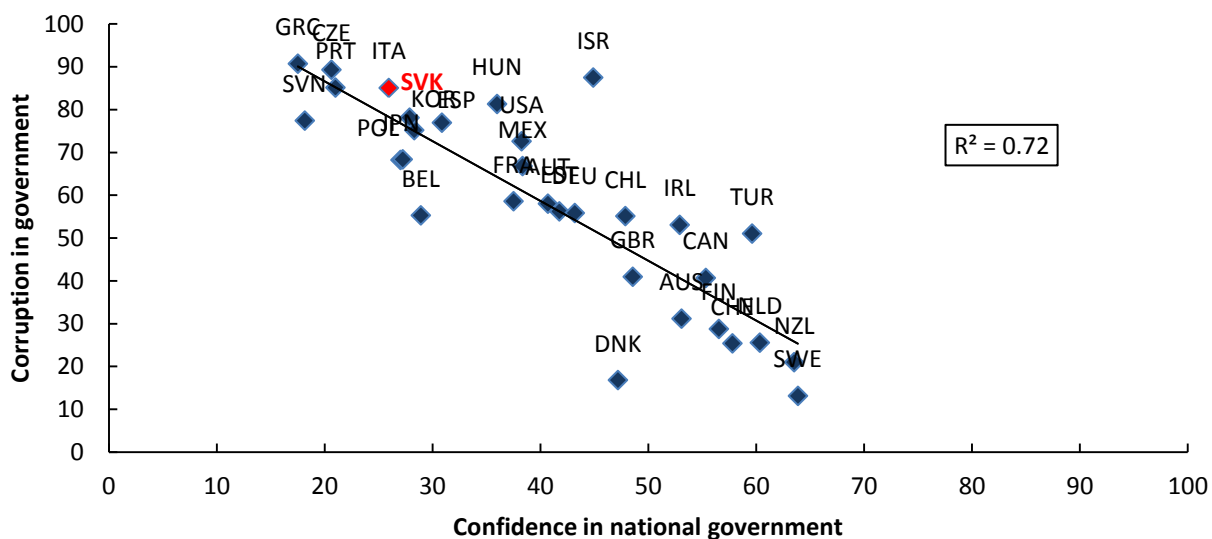
### **Strengthening quality and capacity of the public administration is essential for trust**

The public administration has a key role in the design, development, implementation and monitoring of pro-growth spending programmes and reforms. The effectiveness of public administration as a provider of essential services in the areas of education, active labour market policy and innovation (discussed in the next chapters) is key for the success of Slovakia in continuing the fast convergence towards higher levels of income and well-being.

However, the quality and capacity of public administration needs to improve. Slovakia fares poorly in international comparison of the quality of public governance and effectiveness of public administration. Moreover, there is the perception that corruption in public administration remains an issue, which could in part contribute to the low trust in the Slovak government. Adopting international best practices could improve public administration effectiveness, openness and transparency, and support the effective implementation of the reform agenda. It would also help enhance the quality of public services without increasing spending, supporting trust in the Slovak government (Figure 8).



**Figure 8. Corruption and Confidence in national government (2011)**



Notes: Corruption in government shows the percentage of survey respondents that stated that corruption is widespread throughout the government. Confidence in national government shows the percentage of survey respondents who stated that they have confidence in the national government.

Source: Gallup World Poll

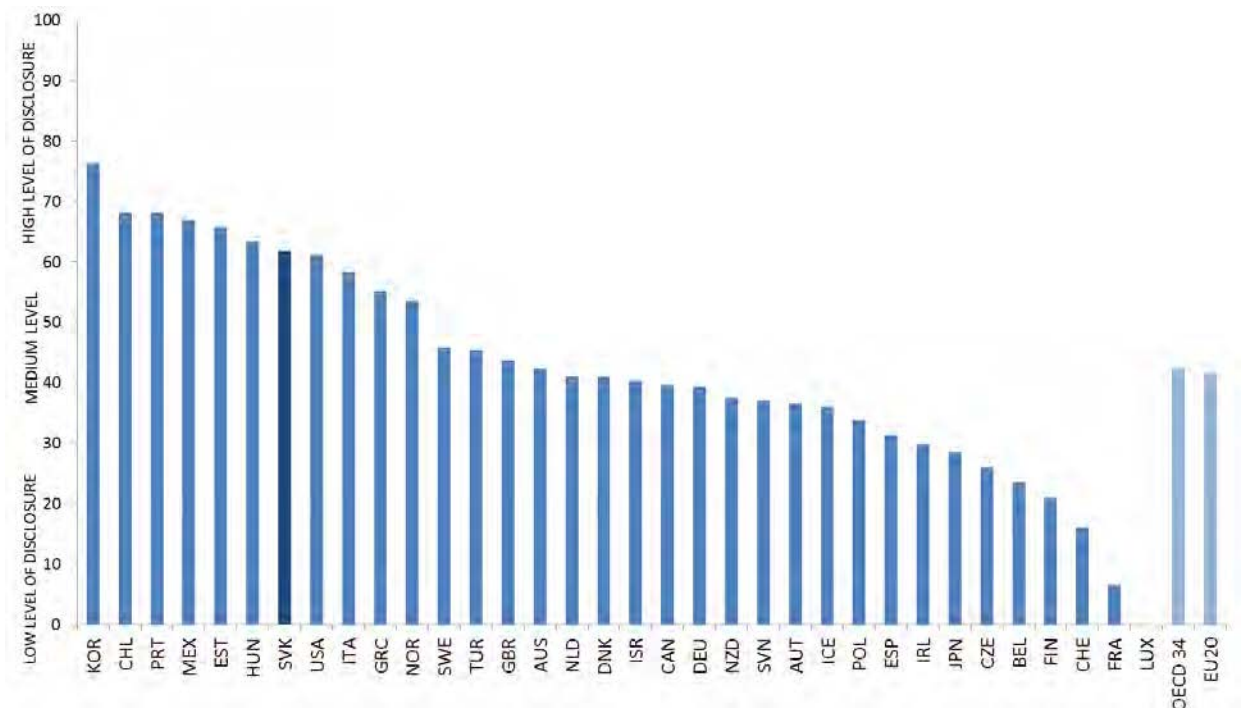
### A strategic approach to public administration reform is needed

In 2012, the government launched the ESO Programme (“Effective, Reliable and Open Public Administration”) to lay the ground for a comprehensive public administration reform strategy.<sup>1</sup> Some envisaged measures, including the streamlining of some de-concentrated state administration offices, have already been implemented. Slovakia also discloses and makes available a relatively high level of information of high-ranking public officials in the executive, judiciary and legislative bodies (Figure 9). This level of disclosure could help reduce biases in policy making and help address corruption and capture in the public administration.

