14th of February 2025

Slovak economy enters global economic uncertainty

Macroeconomic forecast for years 2024 – 2029

IFP Analysts

GDP growth will decelerate slightly to 1.9 per cent in 2025 as a result of growing global trade uncertainty and the stagnation of German industry. On the other hand, the Slovak economy will be supported by investments from the Recovery and Resilience Plan. Real incomes will rise, but households will spend more cautiously and consumption will be further dampened by the consolidation of public finances. The labour market will remain stable and the unemployment rate will decline to a new low of 5.2 per cent in 2026. However, the risks to the forecast are skewed to the downside. Lower absorption of EU funds may lead to lower capital formation. Moreover, there are increasing signs of rising protectionism in world trade. The introduction of tariffs between the US and the EU and China on the other side, may reduce Slovak GDP by up to 0.5 per cent per year under certain circumstances.

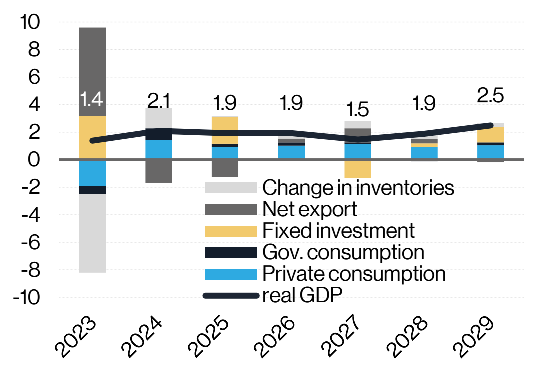
Economic Growth in 2024 Driven by Domestic Demand

Slovak GDP grew by 2.0 per cent in 2024, mainly fuelled by domestic demand. Household consumption was supported by moderating inflation and a stable labour market. Towards the end of the year, the gradual increase in Recovery and Resilience Plan (RRP) disbursements led to slightly higher investment activity. Economic activity was also boosted by the households making precautionary purchases ahead of the VAT increase in January. However, overall investment activity slowed down last year, dampening the economy, as the take-up of capital resources from the new programming period of EU funds was only slow.

The main impetus in 2025 will be the Resilience and Recovery Plan

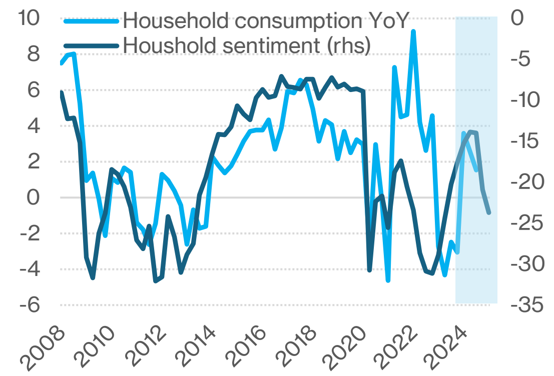
The Slovak economy will grow by 1.9 per cent in 2025, despite another year of stagnation in Germany and growing uncertainty in the global economy. Exports will accelerate compared to last year, but foreign trade will continue to be hampered by stagnation in Germany and limited industrial demand across the euro area. We expect investment in the economy to pick up steam significantly as a result of the drawdown from the RRP. The consolidation of public finances will cut into disposable income and thus put a brake on consumer spending. Employment will rise, mainly as a result of a decline in early retirements.

Figure 1: GDP growth contributions on the expenditure side (constant prices, pp)



Source: SO SR, IFP

Figure 2: Declining consumer sentiment dampens household spending



Source: IFP

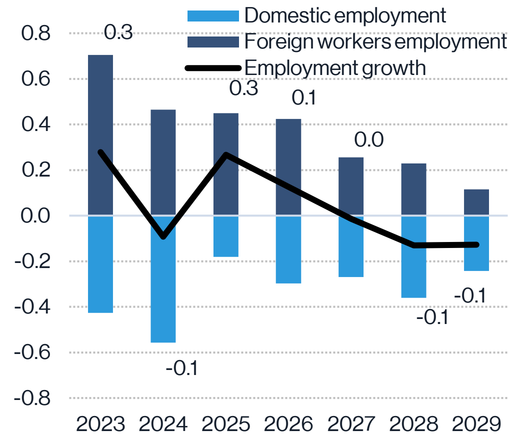
Consolidation of public finances and demographic factors will dampen growth

