Box 4

THE ADOPTION OF THE EURO BY SLOVAKIA

On 1 January 2009 Slovakia adopted the euro, resulting in an increase in the number of euro area countries from 15 to 16. The euro is now the currency of 329 million people in the euro area. The conversion rate between the Slovak koruna and the euro was irrevocably fixed at SKK 30.1260. During its participation in ERM II, from 28 November 2005, the central parity of the Slovak koruna was revalued twice against the euro (by 8.5% in March 2007 and by 17.6472% in May 2008).

Slovakia is a relatively small economy in comparison with the rest of the euro area. Consequently, the statistical and macroeconomic features of the euro area would be only marginally affected following this latest enlargement (see the table).

Key economic characteristics

	Reporting period	Unit	Euro area excl. Slovakia	Euro area incl. Slovakia	Slovakia
Population and economic activity [1]					
Total population [2]	2007	millions	320.5	325.9	5.4
GDP	2007	EUR billions	8,927.6	8,982.5	54.9
GDP per capita	2007	EUR thousands	27.9	27.6	10.2
GDP per capita (PPP)	2007	Euro 15=100	100.0	99.4	61.2
GDP (share of world GDP) [3]	2007	%	16.1	16.3	0.2
Value added by economic activity [4]					
Agriculture, fishing, forestry	2007	% of total	1.9	1.9	2.9
Industry (including construction)	2007	% of total	26.7	26.8	37.0
Services (including non-market services)	2007	% of total	71.4	71.3	60.2
Monetary and financial indicators					
Credit to the private sector [5]	2007	% of GDP	109.5	109.1	41.8
Stock market capitalisation [6]	2007	% of GDP	73.7	73.3	8.3
External trade [7]					
Exports of goods and services	2007	% of GDP	22.3	22.3	86.0
Imports of goods and services	2007	% of GDP	21.1	21.1	86.9
Current account balance	2007	% of GDP	0.4	0.4	-5.3
Labour market					
Labour force participation rate [8]	2008 Q3	%	71.7	71.7	69.3
Unemployment rate	2008 Q3	%	7.5	7.5	9.2
Employment rate [8]	2008 Q3	%	66.5	66.5	63.1
General government					
Surplus (+) or deficit (-)	2007	% of GDP	-0.6	-0.6	-1.9
Revenue	2007	% of GDP	45.5	45.5	32.7
Expenditure	2007	% of GDP	46.2	46.1	34.6
Gross debt outstanding	2007	% of GDP	66.3	66.1	29.4

Sources: Eurostat, IMF, European Commission and ECB calculations.
1) The data in Slovak korunas were recalculated using the market exchange rate.
2) Annual average.
3) GDP shares are based on a PPP valuation of the country GDPs.
4) Based on nominal gross value added at basic prices.
5) Comprises loans and holdings of securities as well as holdings of shares and other equities.
6) The market capitalisation is the total outstanding amount of quoted shares issued by euro area/Slovak residents at market value.
7) Balance of payments data. Euro area data are compiled on the basis of transactions with residents of countries outside the euro area (i.e. excluding intra-euro area flows). Data for Slovakia include transactions with residents from the rest of the world (i.e. including transactions with the euro area).
8) Share of the working age population (i.e. those aged between 15 and 64).

The GDP of Slovakia accounts for only about 0.6% of the GDP of the enlarged euro area. In 2007, Slovakia's GDP per capita in purchasing power parity (PPP) terms was slightly above 61% of the euro area average. In recent years, real GDP in Slovakia has grown significantly faster than that of the rest of the euro area, mainly reflecting an improved production capacity of the economy as a result of large investment projects financed by foreign direct investment inflows. These investment projects have enhanced the industrial capacity of the Slovak economy, in which industry including construction plays a more important role than in the rest of the euro area. The agricultural sector contributes to the total gross value added only slightly more in Slovakia than in the rest of the euro area, while the share of services in the total value added is lower than in the rest of the euro area. The financial sector in Slovakia is still developing, as shown by a significantly lower share of outstanding credit to the private sector than in the rest of the euro area. The more limited role played by the financial sector in the country is even more visible when comparing stock market capitalisation figures. The liquidity of the stock market is very low.

Slovakia is a small open economy and the rest of the euro area is its key trading partner, accounting for 47% of its total exports and almost 43% of its total imports.

The labour market in Slovakia differs to that of the rest of the euro area in several ways. Despite robust economic development in the last few years, Slovakia's unemployment rate is still relatively high and stood at over 9% in the third quarter of 2008. The unemployment rate in the euro area was 7.5% in the same period. Moreover, the labour force participation rate and the employment rate are below the level of the rest of the euro area. Local labour market weaknesses include the high number of long-term unemployed, an unfavourable skill mix among the unemployed and significant disparities between regional labour markets.[1]

The general government deficit in Slovakia has been declining in recent years and stood at 1.9% of GDP in 2007, compared with a deficit of 0.6% in the rest of the euro area. By contrast, government debt is much lower: the ratio of government debt to GDP in Slovakia was below 30% in 2007, while in the rest of the euro area it was above 66%. On 3 June 2008 the Council of the European Union abrogated the excessive deficit procedure for Slovakia.

The adoption of the euro further increases the benefits of the Single Market for Slovakia. The euro offers a credible framework for price stability and eliminates exchange rate uncertainty within the euro area. The benefits of euro adoption for Slovakia have already materialised by way of the stability of the Slovak koruna over the last few months, at a time when many transition economies were suffering from the turbulences in global financial markets. In order to fully reap the advantages of the euro and allow the adjustment mechanisms to operate efficiently within the enlarged currency area, further efforts should be made in Slovakia to maintain sustainable convergence, underpin external competitiveness and strengthen economic resilience. In the short term, following the euro changeover, the conversion of prices into euro should not affect the price level.

Looking further ahead, it will be important for the Slovak economy to maintain sustainable economic convergence. Despite the recent economic slowdown, the authorities should continue to avoid excessive deficits and proceed with fiscal consolidation so as to reach their

1 While many EU Member States opened their local labour markets to Slovak citizens, allowing for greater mobility within the EU, some euro area countries still apply restrictions to Slovakia.

medium-term budgetary objective as soon as possible. The functioning of Slovakia's labour market must be further improved and efforts need to be made to tackle the high structural unemployment rate. There is also a need to further improve the business environment in order to enhance productivity growth and preserve the country's attractiveness for foreign capital. Slovakia's recently achieved low-inflation environment will need to be sustained in the future. Pursuing this ambitious policy agenda is, together with the stability-oriented monetary policy of the ECB, the best means of bringing sustainable economic growth, job creation and social cohesion to Slovakia.