Despite these promising steps in addressing some of the key bottlenecks faced by the public administration in Slovakia, further action would be needed. In particular it is essential to ensure that the reform effort is coordinated across public administration, that openness and transparency are streamlined across the administration, that synergies are fully exploited and that sufficient attention is given to strengthening the capability and resources to develop and implement policies over the long-term.

<sup>1</sup> The ESO Programme aims to streamline the organisation of state administration, improving human resources management, strengthening analytical capacity, enhancing integrity and transparency, modernising the justice system, scaling up partnerships with the third sector, and broadening the use and impact of e-government across public administration.

**Figure 9. Disclosure of selected private interests and public availability of disclosed information (executive, legislature, judiciary)**



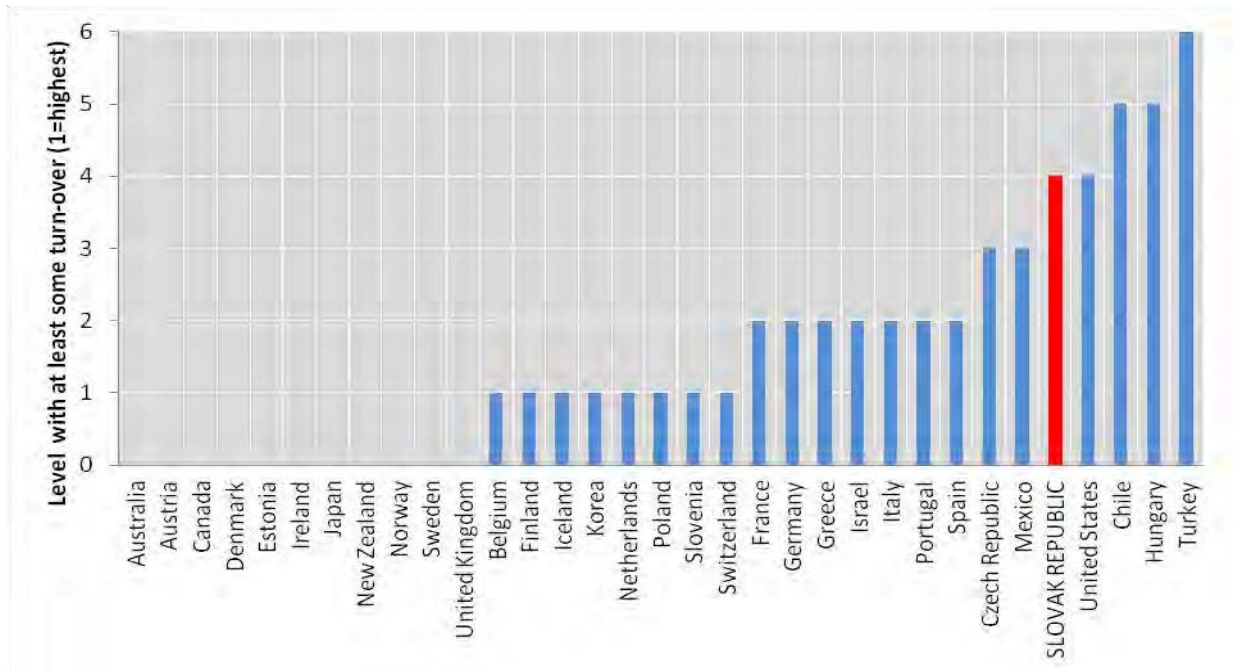
Source: OECD 2012 Managing Conflict of Interest survey

In particular, the public administration still suffers from a high turnover of staff. The Slovak Republic is among the OECD countries with the highest turnover of civil servants following a change of government (Figure 10). While this may increase the ability of public administration to respond to new policy priorities, such high turnover can also affect the continuity and stability of government policies at a time when reforms have to be sustained over a medium-term horizon.

The Slovak public administration also suffers from a limited strategic approach (Figure 11). Strategic human resources management (HRM) helps scale-up investment in the public workforce by aligning incentives with performance. It can increase efficiency, responsiveness and quality of service delivery.

More generally, the capacity of a government to steer and lead policy largely depends on the strength of the centre of government and the senior civil service, which could both be further strengthened in the Slovak Republic.

