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Economic and Social Context of Slovakia's Integration into the EU

Summary

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Economic and Social Context of Slovakia's Integration into the EU
Summary

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Introduction

The Slovak referendum on the EU accession has confirmed the fundamental civilisation decision on the long-term direction of our socio-economic development. This has accentuated the urgent need of a responsible comprehensive preparation not only for accession but also for the post accession stages in compliance with the differing time demands of the integration adaptation even more. Impact studies are the key essential part of the comprehensive preparation.

As the relevant conditions and factors are subjects to evolutionary changes in our economy, as well as in the EU, other candidate countries and also in the globalising world economy, the impact studies need to be updated cyclically. They can, figuratively speaking, be compared to a compass which allows strategic orientation to a moving target.

The Institute of Slovak and World Economy of the Slovak Academy of Sciences elaborated the first national-economy oriented impact study in the first half of 2002. Its basic objective was to draft a relatively compact, *initial* scientific argumentation of the economic and social context giving reasons for the existential justification of the political-strategic direction of Slovakia to the EU. The impact study presented by the ISWE SAS in 2003 links up with the last year study and responds to the development of the situation in the preparation for the EU enlargement in the Slovak Republic, candidate countries and Member States and globalisation processes as well. Its basic objective is *deepening* of scientific arguments supporting the requirements for a pro-integration adaptation of our economy and to contribute, thus, to the so much needed more realistic understanding of integration opportunities, chances and advantages, integration risks, threats and disadvantages. The point is that in many important areas the ideas of: advantages and disadvantages as being given, of benefits coming more or less automatically and of being essentially helpless against the disadvantages, persist. The fact that integration represents, on the one hand, mainly chances and opportunities that must be seized and, on the other hand, is linked with certain risks that *must be* identified and minimised on time, is being ignored overtly and also covertly. The irreplaceable premise of the necessary creative approach to conceptual programmed identification, creation and rational use of integration opportunities, which only then acquire the form of concrete benefits, is often left out of account. And vice versa. A passive waiting approach combined with the incapability to see where the opportunities are and how to use them combined with the incapability of early risk warning and risk management - all this becomes a real disadvantage at the end. One should not forget that the integration process is a unit of economic co-action allowing achieving synergic effects, and economic competition for integration and non-integration effects. From the viewpoint of the theory of games, it could be said that the integration process is basically a game with a win-win result in which all parties gain. However, depending on the capacities and readiness of individual participants also zero-sum games - in which those who are capable and ready gain to the detriment of those less capable and less ready - may occur.

Thus, the integration advantages and disadvantages are not something static that grows from itself, but they represent a dynamic process with various combinations and alternations of positive and negative sides depending on the adaptability, with which the integrating entities respond to occurring opportunities and chances as well as to emerging risks and threats.

Another exceptionally important aspect of a necessarily more realistic approach to our participation in the integration process of the EU results from an insufficient consideration of the fact that our economy with its whole structure, all hierarchic levels and entities, that should participate in the shaping of our integration strategy appropriately to their place and tasks, joins the integration. Experience from other countries that use the benefits of integration in a successful way shows that they arrived to an integration strategy through a multi-level, structured and interactive process. In this process central bodies, businesses and regional authorities, sectoral, employees' and other relevant interest groups, analyse their integration positions, communicate with each other, coordinate their approaches and harmonise their interests to define their integration strategy in their relevant field of activity and, at the same time, to participate in the consensual generation of an overall national-economic strategy of the participation in the EU integration process. A good quality of formal and also informal communication and co-operation of all levels, structures and interest groups with corresponding EU bodies and structures as well as appropriate co-operation with bodies and institutions of those countries that have achieved or are achieving results worth following in the exploitation of integration opportunities, plays an important role in it. It is a method that contributes not only to a more adequate formulation of integration intents but it also improves their passing through the approval procedures in the EU bodies. In this context, the preparations for EU accession in Slovakia have so far suffered from several serious gaps and deficiencies and show a rather campaign-like approach than a systematic systemic one.

Accession requirements formulated by the EU with respect to granting integration assistance from Structural Funds and Cohesion Fund show a critical mirror up to several problems in the transformation of our economy that are not resolved or coped with. The European Union anyway requires manifesting a convincing knowledge of one's own needs, the capacity to make effective use of assistance in their efficient addressing and also the capacity of the country concerned to achieve synergic effect through a rational economic policy and effective use of assistance when investing domestic resources and those of the EU. Serious difficulties in the drafting and approval of the National Development Plan and Sectoral Operational Programmes signal not only lagging behind in the whole system of EU funds drawing but also serious gaps in the transformation of our economy in which a compact economic strategy is absent.

Mentioned weak areas represented one of the main factors influencing the selection of topics for the presented impact study. In addition, it was necessary to include deepening of argumentation and verification of some premises covered in the first impact study and reflections on some launched changes or the ones under preparation in the functioning of the EU integration mechanism into its content.

The study starts with the analysis of the main features of the external environment in the stage of Slovakia's EU integration. It continues with a description of the requirements for the forming of institutional framework for the Slovak economy functioning and with an identification of the Slovak economic policy main tasks under integration. In this context, the issues of Slovakia's preparation for the European Monetary Union (EMU) accession are examined. The study pays particular attention to the regional aspects of integration in the Slovak environment. The subsequent parts of the study focus on the updating of the position of the Slovak economy in terms of its performance and quantification of the effect of integration on the development of our economic structure. The view on the enterprise sphere and its prospects in the EU accession context is being updated. Special attention is paid to deepening the analysis of effects on the foreign trade from the participation in the EU customs union as well as the effects of EU accession on the foreign direct investments (FDI) inflow.

The final parts of the study elaborate on the open issues in the labour market and on the social dimension of integration and updating of the effect on Slovak agriculture from the implementation of the common agricultural policy.

The nature of impact studies denotes that neither this study can give an answer to the whole spectrum of issues linked with Slovakia's EU accession. Linking up with the last year study, this presented one - having the objective to contribute to policy orientation and intensification of works with a view to achieve the desired level of preparedness for EU accession - elaborates on, enlarges and deepens the analytical view on selected national economy links in the accession of Slovakia to the integration grouping of European countries.

The following parts present a brief summary of the main results arrived to in the individual examined areas on the basis of the *Economic and Social Contexts of Slovakia's Accession to the EU* study.

Main features of the external environment in the stage of Slovakia's EU integration

The need to make an understanding of factors determining the development of the external environment and thus also the conditions and consequences of Slovakia's EU accession more realistic is growing even more with the coming date of the largest EU enlargement. From this perspective it is useful to distinguish and examine the following group of factors:

- fundamental influence of globalisation processes and qualitative mega-competition on the EU and the consequent high requirements on its global adaptation;
- on-going and prepared reforms of the EU functioning mechanisms;
- convergent position of Slovakia among the candidate countries.

The nature of globalisation and its decisive influence

The characteristic feature of the whole pre-globalisation development of the economic life internationalisation was the derivate nature of external or better to say international relations and also of the world economy system was derived from the decisive features of state entities economies.

The specific content of globalisation consists in the qualitative turnover in the long term evolution of internationalisation. The material prerequisites for this change were created through a revolutionary transition to a new manufacturing technology, exchange and information technology based on a broad spectrum penetration of information and telecommunication technologies in all areas of the life of society. This has opened the unprecedented possibilities for overcoming the restrictions caused by time and space in global development of economic activities. The process of internationalisation is rounded off by its extent surpassing the critical threshold in which the cumulating quantity of internationalisation of state economic structures enters a new quality - the forming of a *planet-wide* structure. Its creation means that the primary and decisive nature and significance of economic relations and processes moves from the interior of state entities to global economic relations and processes in which the transnational “players” - the transnational corporations (TNCs) - hold a key position and influence.

In addition to the determining direct influence of an increasingly smaller number of global mega-companies on the running of national economies, their strong indirect influence on the governmental bodies of individual states and international organisations and institutions so that they adjust legislation, the rules and focus of their activities to the interest of largest and strongest global corporations, is also important. Thus, globalisation dictates the logics of the development not only for national economies but even large regional integration groupings like the EU must adjust to the relentless pressure of globalisation trends.

Besides the TNCs as decisive components in the structure of globalisation processes, the creation of strong regional integration groupings that are becoming internally more homogenous areas allowing more intense transfers and links and, thus, a higher efficiency of economic activities, also plays an important role in the forming of the global world economy. Their characteristic feature is forming around one or several economically strong state entities - NAFTA (U.S.A.); ASEAN (Japan) and the EU (Germany and France).

Economic competition of the three centres of world economy

When joining the European Union it is necessary to take into account that the Union is also a part of globalising world economy where it is confronted with the exceptionally demanding mega-competition, especially with the U.S.A. and Japan. The EU position in the competition of the three centres of world economy has and will continue to have a fundamental influence on the further development of the integration process, its priorities and conditions. For this reason it is also relevant in the context of the candidate countries' interests. The data on the development of the economies of the U.S.A., EU and Japan exemplifies a long-term declining trend in the average annual growth rates of real GDP in the individual decades from 1950 to 2000. At the same time it reveals significant differences in the declining performance rates of their economies. The deepest drop was experienced by Japan from 8.83 % to 1.37 %, more moderate, however, still an almost two and a half times drop from 4.91 % to 2.06 % was characteristic for the EU 15 and that has been relatively very unfavourable in relation to the U.S.A. where the decline was only from 4.41 % to 3.19 %.

From the EU perspective the growing gap of the scissors effect between its economy performance and the one of the U.S.A. is worrying. According to the projection by renowned foreign institutions the expectation is that even after the year 2000, except 2001, the US economic growth rate will be ahead of the EU by more than one percentage point till 2004.

The long-lasting EU lagging behind in the economic growth rates when the GDP per capita is only at approximately 75 % of the US level, and after the enlargement by 10 countries with a lower level it will even drop more significantly, is a serious problem for the integration community. The EU Member States lag significantly behind in the macro-economic as well as the micro-economic competitiveness. According to the 2002 World Economic Forum competitiveness rank the U.S.A. holds a clear primacy in both cases. US advance started to be gradually visible from the 1970s and it has been based on a higher efficiency of adaptation processes conditioned mainly upon the depth and frequency of technological innovation, generated by a generously supported scientific technological development, encouraging business environment and highly efficient system of brain drain from all over the world. The United States ranks among the countries with the highest R&D expenditures as a share of GDP and are significantly ahead of the EU in this field.

