

## SLOVAK REPUBLIC

Economic growth is projected to rise to around 8¼ per cent in 2007 supported by production at new automobile plants but to ease to 7½ per cent in 2008. Such production also underpins a large reduction in the current account deficit. Unemployment should continue to fall on the back of strong employment expansion. Disinflation is set to resume because of lower energy prices, high productivity growth and appreciation of the koruna.

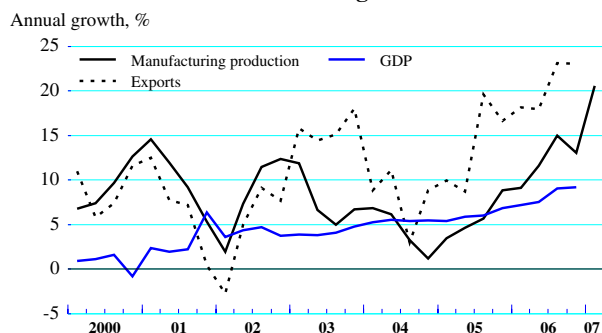
Fiscal policy may need to be more restrictive both to facilitate exit from the Excess Deficit Procedure and to pre-empt a possible post-euro entry overheating. Automatic stabilisers should be allowed to work fully and windfalls from higher than expected growth should be used to reduce the deficit. Further structural reforms are needed for maintaining high growth, notably to bring the long-term unemployed back into employment and to make participation more attractive for older workers and young women.

**Growth has soared as new car plants have entered into production**

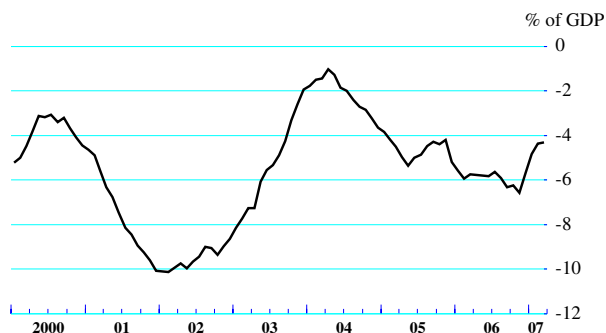
Real GDP growth soared to 9% in the year to the second half of 2006 as new export-oriented manufacturing plants (automobiles and, to a lesser extent, electronics) entered into production. Private consumption remained robust in 2006 as did investment adjusting for the timing of completion of these plants. Economic sentiment has stabilised in recent months at levels well above the historical average, pointing to continued solid growth. A small positive output gap is estimated to have emerged in 2006. Potential GDP should be boosted by some 7% over 2006-08 as production at these plants builds. Domestic employment growth has remained solid, at 2.2% in the year to the fourth quarter of 2006, and with many Slovaks taking jobs in neighbouring countries, national employment growth has been even higher (3.4%) over the same period. Such growth has driven the unemployment rate (Labour Force Survey) down sharply, to 12.0% in the fourth quarter of 2006, three percentage points less than a year earlier. Long-term unemployment has also fallen, albeit more slowly, to around 10% of the labour force. Headline inflation fell to 2.7% (year-on-year) in early 2007 supported by lower energy prices, exchange rate appreciation and low growth in unit labour costs; HICP

### Slovak Republic

**Manufacturing is boosting exports and GDP growth**



**The foreign trade deficit is being reduced**  
(12-month cumulative basis)



Sources: OECD Analytical database, Economic Outlook n°81 and Main Economic Indicators.


