Slovak Republic

A Capital Destination

May 2004

The Team

- **Mr Vladimir Tvaroška**
  State Secretary, Ministry of Finance

- **Mr Martin Bruncko**
  Chief Economic Adviser

- **Mr Daniel Bytčánek**
  Director, Debt and Liquidity Management Agency

- **Mr Tomáš Kapusta**
  Head of Debt Management Department, Debt and Liquidity Management Agency

A Political Sea-Change

Initiated by 1998 Parliamentary Elections

Beginning of a new political era and re-insertion into the global economy:

- EU membership (2004)
- NATO membership (2004)
- OECD membership (2000)
- WTO membership (1995)

An Economic Success Story

1999-2001: Successful macro-economic stablisation launched by 1999 Austerity Package & subsequent reforms:

- Radical improvement in all key fundamentals including fiscal deficit and current account
- Sustained growth rebound

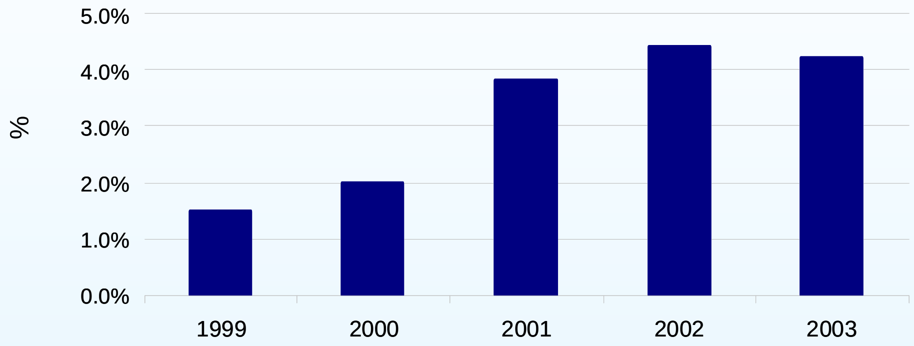
2002 onward: Series of deep structural reforms, which distinguish it not only from Central European peers but also put it ahead of traditional EU members

- A successful privatisation program of the banking sector and utilities
- Deep reform of the pension system, introducing a funded pillar alongside the pay-as-you-go regime
- Innovative tax reform, introducing a single flat tax and radically simplifying the tax system
- Continued reform drive to address health care system, labour market, education and public administration

Robust Economic Growth

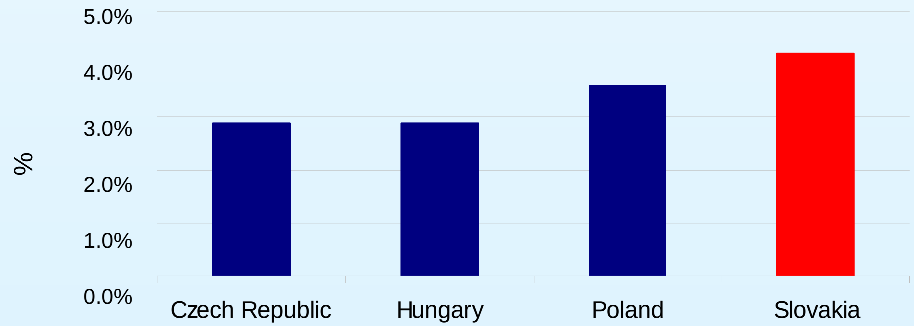
- Sustained solid growth despite weak external demand
- Export driven growth in 2003 increasingly replaced by strenghening domestic demand
- Declining unemployment since 2001
- Highest growth performance in Central Europe

Real GDP



Source: Ministry of Finance, SUSR

Real GDP (2003)

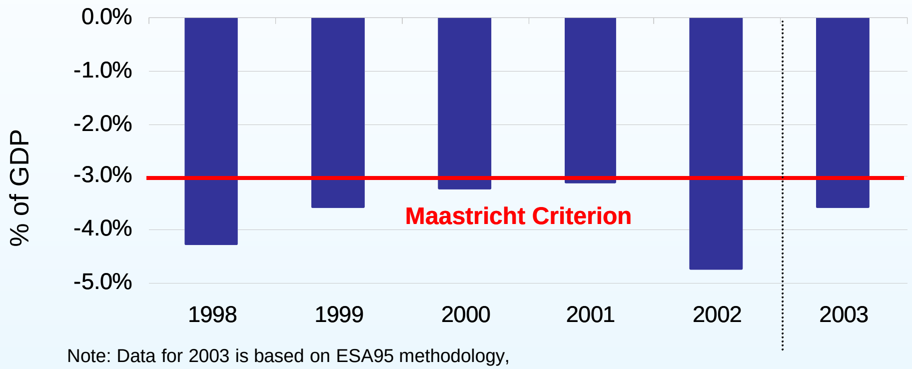


Source: Ministry of Finance, SUSR

Sustained Fiscal Adjustment

- Share of public expenditures in GDP is being reduced dramatically from 49.0% of GDP in 2002 to 40.8% in 2006
- Deficit to be reduced to 3.0% of GDP by 2006, complying with the fiscal Maastricht criterion
- Continuous drive towards increased transparency and fiscal consolidation
- Extra-budgetary funds incorporated into budget in 2001
- Strongest position amongst Central European peers

