SLOVAKIA : MACRO OUTLOOK

# Consolidation shaping Slovakia‘s economic outlook

Matej Hornak
Economy Slovakia - Analyses and Forecasts | Erste Group Bank AG
December 11, 2024

Spot Rates as of: December 11, 2024
Note: Information on past performance is not a reliable indicator for future performance.
Forecasts are not a reliable indicator for future performance.

# Summary

**A key theme that will influence all macroeconomic indicators in the coming years is fiscal consolidation**. The focus is primarily on generating new revenues, which will significantly affect economic growth and inflation rates in the country. **We project year-on-year GDP growth of 2% in 2025**, driven mainly by household consumption. Due to consolidation efforts, our estimate has been revised downward by 0.5 percentage points.

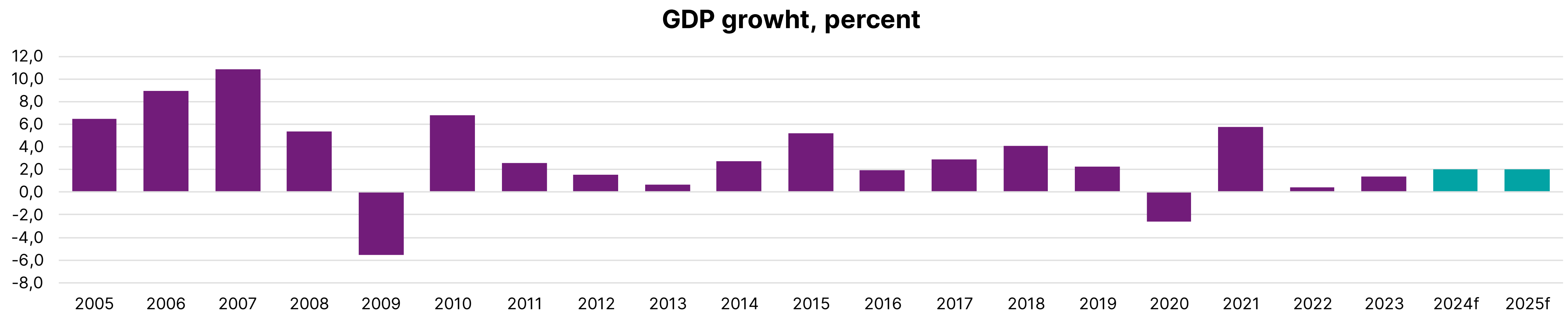
**We forecast an average inflation rate (CPI) of 4.6% in 2025**, approximately 1.5 percentage points higher than the original estimate, primarily due to increased VAT and higher costs for businesses. A potential downside risk is the newly announced energy assistance, but its details and scope remain unclear.

Overall, the consolidation plan comprises 17 measures totaling €2.7 billion. The Ministry of Finance expects the 2025 deficit to reach 4.7%. Rating agencies have assessed the government's efforts as sufficient, though their successful and realistic implementation will be critical. **Increasing concerns about relationships with the EU and institutions are becoming more prominent in rating evaluations.**

# Consolidation to affect economic growth

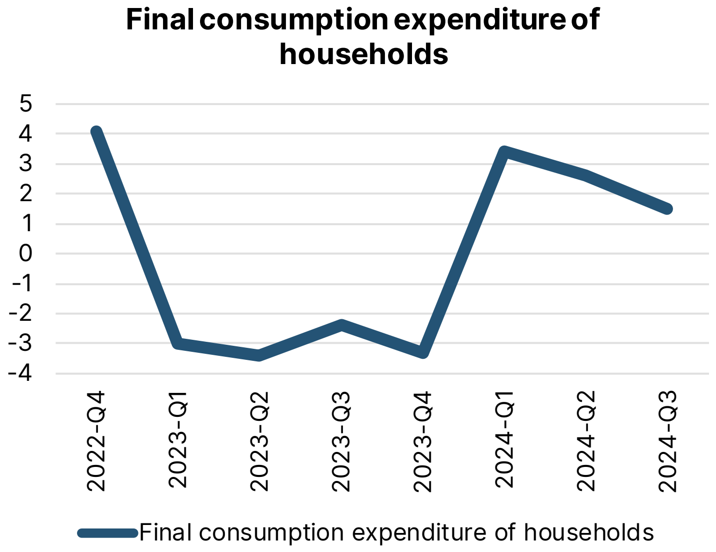
This year began with strong economic momentum, continuing on a growth trajectory in the second and third quarter. Cost-increasing measures for companies, stemming from consolidation efforts announced by the government a few weeks ago, are expected to negatively impact investment activity and GDP growth in the coming years.

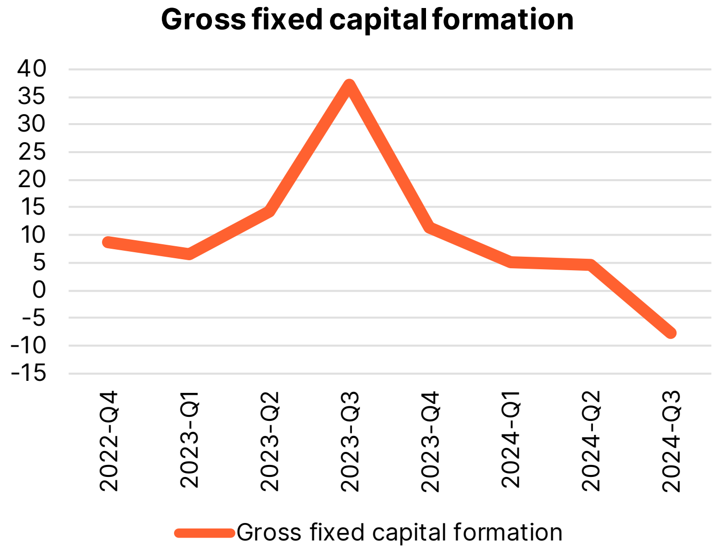
Due to consolidation, GDP growth forecast has been cut by half a percentage point in each of the next two years, as reduced consumption and investment activity may dampen growth over a longer horizon. **For 2025, we forecast GDP growth to reach 2.0%, and in 2026, we expect economic growth to remain at a similar level.** We remain cautious about the threat of increased protectionist measures and trade wars, as Slovakia is a small and open economy

