SLOVAKIA | MACRO OUTLOOK

Solid domestic demand boosting the economy

Household consumption-driven economic growth
ECB: next interest rate cut in October
Consolidation remains in focus
Weaker dollar expected

Economy (%)	2024e	2025e	2026e
GDP (real, y/y)	2.2	2.5	n.a.
Unempl. Rate	5.5	5.4	n.a.
CPI (y/y)	2.8	3.3	n.a.
Retail Sales (y/y)	3.0	2.0	n.a.
Ind. Prod. (y/y)	4.0	5.0	n.a.
Public Debt/GDP	58.2	59.7	n.a.

Source: Erste Group Research

Market	Spot	24Q4	25Q1	25Q2
ECB Target R.	3.65	3.15	2.90	2.65
3M Euribor	3.47	3.09	2.86	2.64
EUR/USD	1.11	1.13	1.14	1.14
10Y Bond (%)*	3.28	3.45	3.40	3.40

Source: FactSet, Erste Group Research

Rating	Current	Outlook
Moodys	A2	neg
S&P	A+	stable
Fitch	A-	stable

Source: Erste Group Research

General	2024
Population mn	5.5
GDP/Capita EUR	23,982

Source: Erste Group Research

Spot Rates as of:
13th Sep. 2024

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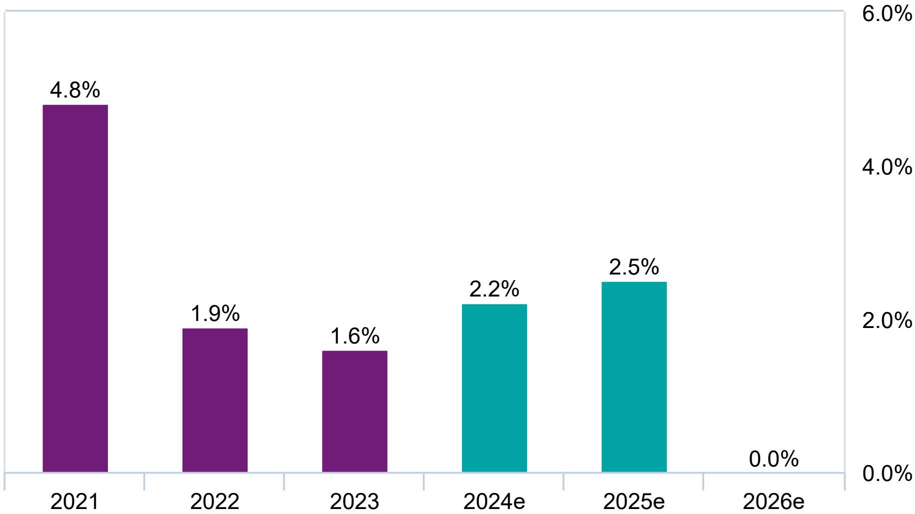
Note:
**Information on past performance is not a reliable indicator for future performance. Forecasts are not a reliable indicator for future performance.*

Economic activity showed a strong performance in the first half of the year. After robust growth in 1Q, the second quarter posted y/y GDP growth of 1.9%. This was mainly driven by domestic demand, particularly household consumption, as household budgets recovered from a prolonged period of elevated inflation. For the rest of the year, household spending is expected to further support growth, alongside investments spurred by NextGen funds. A rebound in foreign economies, anticipated in 2025, could boost activity, especially in Slovakia's industrial sector. GDP growth is projected to reach 2.2% this year.

The disinflation period in Slovakia has ended, as the y/y inflation rate started rising again, due to the fading base effect. Core inflationary pressures persist in the economy, largely driven by a strong labor market. Inflation is expected to average around 3% this year. Slovakia anticipates the long-discussed consolidation plan from 2025, with the Ministry of Finance facing the challenge of addressing both the current deficit and new expenditure measures proposed by coalition parties. Consequently, the total consolidation could amount to EUR 2.6bn. Additionally, potential rule of law violations could jeopardize EU funds.