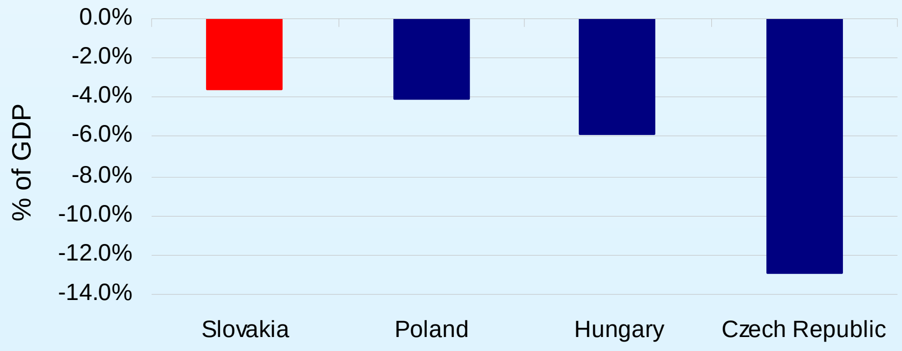
General Government Balance



Note: Data for 2003 is based on ESA95 methodology, previous years on national accounting standard

Source: Ministry of Finance

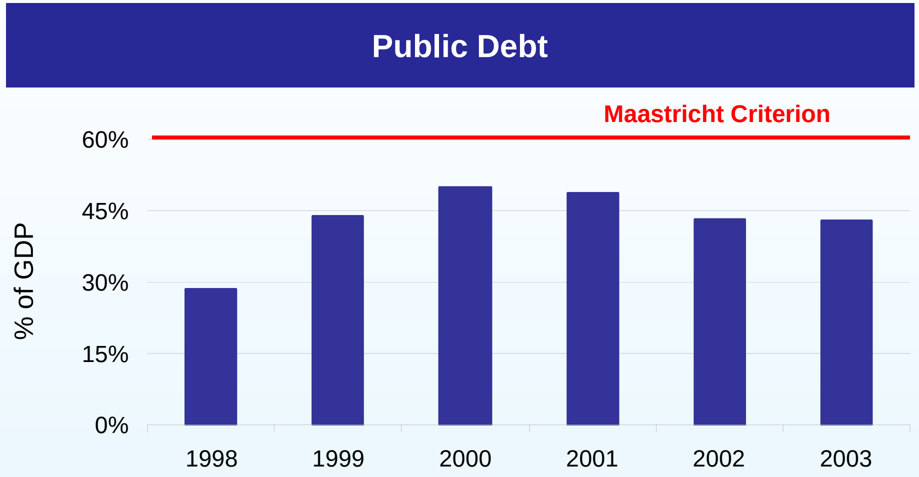
General Government Balance (2003)



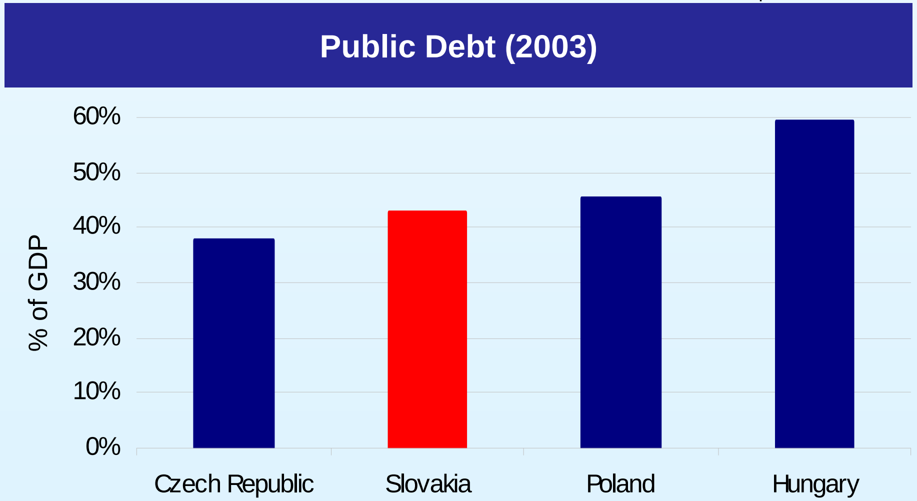
Source: Eurostat

Prudent Debt Management

- Fiscal adjustment and prudent debt management stabilised public indebtedness
- Maastricht criterion (60% of GDP) easily met
- Since 2003, specialised Debt and Liquidity Management Agency in place
- Successive reduction of state guarantees
- One of the lowest debt burdens in the region