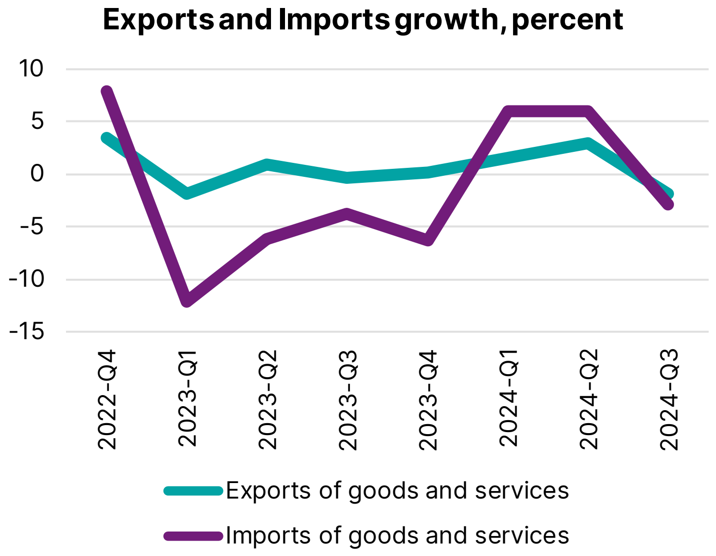



Source: Eurostat, Refinitiv, Erste Group Research

# Households' consumption expected to fuel the economy




A rebound in household consumption, supported by a strong labor market and wage growth, has been the most important factor driving economic growth this year. Investment activity, fueled by NextGen funds, may also provide a positive boost, though its impact will depend on various factors, such as the effectiveness of its implementation. On the other hand, external challenges, caused by a slowdown in foreign demand, could limit Slovakia's economic growth in the coming quarters.

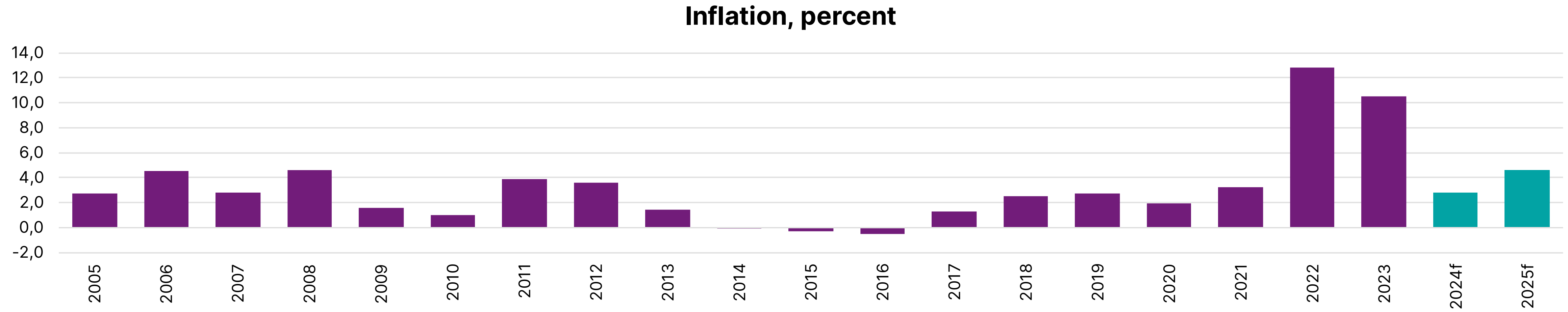


Source: Eurostat, Refinitiv, Erste Group Research
December 11, 2024

# Next year, Slovak inflation could be the highest in EA

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, reaching 3.5% in 4Q24. Core inflationary pressures persist in the economy, driven by factors such as low unemployment and robust nominal wage growth.

Due to the introduced consolidation, the **inflation rate is expected to spike close to 5% on average in 2025**, driven by a higher VAT and various measures that increase business costs. On the other hand, the Slovak government discuss the possibilities to cap the energy prices again, which creates down-side risks for the inflation forecast. **Elevated inflation (above 3%) is also expected to persist in 2026.**