The most important advantage of the U.S.A. in the competition with the EU has, however, been their political and economic compactness and a single goal-dedicated economic policy that Europe has been unable to reach even after 40 years of integration. The competition with the U.S.A. will be a very demanding strategic priority for the EU. Its goals and means of its fulfilling will essentially affect the development in the EU and will also significantly influence the nature of the conditions in which the new Member States, Slovakia including, will find themselves.

The basic direction of the reforms in the European Union

Global mega-competition necessitates the categorical request for improving the competitiveness of the EU as one entity, all its Member States and companies. The comparison with the U.S.A. shows that the key prerequisite for a substantial progress in competitiveness is the forming of the EU as a compact economic complex with an internally harmonised business environment. To achieve that, the EU plans to implement a whole range of fundamental reforms in the field of taxes, banking, financial and capital markets, pension systems, labour market, agricultural policy, public administration and its funding, compliance with the Stability and Growth Pact (SGP) and creating of new principles and mechanisms of decision making processes and also functioning of EU institutional structures within a horizon of 2003 – 2006 period. These reforms should be completed in such a way that they would be fully implemented in practice in the period of the 2007 – 2013 financial framework.

The implementation of the outlined reforms and their effectiveness is tangibly complicated and relative in several aspects in the concrete conditions of the EU, its Member States and the Candidate Countries. The basic reason is the discrepancy between the need to create a compact and homogenous economic environment through an effective harmonised and uniform economic policy on the one hand, and the objective differences in the performance of national economies and their integration maturity, approaches of the individual Member States and their governments often affected by their unwillingness to compromise, excessive advancement of various specific, grouped, short term and other interests, on the other hand. A whole range of problems and risks in the deepening and enlargement of the integration process, relevant also in terms of the candidate countries accession to the EU, results from it.

They are connected with a continuing recession and stagnating recovery and the resulting manifestations of protectionism; the tendency to half-reforms, re-assessment of contributions to the EU budget and the volume of funds for Structural Funds and the Cohesion Fund.

Recession, significantly slowed down economic growth and threatening deficits have a negative effect also on that sphere of the integration process where the harmonisation and homogenisation of the economic environment progressed the most, i.e. on the EMU. Several countries of the Euroland have serious problems in complying with the Maastricht criteria and Stability and Growth Pact.

The difficulties and intricacy of the economic development in the EU, challenges in the implementation of its reforms and the functioning of the EMU are reflected in the modifications of conditions for candidate countries accession, where this may represent several risks.

It is obvious that the conditions under which the current candidate countries join the EU will be significantly more demanding and complicated than it was during its previous enlargements. They will put more requirements on national budgets, own resources and loans of states, regions and businesses. The real drawing of EU funds and the overall useful exploitation of benefits from incorporation in the integration process will probably be significantly lower than the original expectations. The conclusion emanating from the concurrence of these effects is that it is highly probable that the candidate countries will realistically be capable to draw only a half of the amount devoted (42 bn EUR for 2004-2006).

Convergent position of Slovakia among the candidate countries

The candidate countries represent - before as well as after their entry into the EU - potential and also real allies and competitors in many respects. In this context it is important to identify our relative position among them. In the study, we have analysed it by 11 indicators in relation to the Czech Republic, Hungary, Poland and Slovenia. The most comprehensive picture of Slovakia`s relative position among the other candidate countries is provided by the Transformation Effect Indicator and the European Convergence Indicator.

The transformation effect calculated as a difference between the volumes of imported crude materials and fuels (SITC 2 + 3) and exported manufactured products (SITC 6 + 9) in € per capita was € 1,969 in Slovakia, € 2,799 in the Czech Republic, 2,595 in Hungary, and € 4,117 in Slovenia, in 2001.[1]

The European convergence indicator expresses the overall convergence position among the selected candidate countries as well as to the EU average in a synthetic way.

T a b l e 1
The European convergence indicator – June 2002

	Real convergence	Institutional convergence	Monetary convergence	Fiscal convergence	Total
Czech Republic	90	70	90	65	78
Hungary	85	80	80	70	79
Poland	65	75	85	55	69
Slovakia	55	75	80	75	69
Slovenia	100	80	75	65	79

Source: [27].

Slovakia, achieving 69 points together with Poland, has the weakest position among the V4 countries in terms of the total convergence. However, the significantly largest discrepancy between the real convergence on the one hand and institutional, monetary and fiscal convergence on the other hand, is a more serious problem. It seems that the measures of economic policy due to which the convergence level in institutional, monetary and fiscal area increased, have not been sufficiently effective in relation to real convergence which shall, however, be decisive at the EU accession and after it.

[1] This indicator is suitable only for comparing countries of a size the same in order; in our case with the exception of Poland. Transformation effect per inhabitant achieved by Slovakia is significantly lower than in Slovenia - by approx. € 2,400, in the Czech Republic and Hungary (approximately by € 900 – 1,100). The significance and weight of this problem is underlined by the fact that Slovakia has a very open economy (more than 150 %), which is more than most of the candidate countries and also EU Member States.

Forming of the institutional framework of the Slovak economy functioning

The institutional environment makes the activities of companies either easier or more difficult and, thus, it changes their costs, especially transaction and information costs. It also contributes to the attractiveness of a locality or a country for potential investors. In the long-term horizon, it participates in the generation of differences in the economic performance of the regions and countries. Not only the initial state of institutions, but also a dynamism of their changes and their convergence rate with the institutions in particular in the European Union Member States, are of importance.

The purpose of the institutional reforms is to introduce fairness, freedom, accountability, solidarity and the rule of law to the life of the society and at the same time to eliminate phenomena, which are in a conflict with these principles. Public administration institutions play an important role in this respect; its reform is therefore an irreplaceable element of institutional framework forming.

The EU accession means adopting of laws and standards that change the matrix of institutions affecting our citizens and companies. While the current form of the EU is a result of political compromises, its legislation and goals are significantly influenced by the economic interests of individual actors. The power and capacity of a country to put through own interests differ, and therefore the results of the efforts pursuing change or maintaining the rules differ as well.

In the negotiations with the EU, the Slovak Republic will be able to enforce its interests (interests of the population and companies) only through a responsible assessment of the possibilities, challenges and formulation of own standpoints. The accession changes, which are the starting point for the change of the public administration conception, mean a gradual limitation of state competences in some areas on the basis of the EU Treaty itself and also on the authority of intervention into national legal orders.

The current nature of changes in the world prefers countries that have institutions, administrative system and companies prepared to respond to changes and make use of them in a flexible way. Thus, smaller countries can also gain effects thanks to their social capital and capacity of a country to identify world trends, adapt to them or influence them. The companies must have created an effective lobbyist structure that will influence the representatives of the European Parliament, members of the EU Commission, industrial associations and national politicians in a legal way. The knowledge of the Union mechanisms functioning, creation of legislation and forms of effective influencing of the activity of its bodies shall allow them to advance their interests. A diversity of the Member States and their actors gives also a room for flexible creation of international coalitions. Advancing own interests at the level of the Union is exceptionally important because a common policy adopted in the whole EU can have a more extensive and longer effect on the economy and companies than the economic policy measures taken by own government. In the EU Member States, a whole range of associations pushing through the interests of companies, sectors and interest groups operates. Low organisational density or low influence of some interest groups usually allows stronger entities to advance their interests to such an extent that they jeopardise the interests of other groups. EU membership will therefore force our enterprises to organise their interests and to respond to the changes in the Union in such a way that they will have the long-lasting benefits from it.

A differentiation of the needs of companies, inhabitants and regions also requires flexibility of public administration in relation to the local and regional needs. Up-to-now functioning of public administration has caused many problems that contributed to the growth of unemployment and deepening of regional disparities. A transfer of the part of competences and control over the territorial self-government bodies is a way to a more effective operation of the whole public administration system, which would be also reflected in a higher economic performance. Flexibility of all entities will be needed not only for the competition among companies, regions and countries but also for using the funds from the structural funds for Slovakia.

Institutional changes affect the domestic sector in various ways. Some of them create an environment that improves the position of most of the enterprises, the other have a differentiated impact on individual firms. Other changes result in broad disadvantages for domestic enterprises caused by (a) increasing the costs inadequately to the performance of the economy and (b) containing the measures our entities are more sensitive to than the foreign ones. Some changes, thus, contribute to the improvement of the overall business environment and national economy effectiveness while others may reduce the competitiveness of domestic enterprises. Governmental support to enterprises granted by the current EU Member States is being gradually downsized, however, in our environment weakening of some stimuli may have an adverse effect on the position of our industry.

Areas that require high adaptation costs are mainly occupational health and safety, ecological standards and consumer protection. Public orders the opening of which to foreign competition has been postponed in the EU for a long time are also an important area. Before drafting a new legislation, the government must consult their ideas with the interest groups, just as it is in the EU. If the interests are well-organised, the companies may acquire legitimate state support for their interest. The state should therefore support interest groups` forming, organising and also their activities.

Creating an institutional framework compatible with the systems functioning in the EU is an important component of Slovakia's preparation for the membership. It is a highly structured process including a whole range of components with a different time term needed for implementation. Adopting more than five thousand directives and regulations of the Union is an intricate problem also for current Member States taking into account that hundreds new changes are added each year. The transposition of EU legislation varies also in its Member States. Countries that have had lower levels of transposition recently, have gradually caught up with their partners; for instance Italy and similarly Greece or Portugal have improved this rate from 82 % (in 1990) to 94 % (in 1999).

Slovakia's process of pre-accession negotiations of its EU membership conditions was concluded rapidly and adopting EU legislation was swift. However, adopting EU legislation has also certain risks. The first risk is connected with the costs of the society on its application. If the changes result in higher costs for enterprises then the law enforcement system must also be adequate. The missing administrative capacities may cause an absence of the effects expected from the changes. Therefore the relevant capacities must also be reformed and the matrix of institutions adjusted. The second risk is linked with a small support to changes by the public. This can be manifested in the failure to observe laws and in the costs of the state spent on their enforcement. In order to eliminate both mentioned risks the EU legislation drafting is based on democratic principles and harmonisation of interests of various countries and interest groups already at the time of legislation drafting.

While adopting EU legislation, the Slovak Republic has become a part of the "Europeanisation" process. Adapting to this process may change the division of resources and power at the level of the society and it leads to the internalisation of standards and the development of a new identity. However, changes of legislation are not only related to the adaptation to the EU conditions but also to the need to replace obsolete legal norms after the change of the political and economic system.

