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MEMORANDUM OF THE PRESIDENT

OF THE

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

TO THE

EXECUTIVE DIRECTORS

ON A

COUNTRY PARTNERSHIP STRATEGY

WITH

THE SLOVAK REPUBLIC

May 6, 2004

CURRENCY EQUIVALENT
(Exchange Rate as of April 30, 2004)

Currency Unit = Slovak Koruna (SK)
US$1 = SK 33.83
SK1 = US$ 0.029

GOVERNMENT'S FISCAL YEAR

January 1 to December 31

ABBREVIATIONS & ACRONYMS

AAA	Analytic and Advisory Activities
CAS	Country Assistance Strategy
CAP	Common Agricultural Policy
CPS	Country Partnership Strategy
EAGGF	Agriculture Guidance and Guarantee Fund
EBRD	European Bank for Reconstruction and Development
EFSAL	Enterprise and Financial Sector Adjustment Loan
EIB	European Investment Bank
ER	Emission Reductions
SF	Social Fund
EU	European Union
FDI	Foreign Direct Investment
FSAP	Financial Sector Assessment Program
GDP	Gross Domestic Product
ICR	Implementation Completion Report
IDF	Institutional Development Fund
JI	Joint Implementation
NBS	National Bank of Slovakia
OECD	Organization for Economic Cooperation and Development
OED	Operations Evaluation Department
PAYG	Pay-as-you-go
PCF	Prototype Carbon Fund
PPF	Project Preparation Facility
QAG	Quality Assurance Group
RDF	Regional Development Fund
RONI	Regulatory Office for Network Industries
SAL	Structural Adjustment Loan
SDF	Social Development Fund
SECALS	Sector Adjustment Loans
SME	Small and Medium Size Enterprise
SWAp	Sector Wide Approach
TA	Technical Assistance

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THE SLOVAK REPUBLIC-WORLD BANK COUNTRY PARTNERSHIP STRATEGY

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ii. The reforms of the past few years have put Slovakia on a firm footing for future progress. Slovakia achieved sustained growth in excess of EU GDP growth rates as public expenditures declined to an average 39 percent of GDP for 2001-2003, while the fiscal deficit was reduced to 3.6 percent of GDP in 2003. The deficit is expected to further decline to 3 percent of GDP by 2007, and Slovakia is on target to meet this as well as other components of the Maastricht criteria. Slovakia's reform program to support growth, reduce the deficit, and develop a vigorous market economy is impressive, and includes the introduction of sweeping fiscal reforms and large-scale privatization of public sector assets with substantial foreign participation.

iii. Slovakia now faces three broad development challenges. The first is to continue the prudent management of the economy and meet obligations under the Stability and Growth Pact as Slovakia seeks to achieve full benefits from its membership in the EU by adopting the Euro. The recent fiscal reforms have created a strong platform for fulfilling this agenda. A second challenge is to converge to European income levels and be fully competitive in European and world markets, and to build the capacity to productively use newly available EU resources. Structural reforms to improve labor and capital mobility will be important in this regard. The third challenge is to reduce poverty and unemployment and to address the marginalization of the Roma. Unemployment is much too high at over 17 percent, and, while absolute poverty is low, there are deep pockets of poverty, particularly among the unemployed, households living in poor regions, and the Roma minority, who comprise nearly 11 percent of the population. Labor market reforms are needed, small and medium size enterprise (SME) development (which should normally generate a high proportion of new jobs) is lagging, and education reforms are only just beginning while lack of education remains a key determinant of unemployment and poverty.

iv. While these are significant challenges, Slovakia has already demonstrated how much can be accomplished in a short period of time. With the continued commitment of the authorities, Slovakia should proceed in the future as it has in the past, addressing these challenges by formulating and implementing practical and effective solutions. As a partner in development, the Bank stands ready to assist, where needed, in these efforts.

v. World Bank assistance has played an important role in helping Slovakia to achieve its goals. The objectives set out in the last CAS have been met and in some instances, exceeded, and ongoing projects have satisfactory ratings or better. Analytic and Advisory Activities (AAA)

have played an important role, is considered a best practice example by the Bank, and is much appreciated by the Government. The Bank needs to continue to provide excellent policy advice to continue to be relevant.

vi. For the future, assistance will be formulated in the context of the Partnership Strategy guided by agreed criteria. Such assistance should: (a) have a high payoff in terms of either equity or growth, (b) complement other sources of funds or expertise, (c) reflect the Bank's comparative advantage, and (d) have an impact in the near or medium term, other factors being equal. AAA will continue to be an important part of the partnership because of its impact on Slovakia and because lessons learned in Slovakia are applicable in less advanced countries.

vii. There are a variety of ways in which the World Bank could assist Slovakia to meet the challenges outlined above. The World Bank could assist with reforms to enhance competitiveness in selected aspects of private sector development (financial deepening, SMEs), rural development, labor markets, legal/judicial, and education. It could also assist in poverty reduction and social inclusion through proposed work on a poverty assessment and poverty alleviation, education, as well as work to reduce the marginalization of the Roma.

viii. For the present, two projects are under preparation: a Social Development Fund Project and a Legal and Judicial Reform Project. While demand for AAA and technical assistance is high, demand for additional World Bank finance is now low, as Slovakia has excellent access to capital markets. As the World Bank reduces the non-financial costs of borrowing by simplifying and aligning its procedures with EU and country practice and more effectively introduces its products in line with the "Management Action Plan for Enhancing World Bank Support to Middle Income Countries" (Sec M2004-0071/1, April 20, 2004), effective demand for financing could grow in the future. An important initiative is the Bank's proposed approach to lending to the EU8. The EU8 Technical Assistance Loan Facility[1] could be accessed by Slovakia to provide technical assistance beyond the limited capacity of the World Bank's administrative budget in relation to any of the development challenges that Slovakia faces for which it wishes to draw on World Bank support. In addition, sector-wide approaches, pooling World Bank, Government, and possibly the funds of European institutions could be useful to promote or maintain policy or institutional reforms and thereby leverage EU funding, and/or to provide financial support to activities not eligible for EU funds.

ix. Slovakia has made notable progress in recent years. Its accession to the EU both certifies this progress and presages continued achievements in the future. As Slovakia assumes a new status, it is now appropriate for Slovakia and the Bank to enter into a new phase of their partnership. To meet this challenge, the World Bank will endeavor to respond quickly and flexibly to Slovakia's development needs. Through this engagement, the World Bank can also help Slovakia share its development experience with other countries and lay the groundwork for its eventual transition to donor status.

[1] See "Framework for World Bank Support to EU8 Countries," draft Board Paper, May 2004.

Proposed Agenda for Board Discussion

- *Is the proposed post-Accession strategy for Slovakia congruent with the country`s requirements and the World Bank`s capacities?*

MEMORANDUM OF THE PRESIDENT OF THE INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT TO THE EXECUTIVE DIRECTORS ON A COUNTRY PARTNERSHIP STRATEGY WITH THE SLOVAK REPUBLIC

I. INTRODUCTION

1. The Slovak Republic has made great strides in implementing reforms since the FY01 Country Assistance Strategy (CAS), and on May 1, 2004, acceded to membership in the European Union (EU). A new framework to govern relations between the World Bank and Slovakia is needed, one that moves beyond the traditional provider-client relationship to a partnership which builds on the progress that Slovakia has achieved. While financial support will have its place, the emerging partnership is based on facilitating knowledge-sharing and policy dialogue. The Country Partnership Strategy (CPS) proposed for FY05-07 focuses on analytical work and technical assistance operations designed to assist Slovakia to reach its goals, while leaving open the possibility for broader financial support should Slovakia determine it useful to meet specific needs.

II. COUNTRY CONTEXT

A. RECENT POLITICAL DEVELOPMENTS

2. Since winning its second term in September 2002, the Government has been implementing an ambitious reform program with considerable success. However, the four-party coalition lost its parliamentary majority in December 2003, although defecting members of Parliament have stated that they are likely to continue to vote with the Government during the remainder of its four year mandate. While Slovakia has achieved an impressive reform record, political views in the country have been divided; for example, the EU accession vote was decided by a relatively small margin. Popular support for the reform has been variable, especially when reforms to improve the functioning of markets have reduced directed benefits, such as the adjustment in welfare payments to reduce them below minimum wage levels, or the initiative to introduce limited tuition payments for tertiary education which has been shelved for the time being. The recent election of Ivan Gasporavic, who was supported by the Parliamentary opposition, as President combined with the minority position of the Government, could slow down the pace of reform. On the other hand, a referendum in April 2004, to limit the term of the Government, was defeated, which increases the probability that the Government will remain in office for its elected term to mid-2006. The Government is committed to press ahead with its reform agenda and there is little risk of reversal or abandonment of that agenda given the irreversible nature of the key reforms and core of support for reform in the coalition.

B. RECENT ECONOMIC DEVELOPMENTS

3. Progress has been exemplary since the last CAS (January 2001). At that time, gross domestic product (GDP) growth was modest and appeared unsustainable given policies and structural imbalances then in place. Few structural reforms had been implemented, fiscal policy risked high deficits while monetary policy needed for stability resulted in high interest rates, foreign direct investment (FDI) was low, and unemployment was high.

4. Since then, GDP growth has exceeded 4 percent per year, higher than its neighbors and well above the EU GDP growth rate of 0.7 percent for 2003. Public expenditures have declined from over 55 percent of GDP in the early 1990s to an average of 39 percent of GDP for 2001-2003, and are now much lower than the average for EU8 countries. The fiscal deficit was reduced from 5.7 percent of GDP in 2002 to only 3.6 percent of GDP[2] in 2003. Further improvement is needed because part of the reduction was due to one-off effects, and Slovakia will incur some expenditures to meet EU accession requirements and the introduction of the second pillar to the pension system. Taking these into account, the deficit is expected to grow to 4 percent of GDP but then decline to 3 percent of GDP by 2007, to meet one of the key Maastricht criteria and help pave the way for the planned introduction of the Euro.[3]

5. A sweeping tax reform was introduced in January 2004, comprising a tax rate of 19 percent on all personal and corporate incomes, but with an increased deductible allowance for low income earners. Virtually all tax exemptions were eliminated – gift and inheritance taxes were abolished while real estate transfer tax will be abolished in the beginning of 2005. A uniform value-added tax rate of 19 percent is applied to all products, resulting in a major shift from direct to indirect taxes. This simplification of the tax regime should improve governance aspects related to taxation, and further improve Slovakia's competitiveness for foreign investment. The reform is designed to be fiscally neutral, but the impact of such large changes is difficult to predict. While the early results are encouraging, the Government will need to be ready to react in case revenues do not meet projected levels.

6. Core inflation has been kept at about 3 percent in 2003 and overall inflation was limited to 8.6 percent as a result of firm monetary policy which contained second-round effects of increases in administered prices. The trend appreciation of the currency has been kept broadly in line with productivity gains despite large inflows of FDI. As a result, the current account deficit has been reduced from 8 percent of GDP in 2001 and 2002 to less than 1 percent of GDP in 2003. Foreign exchange reserves are robust: the equivalent of 6 months of imports.

