DOCUMENT OF THE EUROPEAN BANK
FOR RECONSTRUCTION AND DEVELOPMENT

STRATEGY FOR THE SLOVAK REPUBLIC

As approved by the Board of Directors on 24 February 2009

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ABBREVIATIONS

BIDSF	Bohunice International Decommissioning Support Fund
CEB	Central Europe & Baltics
EC	European Commission
ECOFIN	Economic and Financial Committee of the European Union
EIB	European Investment Bank
EU	European Union
EU EBRD SME	EU/EBRD Small and Medium Enterprise Financial Facility
EU EBRD MFF	EU/EBRD Municipal Financial Facility
ERM2	EU's Exchange Rate Mechanism
ESCO	Energy Service Company
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
HALE	Health Adjusted Life Expectancy
HICP	Harmonised Index of Consumer Prices
IFC	International Financial Organisation
IMF	International Monetary Fund
IOSCO	International Organization of Securities Commissions
IPO	Initial Public Offering
KOZ	Confederation of Trade Unions
LIS	Legal Indicator Survey
LLU	Local Loop Unbundling
LS-HZDS	People`s Party-Movement for a Democratic Slovakia
MEI	Municipal Environmental and Infrastructure (sectors)
MSME	Micro, Small and Medium Enterprises
NBFI	Non-Bank Financial Institutions
OECD	Organisation for Economic Co-operation and Development
PBK	Priemyselná banka
PPP	Public- Private Partnership
SE	Slovenské elektrárne
SEFF	Slovak Energy
SKK	Slovak Koruna
SMK	Hungarian Coalition Party
SNS	Slovak National Party
SPB	Slovenská poľnohospodárska banka
SPP	Slovenský plynárenský priemysel, a.s.
SPPF	Slovak Post Privatisation Fund
ST	Slovak Telekom
TC	Technical Co-operation
TUSR	Telecommunications Office of the Slovak Republic
URSO	Office for the Regulation of Network Industries
UVO	Public Procurement Office
VAT	Value Added Tax
VUB	Všeobecná úverová banka, a.s.
WB	World Bank
ZSE	Západoslovenská Energetika, a.s.
ZSSK	Železničná spoločnosť Slovensko, a.s (Slovak Railway Company)

EXECUTIVE SUMMARY

The Slovak Republic continues to meet the conditions specified in Article 1 of the Agreement Establishing the Bank. The country is well advanced in its transition process, with price and trade liberalisation, enterprise privatisation and financial sector reforms approaching the standards of more mature market economies. As another testament to its achievements it has joined the Eurozone from January 2009 (it is the second CEB country to do so after Slovenia).

Since the last country strategy was approved Slovakia’s macroeconomic performance has been solid. Growth in real GDP surged to an all-time high of 10.4 per cent in 2007 before moderating again to an estimated 6.4 per cent in 2008. Unemployment has also fallen to 9 percent in 2008 (although regional inequalities have not diminished and structural unemployment remains high). When the country was evaluated for Eurozone membership in May 2008, it comfortably met all the relevant criteria. The fiscal deficit was a mere 1.9 per cent of GDP in 2007 (down from its peak of 12.2 per cent in 2000), thanks to a significant reduction in expenditure and despite the introduction of the second-pillar pensions which reduced government revenues. Inflation was also well within the Maastricht limit.

However, given the rapidly worsening external environment the outlook for Slovakia has deteriorated significantly in the second half of 2008 and the economy is likely to contract in 2009. While the banking system has so far suffered limited impact from the global financial crisis, current indications are that the next strategy period will see a substantial contraction in the availability of finance, not only for households, SMEs and municipalities, but potentially also for large infrastructure projects that were planned to be financed under PPP schemes. In addition, Slovakia will suffer from a significantly weaker demand for its exports (a large share of which are cars and consumer electronics). As a result, unemployment and regional disparities may increase in the short term.

While Eurozone membership from January 2009 represents a commendable achievement, the external environment as well as economic conditions in Slovakia in the next strategy period will be difficult. This may require bold policy responses from the authorities (with the assistance of others) in support of financial institutions, municipalities and infrastructure sectors in order to ensure that the gains made in transition in these areas over recent years are not squandered. The Government’s package of crisis response measures is a welcome initiative. Clearly, past progress with structural reforms has made the Slovak economy less vulnerable to the global financial crisis than other countries in the region, and there is now an opportunity to build on this progress in areas such as infrastructure, governance, non-bank financial institutions and the social sector. The continuation of reforms will help to sustain the economy’s strength in the current environment, assist in the process of industrial diversification, reduce regional inequalities and enable convergence with EU average income over the medium term. The following institutional and structural policy priorities are paramount:

- Improvements to the business environment (in particular reforms to the public administration and judicial systems) and increased labour market flexibility to maintain competitiveness and help mitigate regional income disparities and structural unemployment.