RRP will continue to support the economy in 2026. In the second half of the year, the economy will receive a boost from the first exports from the newly built Volvo factory. The accelerating recovery in the euro area will support the foreign trade. The year 2027 will be marked by the end of the RRP funding, which will be reflected in a decline in investment activity and lower economic growth. Investment will pick up again towards the end of the EU funds programme period in 2029. Throughout the forecast horizon, the consolidation of public finances and unfavourable demographic developments will weigh on the economy.

The tariffs introduction would affect mainly the automotive industry.

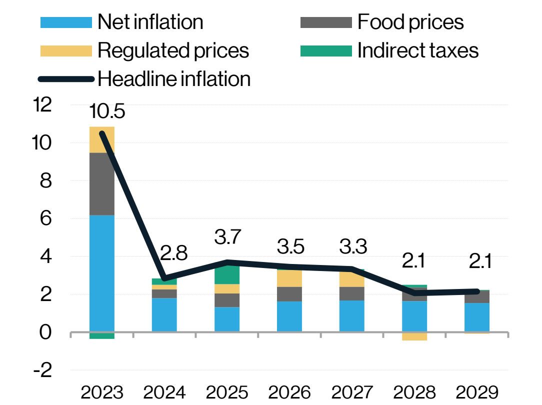
In an environment of high uncertainty at home and abroad, risks are skewed to the downside. Uncertainty stems mostly from the spread of protectionism in international trade. An introduction of tariffs in the US could negatively affect the automotive industry in particular (Box 2). Lower than expected drawdown of the RRP funding poses a significant risk as well, which would translate into less robust investment activity and a sharper decline in employment than projected.

Figure 3: Contributions of domestic and foreign workers to ESA employment (p. p.)



Source: SO SR, IFP

Figure 4: Contributions to inflation (per cent)



Source: SO SR, IFP

Record low unemployment

Employment will return to growth in 2025. Over 6 000 new jobs will be created in the economy, representing an increase in employment of 0.3 per cent. The labour market will be supported by investments from the RRP, accelerating private investments as well as the recovery of economic activity abroad. On the other hand, austerity measures will reduce employment in the public sector. Increased early retirements will continue to a lesser extent this year, affecting mainly the first quarter of the year. Approximately 114 000 foreign workers help to alleviate labour shortages. The unemployment rate will fall to a new low of 5.3 per cent in 2025 and stabilise at this level in the following years.

In the coming years, the labour market will face labour shortages, leading to low employment dynamics. The decline in the economically active population will continue to be offset by labour inflows from abroad. The labour market will be affected in a growing way by the absorption of EU funds, which will compensate for the shortfall in the RRP. Several structural problems, such as skills and regional mismatches among job seekers, will hamper further reductions in the unemployment rate which will therefore not fall below 5.2 per cent over the forecast horizon.

Wage-growth of 5 per cent

The shortage of skilled labour supply will put pressure on wages, which are expected to rise by more than 5 per cent this year. The year-on-year slowdown reflects lower productivity growth, inflation and back-indexation. Wage bargaining in the public sector has been reflecting the need for fiscal consolidation. Thus, the private sector wages will rise faster than public sector wages throughout the forecast horizon. Higher energy prices will support inflation, limiting real wage growth to less than 2 per cent over the next three years.

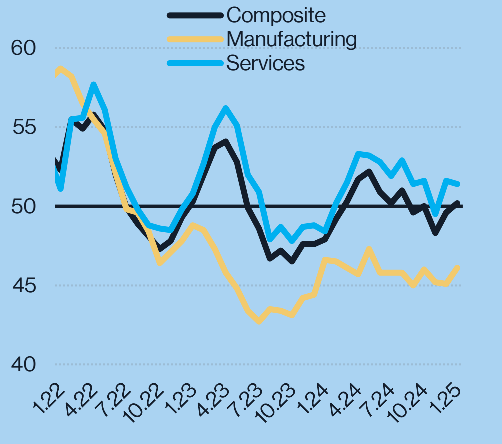
Acceleration of inflation above 3 per cent