Many countries take the way of fiscal decentralisation that gives the citizens a larger participation in the administration of public affairs and the public sector a better response to the needs of the citizens. The change of the system in this respect means not only the restriction of central government's position but it also requires many partial reforms in particular the simplification of the tax system, transparent links between the state budget and other components of public finance and strengthening of competence and responsibility of self-governmental bodies of public institutions as well as enhanced labour market flexibility. Distribution of responsibility in the safeguarding of public goods among the citizens, local governments and local state administration will help the government to concentrate on the conceptual national economy policy tasks.

Main tasks of the economic policy in Slovakia's EU integration context

The EU interventions into the national economic policy that Slovakia voluntarily accepted when deciding on its accession to the EU comply, in principle, with its own interests and leave room for shaping its own economic policy. It is equally valid that the EU is becoming an entity co-determining the economic policy of Slovakia. The study pays attention to the manner in which the EU influence has been and will be manifested in selected areas of Slovakia's economic policy. Not only macro-policies (monetary, fiscal, wage and banking policies) but also industrial and innovation policies, to which only marginal attention is paid in this country in contrast to the EU, U.S.A. and Japan, have also been examined.

The year 2000, when the NBS started to introduce the so-called quality management in which the 2W REPO rate and interest rates for one-night sterilisation and refinancing transactions were used instead of monetary aggregates as the basic tool, was a decisive milestone in the implementation of the NBS monetary policy.

The NBS monetary policy is made more complicated by some specific factors - adjustment of regulated prices, substantial sensitivity of domestic prices to foreign prices and foreign capital influx (the need of extensive sterilisation measures). Compliance with the monetary programme may be further made complicated by pressures on the appreciation of the crown, slower economic growth of main business partners and volatile oil price development outside the OPEC reference area.

NBS currency policy will certainly be influenced by Slovakia's EU accession and later by the membership in ERM II that will be linked with determining the central parity of the Slovak crown exchange rate. Preparation for EMU membership includes important changes in the monetary policy of the NBS, which must be fully compatible with the European Central Bank (ECB) monetary policy at the accession. The National Bank of Slovakia made important steps on this road in a difficult situation. A joint document of the NBS and Slovak

Government – *Slovakia's Strategy for joining the European Monetary Union* is a prerequisite for the further successful advancement.

In contrast to the monetary policy that is administered by the ECB for the whole Euroland, fiscal policy stays under the competence of Member States. In order to support macroeconomic stability and thus also for the benefit of achieving common monetary policy goals the EU adopted (in Maastricht 1992) and detailed (in Amsterdam 1997) a binding criteria for public finance results assessment (nominal convergence criteria). The European Union influences and co-ordinates the way in which fiscal policy is administered in Member States by determining the common development goals of the Union, recommendations, discussing stabilisation, convergence and pre-accession economic programmes drafted by Member states and candidate counties.

Public finance results with respect to criteria values are topical for Slovakia due to its commitment to accede to the EMU. Most EU Member States needed 5 – 7 years to achieve them under favourable internal conditions (standard market economies) and more advantageous phase of world economic boom. Based on this experience and the understanding of the scope and costs of the expected structural reforms in the Slovak Republic it is clear that compliance with the fiscal convergence criteria in 2009 – 2010 would be a success of the Slovak economy.

After EU integration, the wage policy will also be primarily determined by national actors - policy of the government and social partners. At the same time the risk of using the wage policy for goals, which are not compatible with the support of economic stability, persists.

The wage policy should, as a priority, focus rather on the support of employment growth and the stability of the economy than on influencing wage structures, relative wages and wage differentiation (distribution should not be a priority). Wage policy oriented on employment should be complemented with such social, tax and employment policy the goal of which will be the elimination of discouraging factors and barriers restricting the labour market.

The wage policy will have to create a contribution to the stabilisation oriented monetary policy. After Slovakia's accession to the EMU, the domestic wage policy will have to take into account that the central monetary authority will not be in a position to respond to excessively growing wages with an accommodating pecuniary policy. Depreciation of currency that would respond to an excessive growth of nominal wage can also be not considered. Each change of the national level of nominal wages will therefore have a direct effect on competitiveness.

In the last decade the banking sector acted as one of the most dynamically developing sectors intensely involved in the integration processes in Slovakia. The globalisation context like the processes of interlinking, approximation and convergence of national economies including the banks were manifested in them more clearly. Therefore these processes will also determine the further destiny and development of Slovak banking in a decisive way in the coming years.

Strategic reflections on further development of the banking sector in the EU point out the need to devise institutional conditions for its functioning including the central bank activities, public sector funding, banking supervision in the EU national elements, banking legislation harmonisation problems, development of competition in the banking sector and its regulation.

The financial services sector is going through a process of fundamental changes in the EU. They are linked not only with the financial services liberalisation process but also financial crisis risk reduction and quality improvement of services provided for the business sector. The objective is to establish uniform criteria for the participants in financial markets and to interconnect the banking sector, capital markets and other forms of financial services more closely. The introduction of new prudent banking rules resulting in the deregulation of funds that were under regulation so far and the process of coordinating capital markets should play an increasingly more important role in the funding of enterprise development. This process should significantly simplify the financing of the enterprise sphere and, thus, increase the dynamism of the EU economic growth.

The innovated EU industrial policy will, as a priority, focus on the strengthening of processing industry competitiveness on the basis of three key factors - creation and accumulation of knowledge, implementation of innovation, business initiative. Its goal is creating necessary framework conditions allowing the enterprises to develop initiatives, materialise their ideas and utilise their opportunities. Its task is also to follow the contribution of other policies to the competitiveness of the European industry.

In the effort to fully utilise the candidate countries potential for convergence, *the horizontal tools of industrial policy are supplemented by concrete measures focused on weakness of the candidate countries industry.* First of all they should ensure smooth integration of the industry into the single market and support its sustainable growth and long-term catching up with the labour productivity and competitiveness; while assuming that the comparative advantage based mostly on low labour costs *is neither sustainable nor desirable in the candidate countries in medium term.*

It is a challenge for the economic policy of the Slovak Republic to newly formulate its industry policy corresponding to the EU integration and also to create a whole range of policies in other areas which have been completely neglected until now. They include mainly innovation policy without which achieving qualitative changes in industry is unthinkable.

The March 2000 Lisbon European Council meeting identified technological development and innovation as the key factor of economy competitiveness. Consequently it recommended that this issue should become a part of enterprises policy and also national governments policy as well as of the European Union as an entity. This also applies to the candidate countries striving for EU accession.

In this respect the situation in Slovakia is definitely not the most favourable. In spite of technological delay and low share of innovating companies compared with the EU Member states, a compact technology and innovation policy is still absent. In economically developed countries it has even went through three generational changes already. From the first generation linear model with a primary emphasis on the development of science, research and development, through the second generation stressing the support to transfer and diffusion of acquired knowledge and innovation into national economy to the third generation based on the needs of a knowledge economy. The tasks and goals of the technology and innovation policy are shifting to the centre of all areas of economic policy with emphasis on their harmonisation and co-operation. The support to technological development and innovation proper is carried out by influencing the demand and supply sides and by creating a favourable business environment.

Slovakia's preparation for European Union accession

Slovakia's EU accession is linked with the ambition to accede to the European Monetary Union that started to really function from 1 January 1999 and it currently includes 12 countries. The European Monetary Union faces the new prospects of its further enlargement by the new EU Member States including Slovakia.

Compliance of the EMU with the Optimum Currency Area (OCA) criteria has been often discussed not only before the creation of the EMU but also today. These assessments are not easy because there is more than only one criterion to assess the benefits of a monetary union. Monetary Union functioning is assessed mainly from the perspective of asymmetric shocks absorption. The OCA criteria are criteria of sound developed market economies and therefore they are still topical. Concerning the European Union as an entity, the existing analyses in general agree that it does not form OCA. Only the sub-group of countries forming the so-called European Monetary Union hard core could be characterised as the optimum currency area.

The four-year history of the EMU so far confirms that no major disturbances have occurred and that the single monetary policy of the European Central Bank (ECB) has been quite successful. The first serious check of EMU stability has been the recent recession, the even more difficult test will, however, be the accession of several central and eastern European countries. Currently the ECB must cope with the shock caused by euro exchange rate strengthening and a rapid drop in the US dollar exchange rate.

Achieving membership in the EMU assumes implementing such economic strategy that will be aiming at compliance with the Maastricht criteria. Inflation is one of the criteria Slovakia is still failing to comply with. The government and the NBS should harmonise their anti-inflation strategy that should take into account also nominal convergence.

The most demanding tasks in the convergence process shall undoubtedly be the compliance with fiscal criteria, i.e. state budget deficit and state debt. However, the main challenge will rather be creating conditions for sustainable development of public finance in terms of stricter Stability and Growth Pact requirements, than an early compliance with these criteria before acceding to the EMU.

The prerequisites for compliance with the interest rate criteria are more favourable, however, larger difficulties may appear in observing exchange rate stability criteria if the fluctuation zone of exchange rate deviation of countries in the ERM II shall be revised.

Slovakia's approaching to the European Monetary Union will also be determined by other factors - first of all by the implementation of all necessary reforms, progress in real convergence and fulfilment of criteria developed on the basis of the OCA theories.

The views on the date of EMU accession and the accession process strategy differ. The current discussion on possible Euroland accession strategies often concentrate on accession speed and from this perspective the difference is made between the quickest possible accession strategy and the strategy aiming at a slower European Monetary Union accession. In the forming of the accession strategy, however, the criterion of accession process speed should not be the only absolute quantity. The effort should be to draft a balanced, optimum accession process strategy that has as its priority the sustainability of the catching up process, which, again, requires a long term macroeconomic stability.

In case of Slovakia the strategy of the fastest possible accession to the European Monetary Union would not be the optimum one mainly a) with respect to the immense risks connected with a speeded up fulfilment of fiscal criteria in the stricter PSG requirements environment and b) with respect to the need of a longer time interval for finding a balanced Slovak crown exchange rate. The prospects of a prolonged accession process in the Czech Republic and Poland do not support the fastest possible accession of Slovakia in the monetary union, either. A monetary union means a fixed setting of basic parameters not only in the monetary policy (defined by the ECB) but also in the fiscal policy (stricter PSG requirements) that would be difficult to accept for countries with a very low level of nominal and real convergence and a still unfinished transformation. Today even some EMU members (Germany, France, Portugal) are not satisfied with the rigidity of the Stability and Growth Pact.