- Promotion of alternative energy sources, greater energy efficiency and development of renewable energy, which lag behind regional standards. It is not clear that the government's interventions in the energy sector have been helpful in this regard.
- Modernising municipal and environmental infrastructure with the assistance of EU structural and cohesion funds, private sector involvement and commercial co-financing from local sources where possible. This will require the strengthening of municipal administrative capacity.
- Mobilising private sector funding and expertise for development of efficient transport infrastructure network, such as the competitive award of PPP contracts for motorway construction, maintenance and operation.
- In case it becomes necessary, safeguarding the stability of the financial sector through selective support to financial institutions and fostering the continued provision of credit to households, SMEs and municipalities.
- Guaranteeing the operating stability of the well-functioning multi-pillar pension system in order to ensure the long-term sustainability of government finances.
- Promoting the development of equity finance for SMEs, using private equity funds, which lags behind regional peers.

Since the last country strategy was approved, the Bank activities in the Slovak Republic have remained limited as a result of significant progress in transition and, in particular, the emergence of a strong, competitive banking sector. The Bank has signed 13 projects for an amount of EUR 87 million in 2006-2008. The most significant achievement during the period was the extension of the successful SME financing model to provide loans for energy efficiency and renewable projects with the support of the Ministry of Economy and the BIDSF. The Bank's policy dialogue efforts were instrumental in developing critical road infrastructure using PPP financing.

The Bank's operational objectives in Slovakia are determined by the crisis response programme adopted by the Board of Directors. The Bank's priority to assist Slovakia in dealing with the crisis is to expand SEFF in order to encourage local banks to continue lending to SME and housing associations and to work closely with commercial banks and other IFIs to mobilise financing for the initial PPP road projects. In light of the crisis and the external environment outlined above, the Bank's activities in Slovakia will be based on the following operational objectives:

- Foster the continued availability of credit to SMEs and municipalities through local banks.
- Participate in the co-ordinated IFI effort to contribute towards financing of viable public-private concession projects in transport infrastructure which are now coming to the market, following best international practice for tendering and contract award. This will complement the available commercial funding and allow for the successful implementation of the first round of public-private partnerships in the country.
- Promote investments in the diversification of energy supply, in energy efficiency and renewable energy to enhance energy security, reduce energy intensity and meet

environmental targets through the expansion of the existing Sustainable Energy Financing Facility.

- In the context of restrained access to debt finance, provide higher-risk products such as equity for local corporations to support viable companies faced with worsening market conditions due to the crisis and, eventually, fund the growth of local companies emerging from the slow down.. Particular attention will be paid to local companies' investments in the context of cross-border expansion. Such investments could also be supported indirectly by the EBRD through innovative products/financial institutions or venture funds that provide financing for SMEs.
- Proactive review and management of the Bank's portfolio to maintain its high quality.

The Bank will continue to ensure that all EBRD operations in Slovakia meet sound banking principles, have transition impact, are additional and are subject to the Bank's Environmental and Social Policy and incorporate, where appropriate, Environmental and Social Action Plans.

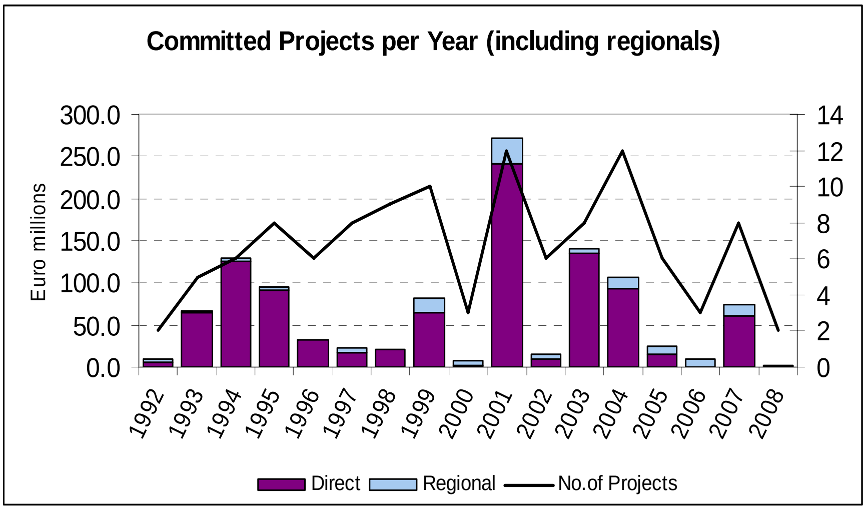
1. THE BANK’S PORTFOLIO

1.1 Overview of Activities to Date

The Bank has been an active participant in the Slovak Republic’s successful transition to a market economy, financing mainly private sector projects across a broad spectrum of economic sectors. Up to the end of December 2008, the Bank has committed EUR 1,257 million or 3 per cent of Bank-wide commitments. Forty per cent of the cumulative business volume relates to FI, a reflection of the Bank’s significant role in the privatisation of the Slovak financial sector and the granting of the EU/EBRD SME Finance Facility to banks and leasing companies. The involvement of EBRD in the corporate sector has also been significant, with 31 per cent of total commitments. The Bank’s role in infrastructure (transport, municipal and environmental infrastructure) has remained marginal with 4 per cent of cumulative business volume. For details on the Bank’s commitment by industry and on a project by project basis, see Annexes 1 and 2.