StatLink  <http://dx.doi.org/10.1787/032664822880>

## Slovak Republic: Demand, output and prices

	2003	2004	2005	2006	2007	2008
	Current prices SKK billion	Percentage changes, volume (2000 prices)				
Private consumption	687.6	4.2	7.0	6.1	6.0	6.4
Government consumption	249.1	2.0	-0.6	4.1	3.0	2.1
Gross fixed capital formation	302.8	5.0	17.5	7.3	7.4	7.1
Final domestic demand	1 239.5	3.9	8.1	6.1	5.9	5.8
Stockbuilding <sup>1</sup>	- 4.3	2.3	0.6	0.3	-1.4	0.1
Total domestic demand	1 235.2	6.2	8.6	6.2	4.4	5.8
Exports of goods and services	927.7	7.9	13.8	20.7	23.4	13.7
Imports of goods and services	950.3	8.8	16.6	17.8	18.6	12.2
Net exports <sup>1</sup>	- 22.5	-0.9	-2.8	1.7	4.2	1.8
GDP at market prices	1 212.7	5.4	6.0	8.3	8.7	7.6
GDP deflator	-	6.0	2.4	2.7	2.7	1.7
<i>Memorandum items</i>						
Consumer price index	-	7.5	2.7	4.5	2.3	2.1
Private consumption deflator	-	7.4	2.6	5.1	2.7	2.1
Unemployment rate	-	18.1	16.2	13.3	11.5	10.3
General government financial balance <sup>2</sup>	-	-2.4	-2.8	-3.4	-2.7	-2.1
Current account balance <sup>2</sup>	-	-3.5	-8.7	-8.3	-3.1	-2.5

1. Contributions to changes in real GDP (percentage of real GDP in previous year), actual amount in the first column.  
2. As a percentage of GDP.

Source: OECD Economic Outlook 81 database.

StatLink  <http://dx.doi.org/10.1787/035254827315>

inflation, which does not take into account owner-occupier housing costs, fell to 2.1% in early 2007. The entry into production of the new manufacturing plants has contributed to a sharp improvement in the current account balance, to a deficit of 7.2% of GDP in early 2007 on a previous 12-month basis.

### Macroeconomic policies are leaning against demand growth

The budget adopted by the government provides for a 0.8 percentage point reduction in the general government deficit (including the costs of pension reform) to 2.9% of GDP in 2007 and a further reduction to 2.3% of GDP in 2008. Government ministries are required to make deep cuts in operating costs by the end of 2007 to make room for increased social expenditures within these budget envelopes. The government's budget estimates are based on conservative growth assumptions. In view of substantial upward pressure on the exchange rate since the second half of last year, it was agreed in mid-March 2007 to revalue the central rate for the Slovak koruna against the euro by 8.5% to SKK 35.4424 under the Exchange Rate Mechanism. In addition, the central bank cut the policy interest rate by 25 basis points at the end of March and by a further 25 basis points at the end of April to 4.25%.

### Net exports will boost growth and slash the current account deficit

Economic growth is projected to rise to around 8¼ per cent in 2007 supported by production at the new car plants and carryover effects, but to ease to 7½ per cent in 2008. Unemployment should continue to decline but more slowly than in recent years as short-term unemployment falls to low levels and the growth in cross-border employment eases. Headline

inflation should fall to 2% in 2008 supported by weaker energy prices and exchange rate appreciation. The general government deficit is projected to fall to 2.7% of GDP in 2007 and 2.1% in 2008. With the start of production in the new manufacturing plants, the current account deficit should fall sharply, from 8.3% of GDP in 2006 to 2½ per cent in 2008.

***Uncertainty about energy prices and economic slack are the main risks***

The main risks to these projections are that energy prices (they have a relatively large, albeit declining impact on production costs and inflation) turn out higher than in the central projection and that there is less economic slack than estimated (such estimates are particularly uncertain owing to the current expansion in manufacturing capacity), resulting in higher inflation and lower growth.

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Twice a year, the *OECD Economic Outlook* analyses the major trends and examines the economic policies required to foster high and sustainable growth in member countries. Developments in major non-OECD economies are also evaluated. The present issue covers the outlook to end-2008. Together with a wide range of cross-country statistics, the *Outlook* provides a unique tool to keep abreast of world economic developments.