C. SOCIAL DEVELOPMENT

7. Slovakia needs to reduce unemployment and poverty, while addressing the particular issue of the marginalization of the Roma community. Slovakia's poverty profile is similar to that of other EU accession countries.[4] Absolute poverty is low, but there are deep pockets of poverty, particularly among the unemployed, households living in poor regions–especially in Eastern Slovakia–and the Roma minority, who comprise nearly 11 percent of the population. Poverty is most severe in geographically isolated and marginalized Roma settlements in Eastern Slovakia which commonly lack basic infrastructure and utilities. Unemployment reaches nearly 100 percent in many of these settlements and education levels and health status indicators are low. For example, only 3 percent of Roma children complete secondary education. At least one-third of the long-term unemployed are Roma. The Government has established an office for Roma

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[2] According to ESA 95 methodology.

[3] In addition to the Maastricht criteria (fiscal deficit <3% of GDP, public debt less than 60 percent of GDP, low inflation and long- term interest rates, and exchange rate stability), further reforms will be needed to enable a successful introduction of the Euro including increased labor market flexibility and financial sector reforms.

[4] *Slovak Republic: Living Standards, Employment and Labor Market Study* (Report No. 22351-SK, February 2002). A full Living Standards Measurement Study is planned for FY05.

affairs headed by a senior official (and supported by an Institutional Development Fund (IDF) grant in FY02) which is responsible for coordinating policy on Roma across the Government (and for coordinating the activities of the Government related to the Decade of Roma Inclusion which grew out of the Budapest Roma conference cosponsored by the World Bank and Soros Foundation in 2003). However the political influence of the Roma is dissipated and none of the coalition partners (and even less the opposition parties) consider the Roma as part of their political base or responsibility.

8. Unemployment is still high at over 17 percent for 2003, although it declined by about 1 percentage point from 2002. Conversely, employment is low, at 57 percent, one of the lowest observed in OECD countries. Low-skilled workers are falling out of the job market as about a quarter million low-skilled jobs disappeared during 1994-2002. There are large gaps between workers in the high productivity FDI sector and, in general, domestic (including state-owned) enterprises. Despite recent reforms, employment is still skewed towards the public sector, with general government accounting for over 20 percent of all jobs.

9. Slovakia has taken several legislative steps to promote gender equality, and follows the recommendations of the 4th UN World Conference in Beijing as well as EU regulations. A National Action Plan for Women was introduced in 1997 and Parliament adopted the Concept of Equal Opportunities for Men and Women. Although, implementation of the new laws has been slow in dealing with gender disparities, available data indicate that gender disparities are not a major problem.

10. The recent tax reform creates strong incentives for business creation and self-employment; but further measures are needed. High welfare benefits approximating the minimum wage and high levels of social security contributions and health care benefits have diminished labor force participation. Recognizing this, welfare benefits have recently been reduced from the equivalent of about 100 percent of the minimum wage to about 50 percent of the minimum wage. Recently enacted pension reform laws increase the retirement age to 62 (and modernize the pay-as-you-go (PAYG) pillar including through the creation of a mandatory second pillar). Sick pay benefits are being reduced to levels consistent with other market economies while co-payments have been introduced, all of which will reduce labor costs, thereby increasing labor demand. This package of reforms should have a positive impact on employment; but the rationale for these reforms is not well understood by the population suggesting the need to increase communication to help ensure their success. For the future, an enhanced focus on education and training is a high priority, as are other measures to induce growth in SMEs and other sectors not directly linked to FDI.

III. DEVELOPMENT CHALLENGES: COUNTRY'S DEVELOPMENT OBJECTIVES AND PROGRAM

A. THREE CHALLENGES FACING SLOVAKIA

11. Slovakia now faces three broad development challenges. The first is to manage the economy prudently and meet obligations under the Stability and Growth Pact as Slovakia seeks to achieve full benefits from its membership in the EU by adopting the Euro. These require further reductions in the fiscal deficit to meet the ceiling of less than 3 percent of GDP, managing public debt to remain under 60 percent of GDP, keeping inflation under control so that it does not exceed by more than 1.5 percent the average of the three best performers in the EU, maintaining

long-term interest rates at no more than 2 percent above the interest rates of the three lowest inflation countries, and, finally, maintaining exchange rates within the ERM2 for at least 2 years.

12. A second challenge is to converge to European income levels and be fully competitive in European and world markets, and to build the capacity to be able to productively use newly available EU resources productively. As it does so, Slovakia will need to implement structural reforms to improve labor and capital mobility thereby enabling the economy to function efficiently after adoption of the Euro when active monetary policy will no longer be an option. Another aspect of this challenge is to enhance communications to build a broader consensus in support of reform.

13. The third challenge is to reduce poverty and unemployment and to address the marginalization of the Roma. Unemployment is much too high – and reciprocally, employment is too low. Labor market reforms are needed. SME development, which should be a major source of new employment and innovation, is lagging and Slovakia's overall long term competitiveness, both for foreign and domestic investment beyond the currently highly successful automotive sector, needs to be reviewed and appropriate reforms introduced. Lack of education is a key determinant of unemployment and poverty, and education reforms are only just beginning. Many Roma children still do not attend school regularly or those that do are often misplaced into low quality special schools or classes intended for the mentally and physically disadvantaged.

B. SECTORAL ASPECTS OF THE THREE CHALLENGES

14. Slovakia needs to build on recent public sector expenditure reforms in order to meet the Maastricht Criteria. A new pension system was approved in 2003, but implementation will need to proceed quickly as the new system is to be operating from January 2005. Systemic reform of social assistance is being implemented to improve work incentives and reduce the poverty trap (see para. 7). Information technology reforms are needed as the country moves to a unified contribution system. Fiscal decentralization to improve effectiveness and accountability is needed with devolution of responsibilities to regional and local political units. These and other reforms need to be carefully explained to the public to broaden understanding and support. This is an example of an area where enhanced Government communications are key to carrying reforms forward.

15. Health sector reforms have been introduced (including co-payments, improved patient management, better control on expenditures for pharmaceuticals) but recently, the pace of reform has slowed. As in the case of pension reforms, Government communication of the benefits of health sector reforms needs to be improved to garner support for the key elements of the reform program, such as hospital restructuring and improved provider payments methods, among others.

16. Education sector reforms have begun but further progress is needed to achieve competitiveness and improve social inclusion. The Ministry of Education's analytical and decision-making capacity needs to be strengthened. Excess capacity in primary and secondary schools is being addressed by local decisions to determine which facilities would be closed, based on national criteria. Tertiary education has been a free good which has limited the availability of resources. The introduction of tuition reform at the tertiary level remains a priority for the Government despite some political opposition. An implementation strategy for life long learning, including the modernization of the vocational education system, needs to be developed.

17. Public administration reform has been pursued by the Government, but further reforms are needed. The merit basis for staffing needs to be enhanced as there are too many seniority-based pay steps. Limited flexibility prevents needed staffing changes. Training for civil servants needs to be enhanced.

18. The judicial system needs to improve its efficiency and effectiveness to become more responsive to the needs of society and the market. This requires enhanced capacity in the areas of human resources, and information and document management. The market for legal services is too exclusive and the poor especially need to be given greater access to this system through better targeting of legal aid. A regulatory impact assessment is needed to better evaluate the impact of laws.

19. Energy sector reforms have proceeded quickly with substantial privatizations of distribution companies, the implementation of a regulatory framework, and the development of an energy efficiency strategy. There is a need to continue ongoing work to improve the regulatory framework for electricity distribution and gas, develop an implementation framework for renewable energy, and prepare an energy efficiency action plan.

20. Wide-ranging financial sector reforms have been introduced with the private banking system now operating in a reasonably competitive framework. However, further reforms are needed to create a more conducive environment for financial sector growth. Creditor rights need to be strengthened, the quality of financial statements needs to be improved, and credit information needs to be made more accessible. Non-bank sources of finance need to be developed, including leasing, factoring, venture capital, commercial paper and bond markets. A strategy should be formulated to promote the development of a capital market. Financial sector oversight should be further strengthened, including through effective implementation of an integrated supervision structure under the auspices of the National Bank of Slovakia (NBS), adequate enforcement of newly applicable international accounting and auditing standards, and enhanced supervision of the insurance sector and of both the new mandatory and existing voluntary private pension funds.

21. There is a need to continue to improve the investment climate, especially to support the development of SMEs as an engine of growth. The regulatory framework should be further streamlined and simplified to reduce the administrative burden that affects the SME sector disproportionately. This reform would include further simplification of licensing, permit and inspection procedures.

22. In agriculture, Slovakia will need to build on an important array of reforms (such as removing the large farm bias and the emphasis on self-sufficiency while observing a hard budget constraint) by implementing the single area payment scheme under the Common Agricultural Policy (CAP), improving market linkages, enhancing the competitiveness of agriculture, and promoting rural development through efficient structural policies.

23. While Slovakia is developing programs to further improve its transportation, communications, and other linkages to its western neighbors as part of its EU accession program, it should also evaluate the need for regional linkages to make sure that development opportunities are not unduly constrained.

24. Slovakia is subject to periodic and devastating floods along the Danube and its tributaries. In response, it has begun implementation of a well formulated flood protection

program. But the pace of investment needs to be accelerated given the apparent increased frequency of severe and costly floods throughout the region.

25. Finally, the Government faces the challenge of improving communications to promote public understanding of and support for structural reforms. The pace of change in Slovakia and the perception of declining welfare for many regions and segments of the population has dominated public perception of reform and its large net benefits. A clear presentation of the benefits of reform is needed, with best-practice comparisons to Slovakia's European neighbors.

26. While these are manifold and significant challenges, Slovakia has already demonstrated how much can be accomplished in a short period of time. With the continued commitment of the authorities, Slovakia should proceed in the future as it has in the past, addressing these challenges by formulating and implementing practical and effective solutions. As a partner in development, the World Bank stands ready to assist where needed in these efforts.

IV. PAST WORLD BANK ASSISTANCE AND LESSONS LEARNED

A. PAST WORLD BANK ASSISTANCE: LENDING

27. The Bank's first CAS for Slovakia covered FY01-03. The CAS proposed assistance to help Slovakia complete transformation reforms, strengthen governance and build institutions, improve social security, enhance human development, and meet environmental standards. At that time, the new Government was planning a rapid acceleration of reforms to move Slovakia to the first rank of EU accession candidates. The authorities also aimed to improve fiscal consolidation to reduce a large deficit, among other objectives. Although there had been an active advisory and technical support program from the late 1990s, there were no projects under implementation.[5] The CAS proposed a lending program of US$415 million, including an Enterprise and Financial Sector Adjustment Loan (EFSAL) in support of sweeping banking and corporate sector reforms, and a number of investment projects: Social Benefits Reform Administration, Public Finance Management, Judicial Reform, and Social Sector Investment.

28. The EFSAL was approved in FY02 for Euro 200 million (US$177.3 million equivalent), and has played an important and wide-ranging role in the reform and restructuring of the banking system, strengthening bank regulation and supervision, implementing a strategy to work out the large stock of non-performing claims taken off the books of the state banks, introducing a new banking law, measures to improve bank accounting and auditing, bank closure and deposit insurance, and improving the legal framework for bankruptcy, collateral claims, and the laws dealing with corporate governance, among others. The third tranche of the loan was released (with full compliance) on April 21, 2004, ahead of Slovakia's accession to the EU.