GDP (real,y/y)



Source: Erste Group Research

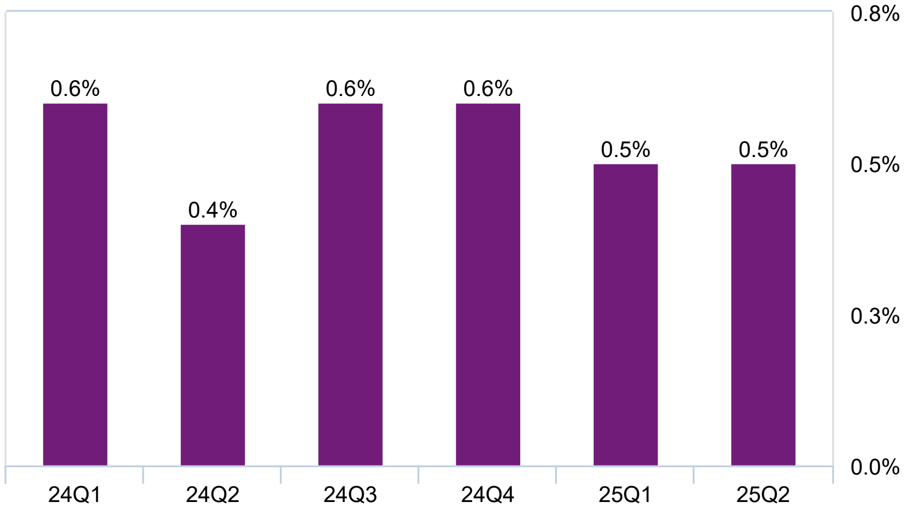
GDP

Household consumption-driven economic growth

This year began with relatively strong economic momentum, continuing on a growth trajectory in the second quarter. A rebound in household consumption, supported by a strong labor market and wage growth, could be the most important factor driving economic growth this year. Government consumption also surprised, increasing at a strong rate. However, investment activity grew at its weakest level since 2Q22, indicating that the impact of the previous EU funds programming period has been fading. A visible rebound in foreign trade will come with rising activity in the big foreign economies.

The labor market in Slovakia remains resilient. The unemployment rate dropped to 5.2%, one of the best figures in the country's history. Although the pace of wage growth slowed and fell below expectations, the rate (above 7% y/y) remains relatively high, supporting strong real wage growth. Households feel more secure, which has improved their confidence. For 2024, we forecast GDP growth to reach 2.2%, with a slight acceleration expected in 2025.

GDP (real, s.a., q/q)



Source: Erste Group Research

Annual	2022	2023	2024e	2025e	2026e
GDP real	1.9%	1.6%	2.2%	2.5%	n.a.
CPI (y/y)	12.8%	10.5%	2.8%	3.3%	n.a.
Private Consumption	6.3%	-3.1%	3.0%	2.0%	n.a.

Source: Erste Group Research

Inflation

Inflation driven by goods and services

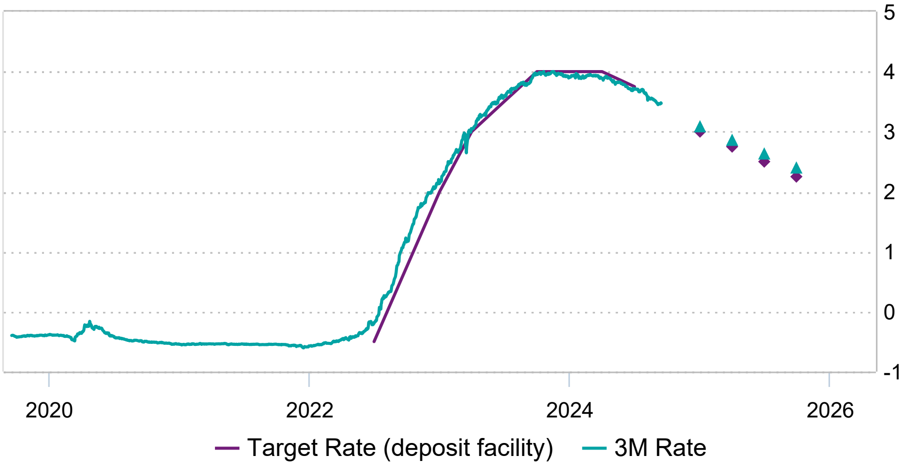
Inflation has slowed significantly since the beginning of the year, mainly due to strong government regulation, which has kept energy prices for households at the same levels as in 2023. As the base effect fades, the inflation rate has been rising again, approaching 3% in 3Q24. Core inflationary pressures persist in the economy, driven by factors such as low unemployment and robust nominal wage growth. On the other hand, households are using higher wages to replenish their savings, which has an anti-inflationary effect. On average, price growth could reach 2.8% y/y in 2024.