Source: European Commission

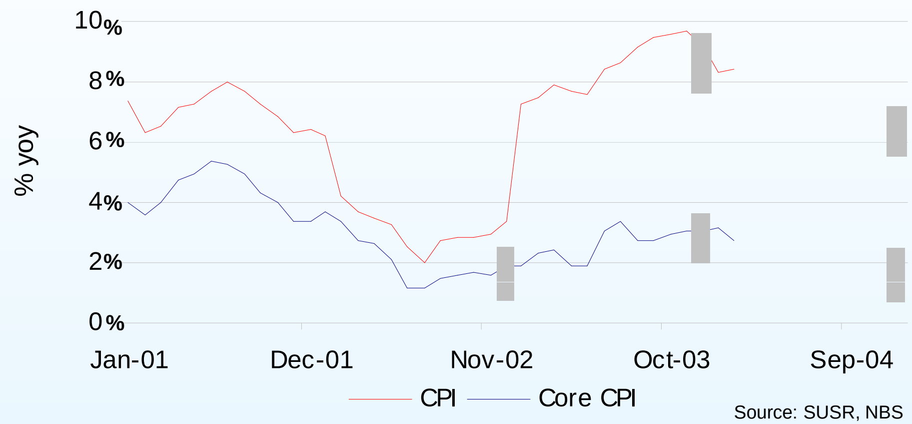


Source: European Commission

Monetary Policy on Course

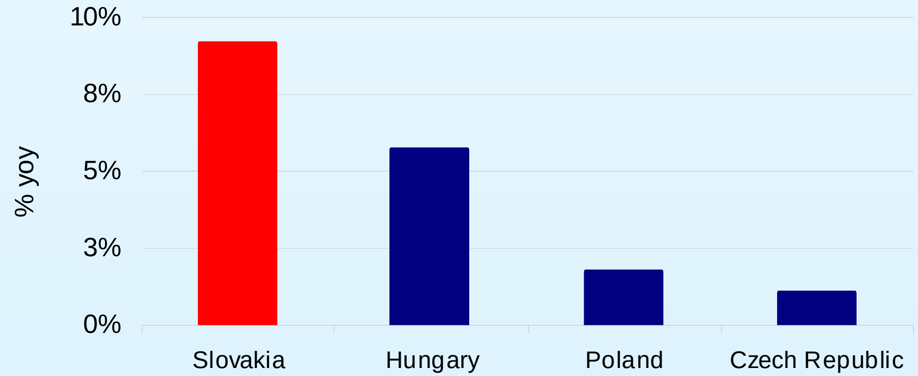
- Inflation on track with central bank targets
- CPI to fall-off sharply as effect of regulated price adjustments fades and to converge to Core CPI
- Free float of the Koruna introduced in 1998
- Successive liberalisation of financial transactions since 2000
- Continued real and nominal exchange rate appreciation

CPI and Targets



Source: SUSR, NBS

CPI (2003)

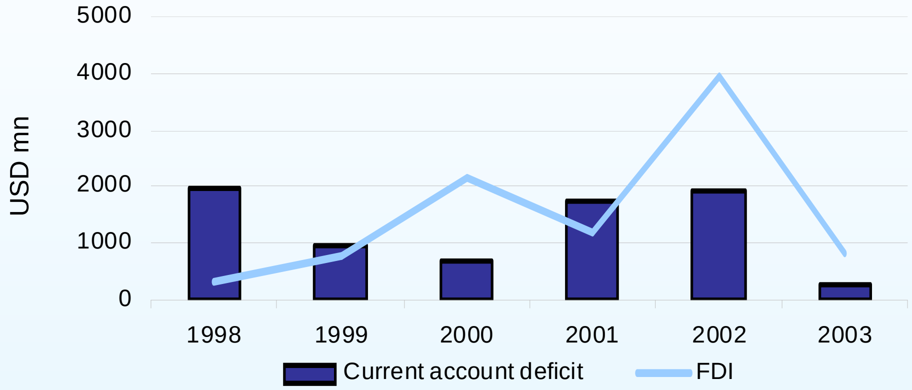


Source: SUSR, NBS

Balance of Payments Improvement

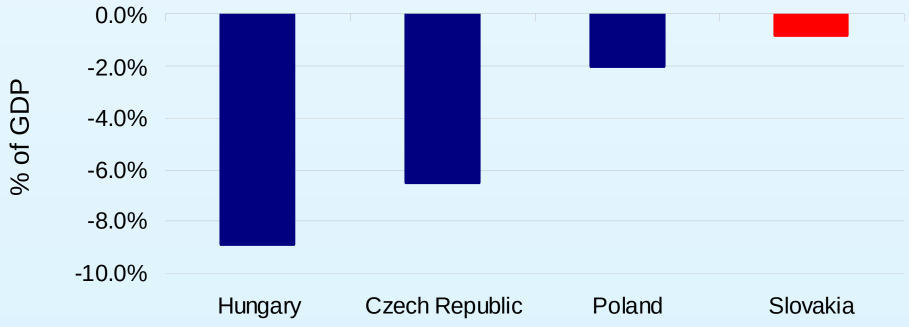
- 1999 Austerity Package reined in the current account deficit
- Sharp current account adjustment to virtual balance in 2003 on the back of 25% export growth
- 61% of total exports go to the EU15 and 85% to the EU25
- Imports largely driven by export growth due to high import component
- Financing needs more than covered by FDI
- Lowest foreign financing need in the region

Balance of Payments Components



Source: NBS

Current Account (2003)