Regional aspects of the integration in the European Union

The socio-economic dimensions of disparities, the long duration of regional equalisation and its political sensitivity require regional policy to become one of the core policies of the government. The second pillar of its successfulness is an active participation of regional and local self-governments. In our view, Slovakia's regional policy strategy and within it also the regulation of EU support policy from the structural funds has two dimensions:

- the *first* includes mutual balance and dynamism of relations between the *growth and equalising aspect* of regional (and also national-economy) strategy,
- in *the second* it concerns the focus of regional and national economy policy on the growth of *competitiveness of regions.*

The process of gradual catching up with the European average at the national-economy level and an increasing regional divergence inside the less developed countries is taking place in the EU. Experience from cohesion countries shows that *structural funds support is not automatically successful* but only when it has an environment of *macroeconomic stability and appropriate localisation conditions*. Some studies even point out that the cohesion countries have focused on regional intervention into regions lagging behind too much and, thus, they limited growth in their main agglomerations and, consequently, also the process of coming closer to the EU Member States average GDP (the case of Spain, Portugal, and partially Greece, and contrary to that public investments of Ireland focused on national-economy catching up).

According to the EU analysis, four factors − *regional structure, innovation activity, regional accessibility and labour force qualification* − explain two thirds of differences in the GDP per capita between the EU regions. The new emphasis is put on less visible, difficult to quantify, factors.

In this study, we recommend a *growth-equalising strategy* for the Slovak conditions after the SR accession. The growth-equalising strategy of regional policy should in our conditions:

§ support and keep *regional centres in growth* (developed agglomerations) that are decisive carriers of national-economy growth and create not only development resources in the Slovak economy but create also a pro-growth environment for the equalisation of regions lagging behind; this part of the overall strategy is called *growth-equalising strategy focusing on regional centres of national-economy growth (developed regions);*

§ remove negative consequences of production decrement and adaptation to new market conditions in the regions lagging behind together with the support of localisation, revitalisation of regions with deformed demographic and professional structure (the threat of social and economic degradation and marginalisation); this part of the overall strategy is called *growth-equalising strategy focusing on regional centres in regions lagging behind;*

§ both parts of the overall strategy should be implemented with a non-scattered *concentrating* model; the practice of regional development proved sufficiently that dispersing of funds, "strewing" an area with investments is a short term solution failing to provide long term changes of regional structures.

In order to pursue effective use of national resources and, in particular, resources from EU structural funds, the assumption that in the first after-accession stage (approximately 10 - 12 years) these funds will be absorbed by those cities and agglomeration that dispose of decisive localisation advantages even today, is realistic.

These facts indicate that towns, which make the skeleton of the poly-centric urban network and are also the focal points of economic stability and potential development of the regions, should become the object of regional policy.

In the concrete Slovak context the character of regional policy should follow *both components of the strategy* in the framework of the growth equalising strategy; i.e. to be applied in two forms as:

1. *Selective support to developed regions* that should mainly consist in the measures for improving the accessibility of the regions (e.g. by completing the higher road and railways infrastructure), in a pronounced support to the enlargement of innovative capacities and further cultivation of available labour force. These urban agglomerations are concerned: Bratislava-Trnava, Trenčín, Žilina-Martin, Poprad, Košice-Prešov and Banská Bystrica-Zvolen and the region of the city of Nitra.
2. *General support to regions lagging behind economically* mainly focused on utilising, restructuring and developing production potential with the objective to support using of own primary resources, establishing new productions and developing market services in such a way that a diversified structure of their economic base would be created. This must be complemented with a support to increasing the educational level of the population and ensuring transport accessibility connected to higher transport corridors. Urban centres must be the carriers of development also in these regions lagging behind. In NUTS II Western Slovakia - the development of the Nové Zámky – Komárno agglomeration is concerned, in the Central Slovakia region - the development of the towns of Lučenec – Rimavská Sobota and in the East Slovakia region the development of the agglomeration Humenné – Vranov – Michalovce.

Preferring the growth-equalising strategy in its proposed concentrating form in the first stage after EU accession does not mean that the smaller regions out of the reach of the agglomeration development effects shall be excluded from the support. Support to these mostly economically lagging behind and peripheral regions should be mainly focused on the support of activities aiming at the use of primary resources (the development of agriculture and related activities is mainly important in them), appropriate development of industry and of market services and on the support to endogenous development factors. Considering the nature of the spatial development so far (in particular settlements), rural development comes to the fore from this perspective.

Human resources, foreign direct investments, innovations, small and medium sized enterprises (SMEs) and infrastructure are analysed in terms of competitiveness changes till the year 2010.

Noticeable changes will occur in the development of human resources, the share of productive population shall cease to grow and it will start to drop significantly after 2010. This tendency will be regionally much differentiated. Similarly, the qualification structure is unfavourably distributed with respect to the equalising process.

In terms of FDI regional influx the *region of Bratislava* clearly dominates (more than 55 % of all FDI in Slovakia) while a *"cascade effect"* can gradually be observed when productive industrial investments move increasingly more towards the Trnava and Trenčín regions. This trend will be even more pronounced due to the development of the PSA Citroen car-manufacturing factory at Trnava and enhanced with a gradual building of highways eastwards. Gradually, the creation of a second centre of investments in eastern Slovakia with the Košice - Prešov central line can be observed, investing activities in the region of Spiš are also developing in a promising way.

Increase differences in *innovation capacity of the regions* have occurred in Slovakia. On the regional level the most significant influence shall be manifested by including the research, technology and innovation policies into a broader agenda of the development policy of the regions. This policy will be important mainly in the growth part of the strategy that is based on supporting the development of the *innovation potential of national-economy growth centres.*

A more dynamic growth of the new SMEs in the regions of Slovakia will be increasingly more dependant on the existence of a qualitative general and regional business environment.

Infrastructure as a "composed" structure of various sectors of activities has right in its integrated form an influence on other economic activities in the region and on its competitiveness. The strategic task in the development of infrastructure in the period till 2010 is to keep a *balanced development* of hard and soft infrastructure so that for instance the "catching up" in the building of the road network, highways is then not followed with catching up in the field internet accessibility and use, educational facilities (e.g. specialised institutions of higher education) or facilities linked with the innovation process.

According to model calculations the consequences of individual policies shall result in changes in the competitiveness of the regions and GDP per capita development according to the individual NUTS II and Slovak regions depending on the selected scenario till 2010. Slovakia would come closer to 71 % (currently it is around 60 %) of the EU 25 average forecast for 2010. With the exception of the region of Bratislava (160 %) Slovak regions achieved values under 75 % of GDP EU 25 per capita.

The discussions in the European Commission so far clearly indicate maintaining of the support mechanism and the GDP criteria per capita to determine the eligibility of regions for the support from the EU funds. The knowledge gained by developed and also cohesion countries, however, shows that mostly the *developed scope of regional institutions* (including on the one hand institutions necessary for the functioning of the support mechanism and on the other hand institutions supporting transfer of technology and innovation, improving qualification, etc.) can, in particular, significantly affect the sustainability and triggering of regional growth.

The need to develop capacities needed for EU membership is more pronounced in the pre-accession period. This has resulted from the evaluation of the current situation of the Slovak public administration and ensuring the equalisation of the difference between this situation and the situation required from all EU Member States - existing as well as the new ones. With respect to Slovakia's interest to achieve EU membership in the year 2004 the building of effective and capable capacities for membership is a *strategic priority.* The invisible hand of the market helps to solve many problems, however, in regional policy equalisation must be helped it. The focal point must be gradually transferred from preference given to administrative management of support and programmes to strategic priorities of regional development.

Updating of the Slovak economy performance assessment - expected trends of its development till 2010

In 2002 Slovakia's economic growth pace accelerated *in spite of an unfavourable economic-cycle situation in the world economy.* It was the result of an improving competitiveness, banking sector and enterprise restructuring in 1999 – 2001, monetary policy focused on maintaining the Slovak crown pro-export exchange rates and decreasing interest rates as well as the increase of investment activities in the main export branches in 2000 – 2002. In contrast to 1994 – 1998, the increase of performance was manifested not only at the macro-level but also the micro-level in good profit/loss results of the enterprises. The most remarkable is mainly the fundamental change in the development of profit/loss results in processing industry enterprises commencing in 1999.

However, the development of balance indicators also points out the risk of overestimating the positive moments in the economic development of Slovakia in 2002. The growth rate of state budget deficit and public finance deficit in relation to the achieved GDP growth rate will unavoidably be manifested in a growing state debt to GDP ratio. Thus, deterioration of the situation in public finance enhances the necessity to continue in the launched structural reforms.

The assessment of social consequences of economic development in 2002 looks positive in terms of employment (unemployment) and also in terms of wage development. In the context of long-term development it is, however, clear that even after 2002 the average social position of the population of Slovakia is still worse than it was prior to the transformation process. With a view to the expected trends in economic development a certain improvement of the situation in the labour market, however, not in the income area, can be expected in 2003.

The favourable development of Slovak economy in 2002 has been fully reflected in the improving position of Slovakia in the convergence process. According to the preliminary results Slovakia has achieved roughly 53 % EU in the economic level.

Detailed analysis of the effect of individual components of the final demand (*all,* not only export, *reduced by their import intensity*) on GDP formation has shown the paramount importance of the export of goods and services in the economic growth of the Slovak economy broadly opened to exports in a convincing way. The sum of points expressing the 1995 - 2002 participation of demand components in GDP increments is equal to –1.0 in household consumption; –0.5 in public administration consumption; 7.3 in gross capital formation and 27.6 in export. *The contribution of export to the formation of the real GDP was, thus, almost 5 times higher than the contribution of the total domestic demand in 1995 - 2002.* A significant part of GDP increase was also due to the growth of export in 2002.

As the international comparison shows the increase of Slovak economy export performance was significantly supported by *qualitative changes in the structure of Slovak export* into EU Member States (e.g. in 1995 - 2000 differences in the technology oriented branches dropped from –18.2 to –8.0 percentage points), as well as closing of the price/quality gap in the export to the EU which in 2000/2001 reached –10.3 % while in 1995 it was by 9.4 percentage points higher.

The though slowly but increasing level of unit labour costs (ULC) in the Slovak economy has significantly supported the export performance so far. After EU accession the wage and price level will gradually come closer to the EU level that will gradually also trigger the growth of ULC, which, however, does not have to jeopardise the competitiveness of economy if the ratio between the effect of price and quality factors on the competitiveness will shift in favour of quality factors.

Expected trends of Slovak economy development till the year 2010

The effects of Slovakia's accession to the EU were quantified on the basis of four macro-economic scenarios.[2] In two of them a more or less successful accession of Slovakia into the EU in the planned period (the optimistic and pessimistic integration scenario) is expected, in other two the assumption is that EU enlargement will not take place at all (inertia scenario) or it will take place without Slovakia (non-accession scenario). The overall overview of 2004 – 2010 development trends of the Slovak economy identified on the basis of individual scenarios are given in Table 2.