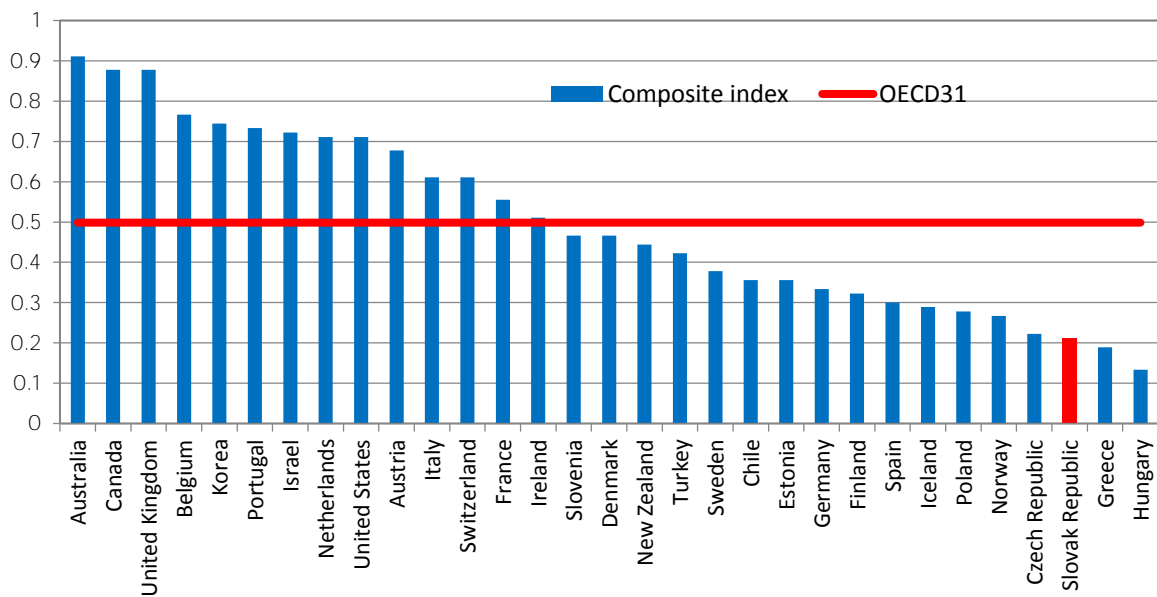
**Figure 10. Turnover of civil servants with a government change (2010)**



Notes: Data for Luxembourg are not available. Data on turnover in level 5 and 6 are not available for Portugal and the United States. Data on turnover in level 6 only are not available for the Czech Republic, Hungary, Israel and Spain. In New Zealand, a change of government does not affect the employment of public servants. The exception to this is a small number of public servants employed in ministerial offices on an event-based contract, with the event triggering the termination of their contract being the conclusion of their relevant minister's term in office.

Source: OECD (2011), *Government at a Glance 2011*. OECD Publishing.

**Figure 11. Utilisation of strategic HRM practices in central government (2010)**



Source: OECD (2011), *Government at a Glance 2011*, OECD Publishing

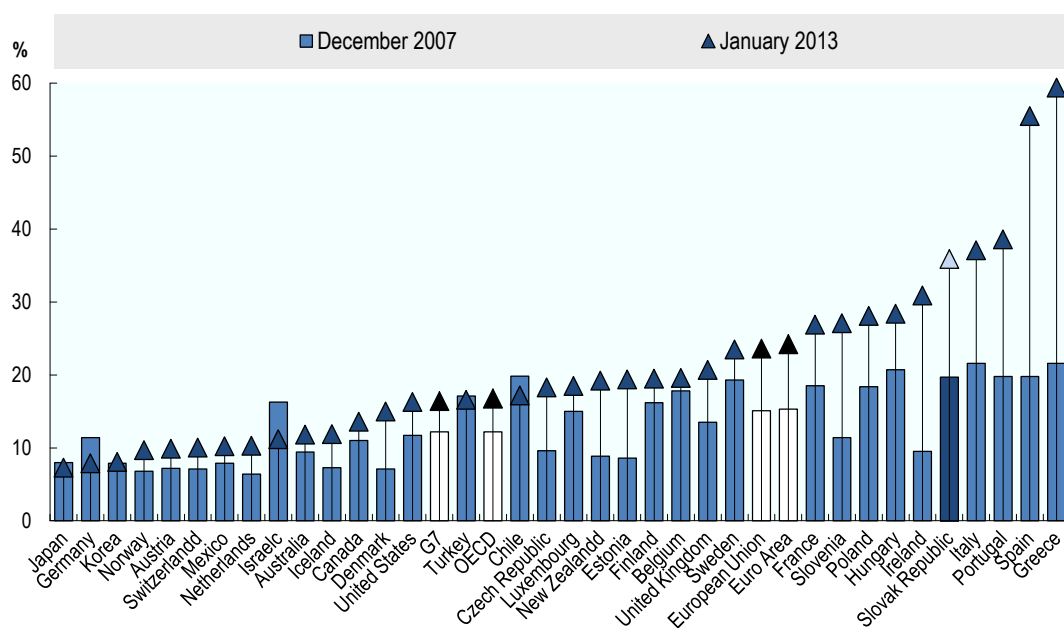
### **Key Policy Recommendations**

- Enhance transparency and integrity across public administration: consider the development and implementation of tools to enhance transparency and reduce opportunities for corruption, including whistleblower protection, a code of conduct, and regulations addressing conflict of interest and lobbying.
- Enhance strategic management of human resources: widen the use of performance elements in promotion, contract renewals and compensation of public staff, and improve workforce planning and allocation.
- Strengthen the role of senior civil servants to provide policy advice: assess the skills and capacities of senior civil servants to develop and evaluate policies, and improve communication and coordination between senior civil servants and the political level.
- To improve the government capacity to steer and lead policy: assess and improve coordination structures between central and sector ministries, improve consultation and coordination between strategy and budget, and evaluate the role of the centre of government in supporting strategy development and implementation across government.

## 4. IMPROVING LABOUR MARKET OUTCOMES

The Slovak labour market recovery is one of the weakest in the OECD area. The unemployment rate rose significantly during the crisis, reaching almost 15%, the fourth highest in the OECD (Figure 3 in Chapter 1). In addition, youth unemployment is the fifth highest in the OECD at close to 36% (Figure 12). The incidence of long-term (12 months or more) unemployment is the highest among OECD countries. At 67.5% of total unemployment in the third quarter of 2012, Slovak long-term unemployment was twice the OECD average (Figure 13). Last, the Roma population is de facto excluded from the labour market with an unemployment rate above 70%. The educational outcomes of the Roma are relatively poor, which contributes to their difficulty to access the labour market (Chapter 5). But this is only one factor: at the same level of education, the unemployment rate of Roma is between two and eight times higher than for non-Roma living in the same region. Remote settlement structures and discrimination on the labour market also play a great role.