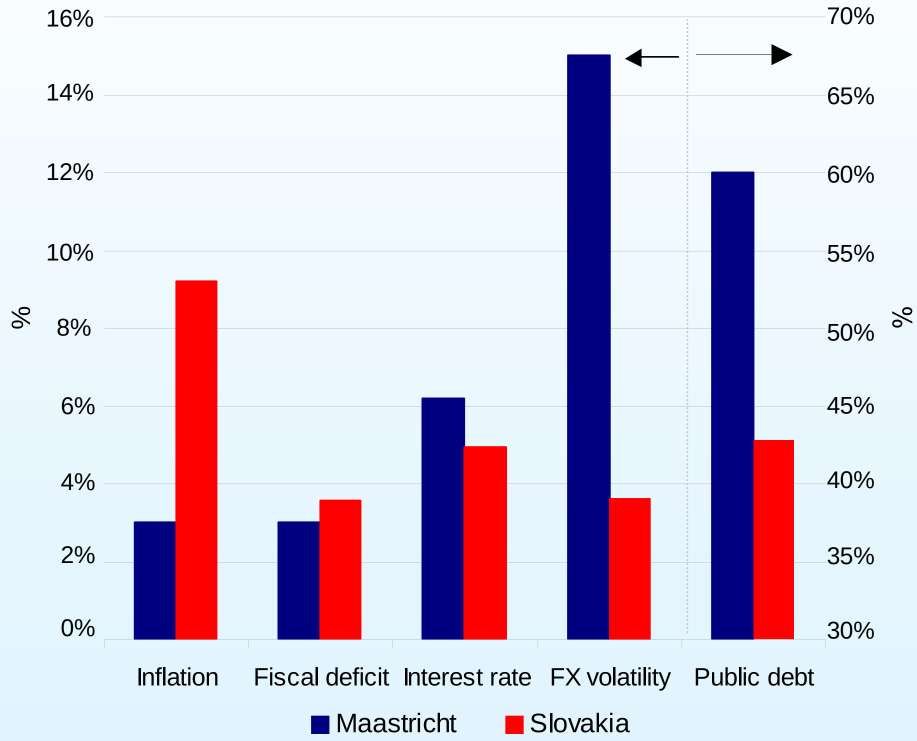
Source: NBS

EMU in Sight

- EMU participation provides incentive for final reform push
- Price liberalisation and adjustment is mostly complete
- Inflation falling off sharply, en route towards meeting the Maastricht criterion
- Fiscal criterion to be met by 2006/07
- Public debt level already below Maastricht threshold

➔ **Expectation to enter EMU by 2008/2009**

Fulfillment of Maastricht Criteria

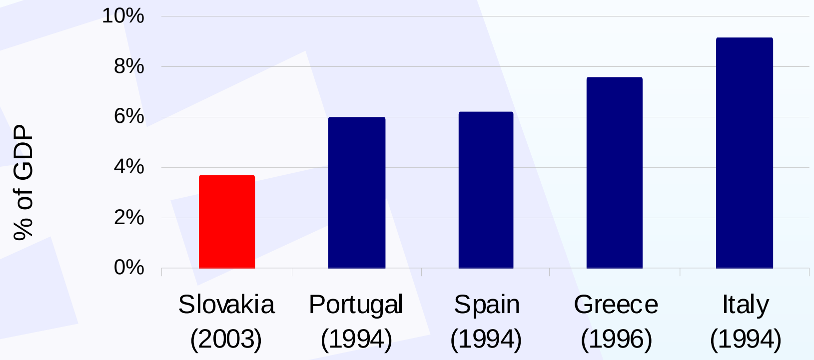


Source: Ministry of Finance, European Commission, NBS, SUSR

Note: FX volatility is defined as the monthly deviation from a 2-yr moving average of the SKK/€ rate as a proxy