The trends identified according to integration and "non-integration" scenarios in the development of Slovak economy in 2004 – 2010 clearly show the positive effect of integration on the economy of Slovakia. In none of the integration scenarios (pessimistic and optimistic ones) any results of macroeconomic indicators worse than in the inertia scenario shall be achieved at the end of the forecast period. Under the non-accession scenario the functioning of the Slovak economy would deteriorate as a result of a certain international isolation.

T a b l e 2

Selected macro-economic indicators - 2004 - 2010 average

Indicator	Scenario			
	integration		inertia	non-accession
	optimistic	pessimistic		
HDP at c.p. 1995, *growth rate, %*	4.7	4.1	4.1	3.4
Household consumption at c.p. 1995, growth rate, %	4.3	4.1	4.0	3.9
Public consumption at c.p. 1995, growth rate, %	2.5	2.7	2.3	2.7
Gross fixed capital formation at c.p. 1995, growth rate, %	6.2	4.9	5.4	4.2
Export of goods and services at c.p. 1995, growth rate, %	6.4	5.7	4.6	4.1
Export of goods and services at c.p. 1995, growth rate, %	6.1	5.5	4.5	4.4
External balance of goods and services at current p.	-3.2	-3.3	-4.4	-5.6
Nominal wage, *growth rate, %*	6.4	6.3	5.7	5.5
Inflation, consumer prices, *growth rate, %*	3.9	4.1	3.8	3.7
Employment, *growth rate, %*	2.1	1.8	1.6	1.5
State budget deficit, *% of GDP*	2.9	3.5	3.0	4.4

[2] An own econometric model - ISWE02q4 - developed from the data base till the end of 2002 was used for quantification. In addition to the basic (reference) scenario three alternative development scenarios were quantified.

Inertia (reference) *scenario S0* describes the theoretical continuation of the current situation, postponing of the enlargement process, i.e. the case when no candidate country would join the EU. However, the accession process mechanisms would continue to act in Slovakia and other countries.

Integration scenarios S1 and S2 are based on the anticipated enlargement of the EU to 25 Member States. The difference between these scenarios is the presumed successfulness of accession, development of foreign demand and applied institutional policies.

Scenario S3 is called the non-accession or catastrophic one. It represents the hypothetical situation of non-accession (terminating the accession process) of Slovakia to the EU while the accession of other countries is assumed.

The integration of Slovakia into the EU will tangibly revive the labour market. The reduction of transaction costs in foreign trade with the enlarged EU and the inflow of foreign investments will have a positive impact on the growth of demand for labour in both the pessimistic and also optimistic integration scenarios. According to the optimistic integration scenario, the employment growth rates will be in average by 0.5 % and under the pessimistic integration scenario by 0.2 % point higher than according to the inertia scenario. The difference between the pessimistic and optimistic integration scenarios in the number of the employed persons will be around 47 thousand employees.

The positive effect of integration will also be reflected in the wage development. The wage growth will, however, not be too pronounced mainly as a consequence of the lasting effort on the side of investors to continue in the best use of the comparative advantage of relatively low wage costs. Therefore the difference in the nominal wage between the optimistic and inertia variants will only be approximately SKK 1,000.

The consumer prices will be influenced mainly by the world prices development and the election cycle. In the pessimistic integration scenario a slightly higher average inflation rate (4.1 %) than in the optimistic scenario (3.9 %) is expected, however, the main difference consists in the distribution of inflation over time.

Elimination of export restrictions in the form of transaction costs and the increase of Slovak production credibility abroad will significantly enhance our export after Slovakia's EU accession. Relatively low labour costs will also support the growth of export production. According to the pessimistic integration scenario export should grow by 1.1 percentage point, in case of the optimistic development by 1.8 percentage point faster than in the case of the inertia variant during the 2004 - 2010 forecast period.

The expected growth of domestic demand together with export growth will affect the growth of import. Therefore in 2004 - 2010 the average growth of import will be 6.1 % annually under the optimistic scenario. Compared with the inertia scenario it is a growth by 1.6 percentage point higher.

The development of export and import under the individual scenarios shall have a differentiated effect on the development of the foreign trade balance. According to integration scenarios the balance of trade shall be gradually decreasing. According to the optimistic integration scenario the foreign trade balance shall be lower by SKK 12 bill. (in constant prices) as its reference value. In the non-accession scenario the drop of interest in our export would result in the deepening of the deficit even by as much as SKK 23 billion.

The positive development in the labour market, foreign capital influx and transformation of public administration will result in the growth of domestic demand in all its components. The most significant differences among the individual scenarios are in the gross fixed capital formation. According to the pessimistic integration scenario its average growth rate is 4.9 % and in case of the optimistic one 6.2 %. If the non-accession scenario becomes the reality the gross fixed capital should only have an average annual growth of 4.2 %. The difference in the average growth rate of final household consumption would only be 0.4 percentage point when comparing the individual scenarios.

The gross domestic product will be influenced by the development of the internal demand and foreign trade balance. Under the inertia scenario GDP will grow on a year-to-year basis in an interval of 3.5 to 4.4 % in the period 2004 – 2010. If the optimistic integration scenario conditions were achieved the GDP growth rates would be by 0.5 – 0.9 percentage point higher. However, if the non-accession scenario were to be the reality the GDP growth rates would not surpass the 4 % limit.

The question of mutual convergence of economic levels - the convergence of Slovakia's economy to the EU average - is discussed legitimately. In case of successful Slovakia's accession to the EU, the GDP per capita in purchasing power parity (PPP) would achieve 62.9 % of the EU 15 average in 2010 that would correspond 70.5 % of the enlarged EU 25.

The convergence process of Slovak economy to the EU average would, undoubtedly benefit from the integration of Slovakia in the EU. The economic level measured by GDP in PPP would grow in average by 0.4 percentage points quicker in a successful integration scenario than in the inertia scenario.

In case of an optimistic development in Slovakia after EU accession the gross domestic product in nominal exchange rate would grow in average by 1.4 percentage points faster than in the non-integration case. The reason for higher growth dynamism is the combination of two factors - currency appreciation and faster GDP growth after Slovakia's EU accession.

In an optimistic integration scenario the comparable price level of Slovakia would achieve 54.5 % of the EU 15 price level and 67.2 % of the EU 25 price level in 2010. The difference is naturally also caused by reducing the average EU price level as a consequence of the accession of low level price countries.

Identically to the convergence in the real area, the positive effect of Slovakia's accession into the EU is also clear for the convergence process in the area of price levels. In case of the optimistic development the Slovak price level would converge to the EU price level quicker in average by 0.5 percentage point annually than in the non-accession variant.

The nominal convergence of Slovak economy is taking place quicker than the real convergence. It is caused mainly by the exceptionally low comparable price level in Slovakia, approximately at the level of Romania. The potential to converge in the nominal area is therefore high. On the other hand the markedly faster real convergence would require GDP growth rates exceeding the economic potential of Slovakia.

In terms of importance evaluation of differences among the debated future macro-economic scenarios of the development of Slovakia we consider achieving the 75 per cent average level of the European Union expressed by gross domestic product per capita in purchase power parity to be the critical target. According to the referential scenario that assumes continuing of the development so far, Slovakia could achieve this EU 15 level in 2022, in case of successful accession already in 2018 and in case of less successful accession in 2020. If the hypothetic situation of our non-accession to the EU occurred then we would achieve 75 % of the average EU economic level only in 2031.

With respect to the debated and considered context of Slovak Republic's accession to the European Union the authors consider the optimistic integration scenario most probable. Our accession to the EU will increase the annual growth of Slovakia's GDP by approximately 1 additional percentage point, thus, making Slovakia achieving 75 % of the economic level of the new, enlarged EU 25 already in 2013.

The effect of integration on the segments of economy development

After Slovakia's EU accession changes will occur both on the side of generating as well as on the side of using the gross domestic product. The individual segments of economy will be affected by various factors that will influence their competitiveness in the domestic market and also foreign markets. To quantify these effects the computable general equilibrium model (the CGE model) was used.

The model scenario assumes accession of Slovakia to the EU together with other candidate countries in 2004. In the modelling of this process, changes that will have the most distinct effect on the Slovak economy, namely the changes in the field of taxes, foreign trade, budgetary rules, environmental policy and foreign investments influx have been taken note of.

According to the *model calculations results* the highest growth of production will be achieved in the sector of other industrial products (additional growth of production by 4.7

percentage point annually[3]) and market services (1.5 percentage point). Moderate additional year-to-year production increase will be noticed in the agro-food sector (1.3 percentage point) and in the construction (+0.9 percentage point). On the contrary, a year-to-year production drop can be expected in the sector electricity, gas and water supply and distribution (−5.2 percentage point), mining and semiproducts (−2.1 percentage point) and also chemical raw materials and chemical products (−2.1 percentage point). The total inter-annual additional growth of production will be at the level of +0.3 percentage point.

The changes will also occur in the volume and structure of foreign trade with the *EU Member States* where a stronger year-to-year increase of our export in the sector of other industrial production (+5 percentage point), and on the contrary a drop in the sector mining and semiproducts (−2.6 percentage point) and also chemical raw stock and products (−2.2 percentage point) can be expected. Our imports will increase in the sector other industrial products, agro-food products as well as in the sector of mining and semi-products.

The *household consumption* will increase by 0.3 percentage point on a year-to year basis as a consequence of Slovakia's EU accession. Positive effects of natural persons and legal entities income tax lowering as well as of additional economic growth will be manifested. Value added tax and excise duties rise will counter-act consumption increase.

Government consumption shall rise more moderately (year-to-year by 0.2 percentage point). The government consumption growth rate will be slower than the GDP growth rate, the government consumption share in the GDP will have a tendency to decline.

The year-to-year *investment* growth shall additionally rise by one percentage point. The growth of investments will mainly influence the need of taking environmental investments in the Slovak economy. It can be anticipated that a part of "clean" technologies will increase the imports. The increase of foreign direct investment and drop of the price of capital will also have a significant influence.

Slovakia's EU accession will further increase the *openness of Slovak economy* and as a consequence of the integration the export shall rise slightly more (by 1.7 percentage point) than import (by 1.5 percentage point) on a year-to year basis, which will be reflected in a favourable development of net export and contribute to the additional GDP growth (0.8 percentage point on a year to year basis). Domestic demand as a sum of final consumption and investments shall increase by 0.5 percentage point on a year-to-year basis.

[3] The results are given in relative prices and the labour price was used as numéraire.