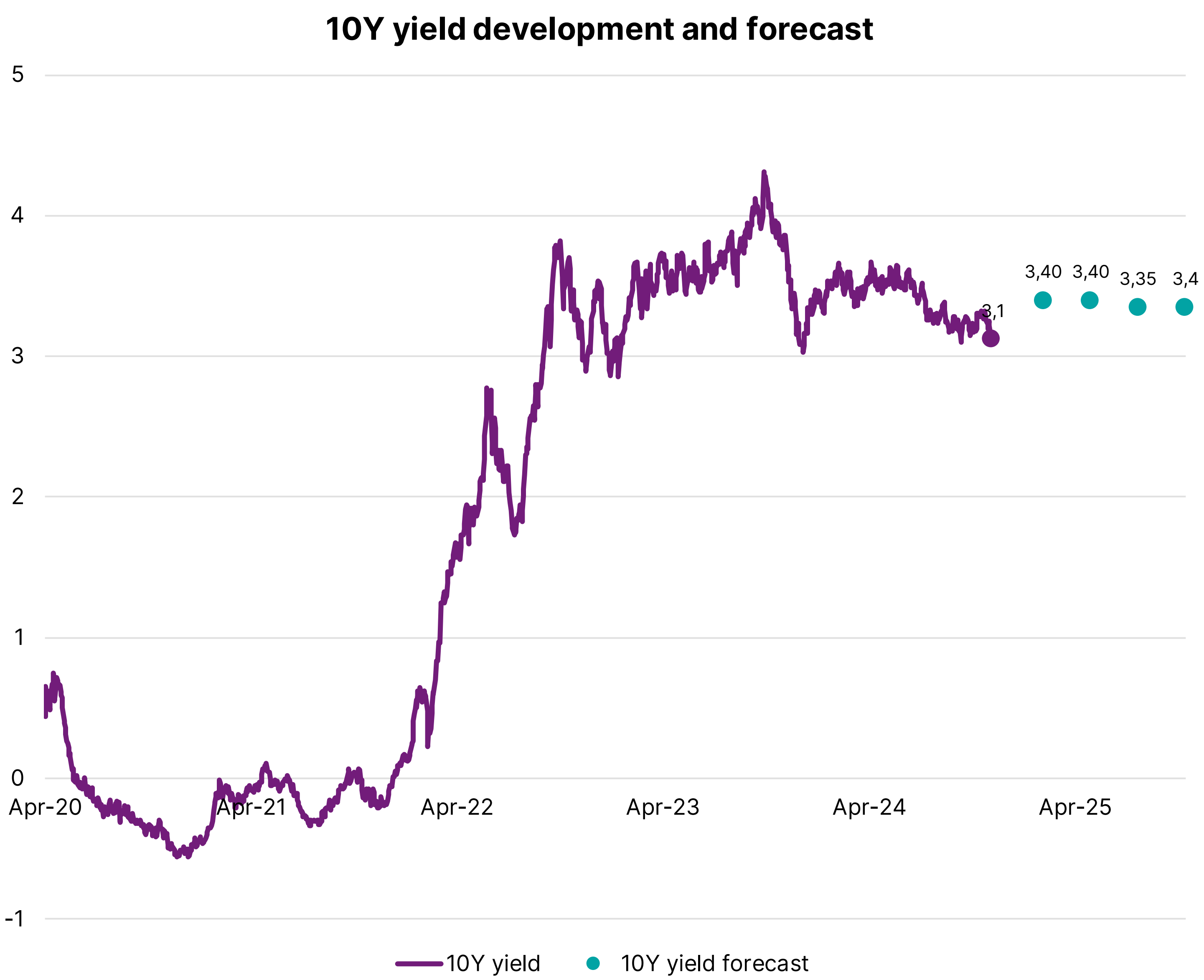

Source: Eurostat, Refinitiv, Erste Group Research

# Risk premia at 110bp

The approved consolidation has been positively assessed by the rating agency S&P, which has kept our rating and outlook unchanged (A+, stable outlook). **The risk premium on our 10-year bonds vs. German bunds is around 100-110 basis points, and we expect it to remain at similar levels next year.**

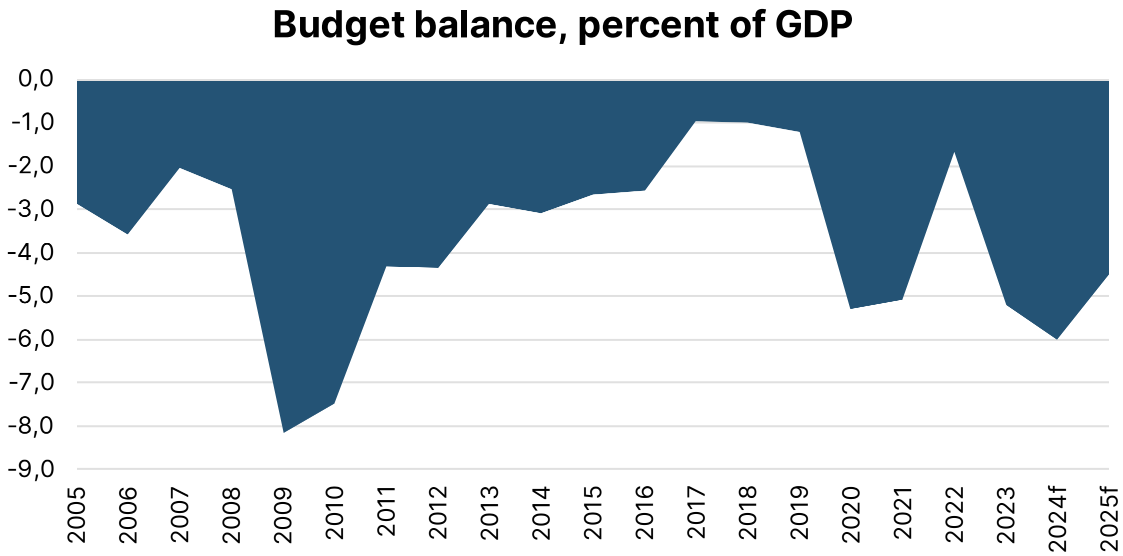
The development of yields on our government bonds will mainly depend on investor confidence in the growth, competitiveness and stability of the Slovak economy, as well as the expected positive trend in ECB interest rates.