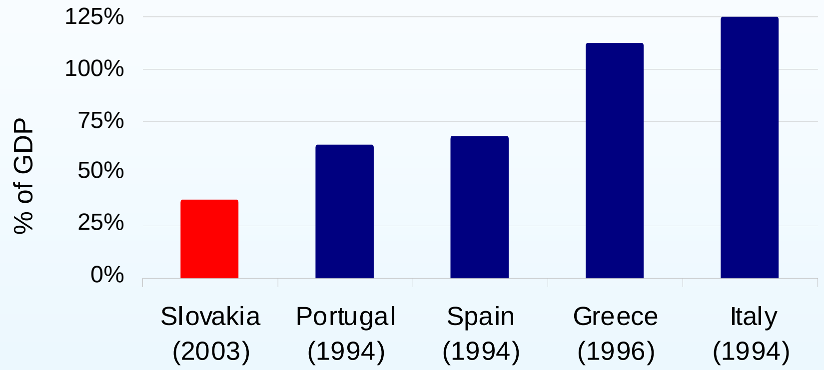
Well Positioned Ahead of EMU

General Government Deficit



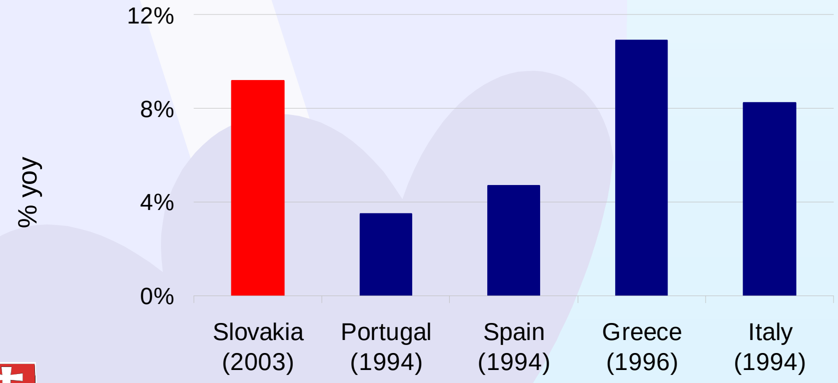
Source: Eurostat, Ministry of Finance

Public Debt



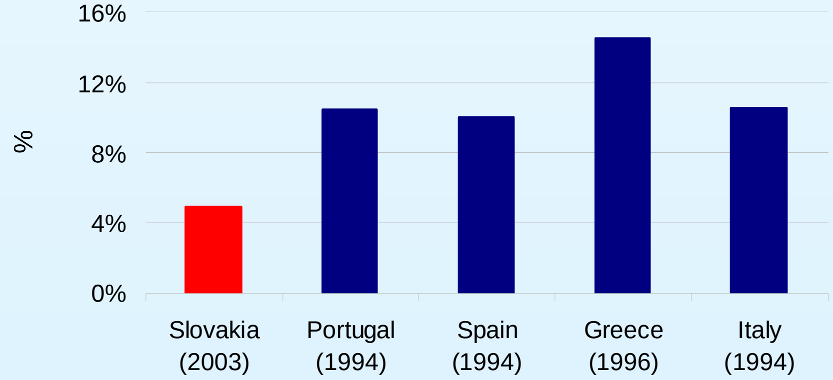
Source: Eurostat, European Commission

CPI



Source: Eurostat, SUSR

Long Term Interest Rate



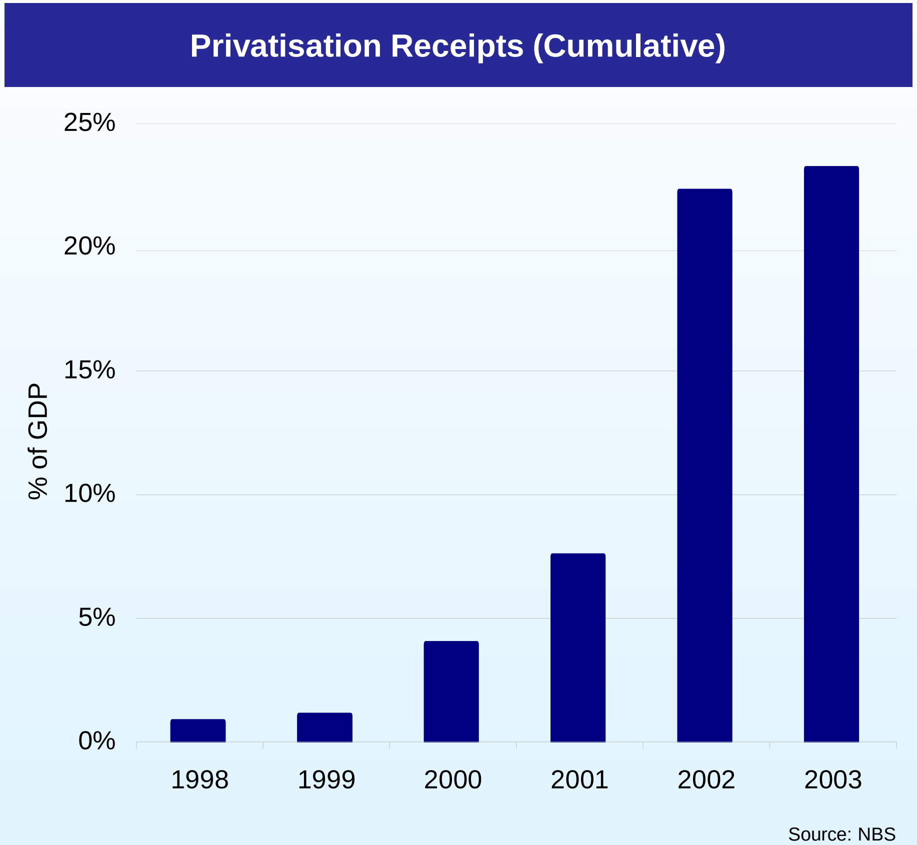
Source: Eurostat, Ministry of Finance

Note: Figures indicate a country's position 5 years ahead of actual or expected EMU entry

Since 2001: Forging Ahead with Structural Reforms

Successful Privatisation

- Privatisation proceeded in two stages:
    - 2000-2001: Banking sector privatisation
    - 2002: Sale of minority (but with management control) stakes in utilities (energy, gas)
- Proceeds used to finance costs of pension reform and repayment of state debt
- Left to privatise:
    - Book value of SKK79bn for sale
    - 60% of book value in SE (electricity) and SPP (gas)



Pension Reform: Well-funded

Key reforms recommended by European Commission to relieve pressures on public financing:

- Provide economic incentives to prolong working lives
- Limit access to early retirement schemes
- Strengthen the link between contributions and entitlements
- Curtail future public spending requirements by instituting more appropriate pension indexation mechanism
- Spread future pensions-related risks across several pension pillars