The estimations of future successfulness in drawing the EU funds introduce a high uncertainty in the effects of Slovakia's EU accession. If we managed an exceptionally successful drawing of net receipts from the EU (by SKK 12 billion annually more than currently), the additional growth could increase even to 1.2 percentage point. If the net receipts from the EU stayed at the current level the additional growth caused by Slovakia's EU accession would drop to 0.3 percentage point according to our calculations.

Another important risk factor affecting the performance and competitiveness of Slovak economy are the environmental investments that will affect especially energy and raw stock intensive industries, agriculture and the non-market services sector.

The results of model calculations allow concluding that Slovakia's EU accession will not result in an immense immediate growth of economy and standard of living, however, the overall benefits of this process will prevail over its costs. The result of intricate processes on the side of generating and also using *gross domestic product* will be its final movement representing the additional average annual GDP growth by 0.8 percentage point.

The corporate sphere and its prospects in the EU accession context of the Slovak Republic

The *enterprise sphere* has a decisive role in the process of candidate countries' coping with the *competition pressures of market forces inside the EU.*

Mobilising the internal potential of enterprises and creating of the external business environment for a successful compliance with this criterion is the task of the economic policy of the government.

The main attribute of the process of creating a functioning market economy is *change.* The success of a concrete enterprise depends on how it manages to cope with the changes. Here, the main role is played by the management. Managing the enterprise is the key to success. Effective utilisation of enterprise competitive advantages and minimisation of competitive disadvantages depends on its quality. Currently, *investments in technologies, innovation and human potential quality* should become the main growth factors. At the same time, these also become the main factors of *productivity* growth.

One of the main conditions for enterprise competitiveness is its *financial strength.* Therefore the financial risk management is the factor of company`s survival and development. The failure to cope with them results in a financial imbalance and finally in insolvency.

Enterprise`s competitiveness depends considerably on the *human potential quality*. The economic growth is anyway increasingly more determined by the intellectualisation of economy and the knowledge potential growth.

Restructuring of the corporate sphere has a significant influence on the effective action of these factors and the increase of enterprise competitiveness. The objective is precisely to achieve standards and performance typical for developed industrial economies. The rate of corporate sphere restructuring has been affected by the deficiencies of the transformation process (in particular the lack of financial resources). Most of the enterprises have already went through the restructuring stage accompanied by a decline in production and dismissals as a response to the market conditions and the enterprises slowly enter the new stage of "strategic restructuring linked with an expansion".

In addition to the government and the business community other entities like regional and municipal institutions join the game. These are important mainly when founding *industrial parks,* which have an important role not only with respect to the development of industrial production and services but also with respect to solving the unemployment problems.

In view of other enterprise sphere development prospects the *business environment* is the decisive factor for increasing its competitiveness. It includes economic conditions and those prerequisites for enterprising that depend on the economic-political measures taken by the state and its specialised institutions. Creating of business environment is mainly the task of the government policy. This, however, does not mean that the enterprises themselves cannot or should not participate in its improvement. On the contrary, their participation is necessary in particular with respect to the communication with governmental institutions, their feedback and communication among the businesses.

All the components and parameters of the business environment go through fundamental changes in the context of the EU accession. The *harmonisation of the tax system* with the European standards is a very sensitive issue that requires mainly taking note of such phenomena as the convergence of rate margins, tax bases and harmonisation time horizon.

Several movements of the harmonisation process are already taking place while many of their attributes are questionable. However, the impact on state budgets is a serious problem.

The *legislation* is not a less sensitive parameter of business environment. The main requirement is making it better arranged and cleared of redundant legislation. This concerns mainly the completion of the bankruptcy law reform. The amendment to the Commercial

Code that simplified the registration process has already caused a certain improvement. The amendment to the Small Licence Trade Act also liberalised the approval process for applications. The Civil Procedure Code also requires new codification.

The liberalisation of prices in general, and liberalisation in the energy sector in particular, is a very serious problem with a view to its convergence to the EU conditions. In contrast to the energy sector, stabilisation of the current price level can be assumed in railway transport because significant support to the railway transport is expected from the EU.

In view of other prospects of corporate sphere development, *reforms in the area of financial relations* are mainly of importance. Pronounced strengthening of enterprise funding not only through the banking market but mainly through the capital market is expected from the side of the EU. The development of the single European financial market is also envisaged.

Export support plays an important role in the development of the corporate sphere. Compared with today the role of export crediting and insurance should significantly increase in particular for medium sized companies.

Infrastructure supporting enterprising is a part of the business environment. However, also that will have to be fundamentally changed and the standards valid for the EU will have to be achieved. It includes mainly legal institutes and their role in the settlement of litigations, and improvement of information assistance. The infrastructure of enterprising is mainly the way in which funding is acquired while making use of specific and atypical forms (leasing, bonds, etc.).

The business infrastructure also includes business federations and associations that promote specific requirements of the entrepreneurs in the framework of economic policy.

The project support is acquiring an important role within the system of business support infrastructure. The project system has become very effective in particular with respect to the regional development support.

Business infrastructure has also an important effect on making the labour market flexible, in particular by creating the essential release standards. The area of innovation policy, mainly the creation of incubator centres for small technology and innovation companies is opening large room for the business infrastructure activities.

So far, the individual blocks and levels of business infrastructure were rather isolated. The new tendency is oriented to the creation of cross-sectional and systemic links, which seems to be much more effective.

The corporate sphere is a highly structured and highly differentiated entity. The category of *small and medium sized enterprises* is gaining an important position in it. They are becoming the basic element of effective economy functioning and they are also called the backbone of the EU economy. Therefore they also need special attention to be paid by the governmental policy.

With respect to their number the SMEs account for more than 99 % of the total number of enterprises and they generate almost two thirds of jobs. These are the reasons why the EU focused its attention on the SMEs. In 2000 the Feira European Council adopted the European Charter for Small and Medium Sized Enterprises. The main purpose of the Charter is to strengthen the SMEs support policy. This policy focuses on concrete areas that represent the essential principles of the Charter. In the context of the knowledge society dawn, *pro-entrepreneurial education* is becoming a priority. Its main purpose is support to the entrepreneurial spirit and the development of entrepreneurial capabilities from an early age on. This goal is being reflected in the school education system and it is also implemented by means of various types of informal education (life-time education).

The area of *legislation and regulation* is extraordinarily sensitive with respect to the development of effective functioning of small and medium sized business. In particular its simplification is exceptionally urgent also in the context of the accession of new countries.

Other challenges the Charter points out include: *reduction of costs and administrative difficulty in starting a business, improvement of communication between the governmental institution and the business sphere, improved access of SMEs to financial sources and strengthening of SMEs' technological capacity and of their innovation capacity*, which is an especially acute issue for the acceding countries.

In terms of further perspective of small and medium sized enterprises development and increasing of their competitiveness in the single market the application of these principles is very important for Slovakia. And indeed, this is what the government and competent institutions strive for.

According to several surveys visible improvement has already occurred in some areas. However, taking into account the accession date and its coming closer the compliance with all criteria requires to even more intensify and improve the quality of a targeted SME support policy.

The impact of Slovakia's participation in the EU Customs Union on the foreign trade

The first relevant area where the theoreticians started to examine the effects of international regional economic integration was - also with respect to the created and often strong customs protection of national economies - the area of movement of goods and services.

Accession to the EU integration bloc will have and in the implementing of the Europe Agreement already has had an impact on the foreign trade of the Slovak Republic. At the same time Slovakia's accession to the EU will mean its participation in the customs union and taking over the EU Common Trade Policy. On the one hand it will result in a final elimination of all remaining tariff and non-tariff barriers to trade and thus the "creation of trade" among the Member States in the enlarged EU according to Viner's theory. On the other hand, the changed customs relations with the so-called "third countries" for the enlarged EU may mean "restriction of trade" with these countries for a newly integrated country (i.e. also Slovakia).

With respect to Slovak trade with the *EU Member States* the very favourable effect initiated through gradual reduction of customs duties on industrial goods in the preparation for integration into the EU was clearly manifested in the period from 1993 to 2001 when the share of Slovakia's export to the EU increased from 30 % in 1993 to 60.5 % in 2002. Many productions of plastics, chemical and wood processing industries and also manufacturing of passenger cars, rail vehicles and ships, and of products made of mineral non-metallic materials will have room to maintain the trend of "creating trade" (according to J. Viner's theory) mainly as a consequence of comparative price advantages.

Orientation calculations show that after the elimination of tariff and non-tariff barriers certain problems with export could occur mainly in livestock products and animal and plant fats and oils, though, on the other hand the elimination of the currently in average by one third higher customs duties imposed on the import of these commodities in the EU than in the Slovak Republic will be in favour of Slovakia. The development of the competitiveness of these commodities manufacturers will mainly influence the situation here.

After taking over Common Customs Tariffs Slovakia's trade with the future EU third countries will be affected in a differentiated way depending on whether it is trade with the so-called non-preferred countries or countries granted preferential (reduced) customs duties by the EU.

In the trade of Slovakia with *non-preferred countries* (U.S.A., Canada, Japan, Korea, Singapore, Hong Kong – China, Tai-wan, Australia and New Zealand) where the differences in the level of contractual custom duties of Slovakia and the EU will be experienced, the import custom duties will totally rise from the average incidence of 4.9 % to 6.4 %, i.e. by 1.5 percentage point. In agricultural commodities as a whole this difference is +6.1 percentage point, in industrial products only +0.1 percentage point. The customs incidence should rise in all agricultural categories, in industrial products only in category VI (chemical products), VIII (leather and furs) and XI (textile and textile products).

Taking over higher custom incidence could increase the protection of the domestic market and restrict import from these countries in the trade with non-preferred countries. However, in cases when the amount of the custom duty and the cost-price relations in these imports will not be decisive in the choice of importing countries from the non-preferred countries and the EU Member States but other specific, quality requirements will be decisive then no shifts from price and cost more expensive imports from non-preferred countries to price and cost cheaper imports form EU countries could occur in the meaning of theoretical hypotheses. However, higher custom duties would increase the value of import from these countries, and consequently, this could be reflected in a price rise in the domestic market.

As far as EU *preferred regimes* are concerned their take over will mean that the Slovak Republic will enlarge their granting to approximately 44 countries. Taking over these regimes (GSP, ACP and on a contractual basis) would only slightly increase imports from preferred countries (some 197 countries) by around 0.3 %. The analysis has also shown that after taking over EU preferential regimes Slovakia should continue to have in average cheaper imports mainly in Category I commodities and in some mainly simpler industrial products from preferred countries than from the EU, that means the tendency of creating trade mainly on the import side to Slovakia from these countries could continue. On the contrary, the import from these countries appears to be more expensive in terms of costs and prices in Categories I to IV and this could result in restricting the import of the commodities concerned from these countries.