**Figure 12. Youth unemployment rates, December 2007-January 2013**

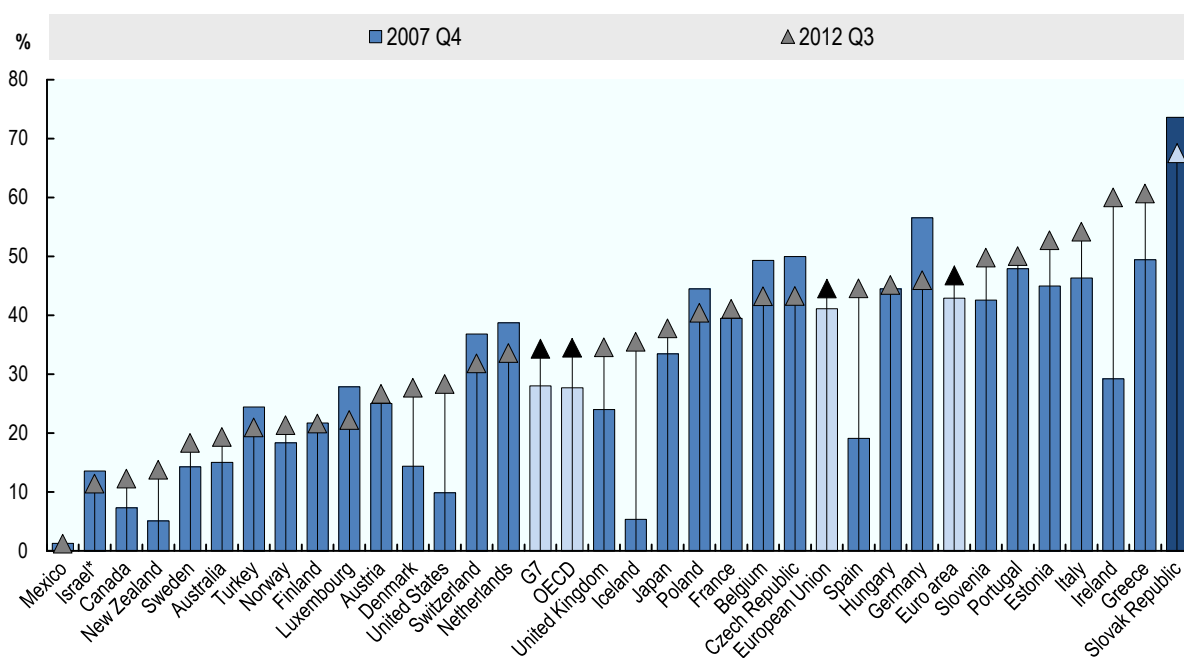


Notes:

1. For Israel, the series have been chained to take into account the break series in 2012.
2. November 2012 for Greece, Turkey and the United Kingdom; December 2012 for Chile, Estonia, Hungary, Italy (number of unemployed only), Norway and Slovenia; February 2013 for Canada and the United States; 2012 Q3 for Switzerland; and 2012 Q4 for New Zealand.

Source: OECD calculations based on the OECD Short-Term Indicators Database.

**Figure 13. Long-term unemployed (more than one year) as a percentage of total unemployed, 2007 Q4 and 2012 Q3**



Notes:

1. Data are not seasonally adjusted but smoothed using three-quarter moving averages. OECD is the weighted average of 32 OECD countries excluding Chile and Korea.
2. 2011 Q4 for Israel.

Source: OECD calculations based on quarterly national Labour Force Surveys.

The recovery has not led to job creation and significant improvements in labour outcomes. These poor outcomes largely reflect structural factors that have to be addressed. Otherwise, this situation could result in substantial increases in inequality going forward. High structural unemployment is also a major drag on productivity growth and labour utilisation, and weighs on public finances. Another challenge is to increase female labour participation, which remains below that of other Eastern European countries. This would help support labour force participation, which is below the OECD average.

Reducing unemployment and supporting labour market participation can lead to multiple benefits of increasing potential growth, facilitating fiscal consolidation by raising revenues from taxes and social security contributions while relieving the budget from social benefits, and reducing income inequalities.

## Supporting youth employment

While Slovakia's employment rate for 25-54 year-olds is above the OECD average, the employment rate for youths (15-24) is well below (by 19 points in 2011). This reflects both high unemployment and low labour force participation (30.2%, against an OECD average of 47.2%). Recent OECD work shows that the poor labour market performance of Slovak youth is primarily the result of high unemployment rates among graduates from vocational schools, who account for nearly two-thirds of all youth graduates. Improving the school-to-work transition of graduates from

vocational schools is crucial, as there is a risk that their long-term career prospects could be permanently compromised. A legal framework for an effective dual apprenticeship system should be created, delivering professional experience during studies and work-based vocational education and training (Chapter 5). Improving the school-to-job transition also requires more general improvement in the quality of the education system (Chapter 5).

Youth employment could also be supported by removing disincentives to take up part-time work. A significant proportion of non-employed youths are likely to be living with their parents in a household that receives social assistance. The earnings of dependent children (up to the age of 25) results in a reduction of the social assistance that a household may receive. Up to the minimum wage (around 300€ per month), the reduction corresponds to 75% of their earnings. If they earn the minimum wage or more, their parents may lose the child element of social assistance altogether. This represents a strong disincentive against part-time work, and act as a barrier to acquiring work experience, while it may also promote undeclared work among those who are no longer in education. Furthermore, this regulation could also turn out to be an unwelcome barrier for the take-up of apprenticeship programmes, which typically combine part-time (low-paid) work with one or two days a week in school.