SLOVAK REFORM IMPLEMENTS ALL THESE RECOMMENDATIONS

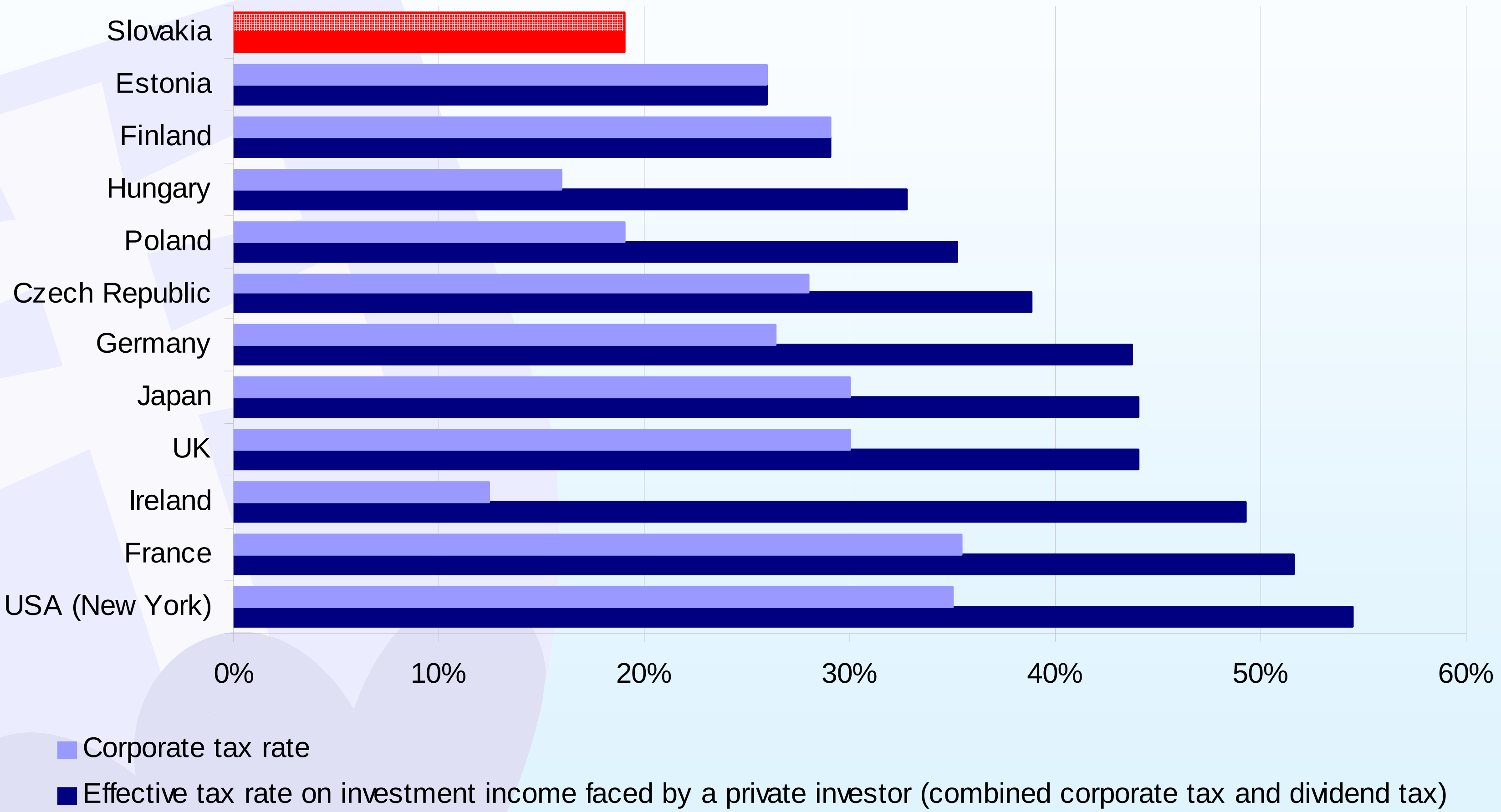
- Through radical reform of 1st pillar (pay-as-you-go pillar)
- Through introduction of the 2nd pillar (private pension accounts invested in capital markets)
- Through improving the regulatory environment for efficient functioning of the 3rd pillar

Tax Reform: Simple and Flat

Created a transparent, efficient and non-distortionary tax system:

- Introduced 19% flat tax on all direct income:
  - Unified five personal income tax rates (previously 10, 20, 28, 35 and 38%)
  - Lowered the corporate tax rate from 25%
- Unified VAT rates into a single 19% rate
- Eliminated virtually all exceptions, exemptions and special regimes
- Eliminated double taxation of income: inheritance, dividend, gift and real estate transfer tax abolished

Tax Rates Faced by Investors



Source: Ministry of Finance, NBS, SUSR

Further Key Structural Reforms

Labour Market and Social Security:

- Dramatically increased labour market flexibility
- Increased employment through incentives that reward activity
- Reduced space for abuse of social benefits schemes

Health-Care

- Made the system financially self-sustainable
- Improving the quality of services provided

Education

- Increased responsiveness of school supply to local demand for schooling and labour market situation
- Increased financial flows into system to expand capacity and improve quality