29. The FY02 Social Benefits Reform Administration project was approved for Euro 23.2 million (US$23.5 million equivalent), with the objective of strengthening institutions (to support pension reform design, human resource training, and public information), establishing a unified contribution collection system, and developing a client database and other information systems. The FY03 Public Finance Management Project was approved for Euro 5.0 million (US$5.5 million equivalent) and is now playing an important role in improving budget processes, strengthening the macro-economic analysis and forecasting capacity of the Ministry of Finance,

[5] Earlier projects included the successfully implemented SAL, telecommunications and rehabilitation loans.

strengthening debt management and treasury capability, and supporting effective coordination of the overall reform effort. The Social Sector Investment Project proposed in the FY01 CAS was modified in concept and focused to address Slovakia's priorities and constraints as the FY04 Health Sector SECAL for Euro 55 million (US$62.9 million), accompanied by a Health Sector Technical Assistance (TA) Loan for Euro 10.58 million (US$12.58 million). These projects support the Government's comprehensive health reform with measures on both the demand and supply side to lower costs, reduce expenditures leading to fiscal sustainability while restructuring the delivery of health services to improve quality including measures to improve access for vulnerable groups. The accompanying TA loan is an important indication of the importance that the Slovak Government attaches to getting the best technical advice to support its reform agenda.

30. The five ongoing projects are rated satisfactory in terms of meeting development objectives and implementation progress, and the one (of three) closed project evaluated by OED was rated highly satisfactory (see annex B2).

B. PAST WORLD BANK ASSISTANCE: AAA

31. Non-lending assistance has played an important role in Bank support for Slovakia, and has had an important impact on policy reforms in priority sectors, as indicated by the Quality Assurance Group's (QAG) rating of the overall quality of AAA as "highly satisfactory." The Development Policy Review (Report No. 26607, June 2003) proposed a range of reforms to promote structural transformation, new expenditure strategies, and improved governance, many of which served as a basis for government programs. In agriculture, the report "Food and Agriculture in the Slovak Republic: The Challenges of EU Accession" (White Cover, September 2002) proposed a series of reforms (remove current policy emphasis on self-sufficiency, prepare for the adoption of EU agricultural policies on accession, eliminate agricultural policy bias in favor of large farms, impose hard-budget constraints, and facilitate the adoption of EU compliance in food safety standards by Slovakia's food processing industry). The report was translated into Slovak and its recommendations were adopted almost in their entirety. In April 2004, an international workshop was organized to share the experience and challenges of preparing for EU accession with Slovakia's neighbors, and to discuss programs and policies, including Bank assistance, for the future. The two FIAS studies in 2000 and 2001 analyzed the regulatory and administrative burdens for foreign and domestic investment and recommended reforms, many of which have been introduced. The "Living Standards, Employment, and Labor Market Study" (Report No. 22351, February 2002) provided new information on poverty and led to systemic reforms of social assistance and labor market policies which improve work incentives while strengthening support to the poor. The study on "Poverty and Welfare of Roma in the Slovak Republic" (Report No. 28768, April 2002) was the first study to address Roma issues as a poverty and economic development issue, and led the Government to request support for a Social Development Fund which will support demand-driven development initiatives from the marginalized communities.

32. The Financial Sector Assessment Program (FSAP) provided a comprehensive review of financial sector strengths and weaknesses, supported the implementation of the reform agenda under the EFSAL, and highlighted key additional policy challenges for further development of the financial system going forward. In energy, the Bank has assisted in providing options on institutional structures to support a new regulatory framework, assisted in the privatization of distribution companies, and provided support for the formulation of a national energy strategy, while working with a bilateral donor (Austria) in developing a renewable energy plan.

33. IDF grants have also been an important component of the Bank's assistance strategy. The IDF grant for Bankruptcy Reform assisted with the preparation of a new modern draft bankruptcy law, and the design of a regulatory framework for bankruptcy trustees. IDF grants have also played important roles in assisting judicial and legal reform, accounting and auditing reform, and capacity building for the Roma office. An IDF grant for Infrastructure Regulatory Reform is assisting the newly established independent regulator, the Regulatory Office for Network Industries (RONI). An FY04 grant will support the Government's efforts to strengthen institutional capacity to formulate and implement a communications strategy for the reform agenda.

C. LESSONS FROM THE PAST, PERSPECTIVES FOR THE FUTURE

34. The World Bank has fulfilled and in many respects exceeded the program outlined in the FY01 CAS. Virtually all products envisioned in the last CAS have been delivered, with appropriate modifications as needed, and these have played an important role in assisting Slovakia to perform as well as it has, which is very well indeed. On the basis of this performance, Slovakia deserves to be robustly supported by the Bank in the critical period of its initial membership years in the EU. Although Slovakia enjoys good access to capital markets at this point in time, it wishes to remain fully engaged with the Bank in recognition of the complex development challenges ahead. Should Slovakia's per capita income continue to grow at recent rates so that it appears to be firmly on a convergence path within the EU and it makes continued progress on structural reforms, it is likely that our future partnership would strongly emphasize Slovakia's emerging role as a donor.

35. During the period of this partnership framework (FY05-07), Slovakia welcomes World Bank technical assistance and modest amounts of lending. Both are seen as useful to bring OECD and other comparator country experience to bear on the problems Slovakia wishes to address, provided the Bank's technical assistance continues to meet high performance standards. The Government's desire for rapid reform design and implementation is constrained by capacity, since there are real constraints on the speed with which public administration can be reformed and rectified. The Bank plays, and would continue to play, an important role in supplying technical assistance to address this constraint. In a similar vein, the Bank is able to assist Slovakia to improve multi-sectoral coordination which constrains effective reform.

36. In addition, Government communication of the reform agenda is not strong, with consequent lack of understanding of goals, nature, and benefits of economic reforms among stakeholders and beneficiaries. Bank participation in and endorsement of the reform program is important in buttressing Government's communications with the public and securing support for the reforms.

37. To continue to provide excellent policy advice and remain relevant, the Bank will align its support with Slovak/EU priorities consistent with Bank corporate priorities. Such advice should continue to be solid technically and draw on the best experience of OECD countries which Slovakia is trying to emulate. For advice to be useful, the Bank has to move exceptionally quickly given Slovakia's rapid formulation and implementation of reforms. The "EU 8 Framework[6]" paper proposes a new framework to facilitate the rapid flow of Bank technical assistance, including pre-approval by the Board of an envelope within which individual country

[6] See "Framework for World Bank Support to EU8 Countries," draft Board Paper, May 2004.

loans would be made through streamlined approval procedures covered by standard loan documentation in line with horizontal APLs.

38. Beyond small amounts of lending for technical assistance, however, Slovakia's demand for Bank funding will be shaped by the competitiveness in underlying financial terms relative to other funding sources, balanced by its flexibility as a risk management tool. The financial terms available in the future on international capital markets will evolve based on general market conditions and the perception of specific country risk. Slovakia has, in recent years, improved substantially the terms of its market access and has been able to borrow on the bond market recently at rates 30 or more basis points below the all-in costs of IBRD lending. On the other hand, IBRD's Fixed-Spread Loan has several embedded flexible features that can make it a useful tool for public debt risk management. Indeed, not only does the Fixed-Spread Loan offer a large number of possibilities in terms of customizing the repayment profile at loan negotiation, it also permits changes to the financial characteristics of all or part of the loan throughout its life (currency, interest rate fixing/unfixing, interest rate caps and collars).

39. There is currently ongoing work with Slovak public debt management authorities to gain better mutual understanding of the possibilities stemming from the above, which would allow a clearer formulation of the Bank's financial role in of the Country Partnership Strategy, including options presented below.

40. Separately from the purely financial terms, there are the additional indirect costs of borrowing from the Bank, such as the number of steps needed to satisfy Bank requirements for each operation, and the time needed to complete them. In the context of the "Framework for World Bank Support to EU8 Countries," the Bank will endeavor to reduce these indirect costs as fully and quickly as possible. Under this approach, the Bank would accredit counterpart institutions in Slovakia for investment or policy support lending (as in the case of technical assistance discussed above) for financial management, procurement, and safeguards. In so doing, the Bank's Institutional Fiduciary Assessments will bear in mind harmonization/alignment with the EU, and reliance on prior assessment/certification work done by EU institutions, as well as the EU's mandatory requirements for Slovakia to comply with EU directives. Based on demand, the Bank could then respond rapidly with streamlined approval procedures for such operations which relied on such accredited institutions.

41. With this new framework, access to policy lending in support of either new reforms or existing good policies would be conditioned on the country's performance at the sector level for SWAps or SECALS while maintaining satisfactory macroeconomic progress in line with the country's own convergence program. There are two ways in which the Bank-Slovak partnership might proceed in this case. First, the Bank can bring value added by assisting Slovakia to access EU funds which will become available to Slovakia as a new member state; in particular, the Structural and Cohesion Funds. In order to be able to utilize this EU funding, Slovakia will need to generate projects and programs which qualify for funding, and the Bank may be of assistance in some of these, for example, by using the Bank's project modalities where appropriate. In this context, the Bank could provide TA to build capacity at the local level for developing and managing the project necessary to access structural funds and use them well.[7] Further, the Funds require co-financing ranging from 50 to 85 percent, which the Bank could assist in providing.

[7] For example, the proposed Social Development Fund would support building regional and local institutions which will develop, propose, and implement projects under EU funds.

Such potential Bank financial support for Slovakia would take the form of co-financing in support of maintaining or implementing policy and programs. The Bank could of course also provide financial assistance outside of co-financing, should that be desired.

42. Operations which are selected for inclusion in the program should meet certain criteria. The reforms that they support should have a high payoff in terms of either equity or growth. Bank assistance should not duplicate other sources of funds or expertise and Bank assistance should reflect the Bank's comparative advantage. Reforms to be supported by the Bank should have a near or medium term impact, other factors being equal.

43. In addition to lending, AAA has been and will continue to be an important aspect of the Partnership. Slovakia is a best practice example in the use of AAA. In addition to the benefits which AAA brings to Slovakia, there is a payoff to the Bank in pursuing AAA in Slovakia because of the lessons learned which are applicable in less advanced countries. Nevertheless in the context of our evolving partnership the Bank would look to Slovakia to take on an increasing share of the costs of AAA both through cost sharing and borrowing for TA if particular activities grew beyond the Bank's budget constraints. In addition, costs will also be reduced by grouping AAA as appropriate into regional studies (as is currently planned in FY05-07 for studies on public expenditure/fiscal reforms and labor markets).

V. THE SLOVAKIA-WORLD BANK PARTNERSHIP FY05-07

A. CONTEXT

44. The macroeconomic scenario on which the Slovakia-World Bank partnership is predicated assumes continued economic growth exceeding the average for EU countries, low inflation, continuing substantial FDI flows, current account deficit averaging about 3 percent of GDP through 2007, and the Government's fiscal deficit declining to 3 percent of GDP in that year. All of this would be satisfactory progress towards meeting the Maastricht criteria and subsequently joining the European Monetary Union.

45. Within this scenario, Slovakia could finance a majority of its fiscal deficit by borrowing externally, with the implication that it would borrow at least US$1 billion per year on external markets. The strategy is to borrow in Euros, so that as the country moves towards the adoption of the Euro, risks are minimized. This is consistent with exploring borrowing opportunities with the Bank which can, of course, lend in Euros. Should Slovakia determine that it would like to draw more substantially on this partnership, the framework could accommodate lending in the range of US$100-150 million per year. The following sections outline how such a scenario might play out, depending on Slovakia's more precise determination of its needs in the context of its partnership with the World Bank.