When summarising the potential effects of Slovakia's accession to the customs union it can be stated that these have been and seem to continue to be clearly positive also in the future. *Duty free trade within the EU where opportunities to further creation of trade seem to exist* has and should have *decisive* influence*. While in the non-preferred countries tendencies to limiting trade may emerge, in the preferred countries a tendency to a moderate trade increase only,* *mostly on the side of import, is expected, however, this may also generate conditions for the growth of export.*

The effect of Slovakia's EU accession on the intensity of foreign direct investment inflow

Besides the international movement of goods and services another relevant area of integration processes is the area of international capital-investment flows. In integration processes they appear as a reaction to the liberalisation of trade in the newly integrating countries and also to differences in opportunities to increase the value of invested capital in various national localities under the pressure of global competition.

The conclusions of the analysis of Slovak economy competitiveness initial situation clearly formulate the need of creating all conditions for a gradual reduction of gaps in factors that condition the convergence of the level of competitiveness to developed countries. Considering the general under-capitalisation of economy, technology obsoleteness and lack of product innovation, not developed international marketing and missing distribution networks and lastly the lack of know-how in the management area that belongs to decisive prerequisites of competitiveness increase, foreign direct investments have been and will continue to be *indispensable* for Slovak economy. In recent years the share of their influx on the gross fixed capital formation oscillated at the level of 15 – 19 %.

It can be proved already today that foreign companies or companies with foreign participation have *significantly higher performance than the domestic companies* in most relevant indicators. It can even be said that without these companies the Slovak economy would not achieve the level it has.

In spite of this positive effect (there are, of course, also some negative effects) FDI in Slovakia have not acquired such a position as e.g. in the Czech Republic, Hungary, Slovenia, Poland and some other countries of central and eastern Europe, where the volume of FDI per capita is in average more than a double.

In the last 4 - 5 years *the FDI influx* shows two main characteristic features in Slovakia. The first one is that the FDI influx in the given period covered mainly building of distribution chains (in 1999) and the privatisation goals of the government mainly in telecommunications (2000), in the banking and insurance sector (2001) and in some energy sectors (2002). These investment, though, meant strengthening of infrastructure in the broader meaning of the word, which is one of the prerequisites for increasing the competitiveness of economy as a whole, however, on the other hand, FDI into processing industry have been modest and from 1998 their weight was constantly falling from 69 % to 6,3 % in 2002 (though in 2002 the FDI influx almost doubled compared with 2001 it was still below the 1998 – 2001 average). It is understandable, that it could not be sufficient with respect to the contribution of FDI to the improvement of competitiveness in this sector of economy.

Another feature of FDI in Slovak economy is the *prevalence of FDI looking for cost advantages and this is, in general, typical for the so-called export oriented FDI.*

Taking into account the empiric experience of some current EU Member States that each EU enlargement was, so far, always linked with a subsequent FDI growth we assume that Slovakia also could see a higher influx of pro export oriented FDI after the EU accession.

The first study on the effects of Slovakia's EU accession presented one possible, one could say optimistic scenario according to which the average annual FDI influx could reach around USD 1.0 - 1.5 billion till 2008 compared with the current influx of around USD 418 mill. (N.B. - *Economist Intelligence Units* prognosis thinking of USD 1.6 billion is even higher).

While the possibilities for a more intensive FDI influx have to be sought in a significant improvement of motivation also inside the economy, the way in which these conditions for this influx will be shaped in foreign investor countries, i.e. the external environment, is decisive. Here, it is mainly the development of the world boom that will exert pressure on the competitiveness of manufacturers in the EU and thus also on the intensification of international production generation and movements in its geographic configuration.

While in the first study the arguments used were impulses resulting from the so-called product life cycles the theory of which was described mainly by R. Vernon, in this study these arguments are further deepened and risks that an increased FDI influx to Slovakia may not occur are mainly presented. It includes mainly the risk that new investments based on specialisation and co-operation may turn their attention to the regions with a certain *sectoral concentration and that in particular this may be more important for the investor than comparative cost benefits of regions for a potential placement.* This will mainly be manifested in sectors with more extensive possibilities for economies of scale and low transport requirements. Naturally, this tendency to sectoral concentration and agglomeration will be differentiated according to sectors.

Agglomerations in the Slovak Republic will thus have to face the competition of other agglomerations not only in the new Member States but also inside the EU 15.

This means that a less optimistic scenario of FDI influx in Slovakia after its accession can also be justified. With respect to the FDI contribution expected in the increase of productivity and real economy convergence one could consider the annual FDI influx level of approx. USD 900 mill. as a still admissible level.

The above mentioned deliberations show that it is really very difficult to estimate the development that will occur in these processes and its impacts on the intensity of FDI influx into Slovak economy. Therefore the only feasible way is to create a certain *information framework (corridor) of phenomena and "actors"* which will influence the FDI influx in a relevant manner.

One of the main spheres of this approach seems to be the acquisition of *relevant characteristics on transnational corporations.* It appears that the TNC of developed EU Member States could mainly have the decisive potential participation of TNC in the efforts to intensify FDI influx. Another important information is the *degree of trans-nationality and the sectoral orientation of the TNC.* These characteristics are presented on the largest TNCs in the study; however, due to a considerable number of TNCs it is a rather illustrative example of this approach.

Considering the importance and challenging nature of the vision of FDI influx in the Slovak economy it is necessary to approach this problem in a more conceptual way. This basically means to chose for a verified and effective so-called *targeted approach,* i.e. an approach based on targeted support to FDI influx also in many developed countries. This requires adopting measures mainly at the level of the government that will support relevant analytical, marketing and co-ordination activities for the purpose of defining and implementing foreign investment priorities.

Other relevant spheres of government involvement in intensifying FDI influx are the improvement of the overall macroeconomic and institutional framework and support of further development of *infrastructure* mainly in the area of capital market development and technology and communication infrastructure. Also the *commercial missions* of government and other top supreme officials of the state should be prepared with a view to the elaborated targeted support of FDI influx in Slovak economy.

Labour market and social dimensions of integration

The Slovak Republic has one of the highest unemployment rates among the European countries (17.9 % at the end of 2002), therefore it should enhance its policies focused on new job creation. Job creation should be supported systematically from the structural funds, private sector domestic resources, re-distribution of public funds and foreign direct investments.

Expenditures from structural funds should be drawn to the maximum and effectively used so that the part channelled to the enterprise sector strengthens the competitiveness of enterprises and maximises the multiplication effect of employment growth.

Formation rate (and also termination rate) of small and medium sized companies is insufficient compared with the EU Member States. In 2002 the number of 1,130 new companies represented only 1.9 % of the total number of companies (without sole traders). The SMEs growth support system (services to enterprises by governmental programmes) in promising segments, mainly in industry, to enable increase of labour productivity and employment, is missing. The "de minimis" rule concerning the granting of subsidies to SME up to € 100 thousand, which is some SKK 4 million in addition to the state aid notification system in a period of three years, should be used in a more intensive way. The governmental employment support strategy should include a clear policy concerning the place of SMEs in economy. If the dominance of foreign sector in the internal trade is not eliminated then the growth of employment in the SMEs is also questionable as there is no possibility to sell their production at the domestic market. The state and regions should support the creation of *clusters* of domestic firms (from production to sale) with a view to increase the placement of domestic production of goods and services on the domestic market and gradually also for export.

Slovakia needed approximately 5 years to reach the level of most EU Member States per year (more than 1 % of GDP) in relative expenditures for active employment policy. At the same the unemployment rate in Slovakia is more than double. In a situation where there are even 16 registered unemployed per one vacancy, active labour market policy should pay more attention rather to the growth of demand for labour than to labour force supply.

In the Slovak Republic the labour costs are clearly the lowest in the V4 region. In 2000 one hour labour costs in industry and services were € 4.48 in Poland, € 3.90 in the Czech Republic, € 3.83 in Hungary and € 3.06 in Slovakia (in 2002 gross monthly wages in € were the following: Poland 591, the Czech Republic 511, Hungary 502, Slovakia 317). Reducing labour costs (which is expressed in the 2003 National Employment Plan by the anticipated reduction of contributions to social funds) may cause shifting of mainly low skill jobs to the Slovak economy and thus more permanent orientation to low paid jobs. Reducing labour costs has no justification also because in Slovakia labour productivity mainly in the foreign sector (subsidiaries of foreign firms) does not lag behind the neighbouring V4 countries at all, it is even not lagging behind the mother companies in the EU Member States and this difference will continue to decrease, although the convergence processes are distorted by transfer prices.

Employment policy (support of new job creation) and also the policy of influencing the wage level (or full labour costs) should result from and take into account the large differences in productivity not only among the individual sectors of economy but also among the individual regions of Slovakia. The low wage and full labour costs policy with respect to employment is not justified also because a more significant foreign capital influx is expected and it will have high productivity so that wages lagging behind the neighbouring countries will result only in the increasing profits of these companies without adequate proportional payments to social funds. Employment, mainly in industry, will not be determined by reducing gross wage tax burden but it will be determined mainly by technology (fixed capital). Low wages may initiate unfavourable effects in substitution processes between capital and labour with negative long-term consequences for the structure of industry and economy as a whole.

If Slovakia is to resolve unemployment that has a pronounced regional character, it must change the support to the creation of new firms (foreign and also domestic) in the regions lagging behind and it shall not rely on marginal employment and production increments in existing enterprises. This would not resolve the structural problem of economy (low rate of value added) either. The optimum employment policy in the Slovak Republic after EU accession will require more effective re-distribution of funds through the state budget (while complying with all European legislation requirements) and preferring re-distribution funds in the form of social insurance contributions to entrepreneurs willing to employ the unemployed (as also practised by EU Member states) to a flat reduction of social funds contributions. In general (flat) reduction of social funds contribution rates, the total rate of potential resources re-distribution to the most backward regions would go down and the marginal labour costs would uselessly decrease where it is not necessary. In the environment with long-term very low price of labour in Slovakia and also in an international context and compared with the high price of fixed capital (the price and quantity of which determine the number of created jobs) labour tax relieves should apply only to a marginal increment of employment.

Low 2002 minimum wage amounting to SKK 5,570 (36.4 – 41.2 % of the average wage level and 25.2 – 41.7 % above the subsistence level) is the main reason for the lack of interest in having a job on the side of the unemployed and it is also the ground for black work on the side of employees (in EU Member States minimum wage is higher than the social income minimum by approximately 80 % to 150 %, which ensures its motivating effect). To eliminate black work stricter sanctioning of entrepreneurs should be introduced. The unemployed should be given more time and means to search for a job.