Chart 1 below illustrates the activity of the EBRD in terms of the number of projects and amounts committed by EBRD in the Slovak Republic since 1992. As shown, the activity of the EBRD increased significantly in years 2001 – 2004. The lower volume since 2005 is a reflection of the progress in transition and the strong presence of commercial banks in the Slovak Republic.

Chart 1 (as of 31 December 2008):



The current portfolio is EUR 281 million or 1.3 per cent of total Bank portfolio. It has shrunk considerably from EUR 680 million at the end of December 2004, as result of repayments, prepayments and equity exits. The portfolio is 100 per cent private and 39 per cent of it is equity. The impaired assets were considerably reduced going from EUR 15.1 million as of 31 December 2007, to EUR 4.9 million as of 31 December 2008. The Slovak portfolio risk rating stands at 4.97, significantly better than the 5.51 rating of the Central Europe and Baltics portfolio.

1.2 Implementation of Previous Country Strategy

During 2006 and 2008, the Bank signed 13 projects, of which eight were regional projects relevant for the Slovak Republic. Overall, the implementation of the strategy for the period was only partially successful as the Bank's efforts were constrained by external factors.

- No direct transactions were signed in the **corporate sector**. The pipeline in the area is weak given the high level of foreign investment in Slovakia while locally-owned enterprises are well served by the local financial sector.
- In the **financial sector**, only one extension to an EU/EBRD SME facility was signed. This product is no longer attractive to local banks now that performance fees are no longer available.
- The one significant success came in the **energy sector** where the Bank successfully committed EUR 60 million to four local banks under the Sustainable Energy Financing Facility.
- In **infrastructure**, the cancellation of planned privatisations of major infrastructure companies (Bratislava airport, rail cargo company, district heating plants) affected the Bank's ability to deliver transition impact in this sector. However, continued policy dialogue efforts did lead to the development of three critical highway projects through PPPs. They have been prepared and tendered out in accordance with best international practice, with the assistance of experienced and well known international advisers. All three were expected to proceed to financial closing in 2009. However, under the current market conditions, the financial closing of these projects may be delayed..

1.3 Transition Impact of the Bank's Portfolio and Lessons Learned

1.3.1 The Financial Sector

Banking – In 2001, EBRD and IFC have acquired equity stakes of Vseobecna Uverova Banka (VUB) and swiftly succeeded in finding a sound strategic investor. The Bank's engagement with Pol'nobanka - later on named UniBanka with a majority stake owned by the Italian Unicredito - contributed to the consolidation of the banking sector and the increased level of financial intermediation. A ***lesson learned*** from the Bank's engagement with VUB is that pre-privatisation equity can increase confidence and help ensure a successful privatisation.

NBFI –The leasing arm of the EU/EBRD Framework Facility for SMEs extended credit lines to local institutions with generally good transition results. The equity investment and privatisation of the dominant insurance company 'Project Bridge' was very successful, particularly in increasing sector-related skills and corporate governance standards. A ***lesson learned*** by the Bank is that a certain degree of pragmatism is required when negotiating conditionalities with strong strategic partners in order to achieve the bigger picture.

MSME –The same SME Facility, mentioned above, provided credit lines to VUB, Ludova Bank, UniBanka and OTP Banka Slovensko. Supplementing TC work helped to facilitate institution building and supported the extension of SME-related activities to areas such as agribusiness and energy efficiency.

Private Equity Funds – The Slovak Post-Privatisation Fund (PPF) proved to be only partly successful[1] and the Value Growth Fund (VGF) was liquidated in 2005 without considerable success. A ***lesson learned*** from the Slovak PPF is, that the Bank should select fund managers with sufficient capacity and resources to provide management support to investee companies.

Overall, transition impact within the *Financial* Sector is rated *Significant*.

1.3.2 The Enterprise Sector

Agribusiness – At the end of the 90s, the Bank pioneered a grain receipts programme that has successfully demonstrated a new method of financing and developed into a replication model elsewhere.

Telecommunication – In 2001, the Bank brought together a group of investors for a private placement of some 36 per cent state-owned shares of the mobile telephone operator Orange Slovensko. A ***lesson learned*** from Orange Slovensko is, that investing in equity requires more modest expectations towards TI. Unlike for its debt operations – the Bank is less in a position to enforce its conditionalities, when it invests in equity.

General Industry – Despite the difficult investment climate, the loan to Slovalco, ultimately demonstrated the possibility of targeted, ring-fenced new investments in old un-restructured conglomerates. The support for an extensive modernisation of the wood processor in Bucina Zvolen, suffered from overestimating the development of the market potential at appraisal time. ***A lesson learned*** from this operation is, that a company expanding to the export market, should seek for securities in advance, e.g. letters of intent to purchase.

Natural Resources – The only recent noticeable EBRD project was the support to the Slovak Gas Company SPP (Slovenský plynárenský priemysel) in a Eurobond issuance. The Government was able to sell a 49 per cent stake in SPP to a consortium of Ruhrgas, and Gaz de France in July 2002.

Property & Tourism – A few regional property funds have been financed with a component in the Slovak Republic, incl. Heitman II and TriGranit III. Investments were focussing on the relatively saturated retail and office segments of the market in main urban areas.