B. THE OUTLINES OF A PROGRAM OF ASSISTANCE

46. The Bank and the Government have identified a number of areas which in effect constitute a menu from which the authorities would determine priorities in the light of pressing needs and perceived advantages of Bank involvement considering the range of instruments available. These can be grouped into three broad headings: a) continued macro and fiscal measures to support prudent and sustainable fiscal management; b) further

structural reforms to enhance competitiveness; and c) poverty reduction and social inclusion. Priorities for Bank engagement are anticipated in each broad category.

C. MACRO/SECTOR FISCAL REFORMS TO SUPPORT PRUDENT MACROECONOMIC MANAGEMENT AND FISCAL CONSOLIDATION

47. The ongoing Public Finance Management loan is supporting the implementation of important fiscal reforms. For the future, the proposed cross-country Public Finance Management Review should offer a further set of reforms to restructure expenditures and reduce the fiscal deficit to meet the Maastricht criterion. There are three aspects which need to be addressed. First, assistance to continue reforms in key sectors, including health, education, and social benefits. Second, to help strengthen the structures needed for effective fiscal decentralization. Third, to review public administration and identify further reforms to promote an improved cost-effective structure. Looking beyond the proposed Public Finance Management Review, there may be scope for policy-based lending to support the implementation of fiscal reforms, especially should these be consistent with Slovakia meeting the priorities identified in the EU's Annual Report.

D. STRUCTURAL REFORMS TO ENHANCE COMPETITIVENESS

48. There will be need for sector reforms to increase productivity and efficiency, beyond the fiscal aspects that may be addressed by the macro/fiscal work noted above. These include addressing issues in:

(a) *Financial and enterprise sector reforms,* building on the reforms supported by the EFSAL and the implementation of reforms identified in the earlier FIAS reports. Creditor rights, credit and financial statement information and corporate governance all need to be strengthened further to facilitate more rapid growth of financial intermediation in support of private sector growth. A corporate governance assessment for banks is planned for FY05 which would assist in defining the need for further improvements. SME sector administrative and structural constraints need to be addressed. The FIAS reports need to be updated and the Bank could help develop a methodology for self-assessment by the Government of the administrative and regulatory barriers to investment. Support for reforms in these sectors could be in the form of analytical work or technical assistance, or in the form of co-financing EU structural funds combined with support for specific policy reforms.

(b) *Labor market mobility constraints and policies which affect employment.* A proposed regional Labor Market Review would look at ways to support the development of a more fully competitive labor force with low unemployment in the new EU members.

(c) *Legal/judicial reforms.* A project (FY05) is under preparation which could include capacity building, improved judicial infrastructure, and reforms to improve the market for legal services. A project preparation facility (PPF) advance if requested would help accelerate project preparation and jump start first phase investment support for restructuring and upgrading the judicial system.

(d) *Education sector reform.* Ongoing TA addresses: (i) measures to improve the responsiveness of higher education to the needs of the global information society; (ii) the

design and implementation of student admission and financing policies; and (iii) the development of a life long learning system in line with other OECD countries and with the Lisbon agenda.

(e) *Agriculture and rural development* which might focus on assistance in implementing the single area payment scheme under the CAP, improving market linkages, and/or promoting rural development in the poorest rural areas of the country, specifically in southeastern Slovakia.

(f) *Flood protection* which would involve support for the implementation of a flood protection program, including advance warning systems and specific containments to protect flood-prone urban areas where damage costs are highest.

(g) *Improvements in the knowledge economy.* This would build on the results of the recent Slovakia Knowledge Economy (KE) workshop and ongoing work in education reform. The aim would be to improve national institutions and programs to enhance the transmission and local adaptation of knowledge and technology to the productive sectors. Thus, the Bank will seek to assist in building on the ongoing reform to increase capacity and efficiency to enable Slovakia to better tap into the global knowledge economy.

(h) *Energy sector pricing and regulation.* Building on the successfully completed and ongoing IDF grants, there is scope for further work on gas/electricity pricing, regulation in the context of continuing support for the RONI, and to support Slovakia's further integration into EU networks.

(i) There could also be scope to assist Slovakia to further *promote the use of renewable energy and improve energy efficiency*. Through the Prototype Carbon Fund (PCF) and related carbon finance vehicles, the Bank could be an important partner in efforts to develop the Slovak Republic's carbon trading market through project development, capacity building and replication of best practices. Potential has been identified for a PCF-financed Renewable Energy project to support a package of small scale renewable energy sub-projects including geothermal, wind and mini-hydro. Further potential opportunities exist to provide PCF support to sustainable waste management and renewable energy projects and projects in the forestry/ land management and transport sectors.

E. POVERTY REDUCTION AND SOCIAL INCLUSION

49. The Bank-Slovak partnership has been working to prepare assistance in developing and implementing policies and programs to address the inclusion of vulnerable and marginalized groups and communities in local governance processes and development. This would improve access to economic and employment opportunities and social services, and further build capacity for excluded communities to propose and implement projects, and work with local governments. Specific issues could be covered as follows:

i) *Poverty Assessment*. There is a need to update information on poverty and identify areas where interventions may be warranted, which would be addressed by the Living Standards Measurement Study (FY05). This would also build urgently needed capacity within the Government for monitoring living standards and the impact of

policy changes through TA to the statistical office and line ministries (especially the Ministry of Labor, Social Affairs and Family). Slovakia will also need regular high quality household surveys for monitoring progress on the EU social inclusion process (e.g. the "Laaken" indicators of poverty and welfare). Finally, the Poverty Assessment will more clearly identify disparities which may be emerging as a result, for example, of reforms affecting public sector employment.

ii) *Poverty alleviation.* There is a need to improve the prospects of disadvantaged portions of the population: (i) through economic development and employment; (ii) improving basic communal services and community infrastructure; (iii) alternative community-based social care services; and (iv) monitoring, and evaluation. The proposed *Social Development Fund (SDF)* project (FY05) would address these objectives. The specific components of the SDF would be: (i) economic development and employment; (ii) basic communal services and community infrastructure; (iii) alternative community-based social care services; and (iv) project management, monitoring, and evaluation. Finally, the project would include technical assistance for capacity building as well as targeted support for developing Roma communities.

iii) *Education.* Beyond improving competitiveness and enhancing links to the knowledge economy noted above, the World Bank could provide financing for the development of higher and vocational education institutions and teacher training as part of an education modernization program. For the present, the focus is on AAA to address higher and vocational education reform issues, including the need to develop linkages between education, research and innovation, and subsequently to pursue project formulation as and when requests develop.

iv) *Decade of Roma Inclusion.* The World Bank will support Slovakia's participation in the regional initiative, the "Decade of Roma Inclusion 2005-2015." The objective of this activity is to accelerate progress in improving the welfare of Roma in the region through setting quantitative national targets for improving economic status and social inclusion of Roma, and developing and implementing national action plans to achieve those targets.

F. CURRENT PERSPECTIVE ON LENDING

50. As noted above, two potential projects are at an advanced stage of preparation: Judicial Reform and the SDF. Both are primarily oriented toward TA and capacity building. Beyond these, the Bank would be prepared to assist financially in other areas of the partnership framework. Future financial assistance could be provided under the proposed EU8 Technical Assistance Loan Facility to assist with institution and capacity building and the EU8 sector wide approach (SWAp) to pool World Bank financial support with Government funds related to priority programs or sectors. This approach could support policy reforms as well as continuation of existing good policies and investment programs, and could be used to co-finance and/or pre-finance EU Structural and Cohesion Funds.

G. RESULTS FOCUS AND COUNTRY PROGRAM MONITORING

51. Given the approach outlined above, the Bank's role in the Partnership will evolve and in any case be supportive of the Government's efforts. Country performance will be the result of

many factors on which the Bank will have only a selective impact. Since the nature of the Bank's relationship with Slovakia precludes precise programming of tasks, it is not possible to project specific outcomes. However, there are two broad possibilities. First, the Bank assistance program could be limited to T.A. lending and AAA, should Slovakia determine that Bank lending is not sufficiently competitive with other sources of finance available in the market or from other institutions. Program monitoring will then need to be tailored to the impact of increased knowledge and policy advice. Second, should the Government conclude that the features now available in Bank lending products make the Bank more financially competitive (para. 38 above), Bank lending for investment programs and implementation of policy reform would be a more likely possibility.

52. In either case, the Bank should be evaluated on the extent to which it has reduced the non-financial costs now associated with its lending (see para. 40). This would entail pre-qualifying counterpart institutions in Slovakia, and aligning Bank procedures (including financial management, procurement, environment, and social safeguards) to the extent possible with EU policies and procedures. The Bank should also be evaluated on its effectiveness in responding quickly to requests for technical assistance lending which may occur.

53. Project-specific evaluation criteria will also be developed for projects which are implemented. For example, in the case of the proposed SDF Project, outcome indicators would be the number of sub-projects implemented jointly by local governments and communities and the number of beneficiaries participating in projects supported by the SDF.

54. The second case is one in which Slovakia determines that Bank lending is competitive with its other sources, either in strict financial terms or if the Bank's presence enhances, by a sufficient margin, Slovakia's access to EU funding or provides other benefits to offset any financial disadvantage. In this case, it would be appropriate to have overall macro outcomes as a monitoring indicator, with a special focus on the fiscal deficit which would be gradually reduced and maintained to achieve the Maastricht criterion of 3 percent of GDP. In addition, key sectoral indicators should be developed which would complement the overall fiscal indicator. This would be determined according to the specific sector or sectors in which policy support was being extended.

55. The case of Bank lending to co finance EU support is slightly different. Here, the Bank's contribution would be to the formulation of programs suitable for EU financing (and Bank co-financing). However, sector specific outcome indicators would be developed concerning the sectors being supported. The Bank would need to be competitive financially for this to materialize, or almost competitive with incremental costs offset by the value of project formulation under the Bank's program. Aligning and making maximum use of Slovakia's implementation of EU policies and procedures with the Bank's as discussed above in para. 40 would be very helpful in this regard.

H. PARTNERSHIPS

56. Support to Slovakia as it progressed toward EU membership has been closely coordinated with the European Commission (EC) under a Memorandum of Understanding (MoU) signed in response to the EC's Agenda 2000 which called upon IFIs to assist in the enlargement process. The signatories to the MoU include the EC in liaison with EIB, the World Bank, the EBRD, IFC, the Nordic Investment Bank, the Nordic Environment Finance Corporation, the Council for

Europe Development Bank, and the Black Sea Trade and Development Bank. Regular meetings of the parties to the MoU help ensure the complementarity of the respective assistance programs, smooth implementation and enhanced effectiveness of their cooperation.

57. The EU program of assistance is wide-ranging and will play a major role in Slovakia's development, and so is presented in some detail below. The Bank will continue to work closely with the EU to ensure that its operations are as closely aligned as possible to EU support.

58. Pre-accession EU assistance to Slovakia under the PHARE program (to help implement the *acquis communautaire,* strengthen administrative capacity and help countries to develop well-prepared investment and institution building projects) totaled Euro 631.5 million during the 1992-2003 period. Under SAPARD (Special Accession Program for Agriculture and Rural Development), with Euro 38.2 million allocated since 2000, the main priorities have been improving agricultural production, upgrading agri-food enterprises to EC standards, and increasing competitiveness. Slovakia has also benefited from ISPA allocations (Instrument for Structural Policies for Pre-Accession, for infrastructure projects) of Euro 171 million to support one motorway and three railway projects, and another Euro 175.6 million for environment.