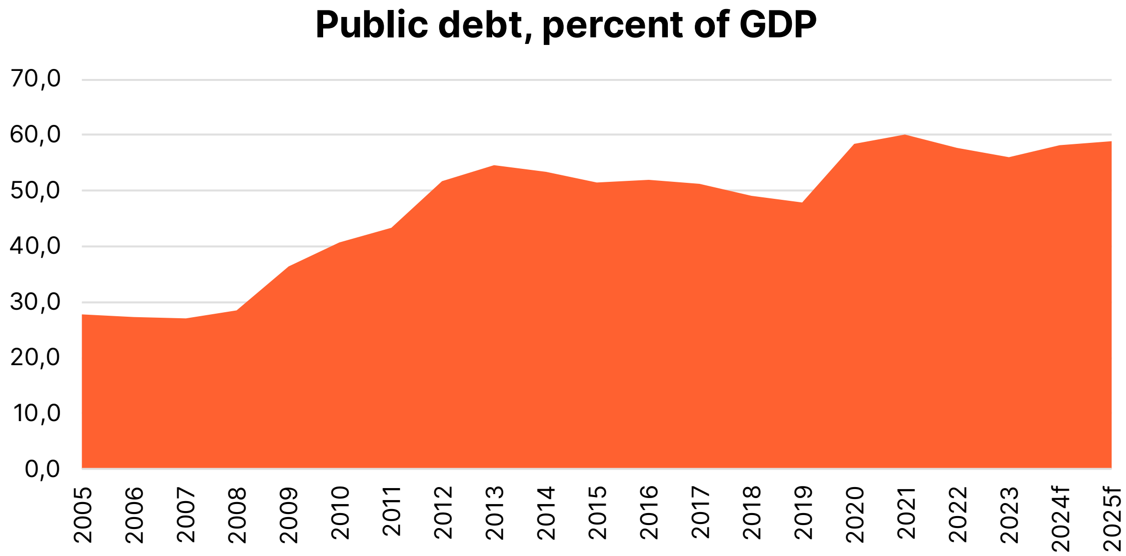
On the other hand, Slovakia's rating could face pressure in the next 12 to 24 months if political or judicial challenges increase. **A strong and transparent relationship with the EU is essential.**




Source: Eurostat, Refinitiv, Erste Group Research

# Deficit could decline by 1pp in 2025, yet stay high



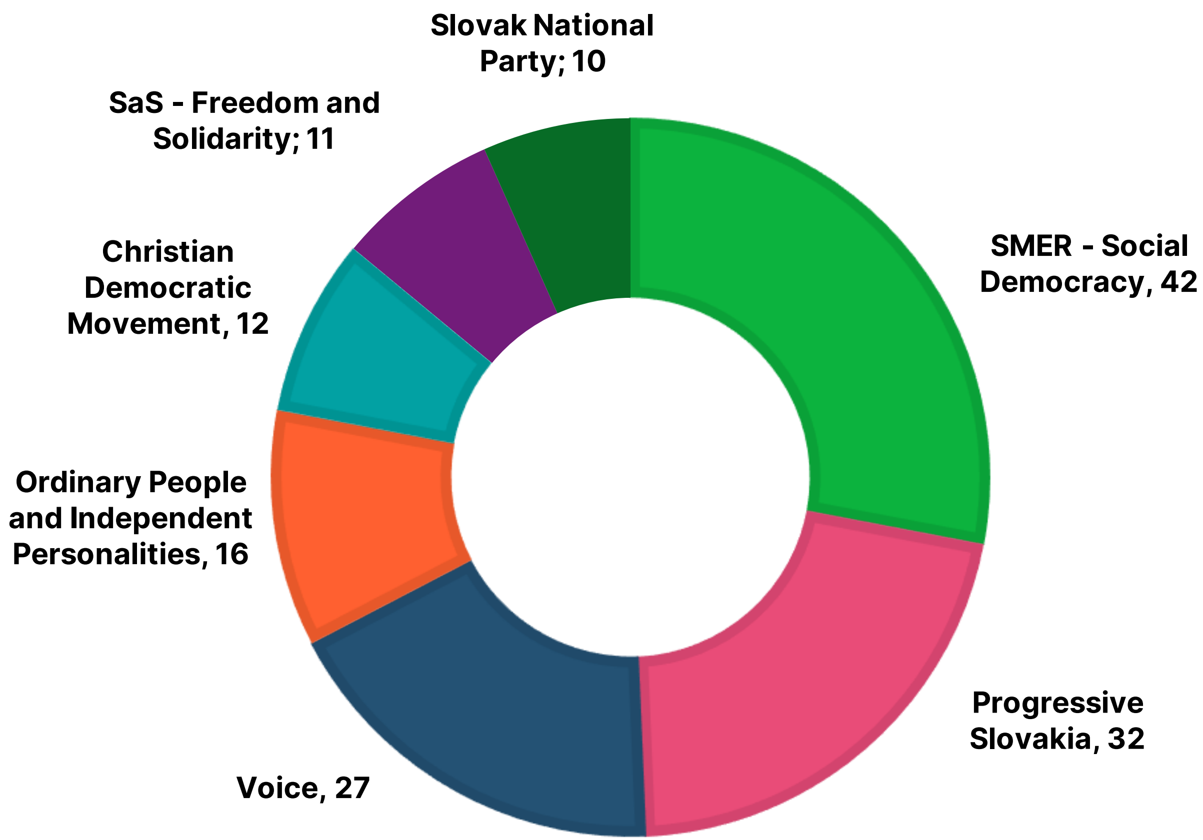

The government has unveiled a long-awaited consolidation plan. According to the Ministry of Finance, the deficit is expected to decline to 4.7% of GDP next year, down from nearly six percent this year. Consolidation efforts are essential, as they have been perceived as a significant negative risk by rating agencies (Fitch downgraded Slovakia's rating by one notch at the end of last year due to the trajectory of budget and debt developments) and the European Commission, which has proposed placing Slovakia under the excessive deficit procedure. **Given the scale of the measures presented, we consider the budget deficit target of 4.7% for 2025 to be a realistic goal.** A more detailed analysis of the consolidation is provided in the Special Topic at the end of the report.

# Political landscape

In recent weeks, the parliamentary majority has also been grappling with internal issues. Several representatives made it to the Parliament through the candidate list of the nationalist Slovak National Party (SNS), with three of them deciding to operate as an independent group outside the SNS structures now.