Overall, transition impact within the *Enterprise* Sector is rated *Moderate*.

[1] The fund made 11 investments in total and indicated in 2005 that it expected not to be able to return to investors the full amount invested, its IRR was estimated negative, with -7.7% in 12/2006.

1.3.3 The Infrastructure Sector

MEI – In 2003, the EU/EBRD MFF, a risk sharing facility, was launched for on-lending to small and medium-sized municipalities and implemented with Dexia Slovensko. Problems in utilisation of the facility have reduced the direct transition impact of the project, although Dexia continues to increase its effects on the municipal market from its own resources.

Transport – The sector did not receive any further investment to the sovereign International Corridor Road Rehabilitation project in 1993.

Power – Two projects with Slovenske Elektrarne – signed in 2002 and 2004 - supported the unbundling of the company and its privatisation. The Bank was also involved in the privatisation of the ZSE Electricity Distribution Company through an open and transparent sale to a strategic investor. A ***lesson learned*** from Slovenske Elektrarne is that the Bank needs to assess its *additionality* carefully over time. If its presence is desirable for the client but not indispensable, this should be made transparent.

Energy Efficiency – Two ESCO projects have been relatively successful and attracted both, private and public sector customers. Although there was a good potential for replication, no further market entry has been seen since.

Overall, transition impact within the *Infrastructure* Sector is rated *Minimal to Moderate*.

2. OPERATIONAL ENVIRONMENT

2.1 The General Reform Environment

The Slovak Republic successfully implemented major structural and institutional reforms from the late 1990s. These reforms included bold changes to the tax regime, important labour market reforms as well as reforms to the pension system. They also included a number of large-scale privatisations, such as the sale of a 51 per cent stake in the fixed line operator Slovak Telekom to Deutsche Telekom in 2000 and the sale of a 66 per cent stake in the dominant electricity generator Slovenske Elektrarne to ENEL in 2006. In addition, the banking sector was completely privatised with 90 per cent of assets now in foreign hands. As a result of this reform progress, the economy attracted large amounts of net foreign direct investments which have averaged USD 1.9 billion per annum in recent years (or around 6 per cent of GDP), particularly to the automotive and electronics sectors.

However, the Government elected in 2006 has placed greater emphasis on social welfare issues. This has led to revisions of key economic policies in areas such as the labour code, healthcare, taxation and pensions and to the reassertion of its role in the energy sector. Nevertheless it is generally felt that the government is intent on involving the private sector in large infrastructure projects, particularly in the road sector. There is widespread recognition that reforms carried out thus far have been successful in stimulating growth and as a result the potential for significant reform reversals is limited.

2.2 Progress in transition and the economy's response

2.2.1. Macroeconomic conditions for the Bank's operations

- ***Slovak macroeconomic performance has been impressive in recent years. GDP growth was exceptionally strong in 2007 at 10.4 per cent, but decelerated rapidly throughout 2008*** (please see Annex 4 for a table on Selected Economic Indicators). Slovakia almost doubled car production in 2007 and became the world's number one car manufacturer in per capita terms (with production by car manufacturers Volkswagen, PSA Peugeot Citroen and Kia Motors in the country). However, given the concentration of its industrial base on consumer goods, output decelerated rapidly throughout 2008. Flash estimates by the Statistical Office suggest that growth in real GDP was only 2.7 per cent in Q4 of 2008 (following growth of 9.3 per cent in Q1, 7.9 per cent in Q2 and 7.0 per cent in Q3), making full-year growth in GDP of 6.4 per cent.

- The ***fiscal deficit was a mere 1.9 per cent of GDP in 2007 and the target for 2008 was 2.3 per cent of GDP*** (down from its peak of 12.2 per cent in 2000), thanks to a significant reduction in expenditure and buoyant tax revenues. The improved fiscal position in Slovakia led the Council of the EU to abrogate the excessive deficit procedure in June 2008. In addition, the state budget ended 2008 Euro 704 million in deficit (or Euro 360 million less than planned) so the actual outcome of the general government budget is likely to be better than targetted. However, the government recently announced that its orginal plan to balance the budget by 2011 is likely to slip by one year as a result of the worsening economic crisis.

- ***Inflation has also been kept under control*** in advance of Euro adoption. In March 2008 - at the time the Convergence Report 2008 was prepared - the EU-harmonized HICP inflation measure stood at 3.6 per cent. This made the 12-month average year-on-year HICP rate 2.2 per cent, which was comfortably below the Maastricht reference level of 3.2 per cent. Since September 2008, HICP inflation has been following a downward trend, decelerating to 3.5% year-on-year in December 2008, mostly on account of declining food and fuels prices. However, although the economy is forecast to slow significantly, inflation may remain sticky as a result of increases in excise taxes and higher utility prices. Moreoever, once Slovakia adopts the Euro, the country will no longer be able to rely on the strengthening currency to restrain inflation. In the medium term, there continues to be a risk that sharp rises in inflation will be difficult to contain and thus start eroding international competitiveness.

- ***The current account deficit also narrowed significantly in 2007, (***reaching 5.3 per cent of GDP), ***but it is estimated to have widened to just under 6 per cent of GDP in 2008*** as a result of worsening trade, income and services balances.