59. Slovakia has been allocated EU financing for 2004-2006 as follows: (i) Structural Funds, Euro 1,186.89 million, and (ii) Cohesion Funds, Euro 570.5 million. Accessing these funds will require budgetary realignment to accommodate requirements, in addition to pre-financing and other expenditures related to EU membership.

Box 1: EU Financial Support for the New Member States

Recognizing that in some cases the new members require additional support to strengthen administrative capacity to implement and enforce EU legislation and to foster exchange of best practices among peers, a Euro 426 million Transition Facility has been established for the new member states until the end of 2006. It is intended to help strengthen administrative capacity to implement EC legislation and has no overlap with the areas covered by the Structural Funds. In addition, like all other EU member countries, the EU8 will have access to four EU Structural Funds and the Cohesion Fund.

The EU Structural Funds totaling Euro 14.1 billion from mid-2004 through 2006 are summarized below:

- the European Regional Development Fund (ERDF) aimed at promoting economic and social cohesion within the EU by reducing imbalances between regions or social groups;
- the European Social Fund (ESF) designed to prevent and combat unemployment, as well as develop human resources and promote integration into the labor market;
- the European Agricultural Guidance and Guarantee Fund (EAGFF) to promote structural reforms in the agriculture sector and to develop rural areas; and
- the Financial Instruments for Fisheries Guidance (FIFG) to promote structural reforms in the fisheries sector.

EU Structural Funds are allocated as follows:

- 70 percent for regions whose development is lagging behind (objective 1);
- 11.5 percent for economic and social conversion in areas experiencing structural difficulties (objective 2);
- 12.3 percent to modernize training systems and create employment outside the objective 1 regions where such measures form part of the strategies for catching up (objective 2); and
- 5.35 percent for four "community initiatives" seeking common solutions to specific problems, such as cross-border and inter-regional cooperation.

The EU Cohesion Fund totaling Euro 7.6 billion from mid-2004 through 2006 is designed to finance projects to improve the environment and develop transport infrastructure in EU8 countries with per capita GNP below 90 percent of the EU average. In this way, the Cohesion Fund contributes to sustainable development of concerned EU regions as well as strengthening cohesion within the EU.

60. The EIB offers Slovakia subsidized credits and has been very active. The EBRD has also been active, having lent Slovakia Euro 625 million, invested Euro 218 million in equity, and put in place guarantees worth Euro 108 million, for a total exposure of Euro 952 million, in support of projects with a total value of Euro 3,280 million.

61. The IMF continues to play a major role in assisting Slovakia. The Article IV consultations and reports play a central role in monitoring developments, identifying needed reforms, and recommending improvements. The IMF has also pursued special reports on fiscal and other matters. As a member of OECD, Slovakia also benefits from the regular, in depth analyses of OECD staff and the collective evaluation process.

VI. CREDITWORTHINESS AND RISK MANAGEMENT

62. At the macro level, Slovakia is strongly creditworthy because of its sound macroeconomic management and its reform program which has attracted large inflows of FDI. Total debt outstanding is 57 percent of GDP in 2003 and is projected to decrease to 52 percent of GDP by 2007. Debt service is only 15 percent of exports of goods and services, projected to decline to 6 percent in 2007. Even though the recent increase in the dollar value of debt has not led to an increase in debt/GDP, this was due largely to the appreciation of the Koruna, although this appreciation in turn reflected real productivity increases. The NBS has been successfully implementing a policy of allowing for appreciation related to such productivity increases, but also seeks to avoid large currency swings and a sharp appreciation that could undermine competitiveness. While current levels of debt and debt service do not raise any serious issues, the Government intends to continue to manage debt very carefully in the future in order to be able to meet the Maastricht criteria, and is being supported in this by the Bank.

63. The large inflows of FDI which have played a central role in the expansion of the automobile industry have raised some concerns about creditworthiness were there to be a downturn in this industry. However, these large inflows need to be put into perspective. The volume of FDI in Slovakia is over US$9 billion,[8] of which US$1.8 billion is in the banking sector, and US$7.3 billion in the corporate sector. Within the corporate sector, US$3.3 billion is in manufacturing, including automobile manufacturing, more than US$1 billion in electricity, gas, and water supply, and another US$1 billion in wholesale and retail sales, including automobile repairs. In sum, something less than half of FDI has gone to the automobile sector. While a serious downturn in this sector would have a noticeable impact on the economy, such risks should be manageable. More important than the macroeconomic risks are risks arising from the fact that three-fourths of automobile sector investment is in the Bratislava region, so that a downturn would pose problems for this region. Thus, prudent macroeconomic management would call for the development of infrastructure in other regions of the country to relax constraints on development there. While FDI is certainly most beneficial to Slovakia, the current patterns of investment do exacerbate regional disparities. Programs to redress these disparities require even more attention in the future than they have received in the past.

64. Potentially large capital inflows are likely to continue complicating the conduct of monetary policy. While the NBS should focus its policy on securing a low rate of inflation, large capital inflows may lead to excessive upward pressure on the exchange rate which could undermine external competitiveness. The key to reducing incentives for speculative capital

[8] See National Bank of Slovakia, Monetary Survey, January 2003.

inflows lies in a sustained reduction in the fiscal deficit and lower interest rates as well as allowing sufficient exchange rate flexibility. Sterilized interventions may also be warranted in the short term, although they are unlikely to be effective over time and further could undermine the income position of the NBS.

65. While a precise lending program is not proposed within the Partnership framework, for purposes of creditworthiness analysis, a Bank lending program in the range of US$100-150 million annually was projected, the maximum amount of lending foreseen in the scenarios outlined above. Again, to test creditworthiness, the extreme assumption was made that all of this would be fast-disbursing. World Bank debt is now less than 1 percent of total debt outstanding and disbursed, and, under these assumptions, would rise to 2.5 percent of total debt by 2007, while IBRD debt service, which is now only 2.3 percent of public debt service, would increase to 3.3 percent of public debt service by 2007. IBRD debt service would be the equivalent of about 0.1 percent of the value of exports of goods and services through 2007. These key indicators are well within the bounds of creditworthiness.

VII. CONCLUDING REMARKS

66. Slovakia has made notable progress in recent years. Its accession to the EU both certifies this progress and presages continued achievements in the future. As Slovakia assumes a new status, it is now appropriate for Slovakia and the Bank to enter into a more mature partnership. To meet this challenge, the World Bank needs to strengthen its capacity to respond quickly and flexibly to Slovakia's development needs. Through this engagement, the World Bank can also help Slovakia share its development experience with other countries and lay the groundwork for its eventual transition to donor status.

James D. Wolfensohn
President

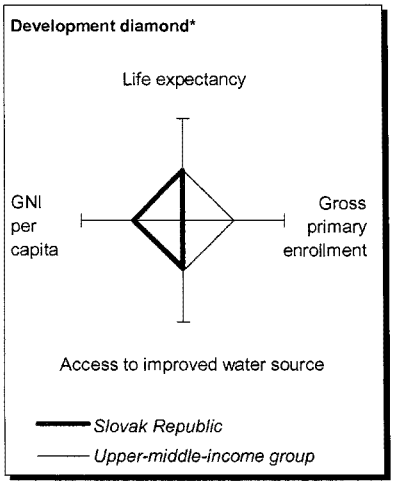
By:
Shengman Zhang

Washington, D.C.
May 6, 2004

Slovak Republic at a glance

4/29/04

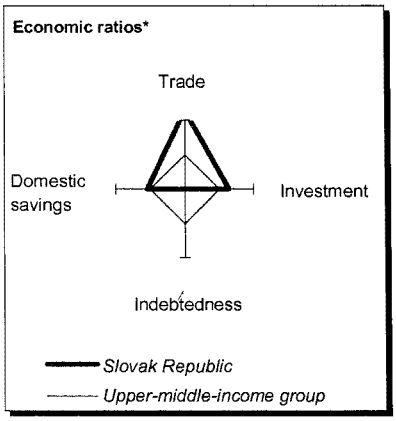
POVERTY and SOCIAL	Slovak Republic	Europe & Central Asia	Upper-middle-income
2003			
Population, mid-year *(millions)*	5.4	476	331
GNI per capita *(Atlas method, US$)*	4,870	2,160	5,040
GNI *(Atlas method, US$ billions)*	26.4	1,030	1,668
Average annual growth, 1997-03			
Population *(%)*	0.1	0.1	1.2
Labor force *(%)*	0.6	0.4	1.8
Most recent estimate (latest year available, 1997-03)			
Poverty *(% of population below national poverty line)*	..	..	..
Urban population *(% of total population)*	58	63	75
Life expectancy at birth *(years)*	73	69	73
Infant mortality *(per 1,000 live births)*	7	25	19
Child malnutrition *(% of children under 5)*	..	..	..
Access to an improved water source *(% of population)*	84	91	90
Illiteracy *(% of population age 15+)*	..	3	7
Gross primary enrollment *(% of school-age population)*	..	102	105
Male	..	103	106
Female	..	101	105



KEY ECONOMIC RATIOS and LONG-TERM TRENDS

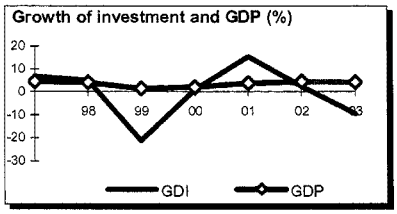
	1983	1993	2002	2003
GDP *(US$ billions)*	..	13.4	24.2	32.5
Gross domestic investment/GDP	..	24.7	29.3	25.3
Exports of goods and services/GDP	..	56.7	71.8	78.0
Gross domestic savings/GDP	..	20.3	22.2	23.8
Gross national savings/GDP	..	20.8	21.1	24.2
Current account balance/GDP	..	-4.0	-8.0	-0.9
Interest payments/GDP	..	1.1	3.8	1.6
Total debt/GDP	..	25.4	53.8	34.1
Total debt service/exports	..	7.7	18.9	9.4
Present value of debt/GDP	..	..	..	..
Present value of debt/exports	..	..	..	..

	1983-93	1993-03	2002	2003	2003-07
(average annual growth)					
GDP	-6.4	4.0	4.4	4.2	4.8
GDP per capita	-6.5	3.8	4.3	4.1	4.7
Exports of goods and services	..	9.3	5.5	22.6	8.9

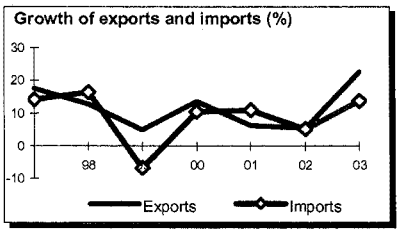


STRUCTURE of the ECONOMY

(% of GDP)	1983	1993	2002	2003
Agriculture	..	5.7	4.1	3.7
Industry	..	33.1	28.6	29.7
Manufacturing	..	18.6	20.1	19.5
Services	..	61.1	67.4	66.6
Private consumption	..	54.9	56.9	55.3
General government consumption	..	24.8	20.9	20.9
Imports of goods and services	..	61.0	78.9	79.5



(average annual growth)	1983-93	1993-03	2002	2003
Agriculture	..	2.6	-1.6	4.4
Industry	..	2.0	0.7	9.2
Manufacturing	..	5.5	-1.2	6.6
Services	..	5.2	6.6	2.0
Private consumption	..	4.1	5.2	-0.3
General government consumption	..	2.9	4.7	3.2
Gross domestic investment	..	5.1	2.2	-9.7
Imports of goods and services	9.6	9.3	5.2	13.8



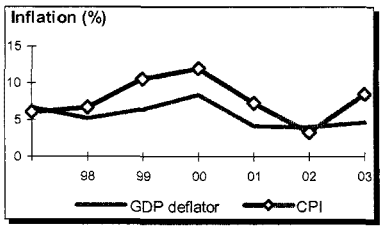
Note: 2003 data are preliminary estimates.