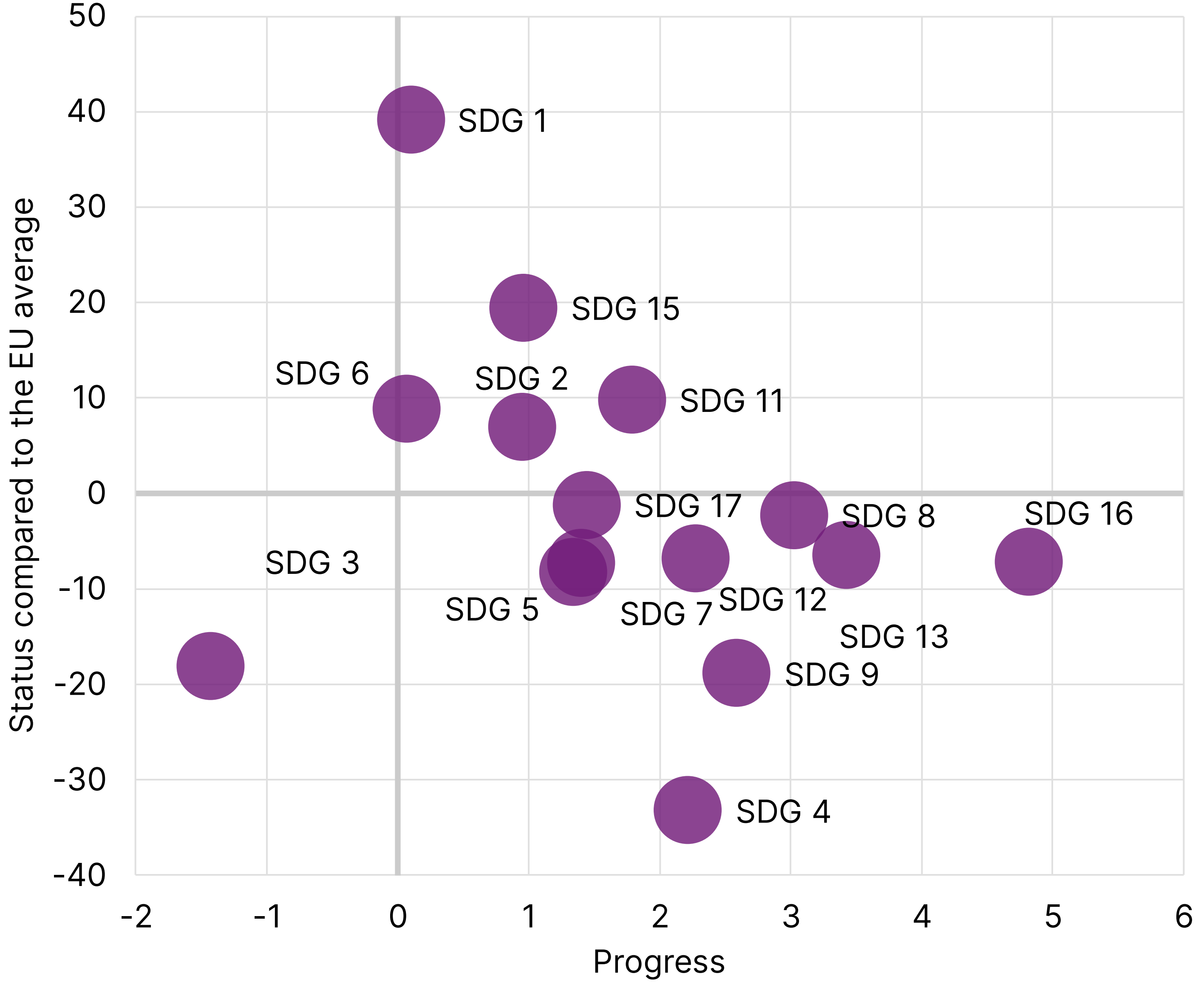
With a parliamentary majority of 79 MPs out of a total of 150, this represents a significant disruption to the coalition's functioning. As a result, during recent votes, the coalition had to rely on the narrowest possible majority of 76 MPs.

## Parliamentary seats




Source: Eurostat, Refinitiv, Erste Group Research

# Social Development Goals




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.