Inflation will accelerate to 3.7 per cent in 2025. Price increases will be mainly driven by the rise of the VAT rate, which will contribute by 1 p. p. to headline inflation. Gas and heat price caps will prevent average inflation from accelerating above 4 per cent this year. According to the URSO decree electricity prices for households will remain unchanged in the medium term. For gas and heat prices we apply the technical assumption of a return to the market price that is spread over the next two years, with a decline at the end of the medium term in line with the evolution of futures prices. As a result, inflation will be slightly above 3 per cent in 2026 and 2027. Thereafter, we expect food and tradable goods prices to return to average pre-pandemic growth rates. Services prices will grow faster, but overall inflation will be dampened by consolidation of public finances in the medium term.

BOX 1: External environment assumptions

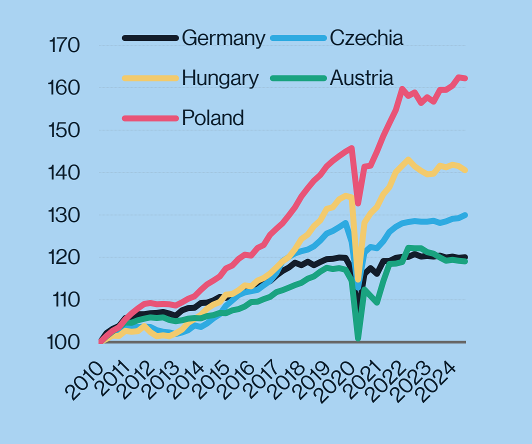
Economic developments abroad disappointed in 2024. The economic recovery of our main trading partners has been very slow and has not met expectations. Germany, the euro area's largest economy, has experienced another year of stagnation, with GDP remaining at the same level as in 2019. Austria has been going through a similar development, with economic activity contracting for the second year in a row. France fell short of expectations as well, despite the Olympic boost at the end of the year. The weak performance of the bloc's largest economies is thus likely to ensure that eurozone growth does not surpass the 1 per cent threshold. However, the ECB has managed to tame inflation in 2024, allowing it to begin a gradual easing of monetary policy. The situation on the other side of the Atlantic is different. Over the course of the year, the US economy continued to grow at a solid pace, outperforming the euro area, yet accompanied by higher inflation. Therefore, monetary easing is progressing more slowly in the US. Low consumer confidence continues to weigh on the Chinese economy, whose economic growth has slowed considerably in recent years.

Figure A: Euro area's manufacturing remains a drag (Purchasing Managers' Index, readings above 50 = expansion)



Source: Bloomberg, IFP

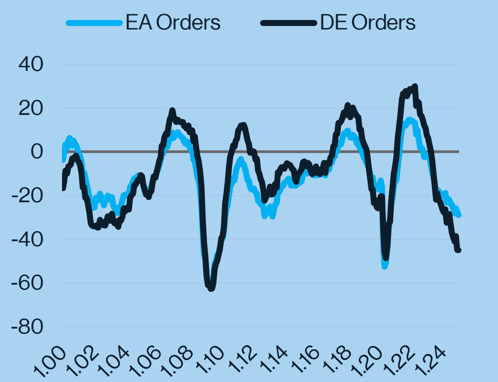
Figure B: Stagnation of our trade partners (real GDP, level, indexed, 100 = 1.kv. 2010)



Source: Eurostat, IFP

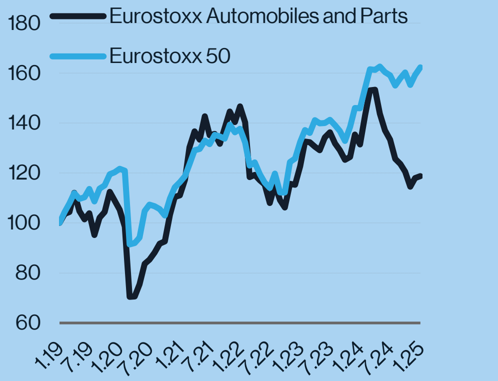
The crisis in European industry continues. The year 2024 was characterised by deepening problems in industrially oriented economies. Germany and its closest trading partners have been hit hard. Industrial orders in Germany and the euro area are now approaching levels reminiscent of the global financial and pandemic crisis. Current data do not suggest a reversal of this situation in the short term. German manufacturers and car companies are facing cheaper competition from China, against which they are losing ground and thus their share of export markets. In addition, Germany has been struggling to respond effectively to the economic shocks of recent years, in particular the rise in energy prices. Political instability and strict fiscal rules, which discourage investment in the country, also play an important role in the poor performance. Thus, both political will and economic reforms will be needed to jump-start the economy. On the positive side, the solid performance maintained by our V3 neighbours, with the exception of Hungary, despite the German stagnation, is a positive development in this context.