* The diamonds show four key indicators in the country (in bold) compared with its income-group average. If data are missing, the diamond will be incomplete.

Slovak Republic

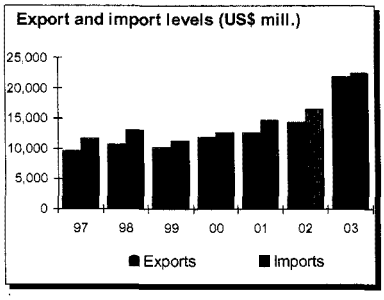
PRICES and GOVERNMENT FINANCE

	1983	1993	2002	2003
Domestic prices				
(% change)				
Consumer prices	..	23.2	3.3	8.5
Implicit GDP deflator	..	28.5	4.0	4.7
Government finance				
(% of GDP, includes current grants)				
Current revenue	..	46.5	44.8	38.3
Current budget balance	..	-3.1	-0.7	-1.1
Overall surplus/deficit	..	-31.2	-5.7	-3.6



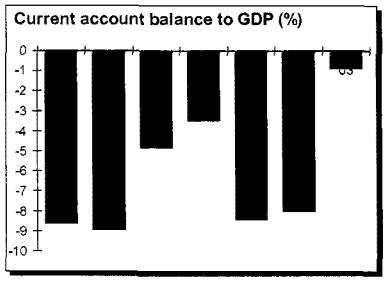
TRADE

	1983	1993	2002	2003
(US$ millions)				
Total exports (fob)	..	5,447	14,382	21,838
Other agriculture	..	..	..	..
Commodity 2	..	..	..	..
Manufactures	..	4,554	12,584	19,510
Total imports (cif)	..	6,379	16,499	22,479
Food	..	556	850	987
Fuel and energy	..	1,324	2,211	2,705
Capital goods	..	..	..	..
Export price index *(1995=100)*	..	..	133	..
Import price index *(1995=100)*	..	..	140	..
Terms of trade *(1995=100)*	..	..	95	..



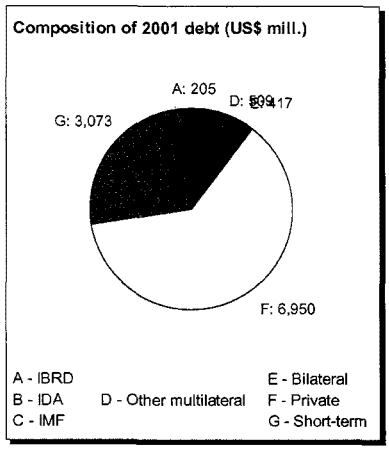
BALANCE of PAYMENTS

	1983	1993	2002	2003
(US$ millions)				
Exports of goods and services	..	7,398	17,151	25,117
Imports of goods and services	..	8,061	18,827	25,524
Resource balance	..	-594	-1,676	-407
Net income	..	-38	-456	-120
Net current transfers	..	100	193	223
Current account balance	..	-532	-1,939	-277
Financing items (net)	..	587	5,585	1,509
Changes in net reserves	..	-55	-3,646	-1,232
Memo:				
Reserves including gold *(US$ millions)*	..	450	9,091	12,126
Conversion rate *(DEC, local/US$)*	..	30.8	45.3	36.8



EXTERNAL DEBT and RESOURCE FLOWS

	1983	1993	2002	2003
(US$ millions)				
Total debt outstanding and disbursed	399	3,393	13,188	18,322
IBRD	0	151	204	179
IDA	0	0	0	0
Total debt service	43	587	1,885	3,734
IBRD	0	9	31	33
IDA	0	0	0	0
Composition of net resource flows				
Official grants	..	529	107	..
Official creditors	-1	96	-78	-73
Private creditors	5	364	1,447	-1,852
Foreign direct investment	..	166	4,007	580
Portfolio equity	..	-263	552	-621
World Bank program				
Commitments	0	55	24	0
Disbursements	0	40	0	0
Principal repayments	0	0	22	24
Net flows	0	40	-22	-24
Interest payments	0	9	9	9
Net transfers	0	31	-31	-33



Slovak Republic
Selected Indicators* of Bank Portfolio Performance and Management
as of March 31, 2004

Indicator	2002	2003	2004	2005
Portfolio Assessment				
Number of Projects Under Implementation [a]	2	3	5	5
Average Implementation Period (years) [b]	0.6	1.1	1.3	1.8
Percent of Problem Projects by Number [a, c]	0.0	0.0	0.0	0.0
Percent of Problem Projects by Amount [a, c]	0.0	0.0	0.0	0.0
Percent of Projects at Risk by Number [a, d]	0.0	0.0	0.0	0.0
Percent of Projects at Risk by Amount [a, d]	0.0	0.0	0.0	0.0
Disbursement Ratio (%) [e]	0.0	0.0	2.9	4.5
Portfolio Management				
CPPR during the year (yes/no)	no	no	yes	yes
Supervision Resources (total US$)	62	206	380	333
Average Supervision (US$/project)	31	103	76	67

Memorandum Item	Since FY 80	Last Five FYs
Proj Eval by OED by Number	3	1
Proj Eval by OED by Amt (US$ millions)	130.4	50.4
% of OED Projects Rated U or HU by Number	0.0	0.0
% of OED Projects Rated U or HU by Amt	0.0	0.0

a. As shown in the Annual Report on Portfolio Performance (except for FY04 and FY05).
b. Average age of projects in the Bank's country portfolio.
c. Percent of projects rated U or HU on development objectives (DO) and/or implementation progress (IP).
d. As defined under the Portfolio Improvement Program.
e. Ratio of disbursements during the year to the undisbursed balance of the Bank's portfolio at the beginning of the year: Investment projects only.
f. FY05 data are projections.
* All indicators are for projects active in the Portfolio, with the exception of Disbursement Ratio, which includes all active projects as well as projects which exited during the fiscal year.

Slovak Republic
IBRD Program Summary
as of March 31, 2004

Proposed IBRD Lending Program [a]

Fiscal year	*Proj ID*	*US$(M)*	*Strategic Rewards b (H/M/L)*	*Implementation b Risks (H/M/L)*
2005	Social Development Fund	10.0	H	L
	Judicial Reform	7.0	H	H
	Subtotal	**17.0**		

a. This table presents the proposed program for the next fiscal year.
b. For each project, indicate whether the strategic rewards and implementation risks are expected to be high (H), moderate (M), or low (L).

Slovak Republic

IFC and MIGA Program, FY 2001-2004

	2001	2002	2003	2004
IFC approvals (US$m)	70.0	0	5.0	0
Sector (%)				
Finance & Insurance	100	0	100	
Total	100	0	100	
Investment instrument(%)				
Loans	0	0	0	
Equity	71	0	0	
Quasi-Equity	29	0	0	
Other	0	0	100	
Total	100	0	100	
MIGA guarantees (US$m) (gross exposure)	10.8	0.8	0.9	0.0

Slovak Republic
Summary of Nonlending Services
as of March 31, 2004

Product	*Completion FY*	*Cost (US$000)*	*Audience a*	*Objective b*
Recent completions				
Development Policy Review	2003	198	G	KG/PS
Food & Agriculture: Challenges of EU Accession	2003	150	G/D/PD	PS
FSAP Follow-up TA Integrated Supervision	2003	52	G/B	KG/PS
Energy TA	2003	52	G/D/PD	KG/PS
Roma/Social Development Fund TA	2003	41	G/B/D	KG/PD/PS
Underway				
Pension Reform	2003-04	72	G/B	KG/PD/PS
Cities of Change	2003-04	36	G/D/B/PD	PD/PS
Education Policy Note	2003-07	475	G/B	KG/PD
CG Assessment	2004	15	G/D/PD	PS
Knowledge Economy Seminar	2004	8	G/D/PD	PS
CG Assessment (Real Sector & Pension)	2004	15	G/B	KG/PS
Living Standards Measurement Study	2004-05	210	G/D/PD	KG/PS
Flood Technical Dialogue	2004-06	76	G/B/D	KG/PS
Agriculture Policy Dialogue	2004-07	280	G/B	KG/PD/PS
Energy EU Accession TA	2004-07	70	G/D/B/PD	KG/PS
National Energy Efficiency Follow-up	2004-07	100	G/D/B/PD	KG/PS
FSAP Follow-up TA Integrated Spn	2004-07	180	G/B	KG/PS
Planned				
Audit of Firms TA	2005	15	G/D/PD	KG/PS
CG Module for Banks	2005-06	90	G/D/B/PD	KG/PD/PS
CG Module for Insurance Companies	2005-06	75	G/D/PD	KG/PD
CFAA	2005-07	90	G	KG/PS
Institutional Fiduciary Assessment for Procurement	2005-07	30	G/B	KG/PS
Public Finance Management - Cross Country	2005-07	750	G/D/B/PD	KG/PD/PS
Labor Market Review - Cross Country	2005-07	175	G/D/B/PD	KG/PD/PS

a. Government, donor, Bank, public dissemination.
b. Knowledge generation, public debate, problem-solving.

Slovak Republic Social Development Indicators

	Latest single year			Same region/income group	
	1970-75	1980-85	1995-2001	Europe & Central Asia	Upper middle-income
POPULATION					
Total population, mid-year (millions)	4.7	5.2	5.4	474.6	503.6
Growth rate (% annual average for period)	0.9	0.8	0.1	0.1	1.3
Urban population (% of population)	46.3	54.2	57.6	62.8	77.2
Total fertility rate (births per woman)	2.6	2.2	1.3	1.6	2.3
POVERTY (% of population)					
National headcount index	..	..	..	..	..
Urban headcount index	..	..	..	..	..
Rural headcount index	..	..	..	..	..
INCOME					
GNI per capita (US$)	..	..	3,760	1,970	4,550
Consumer price index (1995=100)	..	..	159	..	..
Food price index (1995=100)	..	34	232	..	..
INCOME/CONSUMPTION DISTRIBUTION					
Share of income or consumption					
Gini index	..	..	25.8	..	..
Lowest quintile (% of income or consumption)	..	..	8.8	..	..
Highest quintile (% of income or consumption)	..	..	34.8	..	..
SOCIAL INDICATORS					
Public expenditure					
Health (% of GDP)	..	..	5.3	4.0	3.5
Education (% of GDP)	..	..	4.2	4.4	4.4
Social security and welfare (% of GDP)	..	..	10.6	8.8	..
Net primary school enrollment rate					
(% of age group)					
Total	..	..	89	..	96
Male	..	..	89	..	97
Female	..	..	90	..	95
Access to an improved water source (% of population)					
Total	..	..	100	91	88
Urban	..	..	100	96	94
Rural	..	..	100	83	69
Immunization rate (% under 12 months)					
Measles	..	..	99	95	94
DPT	..	..	99	94	94
Child malnutrition (% under 5 years)	..	..	..	..	9
Life expectancy at birth (years)					
Total	70	71	73	69	72
Male	67	67	69	64	68
Female	74	75	77	73	75
Mortality					
Infant (per 1,000 live births)	23	16	8	31	23
Under 5 (per 1,000 live births)	26	19	9	38	27
Adult (15-59)					
Male (per 1,000 population)	..	226	210	317	218
Female (per 1,000 population)	..	105	83	137	114
Maternal (modeled, per 100,000 live births)	..	..	14	..	..
Births attended by skilled health staff (%)	..	..	..	..	..

