

Atradius Country Report

Slovakia – December 2008



Overview

General information

Capital:	Bratislava
Government type:	Republic
Currency:	Slovak koruna (SKK)
Population:	5.5 million
Status:	Upper middle income country (GDP/capita: US-\$ 16,668)

Most important sectors (% of GDP, 2007)

Services:	64 %
Industry:	33 %
Agriculture:	3 %

Main import sources (2007)

Germany:	22 %
Czech Republic:	17 %
Russia:	9 %
Hungary:	7 %
Austria:	5 %

Main export markets (2007)

Germany:	21 %
Czech Republic:	13 %
France:	7 %
Italy:	6 %
Poland:	6 %

Main expenses of foreign exchange

Machinery & transports (43 %), fuels (12 %)

Main sources of foreign exchange

Machinery & transports, especially cars: (53 %)

Key indicators

	2005	2006	2007	2008*	2009*
GDP (US-\$ million)	47,885	55,884	74,956	91,674	98,468
Real GDP growth (%)	6.5	8.6	10.4	4.5	4.2
GDP per capita (US-\$)	8,884	10,368	13,907	16,668	17,903
Inflation p.a. (%)	2.7	4.4	2.8	4.2	3.8
Fiscal balance (% of GDP)	-3.0	-3.1	-2.2	-2.2	-2.5
Total foreign debt (US-\$ million)	23,946	27,085	36,632	45,149	44,567
Foreign debt/GDP (%)	50	48	49	49	45
Foreign debt/XGS (%)	63	55	55	50	47
Short-term debt/inter. reserves (%)	98	125	118	148	135
Debt service ratio (%)	16	8	8	9	10
Current account balance (US-\$ m.)	-4,004	-3,937	-4,103	-5,360	-3,940
Current account/GDP (%)	-8.4	-7.0	-5.5	-5.8	-4.0
Nom. exchange rate to US-\$ (average)	31.02	29.70	24.69	22.10	22.20
International reserves (US-\$ million)	15,640	12,427	17,529	17,737	19,621
In months of merchandise imports	5.1	3.2	3.4	2.9	2.7

* forecast

Source: Economist Intelligence Unit (EIU)

Political situation: Stable

Head of state: President Ivan Gasparovic (since June 2004)
Head of government: Prime Minister Robert Fico (since July 2006)
Form of government: Three-party government led by the left-wing SMER, in coalition with the nationalist/populist LS-HZDS and the far-right SNS

Internal situation

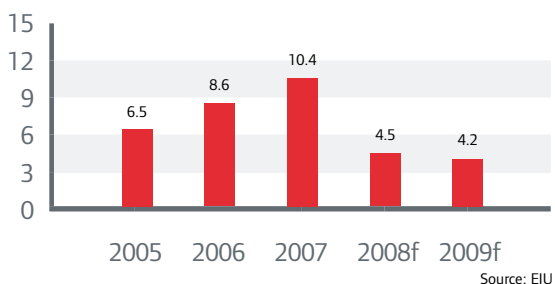
After eight years of successful governance, which strongly enhanced Slovakia's political and economic transition, the centre coalition of former Prime Minister Mikulas Dzurinda lost the early elections in June 2006. SMER, LS-HZDS and SNS formed a new administration. To date, local elections and polls have confirmed the current government's and Prime Minister Fico's solid mandate. Despite its heterogeneity, the coalition has turned out to be more stable than expected.

International relations

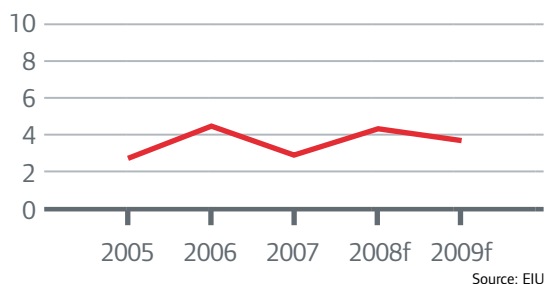
Relations with Hungary cooled down significantly after the SNS entered the coalition government, as party leader Jan Slota voiced some intemperate remarks about the Hungarian minority and Hungary itself in the past.

Internal economic situation: Slowing growth

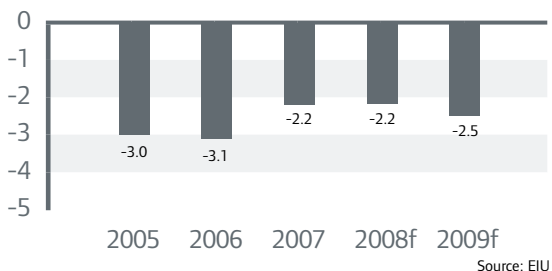
Real GDP growth (%)



Inflation p.a. (%)



Fiscal balance (% of GDP)



General situation

Slovakia is one of the success stories of Eastern Europe's economic transition. The country's once rigid economy controlled by massive state intervention has now been transformed into a dynamic and open economy with high (foreign) investment and export-oriented GDP-growth. Slovakia has become the world's top supplier of cars per capita (VW, Kia, Peugeot, and Citroën) due to its favourable business climate (low wage costs, tax breaks, skilled workforce). Those factors have also attracted foreign direct investment (FDI) in electronics, IT and engineering.

GDP-growth exceeded 10% in 2007, all sectors contributing to the economic upswing, with the booming exports of cars and electronics at the forefront. But this came at the cost of some frictions: labour shortages and risen inflation (4.5% mid-2008). As global demand for cars has sharply dropped, real GDP-growth has substantially decreased since October 2008 and will drop further during 2009. After a still remarkable 7.5% in 2008, GDP-growth for next year is forecast to decrease to 4.2%.