## Tackling long-term unemployment

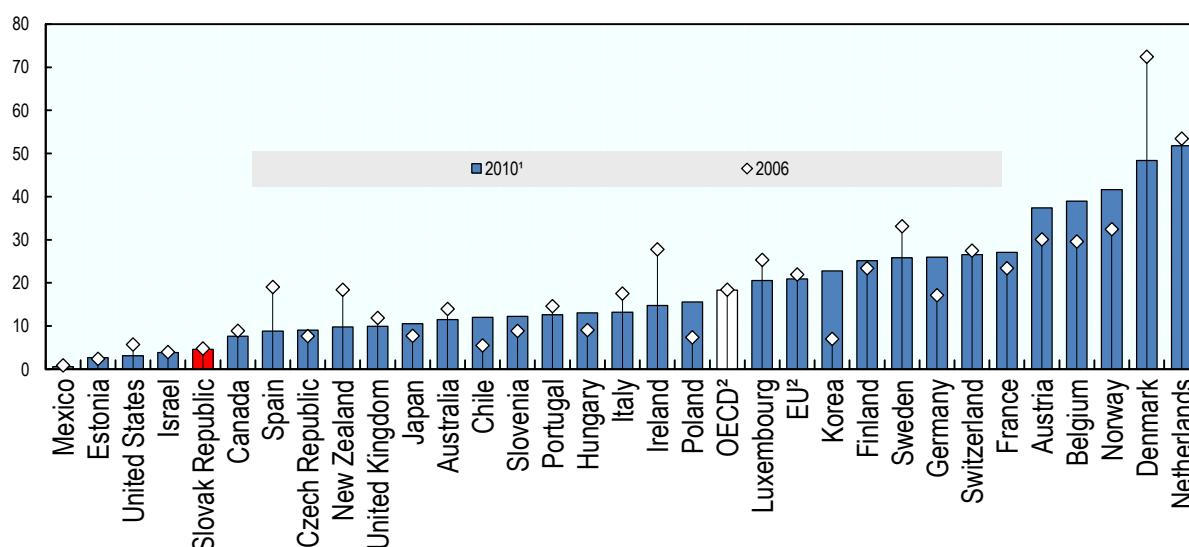
The high level of long-term unemployment, which particularly affects the Roma population, calls for more emphasis on activation policies, which should be designed to encourage and help the unemployed find work. In particular, assistance benefits for those with some ability to work should be conditional on availability to work. Institutional incentives should also be improved either by making municipalities responsible for the cost of assistance benefit payments or by strengthening the national management of benefits, employment services and other activation measures.

Active Labour Market Programmes (ALMPs) are currently underfinanced (Figure 14) and insufficiently evaluated. It is, therefore, essential to strengthen the capacity of the public employment service and expand training opportunities. It is also important to focus these programmes on achieving unsubsidised hiring.<sup>2</sup>

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<sup>2</sup> One risk associated with ALMPs is that the payment of an income supplement to programme participants encourages participation in the programme more than transition into unsubsidised employment. Another risk is that the funding of local authorities or associations to employ unemployed workers results in the creation of programmes that deliver local services, with a preference for taking in and retaining participants who are already relatively employable. One of the chapters for the upcoming 2013 Employment Outlook (“Activating jobseekers: lessons from seven OECD countries”) describes different methods of activation and some of the pitfalls to avoid in this area.

**Figure 14. Public expenditure on active labour market policies per unemployed, percentage of GDP per capita**



Notes:

1. The latest available year is 2007 for Norway and Switzerland, 2009 for the United Kingdom.
2. OECD average excludes Iceland, Greece and Turkey. EU is the average of 21 EU countries members of the OECD.

Source: OECD, Public expenditure and participant stocks on LMP and Economic Outlook Databases.

Promoting labour mobility is also essential. In addition to training, it implies tackling the impediment to mobility coming from the housing market, including removing obstacles to the expansion of a private residential rental market, and improving the targeting of housing subsidies.

### Reducing barriers to labour force participation.

Employment rates are low not only for young people but also for old people and women. There has been a noteworthy increase in older worker employment rates in the last five years, mainly as a result of an increase in the legal retirement age, and recent reforms will continue to gradually increase retirement age. But more needs to be done to reduce barriers to female labour force participation, especially for women with young children and of older ages, including by shortening the duration of parental leave entitlements, expanding the availability of childcare facilities, and removing fiscal disincentives to work for second earners notably by cutting the tax allowance for non-working spouses.



### **Key Policy Recommendations**

- Strengthen the vocational education and training system to facilitate the transition from school to jobs.
- Develop lifelong learning and enhance incentives for employers to allocate more resources and time to training, for instance by improving the system of training vouchers or by introducing tax deductions for training costs.
- Design effective activation policies to encourage and help the unemployed find work, targeted on the long-term unemployed (predominantly Roma population). Make assistance benefits, for those with some ability to work, conditional on availability for work. Improve institutional incentives either by making municipalities responsible for the cost of assistance benefit payments or by strengthening the national management of benefits, employment services and other activation measures. Focus Active Labour Market Programmes (ALMPs) on achieving unsubsidised hirings.
- Support female participation by shortening the duration of parental leave entitlements, expanding the availability of childcare facilities and removing fiscal disincentives to work for second earners.