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### Conventional signs

\$	US dollar	.	Decimal point
¥	Japanese yen	I, II	Calendar half-years
£	Pound sterling	Q1, Q4	Calendar quarters
€	Euro	Billion	Thousand million
mb/d	Million barrels per day	Trillion	Thousand billion
..	Data not available	s.a.a.r.	Seasonally adjusted at annual rates
0	Nil or negligible	n.s.a.	Not seasonally adjusted
–	Irrelevant		

## Summary of projections

	2006	2007	2008	2007			2008				Fourth quarter		
				Q2	Q3	Q4	Q1	Q2	Q3	Q4	2006	2007	2008
	Per cent												
<b>Real GDP growth</b>													
United States	3.3	2.1	2.5	2.5	2.3	2.5	2.5	2.6	2.7	2.7	3.1	2.1	2.6
Japan	2.2	2.4	2.1	1.8	1.9	2.0	2.1	2.2	2.1	2.2	2.5	2.0	2.2
Euro area	2.8	2.7	2.3	2.6	2.5	2.4	2.3	2.2	2.1	2.1	3.3	2.5	2.2
Total OECD	3.2	2.7	2.7	2.7	2.6	2.7	2.7	2.7	2.7	2.7	3.2	2.6	2.7
<b>Inflation</b>													
United States	2.9	2.6	2.2	2.3	2.0	2.2	2.4	2.2	2.1	2.1	2.5	2.6	2.2
Japan	-0.9	-0.4	0.2	-0.4	0.0	0.1	0.2	0.3	0.4	0.6	-0.5	-0.3	0.4
Euro area	1.7	2.0	2.0	1.0	2.0	2.0	2.0	2.1	2.2	2.2	1.6	2.0	2.1
Total OECD	2.2	2.1	2.0	1.9	2.0	2.0	2.0	2.0	2.0	2.0	1.8	2.3	2.0
<b>Unemployment rate</b>													
United States	4.6	4.6	4.8	4.5	4.6	4.7	4.8	4.8	4.8	4.9	4.5	4.7	4.9
Japan	4.1	3.8	3.6	3.8	3.7	3.7	3.6	3.6	3.6	3.6	4.1	3.7	3.6
Euro area	7.8	7.1	6.7	7.1	7.0	6.9	6.9	6.8	6.7	6.6	7.5	6.9	6.6
Total OECD	5.9	5.6	5.5	5.6	5.6	5.6	5.5	5.5	5.5	5.4	5.7	5.6	5.4
<b>World trade growth</b>	9.6	7.5	8.3	7.7	8.2	8.4	8.3	8.3	8.2	8.2	8.6	7.7	8.3
<b>Current account balance</b>													
United States	-6.5	-6.1	-6.2										
Japan	3.9	4.8	5.4										
Euro area	0.1	0.4	0.4										
Total OECD	-1.9	-1.5	-1.5										
<b>Cyclically-adjusted fiscal balance</b>													
United States	-2.5	-2.8	-2.8										
Japan	-2.2	-2.7	-3.2										
Euro area	-1.0	-0.8	-0.7										
Total OECD	-1.7	-1.8	-1.9										
<b>Short-term interest rate</b>													
United States	5.2	5.3	5.0	5.3	5.3	5.2	5.1	5.1	5.0	4.9	5.3	5.2	4.9
Japan	0.2	0.5	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.7	0.4	0.6	0.7
Euro area	3.1	4.1	4.3	4.0	4.2	4.3	4.3	4.3	4.3	4.3	3.6	4.3	4.3

*Note:* Real GDP growth, inflation (measured by the increase in the GDP deflator) and world trade growth (the arithmetic average of world merchandise import and export volumes) are seasonally and working-day-adjusted annual rates. The "fourth quarter" columns are expressed in year-on-year growth rates where appropriate and in levels otherwise. The unemployment rate is in per cent of the labour force while the current account balance is in per cent of GDP. The cyclically-adjusted fiscal balance is in per cent of potential GDP. Interest rates are for the United States: 3-month eurodollar deposit; Japan: 3-month certificate of deposits; euro area: 3-month interbank rate.

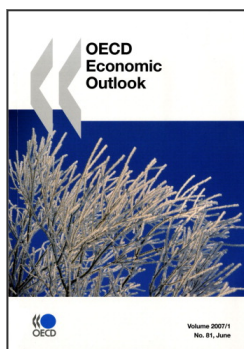
Assumptions underlying the projections include:

- no change in actual and announced fiscal policies;

- unchanged exchange rates as from 9 May 2007; in particular 1\$ = 119.72 yen and 0.74 euros;

The cut-off date for other information used in the compilation of the projections is 15 May 2007.

*Source:* OECD Economic Outlook 81 database.



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