Source: Eurostat, Refinitiv, Erste Group Research

# Consolidation underway in Slovakia

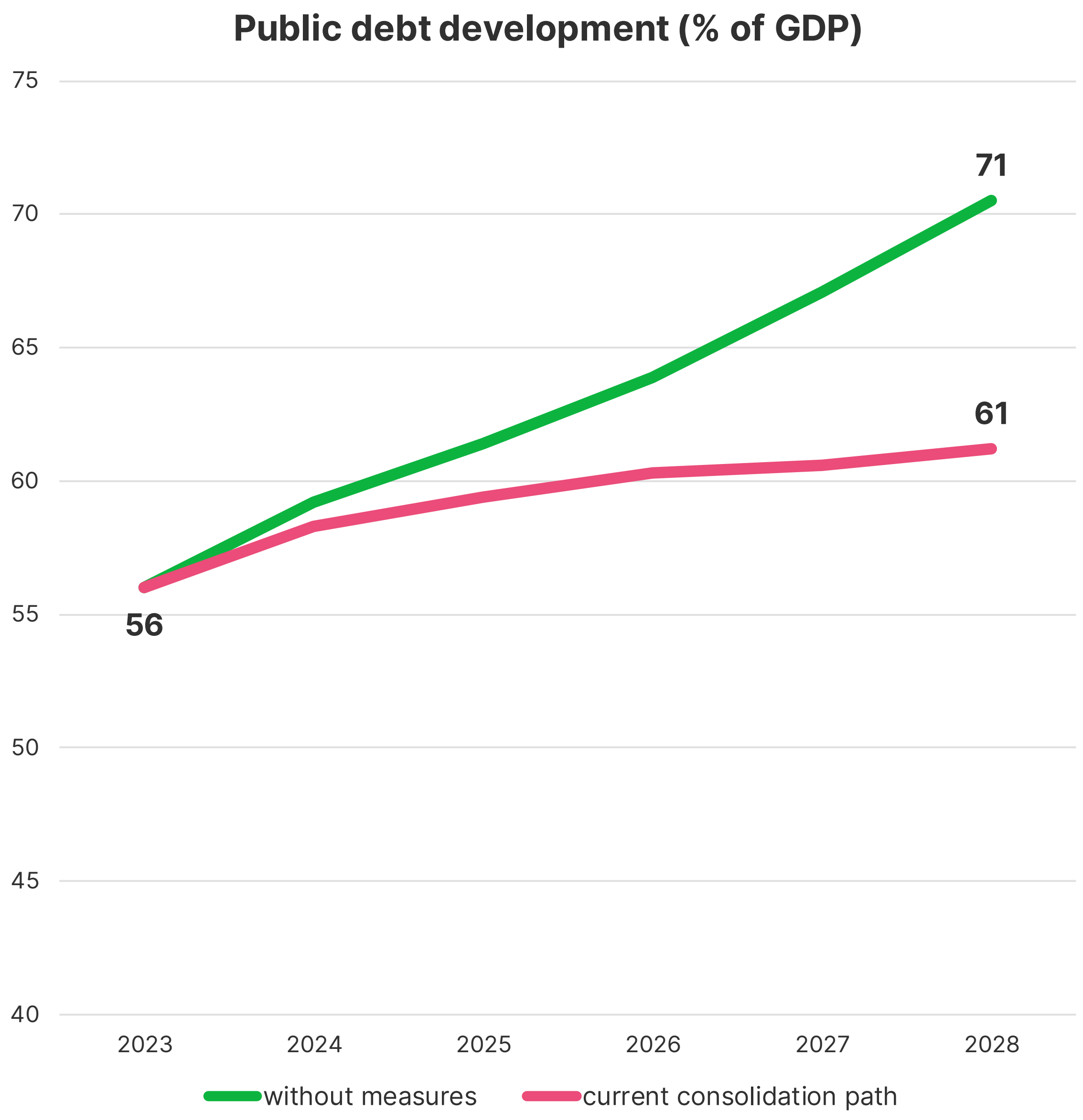
Special topic

# Consolidation package

**The consolidation package consists of 17 measures amounting to EUR 2.7 billion**, aiming to reduce the deficit by approximately 1 percentage point annually and bring it below 3% by 2027.

The most significant measures include a **3-percentage-point increase in VAT** for most goods and services, **a new tax on financial transactions**, and a reform of parental pensions.

In our view, the scope of the proposed consolidation is sufficient. However, the **current plan focuses primarily on the revenue side of the budget, with significantly less emphasis on improving the efficiency of public administration**. We think that the government can achieve its consolidation target for 2025 at 4.7% of GDP, as the measures are theoretically worth 2.7bn and "only" 1.5bn is needed for 2025. The government thus created a buffer in case the introduced measures prove less effective than expected, or for frontloading of the consolidation efforts.




Source: RRZ, Slovenska sporitelna

# Slovakia: Forecasts

| | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024f | 2025f | 2026f |
|---|---|---|---|---|---|---|---|---|---|
| **Percent** | | | | | **Annual average** | | | | |
| Real GDP growth | 4.1 | 2.3 | -2.6 | 5.7 | 0.4 | 1.4 | 2.0 | 2.0 | 1.9 |
| Private consumption growth | 4.1 | 2.9 | 0.7 | 2.9 | 5.2 | -3.1 | 3.0 | 1.0 | FALSE |
| Fixed capital formation growth | 3.4 | 5.0 | -9.6 | 5.1 | -2.0 | 17.0 | -0.5 | 5.3 | FALSE |
| Inflation | 2.5 | 2.7 | 1.9 | 3.2 | 12.8 | 10.5 | 2.8 | 4.6 | 3.3 |
| Unemployment rate | 6.5 | 5.8 | 6.7 | 6.8 | 6.1 | 5.8 | 5.5 | 5.5 | 5.3 |
| **Percent of GDP** | | | | | | | | | |
| Budget balance | -1.0 | -1.2 | -5.3 | -5.1 | -1.7 | -5.2 | -6.0 | -4.5 | -3.8 |
| Public debt | 49.2 | 47.9 | 58.4 | 60.2 | 57.7 | 56.1 | 58.3 | 58.9 | 59.6 |
| Current account balance | -2.2 | -3.3 | 0.6 | -3.9 | -7.3 | -1.6 | -0.6 | -0.2 | 0.3 |
| | | | | | **End of year** | | | | |
| 10Y Yield | 0.96 | 0.19 | -0.46 | 0.10 | 3.64 | 3.19 | 3.45 | 3.35 | FALSE |
| Spread | 115.00 | 110.00 | 110.00 | 110.00 | 110.00 | 100.00 | 100.00 | 100.00 | 100.00 |

Source: Eurostat, Refinitiv, Erste Group Research

# Slovakia: Country overview

Official EU language: Slovak

Capital: Bratislava

Geographical size: 49 035 km2

Population: 5 424 687

GDP per capita (PPS): EUR 27 400, below the EU average

Currency: Euro EUR since January 1 2009

Credit Ratings:

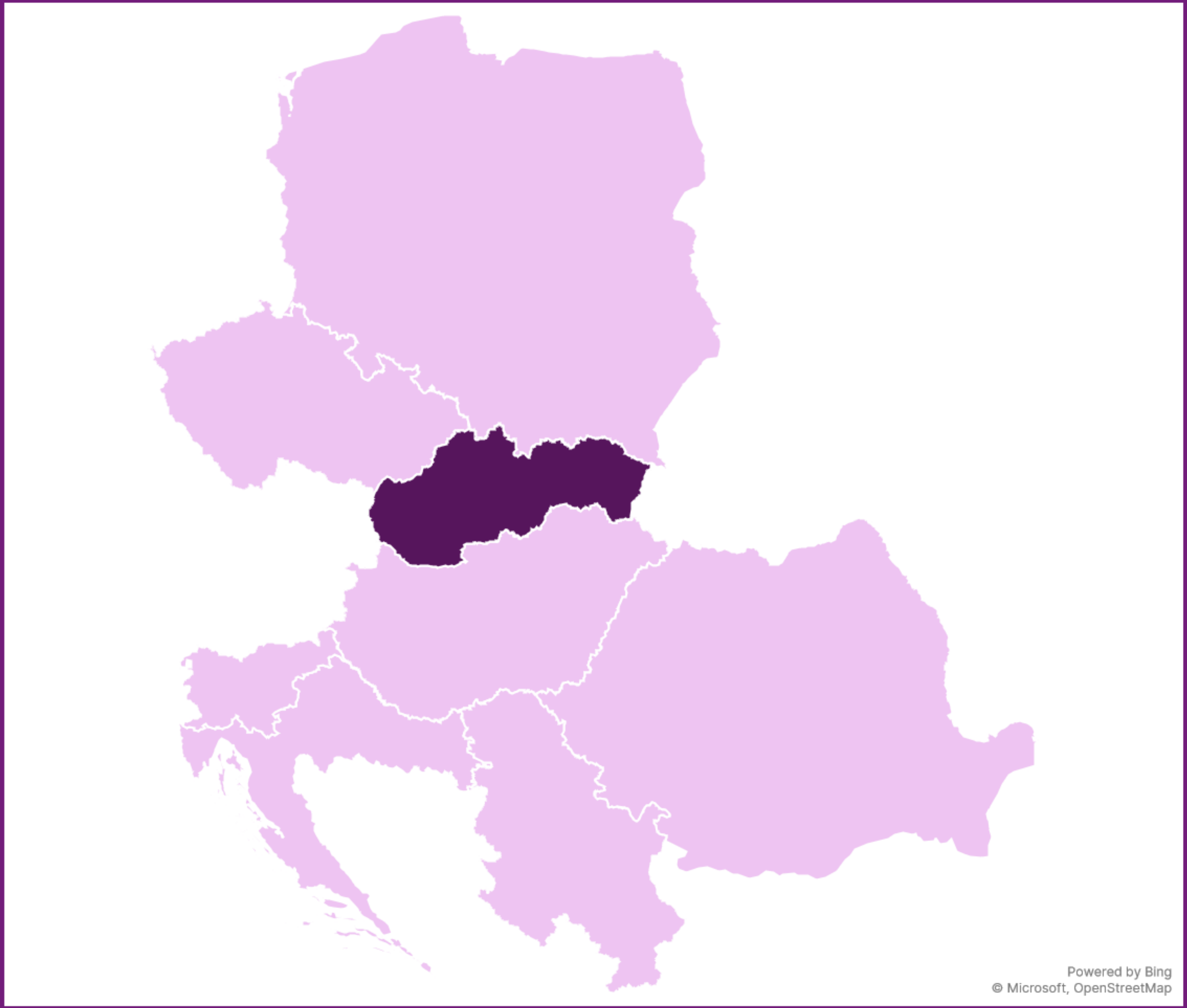
Moody's: A2, outlook negative

S&P: A+, outlook stable

Fitch: A-, outlook stable

EU member state: since 1 May 2004

Schengen: member since 21 December 2007



# Follow #ErsteGroupResearch on LinkedIn

Maria Valachyova

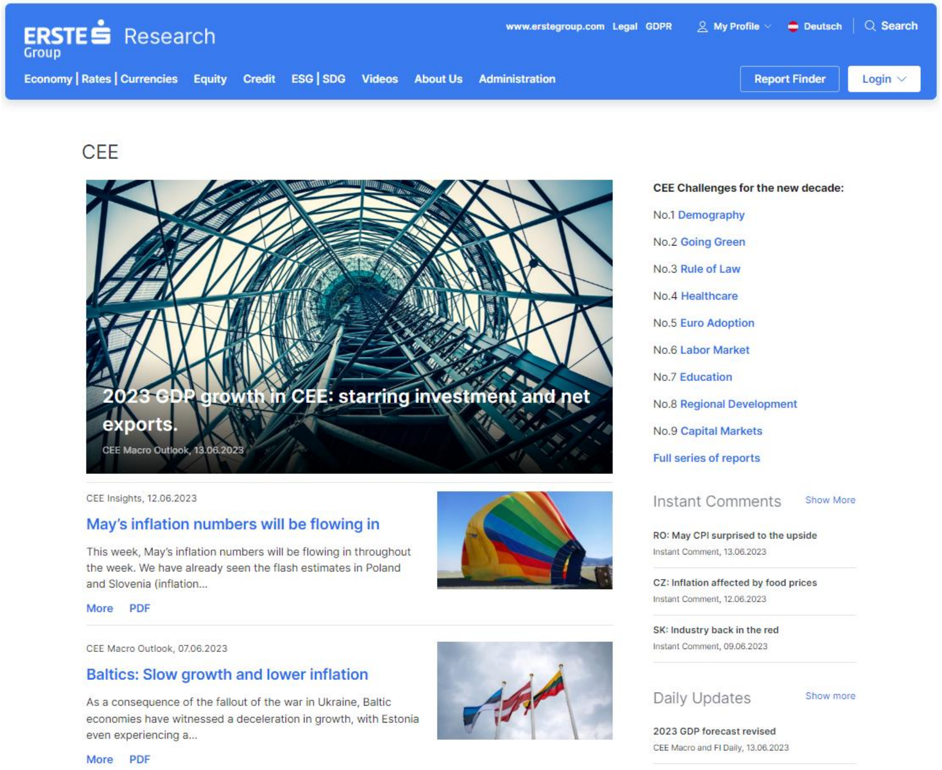
Matej Hornak

Marian Kocis

**Give us feedback!**

# Macro reports & forecasts are publicly available on Erste Group‘s website and our mobile applications

Open in your **browser**




On your **mobile**


**Scan** our QR code

Visit our research page:
**erstegroup.com/en/research**

# Contacts

**Visit www.erstegroup.com or type on Bloomberg ESTE <GO>**

## Erste Group Research (Vienna)


**Fritz Mostböck, CEFA®, CESGA®**
**Head of Group Research**
+43 5 0100 11902
friedrich.mostboeck@erstegroup.com

**Juraj Kotian**
**Head of CEE Macro/ FI Research**
+43 5 0100 17357
juraj.kotian@erstegroup.com

**Henning Eßkuchen**
**Head of CEE Equity Research**
+43 5 0100 19634
henning.esskuchen@erstegroup.com

**Rainer Singer, CEFA®**
**Head of Major Markets & Credit Research**
+43 5 0100 11909
rainer.singer@erstegroup.com


## Local Research Offices


**Bratislava**
**Slovenska Sporitelna**
**Head: Maria Valachyova**
+421 (2) 4862 4158
valachyova.maria@slsp.sk

**Budapest**
**Erste Bank Hungary**
**Head: Jozsef Miro**
+36 (1) 235 5131
Jozsef.Miro@erstebroker.hu

**Bucharest**
**Banca Comerciala Romana (BCR)**
**Head: Ciprian Dascalu**
+40 3735 10 424
ciprian.dascalu@bcr.ro

**Prague**
**Ceska Sporitelna**
**Head: David Navratil**
+420 224 995 439
DNavratil@csas.cz

**Warsaw**
**Erste Securities Polska**
**Head: Cezary Bernatek**
+48 22 257 5751
Cezary.Bernatek@erstegroup.com

**Zagreb/ Belgrade**
**Erste Bank**
**Heads: Alen Kovac, Mladen Dodig**
+385 72 37 1383, +381 1122 09178
akovac2@erstebank.com
Mladen.Dodig@erstebank.rs

# Disclaimer

This publication was prepared by Erste Group Bank AG or any of its consolidated subsidiaries (together with consolidated subsidiaries "Erste Group") independently and objectively as general information. This publication serves interested investors as additional source of information and provides general information, information about product features or macroeconomic information without emphasizing product selling marketing statements. This publication does not constitute a marketing communication pursuant to Art. 36 (2) delegated Regulation (EU) 2017/565 as no direct buying incentives were included in this publication, which is of information character. This publication provides only other information without making any comment, value judgement or suggestion on its relevance to decisions which an investor may make and is therefore also no recommendation. Thus this publication does not constitute investment research pursuant to Art. 36 (1) delegated Regulation (EU) 2017/565. It has not been prepared in accordance with legal requirements designed to promote the independence of investment research and it is not subject to the prohibition on dealing ahead of the dissemination of investment research. The information only serves as non-binding and additional information and is based on the level of knowledge of the person in charge of drawing up the information on the respective date of its preparation. The content of the publication can be changed at any time without notice. This publication does not constitute or form part of, and should not be construed as, an offer, recommendation or invitation for a transaction in any financial instrument or connected financial instruments, and neither this publication nor anything contained herein shall form the basis of or be relied on in connection with or act as an inducement to enter into any contract or inclusion of a financial or connected financial instrument in a trading strategy. Information provided in this publication is