- Following Slovakia's fulfilment of the Maastricht criteria, ***the country successfully joined the Eurozone on January 1st 2009***. The Slovak koruna had been appreciating rapidly over recent years, and in a surprise move the central parity of the koruna was revalued by 17.6 per cent in late May 2008 to SK 30.126 : EUR 1 (following an earlier revaluation by 8.5 per cent in March 2007). The new central parity was then confirmed as the conversion rate by the meeting of the EU Finance Ministers in early July 2008. In light of weakening inflationary pressure and in order to synchronise interest rate levels with the ECB, the Slovak National Bank reduced its interest rates in step with reductions by the ECB towards the end of 2008.

- ***However, the outlook for Slovakia has significantly deteriorated over recent months and growth over the next strategy period is likely to be bleak***. Under current assumptions, EBRD forecasts that the Slovak economy will contract in 2009. While Slovakia has so far witnessed only minor direct impact from the global financial crisis (see Section 2.2.2. below), the economy is being hit by much tighter financing conditions for investment and rapidly weakening demand for its exports (mainly cars and consumer electronics). The most recent data indicate that industrial production shrank by 7.2 per cent year-on-year in November and 16.8 per cent year-on-year in December 2008. Moreover, the recession of the sector is likely to be magnified by the gas crisis at the beginning of 2009 which forced the Slovak gas utility to declare a state of emergency and the government to impose restrictions on gas consumption for large industrial users. As a result, companies such as Kia Motors, PSA Peugeot, the Slovnaft refinery and US Steel Kosice suspended production for several days at the beginning of the year.

- ***The outlook remains very vulnerable to a deeper and more protracted slowdown in Slovakia's main export markets, given the country's concentrated export structure in cyclical industries.*** However, on the positive side its past credit expansion has been conservative, its financial system is liquid and it is now part of the Eurozone. The government has also approved a package of 27 measures to address the likely impact of the financial crisis[2], although it has left its fiscal deficit target for 2009 largely unchanged at 2.1 per cent of GDP .

2.2.2 Transition successes and challenges

<u>Enterprise sector</u>

Progress with privatisation would help to increase the efficiency and competitiveness of the last remaining state-owned enterprises.

- Slovakia's recent economic success can be attributed to past progress with privatisation and improvements in the business climate (please refer to Annex 5 for

[2] These measures include more efficient and effective drawing on EU funds; expenditure reductions on public administration; ambitious investment projects, such as motorway construction and the completion of the Mochovce nuclear-power plant; new loan schemes for small and medium-sized enterprises (SMEs); redesigned active labour market policies; and a reduction from 60 to 30 days in the time necessary for returning excess value-added tax (VAT) payments to businesses.

detail comparative structural indicators). However, the current Government has taken the decision not to proceed with important privatisations, such as the sale of Bratislava airport, ZSKK Cargo (the freight arm of the state-owned Slovak railway company), majority stakes in six state-owned district heating plants and the three regional energy distributors. The decision not to privatise remaining strategic companies and to contest the actions of privatised utilities (see below) is likely to affect their efficiency and competitiveness over the medium term.

- Nevertheless, important improvements in the regulatory environment and labour market regulation in the past have made Slovakia an attractive destination for FDI. The export base continues to grow with FDI inflows, particularly into the automotive sector (with completed investments by Peugeot SA, Kia Motors Corp and Volkswagen AG). Although the economy is dominated by the automotive sector,[3] there have also been important investments in the electronics sector by Sony and Samsung which have helped the economy's diversification. Sectors that have been exposed to international competition, such as the automotive, electronics and financial sectors, have made impressive progress in catching up to the productivity levels seen in more advanced EU countries. However, other sectors, such as SMEs and infrastructure, have performed less well. As elsewhere in the region there continues to be the risk that the economy develops into a "dual economy" with a competitive mainly foreign-owned enterprise sector versus undercapitalised local mostly SME companies and low productivity infrastructure. This highlights the continued need for providing financing to SMEs and infrastructure reform.

Additional improvements to the business environment and increased labour market flexibility are key to addressing regional differences and the high levels of structural and youth unemployment.

- In the World Bank's Doing Business 2008 survey Slovakia was ranked 32th out of 178 countries, ahead of the Czech Republic, Hungary, Poland and Slovenia, but behind the Baltic States. The key areas for improvement identified in the Slovak Republic include reforms of public administration and the judicial systems, as well as the business environment for SMEs.

- Unemployment fell to a record low of 9 percent last year and stood as low as 2 per cent in Bratislava. Real wage growth exceeded productivity growth in the first quarter of 2008 for the first time since late 2005. However, unemployment is very likely to increase and regional disparities may be exacerbated as a result of the deteriorating economic environment. At the same time, regional inequalities in unemployment have not diminished and structural and youth unemployment remains high. The key is therefore to introduce measures that improve labour market flexibility and the skill base of the labour force.