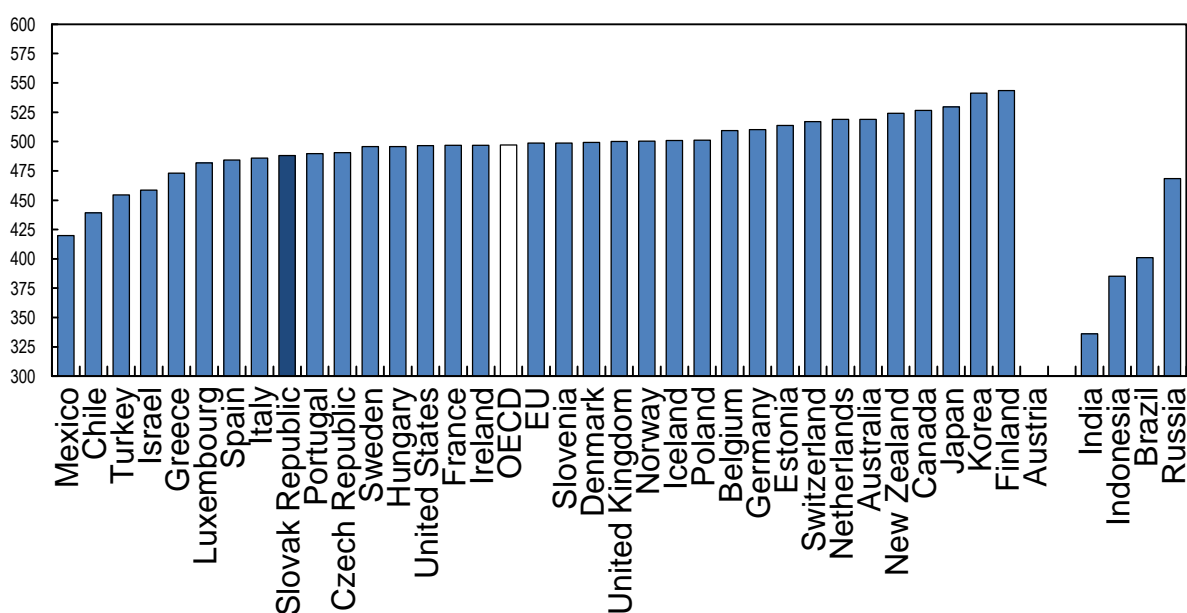
## 5. EDUCATION: IMPROVING QUALITY AND EQUITY

Improving educational outcomes is a priority for increasing productivity, improving the matching between skills and labour market needs and reducing inequality, including through a better integration of socially-excluded parts of the population. While the share of the population that has attained upper-secondary education is among the highest in the OECD, tertiary education attainment remains below the OECD average, although it has seen rapid growth since 2010.

Moreover, educational outcomes as measured by PISA have improved since 2006, they are still below the OECD average (Figure 15) and are fairly strongly dependent on socio-economic background. In particular the Roma population has very poor educational outcomes, with less than 20% of them currently reaching an upper-secondary education level. Best performing school systems are those which commit themselves to ensuring that all students succeed. This suggests that more resources should be allocated to support these disadvantaged pupils.

In addition to the improvements to the education system proposed in this chapter, encouraging and enabling people to learn throughout life through on-the-job training and training for adults is also key in raising the skills of the labour force and matching better the needs of the economy.

**Figure 15. Educational achievement: Average of PISA scores in reading, mathematics and science**



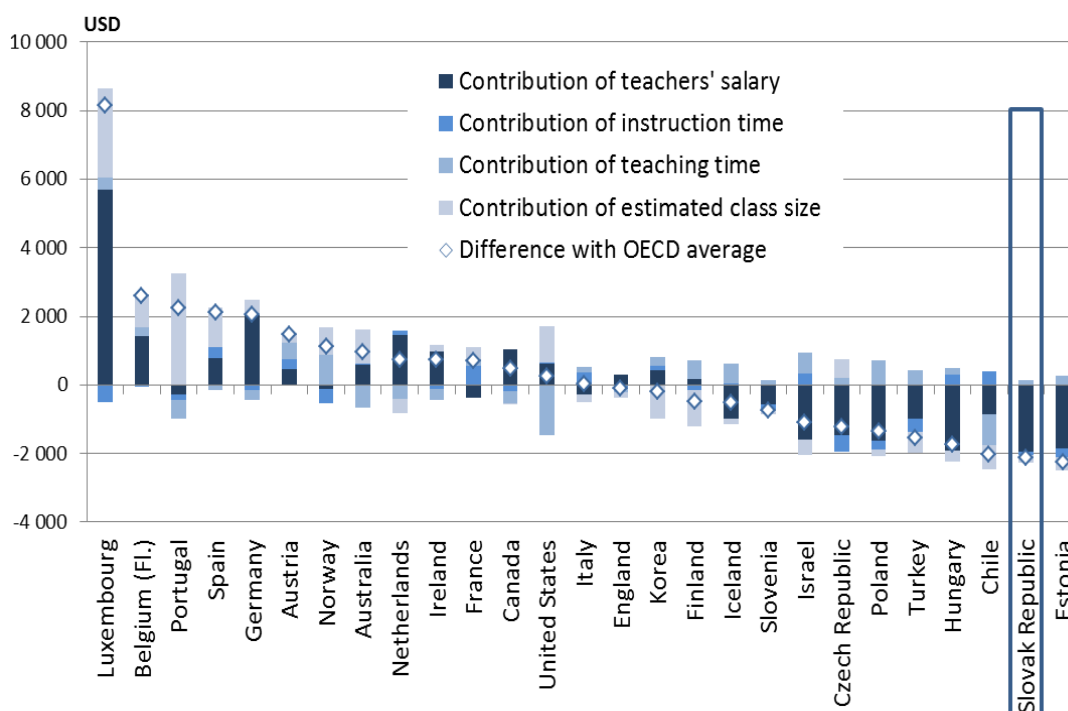
Source: OECD, PISA 2009 Databases.

## Improving the allocation of funding

Notwithstanding strong increases over the past decade, Slovakia is among the OECD countries that spend the least on education per student at all levels of education. Increasing education spending will not necessarily lead to improved educational outcomes. The key is how the money is spent. Better allocation could already lead to a better performance of the education system. The funding system, which allocates premiums to eight-year grammar schools (schools for the best pupils, selected at age 10) is, for instance, encouraging schools to separate out very good as well as poor performers or students with behavioural problems and/or special needs. Financial incentives for integrating pupils with special needs in mainstream education are quite low. These practices are inefficient as they may have no impact on overall educational outcomes, and tend to increase the influence of socio-economic background on learning outcomes. The planned removal of premiums for eight-year grammar schools by 2013 is therefore highly welcome, and existing incentives for integrating pupils with special needs in standard schools or classes should be developed.