based on publicly available sources which Erste Group considers as reliable, however, without verifying any such information by independent third persons. While all reasonable care has been taken to ensure that the facts stated herein are accurate and that the forecasts, opinions and expectations contained herein are fair and reasonable, Erste Group (including its representatives and employees) neither expressly nor tacitly makes any guarantee as to or assumes any liability for the up-to-dateness, completeness and correctness of the content of this publication. Erste Group may provide hyperlinks to websites of entities mentioned in this document, however the inclusion of a link does not imply that Erste Group endorses, recommends or approves any material on the linked page or accessible from it. Neither a company of Erste Group nor any of its respective managing directors, supervisory board members, executive board members, directors, officers of other employees shall be in any way liable for any costs, losses or damages (including subsequent damages, indirect damages and loss of profit) howsoever arising from the use of or reliance on this publication. Any opinion, estimate or projection expressed in this publication reflects the current judgment of the author(s) on the date of publication of this document and does not necessarily reflect the opinions of Erste Group. They are subject to change without prior notice. Erste Group has no obligation to update, modify or amend this publication or to otherwise notify a reader thereof in the event that any matter stated herein, or any opinion, projection, forecast or estimate set forth herein, changes or subsequently becomes inaccurate. The past performance of a financial or connected financial instrument is not indicative for future results. No assurance can be given that any financial instrument or connected financial instrument or issuer described herein would yield favorable investment results or that particular price levels may be reached. Forecasts in this publication are based on assumptions which are supported by objective data. However, the used forecasts are not indicative for future performance of financial instruments incl. connected financial instruments. Erste Group, principals or employees may have a long or short position or may transact in financial instrument(s) incl. connected financial instruments referred to herein or may trade in such financial instruments with other customers on a principal basis. Erste Group may act as a market maker in financial instruments, connected financial instruments or companies resp. issuers discussed herein and may also perform or seek to perform investment services for those companies resp. issuers. Erste Group may act upon or use the information or conclusion contained in this publication before it is distributed to other persons. This publication is subject to the copyright of Erste Group and may not be copied, distributed or partially or in total provided or transmitted to unauthorized recipients. By accepting this publication, a recipient hereof agrees to be bound by the foregoing restrictions.

Erste Group is not registered or certified as a credit agency in accordance with Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies (the Credit Rating Agencies Regulation). Any assessment of the issuers creditworthiness does not represent a credit rating pursuant to the Credit Rating Agencies Regulation. Interpretations and analysis of the current or future development of credit ratings are based upon existing credit rating documents only and shall not be considered as a credit rating itself.



Published by:
Erste Group Bank AG
Group Research
1100 Vienna, Austria, Am Belvedere 1
Head Office: Wien
Commercial Register No: FN 33209m
Commercial Court of Vienna

Erste Group Homepage: www.erstegroup.com