- However, in July 2007 the government approved a new labour code that tightens labour protection laws and increases workers' rights. The new code introduces strict limits on short-term contracts and overtime, increases severance pay and makes

[3] The sector accounts indirectly for one-quarter of GDP and one-third of exports.

collective bargaining agreements binding for all enterprises operating in a given sector. The minimum monthly wage was increased from SK 8,100 (Euro 268.9) to SK 8,902 (Euro 295.5). The government also tightened regulations in the retail sector. In April 2008 the government introduced revisions to the retail law, which includes clauses such as prohibiting the sale of goods below cost, putting a cap on fees paid by suppliers to retailers, and the possibility of stepping in to intervene in price setting. It established a council to monitor the development of prices.

Energy and Infrastructure

Further privatisation and the promotion of energy efficiency and renewable energy remains a priority.

- The power sector has been successfully unbundled with independent transmission, distribution and generation companies. A regulator for network industries is in place since January 2002. Prices were brought to cost-recovery levels over 2003-04. The sale of a 66 per cent stake in the dominant electricity generator Slovenske Elektrarne to ENEL (the Italian electricity company) for EUR 840 million was finalised in 2006. The new Government decided not to pursue the sale of additional 51 per cent stakes in the three regional power distributors to the existing minority shareholders.

- Over the past year the government has increased its involvement in the energy sector. In July 2008 the government gave the Regulatory Office for Network Industries (URSO) more authority to control rising energy prices. In the fall of 2008 URSO rejected two applications by Slovak gas utility SPP for price increases in the order of 13-24 per cent before agreeing on much lower increases. Moreover, in October 2008 Parliament passed a new law for imposing new regulations on the setting of energy tariffs from 2009. The proposal would give the government stronger control in setting gas and electricity prices for households and SMEs. Industry experts believe this will lead to further distortions and cross subsidisation among customers. Direct grants or tax credits to low-income citizens would be a more efficient way to address the social impact of rising energy prices.

- In April 2008 the government also announced its intention to increase its role in strategic energy projects, such as by involvement in the planned construction of new nuclear capacity, by buying back its minority 49 per cent stake in the oil transit company, Transpetrol, that was sold to Yukos in 2002, and by initiating an investigation into the lawfulness of SE's privatisation.

- According to a recent EBRD analysis, the Slovak economy ranks worse than its regional CEB peers (except for Estonia) in the EBRD's Index on Sustainable Energy.[4] Nevertheless, important steps in creating a market for energy conservation have already been taken (*e.g.* in residential energy efficiency) and the market for renewable energy projects is developing slowly. The Slovak Government is attempting to further improve the situation through the approval this year of the Strategy for Energy Efficiency and the Government's Plan for Action on Energy

[4] EBRD, "Securing sustainable energy in transition economies", http://www.ebrd.com/pubs/econo/sse.pdf, May 2008.

Efficiency. In addition, the Government approved its Strategy for Developing Renewable Resources in 2007 and the Act on Energy Production from Renewable Energy Resources and Combined Energy and Gas Production is expected in 2009.

Municipal and environmental infrastructure will have to be modernised with the assistance of EU structural and cohesion funds, private sector involvement and commercial co-financing from local sources.

- Reform and private sector participation in municipal services has been slow. The municipal sector in Slovakia remains fragmented, and is often suffering from poor administrative capacity. Although there are around 2,800 municipalities, only few large cities can access external financing on reasonable terms, and this situation is likely to be aggravated by the current crisis. There is noteworthy private sector participation in district heating, but the Government has decided not to pursue the sale of the remaining 51 per cent stakes in six Slovak heating companies. There is very limited private sector participation in public transport, water, waste water and solid waste management.

- The institutional framework for municipal finance is in place and tariffs have been mostly adjusted to reflect costs, but experience of revenue-based financing is very limited. Further reform in this area will require the strengthening of municipal administrative capacity and co-operation as well as improvements in procurement and project management standards.

- With substantial fiscal pressures on municipal finances there is an increasing scope for private involvement in increasing efficiency in the delivery of public services. However, this will require clear rules and regulations concerning financing, purchasing and delivery of services, especially in the current environment were private sector financing is becoming more limited and selective.

Increased private sector participation should also be encouraged in the transport sector, especially through the competitive award of PPP contracts in road building.

- In railways, operating and policy setting functions have been separated and core railway businesses (infrastructure, passenger, freight, etc.) have been unbundled, while ancillary services have been divested. In June 2004, the government split of the public railway company, Zeleznicna Spolocnost (ZSSK), into two entities in charge of passenger and freight transport, and was planning the privatisation of the freight company. However, the Government has since decided not to pursue the privatisation of a 100 per cent stake in the freight company ZSSK Cargo. Instead, the government in June 2008 announced its plan to merge the freight operator with the Czech freight operator CD Cargo. Together the two companies would rank in second place with Polish PKP and behind Deutsche Bahn in terms of market share in the EU. The Czech government would wish for the merger to lead to the eventual privatisation of the entity, but the Slovak government opposes any move in that direction.