Figure C: Manufacturing orders reminiscene past recessions (ESI, points)



Source: EK, IFP

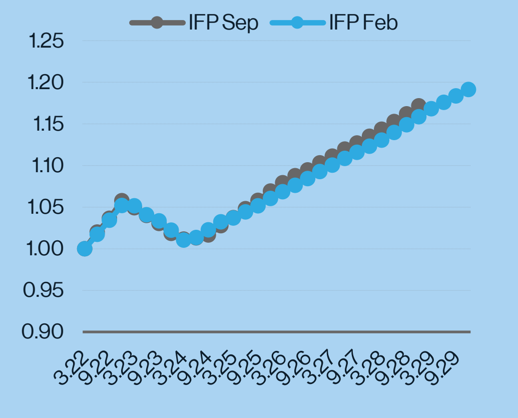
Figure D: Car manufacturers lag behind the market (stock indices, indexed)



Source: Bloomberg, IFP

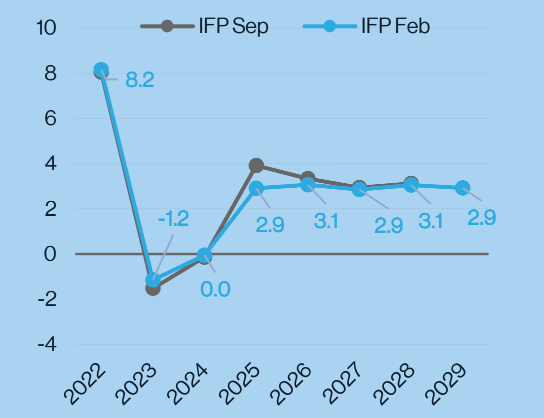
External demand is expected to recover in the coming years. The economies of our close trading partners in the V3 should accelerate this year and next. Activity will be supported by both looser monetary policy and investment incentives in the form of the RRP. These countries will support our external demand in the short term. The German economy will grow only moderately this year, close to stagnation. However, we expect a gradual recovery of the euro area economy and a return to growth of around 1 per cent per year in the period ahead. However, the risks to the forecast are particularly high at present. The new US administration is threatening to impose tariffs on imported goods, not excluding Europe. Given the importance of the US as an export market for the automotive industry in Germany and the V3 countries, this poses a significant threat to the economic growth of our foreign partners and to our external demand, which could jeopardise the ongoing recovery.

Figure E: A slowdown of our trading partners weighs on external demand
(weigh. ind. of ex. dem., level, indexed)



Source: IFP

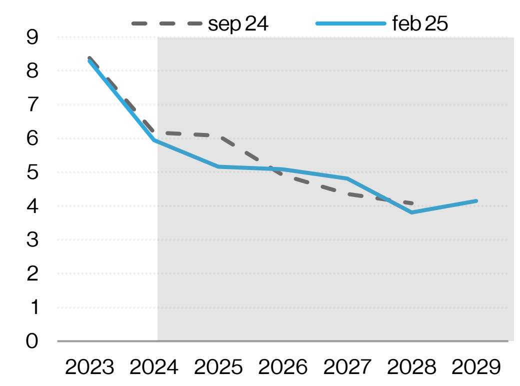
Figure F: Eventual recovery will be softer
(yoy, weigh. ind. of ex. dem., per cent)