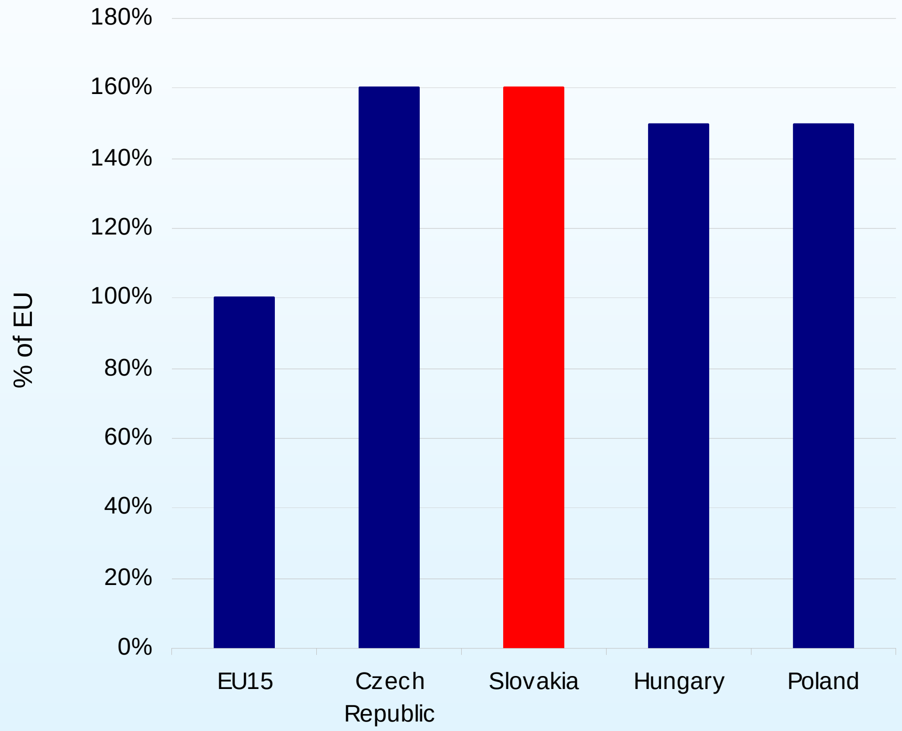
Public Administration

- Improved the quality of public services
- Continued the de-centralisation of public administration

Competitive Industrial Location

- Favorable geographical position
- Highly open and deregulated economy
- Well-educated and highly skilled labour force
- High level of productivity
- Strongly competitive labour costs
- Low degree of labour unrest

Labour Cost-adjusted Productivity



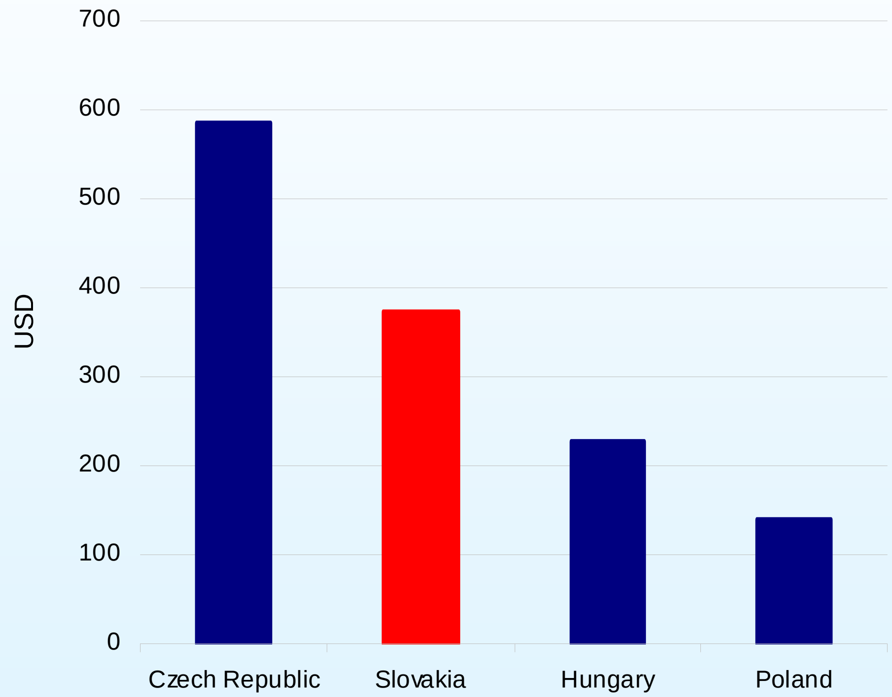
Source: Market Sources

Steadily Growing FDI

Slovakia the location of choice for productive investment:

- One of the highest direct investment ratios in the region
- A well-diversified investor base
- Peugeot Citroen and Hyundai/Kia are to triple car production in years to come, investing in excess of a combined €1.5 bn

FDI per capita (2000-2003 avg)