ECB Monetary Policy

ECB: next interest rate cut in October

As expected, the ECB Governing Council decided to cut the deposit rate by 25 basis points to 3.50% at its meeting in September. The forecast for core inflation was raised slightly, while ECB economists continue to expect the core rate to fall rapidly from 2025. Leading data (including wage growth) give the ECB confidence that services inflation will lose momentum in 2025. We expect economic data to confirm disinflation and thus allow the ECB to make the next rate cut in October, which should be followed by a further rate cut of 25 basis points in December.

Eurozone Short Term Yields



Source: FactSet, Erste Group Research

Market (%)	Spot	24Q4	25Q1	25Q2	25Q3
Target Rate	3.65	3.15	2.90	2.65	2.40
3M Rate	3.47	3.09	2.86	2.64	2.40

Source: FactSet, Erste Group Research

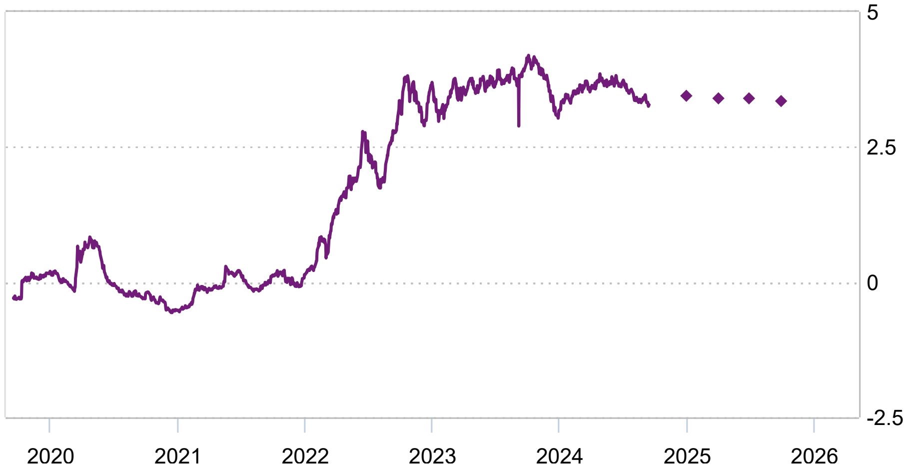
Bond Yields

Consolidation remains in focus

The status quo remained unchanged after evaluations by major rating agencies in the first half of the year. The agencies have given themselves and Slovakia time until the fall. The need for the consolidation of public finances remains a prominent issue. Slovakia's rating is supported by its EU and Eurozone membership, which underpins a relatively stable and credible macroeconomic framework. There is still a possibility that EU funds will be temporarily suspended by the European Commission.

The Debt and Liquidity Agency (ARDAL) has already covered more than 80% of expected financing needs. The continued easing of the ECB's monetary policy should reduce pressure on the risk premium of government bonds compared to German bonds. However, the threat of suspended access to EU funds, which could result in lower economic growth and a likely deterioration in ratings, may lead to a further widening of spreads. We expect yields to remain elevated, around 110bp.

10Y Generic Govt. Bond Yield (%)



Source: Refinitiv, Erste Group Research

Market	Spot	24Q4	25Q1	25Q2	25Q3
10Y Bond*	3.28	3.45	3.40	3.40	3.35

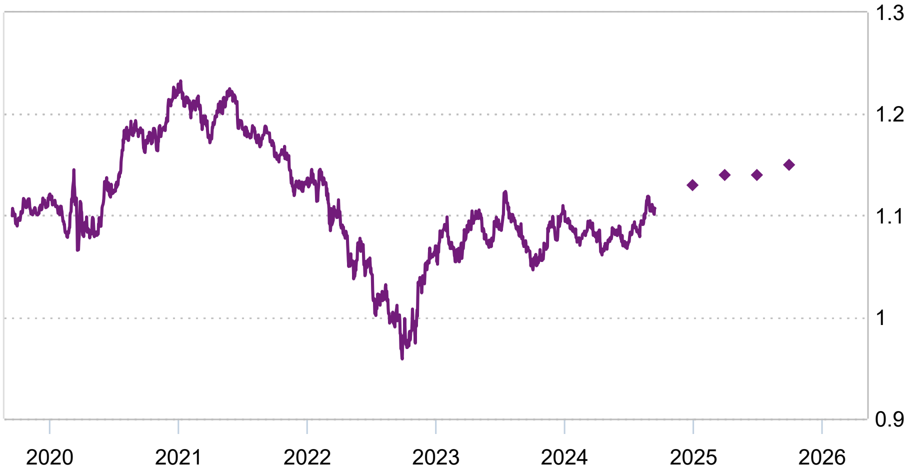
Source: Refinitiv, Erste Group Research

Euro

Weaker dollar expected

Weak US labor market data for July raised expectations of interest rate cuts in the US and triggered a weakening of the dollar. In addition, recent statements by the Fed Chairman contained clear indications of an interest rate cut in the US in September. From the market's perspective, this heralds the start of a series of US interest rate cuts. The speed will depend on the incoming data. The labor market offers risks for a faster approach by the central bank than the three interest rate cuts of 75 basis points in total that we currently expect by the end of the year. The ECB will also cut interest rates further. However, the momentum in the USA will be the main focus for the markets. We expect a further slow weakening of the dollar.