- In roads, a National Highway Company was established in 2005 to develop highways and motorways under the Ministry of Transport, Post and Communications. The government policy for the sector involves support for private sector involvement in the construction and maintenance of selected stretches of motorway network to complement the available EU funding for public sector road construction. This will speed up the development of an efficient road network in the country. The PPP Project Implementation Unit, with the assistance of reputable international advisors, have prepared and conducted the tenders for sections of the D1 and R1 highways via PPP schemes with the objective to close R1 in the first half of 2009, although it may be more difficult to attract private investment in the current environment. These projects are large (estimated at more than EUR 4 billion in total) and considered as key priority investments in view of the significantly underdeveloped motorway network in Slovakia and the continued regional income inequalities. In another PPP project, despite the fact that only one from the consortia participating in the tender for the supply of a national toll collection system submitted a compliant bid (the consortium of SanToll and Ibertax in which French Sanef is involved), the tender is nearing its successful completion. Although all other bidders challenged the tender, the Public Procurement Office (UVO) has dismissed all of the complaints to date.

Financial Institutions

Financial institutions would benefit from the introduction of new products and improved risk mitigation instruments.

- The financial sector has been completely privatised, with close to 90 per cent of banking assets controlled by foreign investors. All the main foreign parent banks active in the region have banking subsidiaries in Slovakia (including Raiffeisen, Erste, KBC, Intesa SanPaolo, Unicredit, Société Générale and Dexia). The supervision of the financial sector was unified in January 2006, under the auspices of the National Bank of Slovakia. Domestic credit to the private sector as a per cent of GDP remains low by regional standards.

- Despite the global financial crisis, the Slovak banking sector as a whole has been relatively stable and so far there have been no indications of significantly deteriorating asset quality[5]. However, banks are mostly owned by strategic parents and there is a risk that parent bank recapitalisation plans may include a reduction of balance sheets in their CEB subsidiaries. Still, the Slovak banking sector sector has until now had sufficient and stable domestic funds at its disposal and has not been overly dependent on short-term interbank funds. In July 2008, for example, the loan-to-deposit ratio stood at 86 per cent, whereas it was more than 100 per cent in many other countries in the region. However, it is becoming increasingly apparent that financing conditions have tightened substantially in recent months. There are some signs that lending to households, SMEs and corporates in general has all but stopped (either for investment or working capital - including pre-export financing). There is also growing concern that companies and municipalities may not be able to attract commercial co-financing for large infrastructure investments as originally planned.

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[5] Except in one bank, Dexia, which has suffered a sizeable foreign exchange speculative loss by some of its clients.

- Until recently Slovakia had an unfunded pay-as-you-go state pension system which was forecast to accumulate rising deficits on account of the country's adverse demographic profile. As a result, a new 3-pillar system was introduced in January 2005 aimed at ensuring an adequate level of pensions for beneficiaries and the sustainability of government finances over the long term. The reformed system consists of a mandatory non-funded pay-as-you-go first pillar, a mandatory privately managed fully funded second pillar, and a voluntary fully funded third pillar. It is subject to strict regulatory oversight and clear restrictions on the investments of the privately managed funds. However, over the past two years a number of amendments have been made to the system that may once again put at risk the long-term sustainability of the whole as changes tend to induce a shift back into the unfunded pay-as-you-go pillar. Specifically, these changes include the right of young people to switch out of the second pillar into the PAYG pillar by repeatedly opening the second pillar to allow people that choice.[6] Independent analysts agree that these changes risk the sustainability of the PAYG pillar over the long term since the state is again accumulating debt that it will find difficult to honour given the country's demographic profile. In addition, these changes have made the operating environment for privately managed pension funds more unstable and can discourage the habit of accumulation of private savings over the long term.

2.3 Access to Capital and Investment Requirements

- **Domestic credit:** As a result of the advanced stage of development of the banking sector, competition is strong. As local banks rely significantly on deposits for their funding, they have suffered very little from the "credit crunch" so far. However, recent evidence suggests that the availability of credit has become much more difficult and that interest rates have started to go up (see above).

- **Capital markets:** The Bratislava Stock Exchange is small (market capitalisation equals only around 10 per cent of GDP) and illiquid (annual turnover is only 20 per cent of market capitalisation). It has suffered in line with other equity markets in the region over the past year from the retrenchment from emerging market equities, although not as much as some other countries in the region. The development of private equity funds started later than in the neighbouring countries and the Slovak Republic is still trailing Poland, Hungary and the Czech Republic.

- **Foreign direct investment:** After a record USD 3.8 billion in 2006, net FDI inflows in Slovakia have amounted to USD 2.9 billion in 2007. Over the 1989-2007 period, Slovakia benefited from cumulative FDI inflows equivalent to USD 4,366 per capita, putting it only below the Czech Republic, Hungary and Estonia among the Bank's countries of operations. However, given the worsening climate, it is also highly likely that net FDI inflows will decrease in 2009.

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[6] The system was opened by the government for six months from January 2008 and again for seven and a half months from November 2008.

2.4 Legal Environment

Over the past decade the Slovak Republic has introduced notable reforms to its legal environment. Accordingly, the legal system has strongly evolved towards an internationally acceptable level and the Slovakia Republic is one of the most advanced EBRD countries of operations in terms of legal transition.