Note: 0 or 0.0 means zero or less than half the unit shown. Net enrollment rate: break in series between 1997 and 1998 due to change from ISCED76 to ISCED97; ratios exceeding 100 indicate discrepancies between the estimates of school-age population and reported enrollment data. Source: 2003 World Development Indicators CD-ROM, World Bank.

Slovak Republic - Key Economic Indicators

Indicator	Actual 1999	2000	2001	Estimate 2002	2003	2004	Projected 2005	2006	2007
National accounts (as % of GDP)									
Gross domestic product[a]	100	100	100	100	100	100	100	100	100
Agriculture	5	5	5	4	4	4	4	4	4
Industry	36	32	31	31	30	30	29	29	28
Services	59	63	64	65	66	66	67	67	68
Total Consumption	77	76	78	78	76	77	78	77	77
Gross domestic fixed investment	30	26	29	27	26	26	26	26	26
Government investment	10	13	6	5	3	4	4	4	4
Private investment	20	13	23	22	22	22	22	22	21
Exports (GNFS)[b]	61	71	73	72	78	75	76	78	80
Imports (GNFS)	66	73	82	79	80	78	80	81	82
Gross domestic savings	23	24	22	22	24	23	22	23	23
Gross national savings[c]	23	23	21	21	24	24	22	23	23
Memorandum items									
Gross domestic product (US$ million at current prices)	20381	20218	20887	24184	32519	34312	36212	38217	40251
GNP per capita (US$, Atlas method)	3900	3860	3830	4050	4920	5189	5468	5765	6064
Real annual growth rates (%, calculated from 1995 prices)									
Gross domestic product at market pric	1.5	2.0	3.8	4.4	4.2	4.0	4.0	4.0	4.5
Gross Domestic Income	-0.1	2.2	1.6	5.1	3.6	2.0	1.6	5.8	4.0
Real annual per capita growth rates (%, calculated from 1995 prices)									
Gross domestic product at market pric	1.4	1.9	3.7	4.3	4.1	3.8	3.9	3.9	4.5
Total consumption	0.1	-0.3	4.6	4.9	0.6	2.1	3.7	4.5	3.3
Private consumption	2.7	-1.0	4.8	5.1	-0.4	2.3	4.4	5.5	4.1
Balance of Payments (US$ millions)									
Exports (GNFS)[b]	12292	14118	15134	17151	25117	25768	27440	29765	32327
Merchandise FOB	10229	11872	12645	14365	21838	22185	23639	25615	27986
Imports (GNFS)[b]	13166	14584	16780	18827	25524	26645	28874	30894	33166
Merchandise FOB	11321	12777	14770	16497	22479	23403	25471	27190	29320
Resource balance	-874	-466	-1646	-1676	-407	-877	-1433	-1129	-840
Net Income Receipts	-301	-353	-313	-456	-120	-84	-107	-113	-172
Net current transfers	196	118	212	193	249	158	156	154	151
Current account balance	-980	-702	-1746	-1939	-277	-803	-1384	-1088	-860
Net official capital grants	160	92	78	107	100	264	390	436	404
Net total private investment inflows	1384	2723	1314	4559	-40	1320	1386	800	598
Net private foreign direct investment	761	1904	1542	4007	580	1405	1477	897	684
Long-term loans (net)	248	-497	-221	-102	-348	-297	322	241	224
Official	281	-30	60	-78	-7	0	-10	-8	68
Private	-33	-467	-281	-24	-341	-297	332	249	156
Other capital flows, net	-92	-793	720	1020	1797	500	500	500	500
Change in reserves[d]	721	824	143	3646	1232	984	1215	888	866
Memorandum items									
Current account balance (% of GDP)	-4.8	-3.5	-8.4	-8.0	-0.9	-2.3	-3.8	-2.8	-2.1
External debt (% of GDP)	51.6	53.4	52.9	54.5	56.3	54.0	53.4	52.6	51.7
Real annual growth rates (YR00 prices)									
Merchandise exports (FOB)	..	5.0	13.7	6.3	5.5	22.6	8.6	11.3	10.1
Primary	..	..	..	..	..	..	..	..	..
Manufactures	..	..	..	..	..	..	..	..	..
Merchandise imports (CIF)	..	-6.7	10.5	11.0	5.2	13.8	8.3	11.2	10.8

Slovak Republic - Key Economic Indicators
(Continued)

Indicator	Actual			Estimate		Projected			
	1999	2000	2001	2002	2003	2004	2005	2006	2007
Public finance (as % of GDP at market prices)[e]									
Current revenues	49.4	47.3	45.1	44.8	38.3	35.9	36.3	35.9	35.4
Current expenditures	47.0	46.7	45.3	45.6	39.4	37.3	37.9	37.7	36.6
Current account surplus (+) or deficit (-)	2.4	0.6	-0.1	-0.7	-1.1	-1.5	-1.5	-1.8	-1.2
Capital expenditure	9.9	13.3	6.2	5.5	3.3	3.9	4.2	4.2	4.1
Foreign financing	7.1	12.3	6.0	5.7	3.6	4.0	3.9	4.0	3.0
Monetary indicators									
M2 Flow/GDP	6.1	7.7	6.8	3.0	4.1	4.5	4.5	4.3	4.0
Growth of M2 (%)	11.2	14.0	11.9	5.0	6.4	8.0	8.0	7.5	7.0
Private sector credit growth /	4.1	0.3	0.0	11.7	9.7	8.0	5.3	5.2	5.3
total credit growth (%)	6.1	9.1	13.3	0.0	16.9	..	..	..	..
Price indices(YR00 =100)									
Merchandise export price index	88.0	100.0	106.3	112.1	137.4	149.2	166.1	182.9	203.7
Merchandise import price index	90.5	100.0	111.0	116.8	133.0	144.0	160.1	177.4	195.3
Merchandise terms of trade index	97.2	100.0	95.7	95.9	103.3	103.7	103.8	103.1	104.3
Real exchange rate (US$/LCU)[f]	90.8	100.0	109.2	106.4	82.2	85.2	89.9	91.7	93.4
Real interest rates									
Consumer price index (% change)	10.6	12.0	7.3	3.3	8.5	7.8	3.7	3.2	2.8
GDP deflator (% change)	6.5	8.5	4.2	4.0	4.7	4.5	3.0	3.0	2.3

a. GDP at market prices
b. "GNFS" denotes "goods and nonfactor services."
c. Includes net unrequited transfers excluding official capital grants.
d. Includes use of IMF resources.
e. General government.
f. "LCU" denotes "local currency units." An increase in US$/LCU denotes appreciation.

Slovak Republic - Key Exposure Indicators

Indicator	Actual			Estimate			Projected		
	1999	2000	2001	2002	2003	2004	2005	2006	2007
Total debt outstanding and disbursed (TDO) (US$m)[a]	10518	10804	11043	13188	18322	18525	19347	20088	20812
Net disbursements (US$m)[a]	248	-497	-221	-102	-348	-297	322	241	224
Total debt service (TDS) (US$m)[a]	1612	2298	1954	1885	3734	2805	1752	2459	2082
Debt and debt service indicators (%)									
TDO/XGS[b]	85.6	76.5	73.0	76.9	72.9	71.9	70.5	67.5	64.4
TDO/GDP	51.6	53.4	52.9	54.5	56.3	54.0	53.4	52.6	51.7
TDS/XGS	13.1	16.3	12.9	11.0	14.9	10.9	6.4	8.3	6.4
Concessional/TDO	..	..	..	..	..	..	..	..	..
IBRD exposure indicators (%)									
IBRD DS/public DS	4.9	3.8	3.3	3.5	2.3	1.6	6.2	3.8	3.3
Preferred creditor DS/public DS (%)[c]	19.7	30.1	9.3	10.4	6.9	11.2	21.5	13.8	13.4
IBRD DS/XGS	0.3	0.2	0.2	0.2	0.1	0.1	0.1	0.1	0.1
IBRD TDO (US$m)[d]	219	184	205	204	179	275	355	428	487
Of which present value of guarantees (US$m)									
Share of IBRD portfolio (%)	..	..	..	..	..	..	..	..	..
IDA TDO (US$m)[d]	0	0	0	0	0	0	0	0	0

a. Includes public and publicly guaranteed debt, private nonguaranteed, use of IMF credits and net short-term capital.
b. "XGS" denotes exports of goods and services, including workers' remittances.
c. Preferred creditors are defined as IBRD, IDA, the regional multilateral development banks, the IMF, and the Bank for International Settlements.
d. Includes present value of guarantees.
e. Includes equity and quasi-equity types of both loan and equity instruments.

Slovak Republic

Operations Portfolio (IBRD)
as of March 31, 2004

Closed Projects 3

IBRD/IDA *	
Total Disbursed (Active)	134.51
of which has been repaid	0.00
Total Disbursed (Closed)	130.43
of which has been repaid	57.33
Total Disbursed (Active & Closed)	264.95
of which has been repaid	57.33
Total Undisbursed (Active)	201.28
Total Undisbursed (Closed)	0.00
Total Undisbursed (Active & Closed)	201.28

Active Projects

Project ID/Project Name		Last PSR Supervision Rating: Dev. Objectives	Last PSR Supervision Rating: Imp. Progress	FY	Original Amount in US$ Millions: IBRD	Original Amount in US$ Millions: Undisb.	Diff. Between Expected & Actual Disbursements [a/]: Orig.	Diff. Between Expected & Actual Disbursements [a/]: Frm Rev'd
P064542	EFSAL	S	S	2002	177.30	80.19	43.35	
P065954	Health Reform	S	S	2004	62.92	70.08		
P082879	Health TA	S	S	2004	12.38	13.48	2.25	
P069864	Public Finance Mgt	S	S	2003	5.45	5.56	0.44	
P038090	Social Benefit Reform	S	S	2002	23.50	31.98	13.89	
Overall Result					281.55	201.28	59.93	

a. Intended disbursements to date minus actual disbursements to date as projected at appraisal.