EUR/USD



Source: FactSet, Erste Group Research

	Spot	24Q4	25Q1	25Q2	25Q3
EUR/USD	1.11	1.13	1.14	1.14	1.15
vs. Spot		*1.8%*	*2.7%*	*2.7%*	*3.6%*

Source: FactSet, Erste Group Research

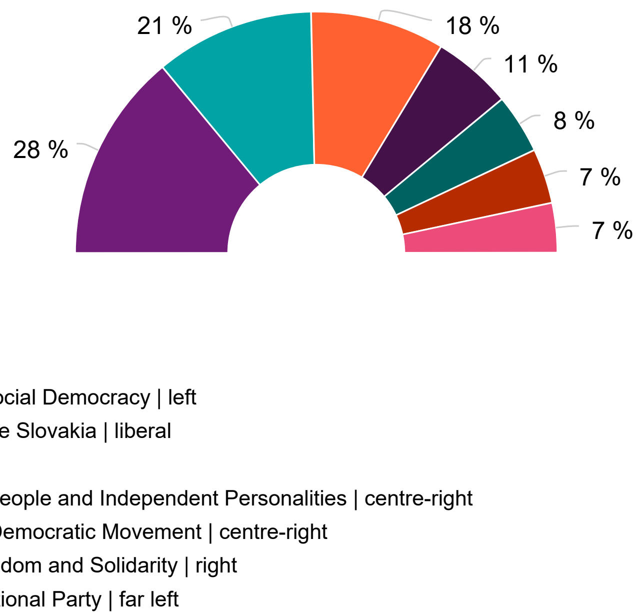
Politics

Slovakia scrutinized by EC

The ruling coalition, led by Robert Fico, continues to implement changes in the functioning of the state and its institutions, many of which affect the police, the justice system, or cultural organizations. Unsurprisingly, changes of such a magnitude have come under the scrutiny of the European Commission (EC). It is known that the government has previously held discussions with the EC, but according to press reports, there is a possibility that EU funds for Slovakia could be frozen, due to violations of the rule of law.

Meanwhile, coalition parties are working on the budget proposal for the coming year. Although the Ministry of Finance has already announced a necessary consolidation of around EUR 1.5bn, Prime Minister Fico stated that, due to new expenditures proposed for the next year, the consolidation could reach up to EUR 2.6bn. Specific measures have not yet been introduced, but potential actions being discussed include a higher VAT (excluding basic food products) or a tax on financial transactions for legal entities.