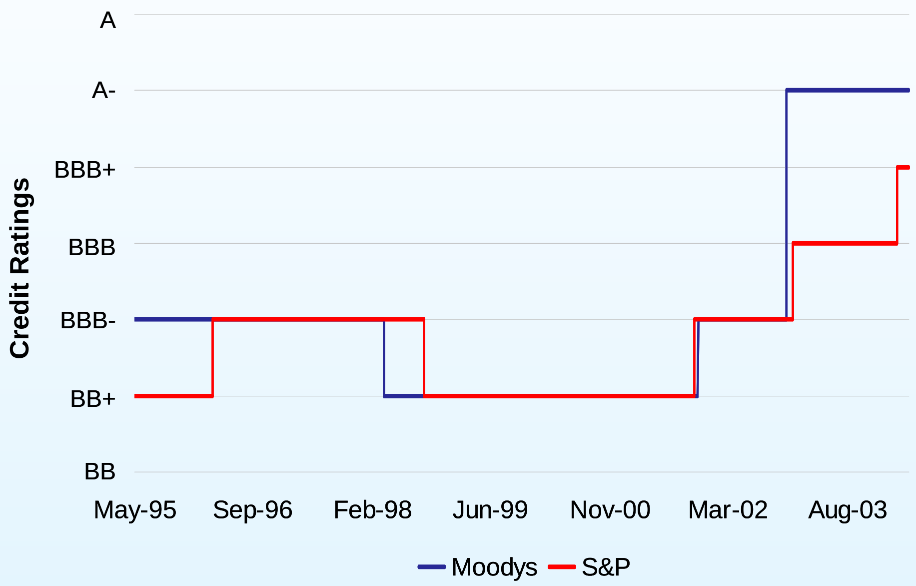


Source: Ministry of Finance

Upward Rating Trajectory

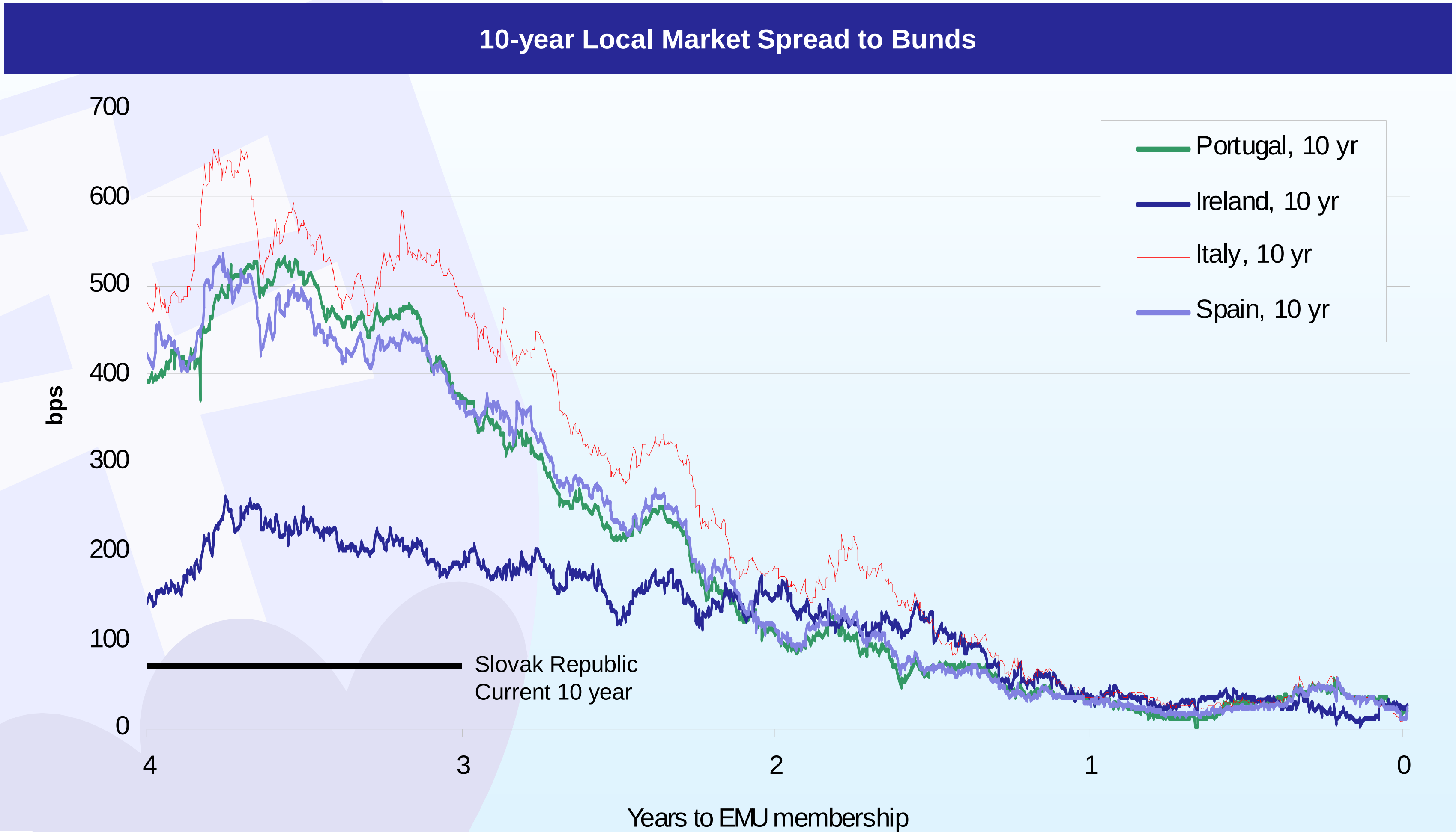
- Slovakia's reform efforts have been recognised by the rating agencies through a series of upgrades
- Slovakia first regained its investment grade rating in 2001
- Further upgrades have followed, with Moody's rating Slovakia A3 and S&P BBB+

Credit Rating Dynamics



Source: Standard & Poor's, Moody's

Debt Performance – Market Ratification



Note: Local Currency Market

Source: Bloomberg

Debt and Liquidity Management Agency

- Established as part of the reforms aimed at creating a state-of-the-art platform for debt and liquidity management, based on the best international practices

- The role of the Debt and Liquidity Management Agency:

    - Provide professional debt and liquidity management for cost optimisation

    - Separate operational debt and liquidity management from policy formulation and regulatory controls

    - Maintain permanent dialogue with financial intermediaries and investors

    - Develop a flexible approach to debt management

    - Support the integration of Slovak financial markets and the management of Slovak public finance within the European Union