Source: IFP

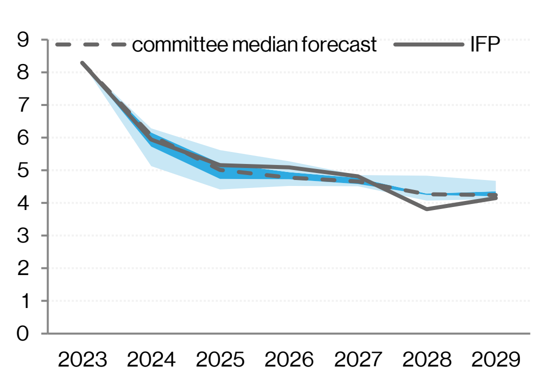
The update of the Ministry of Finance's macroeconomic forecast was the subject of a meeting of the Committee for Macroeconomic Forecast on 5 February 2025. **The forecast was assessed as realistic by all of the Committee members.** The forecast update as well as the minutes of the Macroeconomic Forecast Committee and background materials are available on the IFP website.

Figure 5: Evolution of macroeconomic bases compared to the previous forecast (growth, per cent)



Source: IFP

Figure 6: Comparison of tax bases forecasts1 by members of the MFC (growth, per cent)



Source: IFP

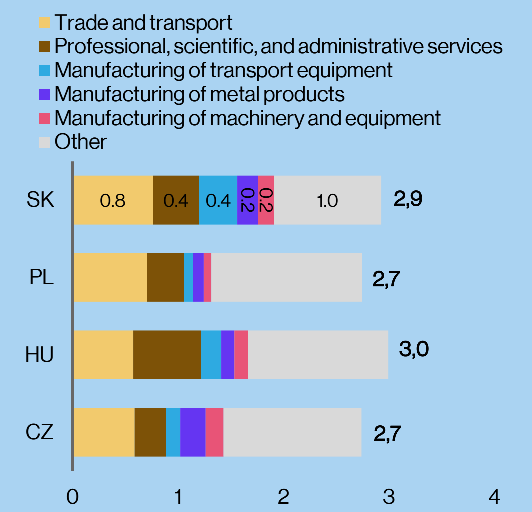
BOX 2: The Importance of the USA for the Slovak Economy

Exports to the United States represent a significant share of Slovakia's total exports. In 2024, Slovakia exported goods worth €4.8 billion to the U.S., accounting for 4.1 per cent of total exports. As much as 90 per cent of these exports consist of machinery and transport equipment, primarily automobiles and their components. This high degree of specialization increases Slovakia's economic vulnerability, particularly in the event of U.S. tariffs on car imports.

U.S. demand for goods and services supports approximately 70 000 jobs in Slovakia, representing 2.9 per cent of total employment. These jobs are primarily in trade, transport, and services, but also in professional and administrative activities (Figure G). In the automotive sector, nearly 9 000 workers depend on exports to the U.S., while in the entire manufacturing industry, this figure rises to approximately 30 000.

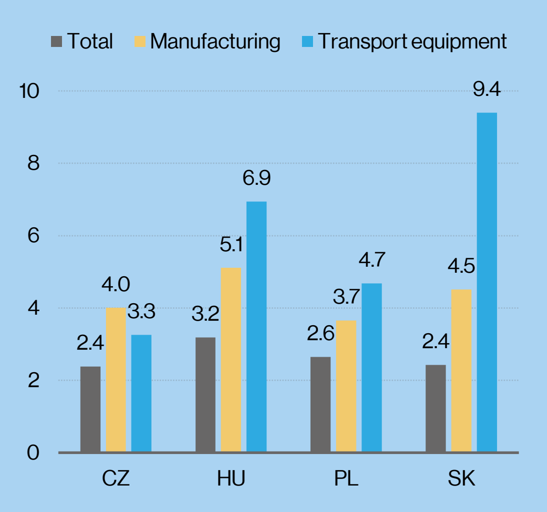
Overall, demand from the U.S. generates about 2.4 per cent of Slovakia's total added value, with the automotive sector accounting for as much as 10 per cent. If the U.S. were to impose tariffs on cars, industrial jobs would be the most at risk. The vulnerability is particularly pronounced in the automotive industry, where almost 10 per cent of the sector's added value is tied to U.S. demand (Figure H).