Slovak Republic
Statement of IFC's
Held and Disbursed Portfolio
as of February 29, 2004
(In US Dollars Millions)

		Held				Disbursed			
FY Approval	Company	Loan	Equity	Quasi	Partic	Loan	Equity	Quasi	Partic
1999	SEF West Exp-Imp	0.79	0	0	0	0.79	0	0	0
	Total Portfolio:	0.79	0	0	0	0.79	0	0	0

Approvals Pending Commitment

	Loan	Equity	Quasi	Risk Mgt	Partic
None					

Slovak Republic - Bank Engagement

Priority	Ongoing Activities	Proposed New Activity	Possible New Activity (T.A. loan and/or budget support)	Additional Possible Areas for Lending or budget support
Fiscal Consolidation	1. Lending: Public Finance, Health Pensions 2. T.A.: Education	1. AAA: EU8 Comparative Fiscal Study		
Convergence: Competitiveness	1. Lending: EFSAL 2. T.A. Education, Legal Sector, Energy Sector, Agriculture	AAA: EU8 Comparative Labor Market Study	Legal/Judicial Reform, Infrastructure (flood protection), energy sector, financial sector	1. Assistance to meet EU Acquis Communautaire; 2. Cofinance EU Structural Funds (i.e. for private sector/SME development); 3. Knowledge economy (t.a. or budget support)
Social Inclusion	SDF Project Preparation	1. SDF Project 2. AAA: Poverty Assessment	Fiscal Decentralization	

Slovak Republic – Summary of Development Priorities

Network Area	*Country Performance[1]*	*Major Issue[2]*	*Country Priority[3]*	*Bank Priority[4]*	*Reconciliation of Bank and Country Priorities[5]*
Poverty Reduction and Economic Management					
Poverty Reduction	Good	Social exclusion Unemployment	M	H	Major CPS focus
Economic Policy	Excellent	Fiscal sustainability	H	H	
Public Sector	Good	Public administration, centralization	H	H	
Gender	Good	Labor force participation	L	L	
Human Development					
Education	good	Inclusion, competitiveness, sustainability	M	H	CPS focus
Health, Nutrition, and population	Good	Low efficiency, fiscal sustainability, excess capacity	H	H	
Social Protection	Good	Fiscal sustainability	H	H	
Environmentally and Socially Sustainable Development					
Rural Development	Fair	Rural areas underserviced	M	L	EU funding,programs
Environment	Fair	Legal framework	M	L	EU standards, funding
Social Development	Poor	Social exclusion of Roma	H	H	
Finance, Private Sector & Infrastructure					
Financial Sector	Good	Competitiveness, access	H	H	
Private Sector	Good	Governance	H	H	
Energy& mining	Good	Regulation	H	H	
Infrastructure	Good	Management	M	M	EBRD, EIB lead

[1] Use "excellent", "good", "fair", or "poor".
[2] Indicate country specific problems
[3] To indicate priority use "low", "moderate", or "high".
[4]To indicate priority use "low", "moderate", or "high".
[5] Give explanation if priorities do not agree.

Slovak Republic: Consultations on the Country Partnership Strategy

As part of the preparation of the CPS for 2005-2006, a program of consultations on the draft Strategy with the representatives of Slovak civil society was launched in Slovakia. The primary purpose of the program was to seek inputs from a wide spectrum of stakeholders in regard to the future activities of the World Bank in Slovakia. The Bank team also used this opportunity to meet its partners including in the remote regions of the country.

The draft CPS document was prepared following discussions with the representatives of the Government of Slovakia and leading opinion makers. As background, a baseline survey was conducted covering a nation-wide sample of 1,040 respondents. The survey showed that more than half of the country's population (59 percent) was aware of the World Bank. Among those who heard about the Bank, 59 percent had a favorable opinion, while 13 percent held unfavorable opinions. The World Bank is regarded less favorably in comparison to the EBRD, but more favorably than the IMF.

Almost half of the respondents were unable to identify the World Bank's activities in Slovakia and more than 30 percent could not see a link between the World Bank's operations and the reforms program of the Slovak Government.

The CPS consultation process consisted of several feedback instruments/ events: (i) presentation of the Strategy to the government officials at the Joint Portfolio Review Meeting in February 2004, (ii) electronic consultation through the Country Office website (March-April 2004), (iii) a series of consultation meetings held in three major cities in Slovakia: Kosice, Banska Bystrica and Bratislava (March 29- April 2, 2004).

Both, the Slovak and English versions of the Strategy were placed on the Country Office website in the beginning of March 2004 and were subjected to comments by wider public. In addition, the draft CPS in Slovak was distributed along with invitation letters to more than 700 individuals and organizations prior to the consultation meetings. This public access resulted in a number of comments submitted by representatives of the NGO sector, local governments, and academics. All comments were made available on the World Bank web site.

For the consultation meetings, a methodology was developed by representatives of the World Bank, in cooperation with the Bank's key NGO counterparts in Slovakia, a Slovak consultancy company hired as an independent facilitator for the CPS consultations. Information about the public consultations was also placed on the Country Office website as well as on the information server of the civil society organizations in Slovakia www.changenet.sk.

Up to 60 people participated in each of the three consultation meetings bringing together representatives from the NGO sector, local governments, academics, business, and media. Each meeting consisted of two parts. The first session focused on the socio-economic analysis of the Slovak economy and the challenges to be addressed. In this regard, the participants were encouraged to review the analysis provided in the CPS and comment on issues that were either omitted or insufficiently addressed. The second session centered on how these challenges could be addressed and the possible role of the World Bank in this process. Discussions following each of the presentations took place in one or two working groups established on the basis of main themes introduced in the CPS. The working groups then reported their observations and recommendations during the plenary session.

In the process of consultations the Bank indicated that all the comments and views made by the participants would be recorded, analyzed and discussed among the sector staff. They were also informed that the comments would be conveyed to the Slovak government.

Participants felt that the draft CPS presentation was a good starting point for consultations and that the analysis of the social and economic situation in Slovakia included in the document was comprehensive and

objective. Participants also appreciated some of the special points of concern, including poverty, unemployment, and minorities. Overall, it was agreed that the presentation of the positive and negative aspects of the ongoing transformation of public administration formed an important cornerstone of the analysis. However, the claim was made that the CPS should note that corruption and clientism is not sufficiently combated, and many institutions are too weak to redress this problem.

There was some concern about aspects of the analysis which were felt to be missing or underemphasized, including: (a) the brain drain, especially the number of people with university education who leave Slovakia, (b) gender issues, and the greater impact on women than on men in implementing education, social, pension and health reforms, (c) impact of long term unemployment (economic, psychological, and social), (d) the need to give a better qualitative as well as quantitative description of poverty, (and that social safety nets have been weakened for fiscal reasons while subsidies increased for large corporations), (e) analysis of the role of life-long learning; and (f) transparency of the ongoing reforms, and the causes of insolvency of the health service. The participants also felt that the CPS should look at income distribution with a view to assessing changes needed to sustain long-term support for the reform.[9] The strong decline in the support of the Government coalition was caused by the fact that structural reforms were not adjusted to the situation faced by low and middle income classes. Social inclusion and poverty reduction strategies should be introduced before transformation programs are started, to prevent rather than trying to undo the problems they create.

Concerning the proposals made in the CPS presentation, most of participants felt that a number of recommendations could be improved. They felt that the CPS should present a more integrated and coordinated view of all the ministries in the context of a long term vision of growth and development. Concerning the energy sector, the participants suggested a stronger focus on renewable energy while greater emphasis might be given to the use of nuclear energy. Generally, adequate supply of electricity should be ensured. The CPS might look more closely at agriculture and how to strengthen rural development. The CPS might also re-evaluate the impact of the introduction of uniform VAT.

Concerning health care reform, participants felt that the Bank had appropriately emphasized the need to ensure a balance between supply and demand, but that the implementation of health sector reform suffered from poor communication resulting in a general perception of a lack of coordination.[10] It was emphasized that the quality of service should be enhanced, possibly by creation of a specialized institution to evaluate service delivery. Both quality and quantity needed to be taken into account in health care financing. It would also be important to analyze the existing labor market for the medical professions in order to better accommodate the needs of the health sector. Primary health care should become a vehicle to better address poverty.

Education was another important focus of discussion. While the Government had accepted the concept of reform through the year 2010, implementation was inadequate. Education expenditures accounted for only a small percentage of GDP. Resources flowing to science and research should be increased, especially since their share in GDP was lower than in Poland, Hungary, or the Czech Republic. There was a high degree of mistrust in the academic community towards the Ministry of Education concerning implementation of accepted targets. It would be important to depoliticize the quality assessment system for the universities by creating an independent body rather than leaving this with the Ministry of Education. The Government should enable and encourage the flow of funds to universities, including from external sources. There was also some support for funding university tuition from the state budget. The participants felt that stronger support should be given to enriched/accelerated education for talented and gifted children, especially outside Bratislava where such facilities were particularly lacking. Primary education should be emphasized to better address poverty/social inclusion.

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[9] The proposed LSMS (Living Standard Measurement Study) for FY05 would address this point.

[10] This is to be addressed by the DGF (Development Grant Facility) for communications

Education reforms being implemented had addressed low teachers' salaries, lack of resources for research and development and libraries. Facilities were so poor that it would be difficult to implement a merit based faculty selection. Any plan to introduce tuition payments for university students should be accompanied by a carefully formulated plan to assist poorer students Adult education was not lacking as many schools and businesses had established Lifelong Learning Institutes. But there was little demand for these due to costs, insufficient assistance from employers, and little social impact. A system is needed to be implemented to support efforts of adults striving for a university degree.

With respect to Slovakia's development agenda, inclusive development should also promote equality between men and women. There is a need to pro-actively reduce gender disparities, taking account of gender analysis under all reforms. The CPS should also take into account the aspect of poverty among females and the increasing income gap between women and men. Concerning social benefits reform, the new system to be launched in January 2005 should take account of gender analysis and adopt measures to prevent the poverty of females in retirement age groups. A gender mainstreaming strategy as well as gender budgeting should be adopted, and a gender analysis system and related measures for government reforms introduced. Eventually, the expected broad outcome from the World Bank–Slovak partnership should be the reduction of gender disparities and equal opportunities for men and women.

Concerning public administration, reforms to derogate responsibilities to regional authorities had not been accompanied by fiscal decentralization. There is also some duplication between the central and regional administrative authorities. The civil service was overstaffed with continuing staffing increase, without commensurate increases in administrative capacity. Service standards were low, and the administration was heavily politicized.

Concerning private sector development, there was a need to remove administrative constraints and otherwise improve the environment for SME development.

There were also a number of suggestions concerning poverty and social inclusion. The CPS should look at regional disparities and regional development patterns which lead to the marginalization of particular social groups. Many measures of the Government (e.g. FDI incentives) promoted rather than reduced regional disparities. Unemployment needed to be tackled through sustainable job-creation in rural areas. Grants and loans by the World Bank through commercial banks could be important if transparency and involvement of local stakeholders was assured. Assistance should be allocated regionally. Quality standards needed to be introduced in social services. Some participants felt that independent institutions should be developed to provide information and counseling in the social and legal spheres. There was also a suggestion for a law to be passed to protect vulnerable groups. Regarding the Roma in particular, examples of successful projects for the Roma population should be more broadly disseminated. Ecological agriculture for the Roma should be supported.

Education for Roma children is not satisfactory and should be enhanced, from pre-school through university. For example, many Romas attend primary schools for handicapped children. A task force of Roma experts is needed to comment on and improve the National Action Plan for Roma Communities.

For the future, institutions needed to be strengthened through transparent technical assistance and twinning. The World Bank's activities should help ensure transparency, partnership, sustainability, and implementation of environmental and social impact assessments. A thorough evaluation of past and ongoing structural reforms which were supported by the Bank should be carried out by an independent agency.

Following the consultations, comments were placed on the World Bank's Slovak Country Office website.

MAP SECTION