There is potential for investing more in the quality of teachers to help improve learning outcomes. Slovakia's low expenditure per student is largely the result of relatively low teacher salaries (Figure 16). Increasing the wages of teachers, which are amongst the lowest in the OECD, could serve to improve the attractiveness of the profession while at the same time creating incentives for quality improvements.

**Figure 16. Contribution (in USD) of various factors to salary cost of teachers per student, at upper secondary level of education (2010)**



Source: OECD Education at a Glance. Table B7.4. ([www.oecd.org/edu/eag2012](http://www.oecd.org/edu/eag2012)).

This could be partly financed by efficiency gains in primary and secondary schools. Further efficiency gains could notably be achieved by reducing the network of schools, increasing the size of classes and making better use of evaluations. For example, external school evaluations remain focused on school compliancy with rules and regulations and could be better used to evaluate the quality of teaching and learning. Less than one third of Slovak teachers report that the appraisal and feedback they receive has a substantial impact on their opportunities for professional development, their career advancement or any growth in their work responsibilities. There is also a need to publish school performance information with adequate contextual information, so as to avoid misinterpretation and superficial competition among schools. The education system should also adapt to the rapid development of demand for higher education, and provide opportunities for pupils to pursue their studies.

### **Better supporting disadvantaged pupils**

The share of students performing below the basic reading proficiency at PISA is significantly higher than the OECD average and is mainly attributable to the weak performance of boys. Socio-economic background also has a relatively strong impact on student performance. More resources should be provided to support socio-economically disadvantaged pupils, including through good-quality early childhood education for children from disadvantaged backgrounds, notably children from the Roma minority.

It is also essential to integrate better children from the Roma minority in standard classes instead of placing them in special educational programmes, which provide a low quality of education and prevent them from accessing higher levels of the education system. Providing teachers with the skills to better provide for the individual needs of a diverse student population will be key to making this a success. With already relatively low engagement in professional development activities, Slovak teachers themselves report that this is an area in which they need better training.

### **Improving the school-to-job transition process**

Labour market outcomes for the youth could be improved by facilitating the school-to-job transition, which is weak in Slovakia and hampers both productivity and labour utilisation. Vocational education needs to be improved, notably by developing work-based vocational education. While in the Slovak Republic 70% of upper-secondary students follow vocational studies (one of the highest rates among the OECD countries) only a few of these students receive meaningful training with employers as part of their upper-secondary education.

Learning in the workplace allows young people to develop “hard” skills on modern equipment, and “soft” skills, such as teamwork, communication and negotiation, through real-world experience. Simulating these situations in workshops is more difficult. Workplace training also allows employers to learn about a potential recruit and vice versa.

By the end of basic education (around the age of 14) students choose one of the upper-secondary pathways. Those that choose a vocational track will then select an occupational specialisation. This is relatively early compared to some other countries (e.g. Norway and Poland) where the choice of upper-secondary track is taken at the age of 15. Given the early career choice, the provision of career guidance at the second stage of basic education and at the beginning of upper-secondary studies is not sufficient. According to school principals' responses recorded in PISA 2006, only 35% of students in basic education were in schools where career guidance was formally scheduled.

As with several other Eastern European countries, at post-secondary level students choose among university (or equivalent) degree programmes. Shorter professionally-oriented post-secondary education and training has yet to be developed. This contrasts with many OECD countries (such as Denmark, Sweden, Switzerland and the United States) where post-secondary vocational education and training is an important source of skilled workers for many technical occupations.

#### **Key Policy Recommendations**

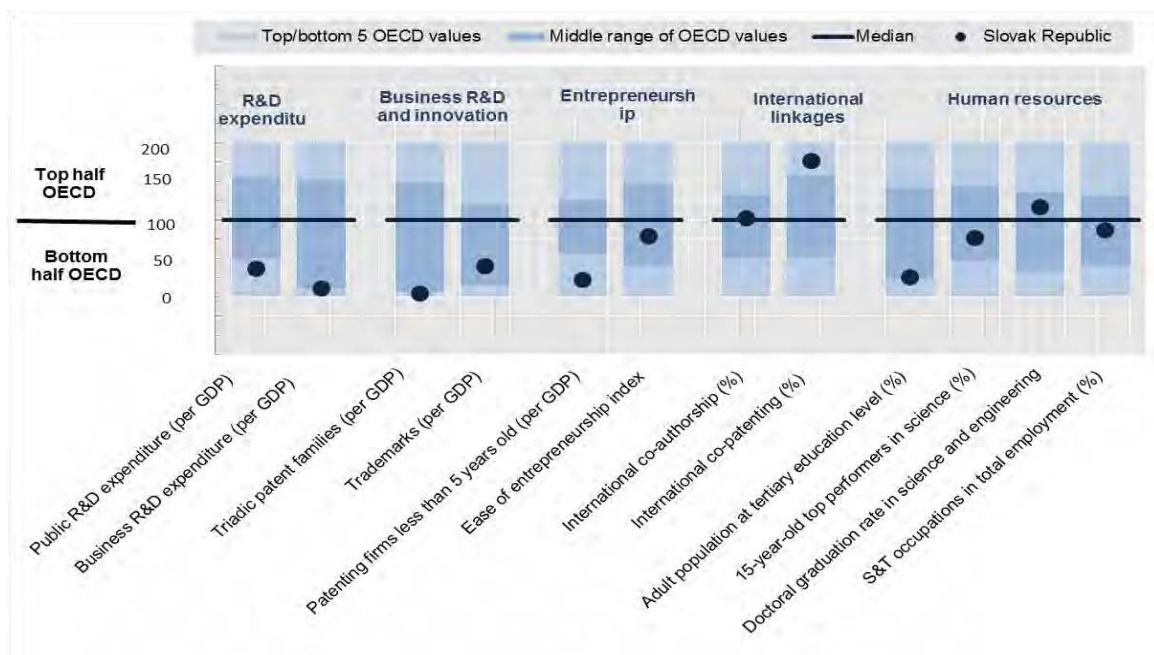
- Improve the use of existing evaluations to identify schools in need of educational improvement, as well as to identify and promote best practices in high quality schools.
- Increase support to disadvantaged pupils. Further encourage participation of children from low-income families and the Roma minority in pre-primary education and the integration of children from the Roma minority in mainstream education.
- Reduce stratification of the education system. Remove premiums to eight-year grammar schools as planned and strengthen incentives for the integration of pupils with special educational needs in the mainstream of schooling.
- Facilitate the school-to-job transition through the creation of a legal framework for an effective dual apprenticeship system, delivering professional experience during studies and work-based vocational education and training.
- Develop the national system of certification of competences acquired in the VET system by providing a consistent method to assess the learning outcomes of vocational programmes. Monitor the effectiveness of VET councils and ensure they closely co-operate.
- Develop short (2-3 year), flexible and more vocationally-oriented tertiary programmes.
- Increase involvement of VET schools in adult education.