Parliament Seats



Source: Erste Group Research

Last Election:
2023, September

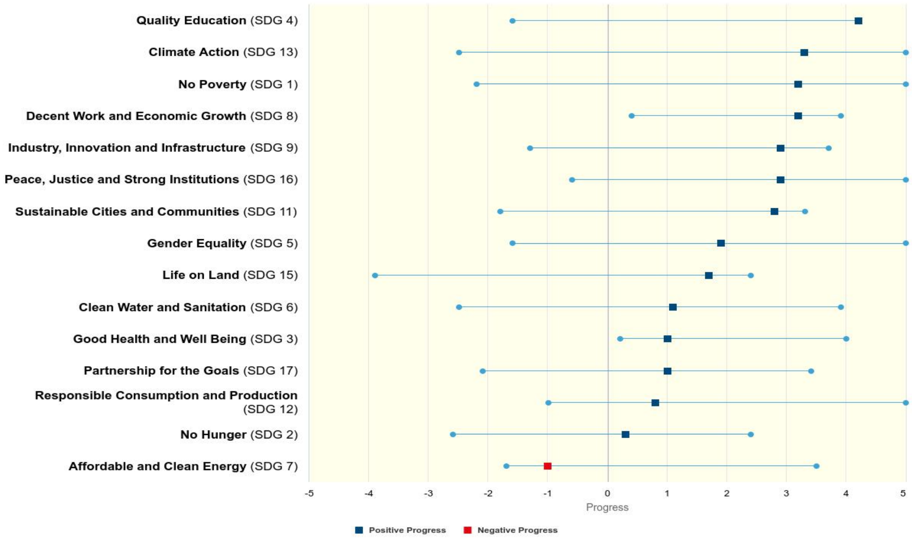
Next Election:
2027, September

Sustainable Development Goals

Slovakia on its way to sustainable development

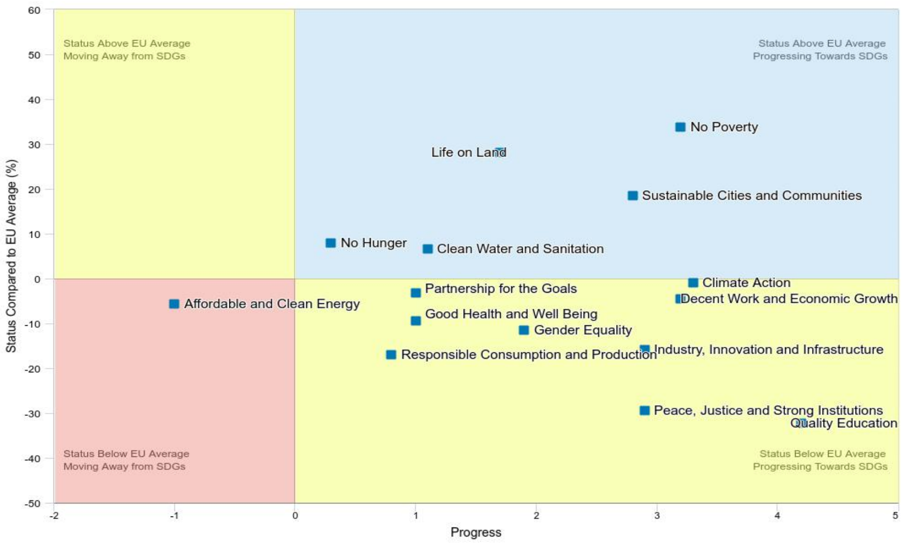
Compared to the EU, Slovakia ranks among the less successful countries in terms of meeting the sustainable development goals (SDGs). For two thirds of the goals, Slovakia's performance is below the EU average however, the good news is that progress has been made on almost all SDGs. The only exception is the goal of Affordable and Clean Energy. In the upcoming years, the most significant challenges will be the targets associated with the aforementioned Available and Clean Energy as well as areas such as Quality of Education, or Peace, Justice and Strong Institutions.

Progress Overview



Source: Erste Group Research

Progress Overview



Source: Erste Group Research

Forecasts

Annual	2018	2019	2020	2021	2022	2023	2024e	2025e	2026e
Real GDP growth	4.0	2.5	-3.3	4.8	1.9	1.6	2.2	2.5	n.a.
Inflation (CPI, avg)	2.5	2.7	1.9	3.2	12.8	10.5	2.8	3.3	n.a.
Unemployment rate (avg)	6.5	5.8	6.7	6.8	6.1	5.8	5.5	5.4	n.a.
Retail sales growth	3.6	-1.4	-1.1	1.4	4.3	-4.5	3.0	2.0	n.a.
Industrial output growth	4.3	0.5	-9.1	10.4	-4.7	-0.5	4.0	5.0	n.a.
Private consumption growth	4.2	2.6	-1.1	2.6	6.3	-3.1	3.0	2.0	n.a.
Fixed capital formation growth	2.8	6.7	-10.9	3.5	5.2	10.5	1.0	5.6	n.a.
Percent of GDP									
Trade balance	0.8	0.1	2.1	0.2	-5.2	1.8	1.8	1.6	n.a.
Current account balance	-2.2	-3.3	0.6	-4.0	-7.3	-1.6	-0.6	-0.2	n.a.
Foreign direct investment	1.6	2.4	-2.3	1.5	2.5	3.3	2.7	1.8	n.a.
Budget balance	-1.0	-1.2	-5.3	-5.2	-1.7	-4.9	-6.0	-5.0	n.a.
Public debt	49.4	48.0	58.8	61.1	57.7	56.0	58.2	59.7	n.a.
External debt, gross	114.5	112.3	118.7	132.7	103.0	96.0	83.4	n.a.	n.a.
(percent)									
10Y Yield (average)*	0.86	0.28	0.00	-0.15	2.05	3.62	3.65	3.80	n.a.

Source: Erste Group Research

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