Slovakia's banking sector is mainly privately (foreign) owned. Because of a strong domestic deposit base, banks are less reliant on foreign funding than other Eastern European economies.

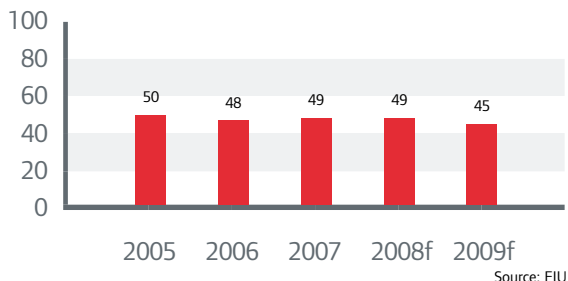
Economic policy

Slovakia will enter the eurozone on January 1st 2009. With this step the currency risk will disappear as monetary policy is to be fixed by the European Central Bank (ECB). The entry is thanks to years of fiscal discipline, leading to a public debt of only 35%. But the budget deficits in 2008 and 2009 are only slightly below the threshold of 3% of GDP which permits euro adoption. The monetary policy is based on an inflation-targeting framework but the central bank has lowered the key repo rate to 3.25%, in harmonization with the ECB-rate.

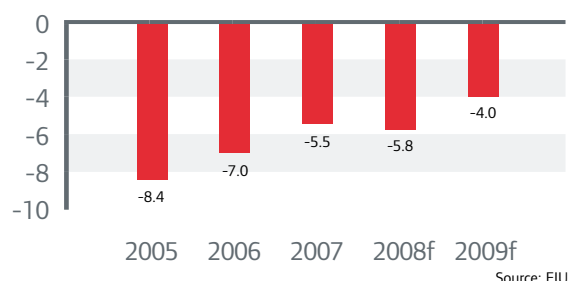
The current government has reversed some of the economic reforms of the former, more market-friendly administration (labour market, health care, pensions) but the bulk of the reforms have remained in place. The Fico administration has backed down from overhauling the flat direct (income and corporate) tax system. However, it has stopped the privatisation of state property deemed to be strategic (residual stakes in gas/oil/electricity, airport, and railways).

External economic situation: Good – but large share of short-term debt

Foreign debt/GDP (%)



Current account/GDP (%)



Foreign debt

Level: Foreign debt has increased to more than US-\$ 45 billion by the end of 2008. This is high as a percentage of GDP (49%), but low as a percentage of exports of goods and services (50%).

The share of private sector debt is about 60%.

Structure: Unfavourable in view of the very high short-term share (58%)

Debt service ratio: Low (below 10%), but much higher when including short-term (above 30%)

Remarks:

Part of the large capital inflow is foreign debt-creating and has contributed to the significant rise of Slovakia's external obligations: from US-\$18 billion end of 2003 to about US-\$ 45 billion in 2008. Overall the liquidity position is stable, but the short-term debt/reserves ratio is high, due to large private sector short-term debt.

Balance of payments

Trade balance: High deficits, although declining

Current account: Lower deficits: from 8.4% of GDP in 2005 to 5.8% in 2008

Capital account: Positive

Total Account: Positive

Remarks:

Since 2002 exports have soared thanks to record sales of cars, metals, machinery and furniture, but FDI-related imports have increased even faster, causing large current account deficits. Positive net exports since 2007 have strongly curbed these shortfalls but, with global demand falling, the prospects have become less certain.

In November 2005 Slovakia entered ERM-2; in March 2007 the central rate of the koruna was revalued by 8.5% against the euro. Since then the currency has traded above ERM 2 parity, but within the +/- 15% limits.

International reserves - in months of imports (cif)

Moderate due to high imports (less than three months of import cover).

Outlook: Depending on export performance

Political situation

SMER continues to have a strong lead in the opinion polls, enhancing the coalition's stability until the next general elections scheduled for 2010.

Internal economic situation

As Slovakia's economy is very dependent on the global automobile cycle, GDP-growth will decrease sharply in 2009. There are serious downside risks if global demand for cars, machinery and electronics fall even deeper. Slovakia's EMU-membership will hold back government's inclination to step up welfare spending and state intervention.

External economic situation

The eurozone membership will shield Slovakia to some degree from the global financial turmoil, but at the price of lost monetary/currency autonomy and a much stricter fiscal discipline. The current account deficit is projected to diminish over the next two years but, as automotive exports are expected to drop sharply in 2009, negative net-exports pose a downside risk.

In general, Slovakia's liquidity position is stable. Due to the large private sector short-term debt the country is faced with a potential roll-over risk of corporate and banking sector debt. However, as many corporates (especially in the car industry) and banks in Slovakia are foreign-owned, the major part of those short-term debts consists of liabilities of Slovak subsidiaries to their foreign parent companies.

The koruna has entered EMU at a strong rate of exchange. Together with rising wage costs (due to labour shortage) this could hurt the export performance in the medium-term.

Useful Webpages

Atradius:	www.atradius.com
General country information:	www.odci.gov/cia/publications/factbook/index.html
Ministry of Economy:	www.economy.gov.sk
National Bank of Slovakia:	www.nbs.sk
Statistical Office of the Slovak Republic:	www.statistcs.sk
Slovak Chamber of Commerce and Industry:	www.scci.sk

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