## 6. SUPPORTING ECONOMIC DIVERSIFICATION AND PRODUCTIVITY WITH A STRONGER INNOVATION PERFORMANCE

Despite being one of the fastest-growing economies in Europe, attracting significant foreign direct investment, including in manufacturing, Slovakia has progressed slowly in advancing its domestic science, technology and innovation (STI) capabilities over the past two decades. To continue to sustain productivity gains and develop new sources of growth, Slovakia needs to improve its innovation performance by strengthening its innovation support framework.

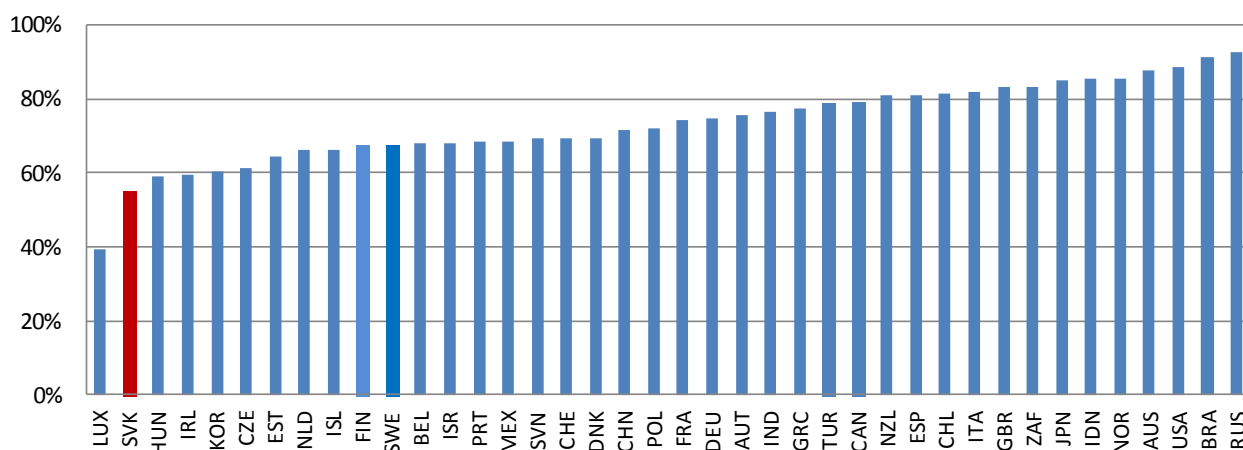
Public expenditure on research and development (R&D) as a share of GDP is among the lowest five of OECD countries (Figure 17). Industry-financed expenditure on R&D dropped from 0.65% of GDP in 1995 to 0.2% of GDP in 2010 – indicating a widening gap to many advanced and emerging economies. Business R&D outputs are among the lowest in the OECD area, and the domestic value added content of Slovak exports is very low by international comparison (Figure 18 and Chapter 1). Moving up the value chain and closing the remaining income and productivity gaps will require a sustained effort to advance innovation capabilities throughout the Slovak economy.

**Figure 17. Slovak R&D and Innovation Performance**



Source: OECD Science, Technology and Industry Outlook 2012

**Figure 18: Domestic value added content of gross exports, 2009, %**



Source: OECD-WTO, Trade in Value Added database.

There is scope for improving the framework conditions for innovation and entrepreneurship, which are critical for the rejuvenation of the economy.

Increased private and public investment in human resources, innovation and related infrastructure is a prerequisite for boosting innovation in the Slovak economy and society. The ICT infrastructure for innovation remains to be further developed, as broadband subscription rates and the government use of the Internet were low. The skills base for ICT is also weak, with only 17% of the adult population having tertiary qualifications (Chapter 5). However, the share of Science and Technology occupations, at nearly one third, in total employment is closer to the OECD median. There is also potential for future human resources in STI, given the performance of 15-year olds in science in the middle range of OECD countries and a doctoral graduation rate well above the OECD median.

In order to realise the expected returns, efforts in these direction have to be underpinned by good practices in the governance of the innovation system, including effective co-ordination of policy across government, the use and administration of national and European funds for innovation, and state-of-the-art steering and funding of public research institutes and universities, helping to increase their contribution to economic and social development.

#### Key Policy Recommendations

- Reverse the downward trend in private investments in R&D and ensure support for businesses R&D. Encourage cooperation between public and private R&D institutions, and improve the efficiency of public funding for R&D.
- Strengthen the quality of human resources from primary to tertiary levels.
- Improve the governance of the innovation system (transparency, co-ordination, use and administration of EU funds, and institutional reforms of public research institutes and universities).

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