Increasing minimum wage and price of labour in general should increase employment in the form of part time employment contracts which is also in compliance with the trends in EU Member States. In general, the importance of labour market flexibility is overestimated in Slovakia as also pointed out by J. de Koning in his presentation at a MATRA project conference.

Every regulating measure, which also includes determining the minimum wage, has, in general, side effects. The need of minimum wage growth in terms of positive effects on labour offer (increase of motivation to work) and also in terms of aligning wage level with the V4 countries and the EU Member States as one of the means of pressure to align the price level, can have negative impacts on the reduction of demand for labour in lower wage zones (wages around minimum wage). According to the last statistical survey of employees' wage structure in 2001, when the minimum wage calculated over the whole year was at the level of SKK 4,790 (9 months SKK 4,400 and 3 months SKK 4,920), 1.35 % employees were remunerated in the band from SKK 3 - 4 thousand and 2.95 % employees in the band SKK 4 – 5 thousand employees, the sole trader sector excluded. Raising minimum wages would, however, probably also influence the increase of wages on the higher tariff bands, when in the SKK 5 - 6 thousand bans other 5.33 % of workers were remunerated and in the SKK 6 – 7 thousand it was 7.3 % workers.

According to population development forecasts the impact of demographic factors on the growth of labour supply will attenuate and starting with 2008 the number of population in productive age will start to go down with positive effects on the unemployment development, but the prolongation of the productive age can make the start of employment more difficult for school graduates.

Households of the unemployed significantly determine the social situation of the society. 321 thousand persons received social security contributions in 2002. If to take into account also maintained persons of the social benefit recipients then 618 thousand persons, i.e. 11.5 % of the population, live in poverty. As much as 90.4 %, i.e. 290 thousand persons were unemployed persons. This is an evidence of the very low level of unemployment benefits as well as of poverty in Slovakia being generated by unemployment and not the pension system (old age, disability and other pensions system). The introduction of the capitalisation pension pillar to which even 35.7 % of obligatory pension funds contributions should be channelled, combined with a reduction of the re-distribution rate will result in generation of poverty from the pension system and for the elderly people.

The reduction of expenditures on social assistance may deteriorate the situation of low-income groups. While in 1995 social income of households below the 1.5 subsistence minimum multiple was 33 %, and below the two times subsistence minimum level almost 27 % of net pecuniary income, in 2001 this share was almost 52 % and 41 % respectively. The households in lower income bands depend increasingly more on social income. In the society the differences in net monthly income per member of households in the lowest and the highest income group are increasing in absolute terms (in the examined period by some SKK 3 thousand per year).

Households show extensive capacity of adaptation behaviour oriented to mobilising all available productive resources for increasing the income. The traditional orientation to informal and domestic economy outside the area of formal work not only continues but it even has become the essential adaptation mechanism of households in situations of failing opportunities in the legal labour market.

Orientation of Slovak economy to wage-cost and price competition has the long term negative consequences from the perspective of EU accession: it leads to the orientation of economy on simple products, insufficient appreciation of qualification and the risk of gradual lagging behind in the position of developed Europe's "periphery".

A cultivated social dialogue among social partners that should become the standard for addressing economic and social problems ex ante also in Slovakia, mainly in the context of compliance with the demanding criteria applied to an EMU accession by a country, is the standard in the European Union.

The impact of taking over the European Union Common Agricultural Policy on the Slovak agriculture

The future situation of our agriculture in the EU environment is considerably determined by its current performance and position in the national economy compared with the EU Member States and other candidate countries.

Compared with the EU the productivity of Slovak agriculture is significantly lower. Value added generated per 1 hectare of land and per one worker is several times less. It is also caused by a different price level and amount of support to production, however, differences in production intensity manifested in a lower effectiveness of spent inputs are also important.

Overcoming this lagging behind will mainly require increased inputs of intensification factors, in particular fertilisers and protective chemicals, irrigating, systemic measures eliminating the negative impact of weather and also motivation to production reallocation. It is necessary to emphasise that competitiveness of some production oriented Slovak enterprises would be higher than in small ones in average in the EU under equal conditions, mainly in crop production. In livestock production the effect of individual care per production parameters is, however, more in favour of the EU.

The Copenhagen summit conclusions closed the issue of production quotas. Though not all quotas are fully acceptable, Slovak negotiators achieved a compromise and an acceptable solution. The achieved level of base area for cereals, oil-plants, protein crop and flax is a clear success of negotiations in comparison with other candidate countries. Reference harvest of 4.06 t/ha per base area cannot be considered such a success because it is the basis for generating significant differences in direct payments not only between Slovakia and the EU but also with respect to other candidate countries. In livestock production commodities the achieved milk quota is adequate to the circumstances and argumentation options. We anticipate that fulfilling of the milk quota and its breakdown will result in insufficiently progressive and effective producers leaving the market. The development of cattle rearing mainly in submontane and mountainous areas will be also limited with dairy cow quota.

At the December 2002 Copenhagen summit, the delegation of the Slovak Republic publicly declared its commitment to supplement direct payments to Slovak farmers to the level of 55/60/65 %, i.e. by 30 % above the level of EU direct payments (25/30/35 %) that will be paid from the guarantee section of the European Agricultural Guidance and Guarantee Fund (EAGGF). This position was a direct reaction to the declaration by the supreme representatives of Hungary, Poland and the Czech Republic who promised such a support to their farmers.

In spite of the same level of direct payments, i.e. 55, 60, or. 65 % of EU payments in 2004 – 2006 there will be considerable differences among the candidate countries. This applies mainly to the payments per base area which should reach € 153.5 /ha in Slovakia in 2004 – 2006. The difference between the lowest payment (€ 90.7 /ha Estonia) and the highest (€ 199.2 /ha Slovenia) will be almost € 110/ha of base area. Similarly as in crop on base area, the milk production per capita will be the lowest in case of Slovakia with the exception of Malta.

According to the majority of analyses the Slovak farmers will receive more payments after the EU accession than prior to it (according to the Ministry of Finance SKK 19 – 21 billion in 2004 compared with SKK 13 billion in 2003). The binding part of this package, however, represents maximum 40 % of available means supporting production, 60 % are "programme and project payments" with a time shift and not all of them directly concern agricultural primary production. Maximum SKK 10 – 11 billion apply to agriculture and direct compensation of production detriment. In fact, the support to disadvantaged regions is also targeted to them with a similar aim.

In addition to the significantly disadvantaged situation of all candidate countries in relation to the EU 15, *every reduction of the Slovak national supplement to direct payments* (against the possible 30% supplementary payment) would mean extra disadvantaged situation, this time in relation to other candidate countries. The large EU 25 market will strongly be influenced by the differentiated competitive level of agriculture of the new Member States, which is the result of soil- economy and technology differences and also of different approaches to the support of agriculture. After EU accession trade barriers will be abolished in the enlarged EU 25 market and the price of agricultural production will be the function of costs, supports, quality and purchase power. If the assumption is that in the new EU Member States the growth of purchase power will be roughly the same and regular then the relative decline in competitiveness will be caused by a lower reimbursement of costs with supports (lower national supplement), and thus, also a higher weight of price payment of costs of producers in the competition with producers from other candidate countries. Lower national supplement to direct payments than in other candidate countries would fail to stimulate production (and market prices) equally in Slovakia and would result in easier marketing of agro food production of other candidate countries on the Slovak market, in particular.

The real direct payment per *base area* is different also with the same percentage of direct payments in candidate countries because it is the conjunction of the base area and rate per ton of reference yield and its level is low in Slovakia (4.06 t/ha of base area). At the level 55 % of payments Slovakia will have the second lowest payment per hectare of base area after Poland. In case Slovakia will not add 30 % of direct payments up to 55 % but only up to 40 % (EÚ 25 %, SR 15 %), the Slovak agriculture − in case of a 30 % supplement in other V4 countries − will get by € 61/ha less than in Hungary and by € 43/ha less than in the Czech Republic.

In a calculation per 1 *hectare of agricultural land* the Slovak agriculture will have the lowest level, namely € 66/ha at a 55 %-level of direct payments. It is 75 % from the level of payments in the Czech Republic, 66 % of Hungary, 98 % of Poland. If the supplement were reduced to 15 % of direct payments (up to a total of 40 % EÚ), i.e. to a level of € 48/ha, considerable problems of Slovak agriculture with respect to new EU Member States could be expected.

We expect that in Slovakia the price adjustment to EU prices will be gradual and it will be affected mainly by the purchase effective demand of domestic consumers. Taking into account the adjustment of the wage and income level of the population, that demand will also be only gradual and it will soften the growth of agricultural prices.

Compared 2000 - 2001 the estimated crop and livestock production price index is in the range of 108 − 110 % in 2004 – 2006, of which crop production around 103 % and livestock production around 113 %. The profitability of most crop products should increase. If the level of direct payments will be 55/60/65 %, the return on cereals and oil-plants would reach 15 – 25 %, if 40/45/50 % of direct payments were to be applied it would only reach 7 – 15 %.

Net trade profit (without payments for rural development, and thus, support to disadvantaged areas) will increase from a loss of SKK –2.5 billion (2001 – 2003 average) to a profit of SKK 2.1 to 4.4 billion depending on the amount of direct payments. From the regional perspective the profit increment will be allocated mainly to production areas. In disadvantaged areas its lower increment will be compensated mainly with payments for rural development that are also a part of agriculture income, however, the issues of the scope of disadvantaged areas and the compensation amount for the disadvantaged status are still not finalised. The estimated amount of funds for rural development could reach SKK 6.5 billion in average in 2004 - 2006, of which SKK 5.2 billion from the EU and SKK 1.3 billion from the budget of the Slovak Republic.

Consumer expenditures on foodstuffs will affect not only the price of food but also consumer quality preferences influenced by disposable income. Taking the optimistic assumption that population wage income will grow faster than prices and also with a view to the forecasted relative drop of prices of main agricultural commodities in the enlarged Union market, the consequences of Slovakia's EU accession should not be so dramatic for consumers as originally assumed. Nevertheless, food consumer price index that always lagged behind the inflation rate so far will increase approximately identically to the overall consumer price index in the first years after accession. We assume that the consumption of staple food will not drop. Although the expenditures on foodstuffs will increase for a short period after EU accession (in 2004), they will drop again in the following period. It will be a consequence of slowed down price increase of food and also a consequence of a relative stability of food prices in the EU markets, further appreciation of Slovak crown exchange rate and the development of non-foodstuffs goods prices.