Figure G: U.S. demand supports nearly 3% of employment in Slovakia (share of employment in %, 2022)



Source: *IFP*

Figure H: U.S. demand accounts for nearly 10% of the added value in the automotive industry (sector's share of added value in %, 2022)



Source: *IFP*

According to an analysis by Oxford Economics[1], Slovakia would be the most vulnerable economy in the EU in the event of a large-scale trade war. The model scenario assumes that the U.S. and the European Union would introduce reciprocal 10 per cent tariffs, while the U.S. would impose 60 per cent tariffs on Chinese imports, and China would respond with 40 per cent tariffs on U.S. goods. As a result, Slovakia's GDP would be nearly 2 per cent lower by the end of 2029 (equivalent to a 0.5 per cent decrease per year) compared to a scenario in which current trade conditions remain unchanged. This is primarily due to the structure of Slovakia's economy, which is heavily reliant on industrial production and focused on automotive manufacturing.

[1] Dostupné na: https://www.oxfordeconomics.com/resource/what-trump-2-0-would-mean-for-european-growth/

MF SR FORECAST – MAIN MACROECONOMIC INDICATORS (February 2025)

Indicator (growth in per cent unless otherwise noted)	2023	forecast 2024	2025	2026	2027	2028	2029	diff. to September 2024 forecast 2024	2025	2026	2027	2028
Gross Domestic Product												
GDP, real	1.4	2.1	1.9	1.9	1.5	1.9	2.5	-0.2	-0.3	-0.4	0.4	0.0
GDP, nominal (bn. €)	122.9	130.1	136.7	144.1	150.9	157.3	164.9	-1.1	-3.2	-3.2	-1.3	-1.3
GDP, nominal	11.7	5.9	5.1	5.4	4.7	4.3	4.8	-1.0	-1.6	0.1	1.4	0.0
Private consumption, real	-3.3	2.6	1.6	1.8	2.0	1.6	1.9	-0.4	0.2	0.0	-0.3	-0.1
Private consumption, nominal	6.7	5.7	5.6	5.3	5.4	3.8	4.2	-0.3	-1.4	0.6	0.9	-0.4
Government spending	-3.0	4.3	1.3	1.2	0.5	-0.6	1.1	0.8	1.1	1.7	0.8	-0.3
Fixed investment	16.6	-0.3	8.9	-0.3	-5.9	1.4	5.4	0.0	-1.7	-0.7	-1.1	-1.7
Export of goods and services	-0.7	1.1	2.7	3.9	4.0	3.2	2.8	-0.7	-1.0	-0.5	-0.5	-0.7
Import of goods and services	-7.7	3.1	4.4	3.7	3.0	3.0	3.1	-1.7	-2.3	0.6	-0.8	-0.8
Labour market												
Registered employment	0.2	-0.2	0.3	0.1	0.0	-0.1	-0.1	0.0	-0.2	-0.1	-0.1	0.0
Wages, nominal	9.7	6.9	5.3	5.3	5.1	4.2	4.5	0.0	-0.6	0.2	0.2	-0.3
Wages, real	-0.8	4.0	1.5	1.8	1.7	2.1	2.3	0.0	1.0	-0.6	-0.9	0.0
Unemployment rate	5.8	5.3	5.3	5.2	5.2	5.2	5.2	0.0	0.0	0.0	0.2	0.2
Inflation												
CPI												
Gross Domestic Product	10.5	2.8	3.7	3.5	3.3	2.1	2.1	0.0	-1.7	0.8	1.1	-0.3

Note: Historical data available as of the Committee meeting on 5.2.2025 *Source: SO SR, IFP*

Recovery and Resilience Plan funds absorption (million EUR, w/o VAT, ESA2010)

	2022	2023	2024	2025	2026
RRF total	**49**	**359**	**938**	**2 838**	**2 187**
Public investments	2	81	731	1 943	1 320
Public compensations	23	37	102	94	93
Public intermediate consumption	15	25	42	85	68
Social transfers in kind	2	2	2	4	10
Social transfers	4	9	7	20	33
Private compensations	0	1	1	32	22
Private intermediate consumption	0	1	0	15	14
Private investments	3	24	42	483	513
Household investments	0	180	9	162	114

Source: IFP