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**Statement by Mr. Pösö on Slovak Republic  
(Preliminary)  
Executive Board Meeting  
June 18, 2021**

We thank Staff for their clear and insightful reports in the context of Slovakia's Article IV consultation. We also thank Mr. Palotai and Mr. Harvan for their informative Buff statement. We commend the national and EU authorities' resolve to fight the health, social and economic consequences of the ongoing pandemic.

The strong policy response has played an effective role in mitigating the impact of the COVID-19 crisis on the Slovakian economy and society at large, and the economy is now set for a strong rebound. Once uncertainty recedes and economic conditions improve, fiscal sustainability should be ensured in the medium-to-long run, also paying attention to the composition of public finances. A timely and effective execution of the investments and reforms foreseen in the Recovery and Resilience Plan (RRP) would help lifting the economy's growth potential while securing a sustainable and inclusive recovery.

*Macroeconomic developments*

**Despite slight differences in the expected composition of growth, we broadly agree with Staff's strong growth outlook and risk assessment, which remains broadly balanced amid still high uncertainty.** The negative impact of the COVID-19 pandemic on the Slovakian economy has been sizeable, but milder than foreseen owing to strong policy support, which helped sustaining resilient private consumption. After a weak start in 2021, we expect a sharp rebound in activity from the second half of the year onwards as vaccinations progress and containment measures are lifted, also driven by the strong performance of the manufacturing industry and export sectors. On that basis, we do not project such a negative contribution of net exports to growth as Staff does in 2022, also in line with improved external demand, resulting in slightly higher growth next year. Private

consumption is expected to gradually gain momentum as the labor market improves and precautionary savings ease, providing a significant boost to growth in 2022. We project buoyant investment growth, well above Staff's projections in 2021, supported by sizeable public investments linked to the RRP and planned capital expenditure in the automotive sector. Amid high uncertainty regarding price developments, we expect slightly stronger inflation than Staff due to dynamic food prices. We share Staff's view that risks to the outlook appear broadly balanced, with upside risks mostly linked to a successful containment of the virus and external demand, and downside risks mainly related to potential supply-chain disruptions that could affect the export-oriented automotive industry.

### Fiscal Policy

**While Slovakia should maintain a supportive fiscal stance in 2021 and 2022, policies should become more targeted over time to enable resource reallocation, prevent scarring, and ensure fiscal sustainability over the medium- and long-run.** While the current fiscal policy stance in Slovakia is broadly appropriate, some of the discretionary measures do not appear to be temporary or matched by offsetting measures. As temporary support measures are discontinued, the deficit is forecast to decrease over the forecast horizon, and the debt-to-GDP ratio is expected to be contained by strong output growth and low interest rates. However, substantial public investments from Next Generation EU (NGEU) grants should provide additional fiscal impulse from 2022 through 2026. Slovakia faces long-run fiscal sustainability challenges due to ageing-related costs, and therefore a successful implementation of the planned pension reform and of the health system reform appear necessary to create buffers. We also share Staff's assessment that the authorities should continue to strengthen tax collection and improve the efficiency of public spending. Planned reforms in taxation, public finance administration, and the fiscal framework will also contribute to rebuilding fiscal buffers while addressing structural weaknesses, while raising real estate and environmental taxation could also yield additional revenues.

### Structural Policies

**We agree that investments in human capital, reforming the labour market, and public governance and fostering innovation, with a focus on the green and digital transformation, are crucial to support the recovery, minimize scarring, and set the stage for sustainable and inclusive growth.** The pandemic has highlighted some structural challenges in the labor market and made the strengthening of human capital, including preparing for technological change and the digital transformation, all the more urgent. As demand for skills rapidly changes, investment in lifelong education, up-skilling and labor-market policies to facilitate resource reallocation would be needed. Raising the participation of low-skilled workers, women and marginalized communities are fundamental to increase labor supply, also considering demographic challenges. We agree that the investments and

reforms foreseen in the RRP seem to be well-aligned with Slovakia's needs, also to boost productivity via increases in R&D spending and greening and digitalizing of the economy. Governance reforms could aim at strengthening the effectiveness and independence of the justice system, along with improved and accelerated public procurement procedures while ensuring proper safeguards. Improving the business environment, particularly for SMEs, can also contribute to boosting productivity.

### Financial Sector Policies

**We broadly concur with staff's analysis of the financial sector and agree that policies should be carefully balanced to continue supporting credit supply, while preventing a further build-up of vulnerabilities, related in particular to the real estate market.** Slovak banks entered the crisis with strong liquidity, adequate capitalization, and above EU-average profitability. Liquidity support measures also helped preventing a strong increase in bankruptcies, whereas credit provision was supported by bold policy action. With capital sufficiently above minimum requirements, lending activity is not constrained, and there are no signs of liquidity strains so far. Banks have also proactively increased provisions ahead of the withdrawal of support, and the crisis has not resulted in higher NPL ratios yet. Nevertheless, insolvency risks have built up, and improvements in restructuring mechanisms and insolvency frameworks would help support resource reallocation. While near-term risks are primarily related to the deterioration of credit risks once support is withdrawn, medium-term vulnerabilities are linked to pre-existing real-estate risks. Despite the pro-active stance of Slovakia's supervisor, rapid mortgage growth has contributed to fast increases in household indebtedness and housing prices. In this context, we concur with Staff that while the macroprudential stance is broadly adequate, policies should be carefully balanced to continue supporting credit supply, while preventing a further build-up of vulnerabilities. Finally, although Slovakia has taken steps to improve its anti-money-laundering framework, the system should continue to be upgraded, for instance in the human resource area or by extending beneficial ownership registers.