The Slovak Republic's laws are approaching international standards and are supported by properly established institutional mechanisms to implement them. In particular, the legal frameworks for secured transactions and insolvency, as well as the rules for securities markets regulation are well developed. However, improvements are still needed in some areas crucial to the business environment and to foreign investment, in particular in the fields of concessions law and the protection of minority shareholders. In additional, the surveys of legal effectiveness conducted by the EBRD indicate that commercial laws may at times suffer from inadequate administrative and judicial support.

2.5 Environmental Issues

Upon entry to the EU on 1 May 2004, the Slovak Republic had to comply with all the *acquis*.

3. STRATEGIC ORIENTATIONS

For the years covered by this Strategy, the Bank is projected to be active in the Slovak Republic in accordance with the operational principles of transition impact, sound banking and additionality.

The Bank's operational objectives in Slovakia will remain in accordance with the strategice outline for the years 2006-2010 agreed upon in Capital Resources Review 3, while also addressing the crisis needs in Slovakia and across the region, without questioning graduation, as determined by the crisis response programme adopted by the Board of Directors. The Bank will expand SEFF in order to encourage local banks to continue lending to SME and housing associations and to work closely with commercial banks and other IFIs to mobilise financing for the initial PPP road projects. The Bank will also look for other opportunities to address the enhanced needs in Slovakia due to the ongoing financial crisis.

3.1 Bank's Priorities for Strategy Period

In an attempt to respond to the worsening external environment in a manner consistent with the analysis of Slovakia's remaining transition challenges, the Bank's immediate focus will be to respond to the exceptional economic circumstances by focussing on the following critical areas:

- **Ensure the continued availability of credit to SMEs and municipalities.** This is best achieved through the provision of credit lines to local banks.

- **Participate in a co-ordinated IFI effort to contribute towards financing of viable public-private concession projects in transport infrastructure** which are now coming to the market, following the best international practice for tendering and contract award. This will complement the available commercial funding and allow for the successful implementation of the first round of public-private partnerships n the country. Priority will be given to highway PPP projects as better road infrastructure will reduce transport costs and help integrate eastern Slovakia with the western part of the country.

- **Consider other investments to improve energy efficiency and support selected new generation projects, particularly from renewable energy sources.** This will again increase competitivess by reducing the high energy intensity of the Slovak economy and contribute to improving energy security and could be most rapidly implemented by the expansion of the Sustainable Energy Financing Facility.

- **In light of the decrease in available debt financing, support local companies, most of which are SMEs, with equity capital.** The provision of higher-risk financing to well managed local companies will have a significant demonstration effect. It will also contribute to reducing the growing performance gap between foreign-owned and local companies. This could be achieved directly through, for example, the Facility for Medium-Sized Projects, or indirectly through venture capital funds.

3.2 Sectoral Challenges and Bank Objectives

The Bank will continue to focus on improving the competitiveness of enterprises in Slovakia. The sectoral challenges and objectives outlined below would be pursued once the effects of the credit crisis have subsided and the commercial bank market has returned to normal operation.

3.2.1 The Enterprise Sector

Transition Goals. Reduce the widening gap between successful international companies and local companies in the Slovak Republic through company restructuring, support for SMEs and mergers and acquisitions.

Operational Priorities

- Provide higher-risk products such as equity and structured debt for local corporations to support viable companies faced with worsening market conditions due to the crisis and, eventually, fund the growth of local companies emerging from the slow down. Particular attention will be paid to local companies’ investments in the context of cross-border expansion.
- In addition, make use of the Facility for Medium-Sized Projects to support smaller local companies’ expansion plans.

3.2.2 The Financial Sector

Transition Goals. Increase the range of financial products available to the SME sector.

Operational Priorities

- Support innovative products/financial institutions that provide financing for SMEs.
- In particular, consider the involvement in a private equity fund focusing on start-ups, possibly in conjunction with the provision of subordinated funds from the EU and the granting of SME credit and risk sharing lines to financial intermediaries on a selective basis. Attracting private sector investors to such funds will be challenging in the present circumstances but makes EBRD involvement and co-operation with the EU and EIB that more important to succeed in leveraging private capital.
- With the support of the Ministry of Economy and BIDSF, expand SEFF to include more banks.

3.2.3 Infrastructure and Energy

Transition Goals. Increase the involvement of the private sector in infrastructure through the promotion of PPPs, where appropriate and feasible.

Assist in the installation of new and replacement power generation capacity (non-nuclear) necessary as a result of the closure of Units 1 and 2 of Bohunice V1.

Encourage the privatisation of important infrastructure companies (transport, municipal and energy companies).

Operational Priorities

- Support private investors developing renewable energy projects, particularly using Slovakia's significant geothermal potential.
- Assist Independent Power Producers in installing new and replacement capacity.
- Support the use of PPPs for the construction, funding and operation of an efficient motorway network in the country. This will complement the on-going road network development and use of EU funds with the overall goal of furthering economic growth and regional integration.

3.3 Portfolio management challenges

The Bank will structure its portfolio management in such a way that it is able to maintain the current high quality of the portfolio. At the regional level, this was achieved by providing additional resources for monitoring of local bank exposure which is supported locally. Particular attention is being paid to keeping in touch with local banks, be they EBRD clients or not, to better assess the impact of the credit crisis on the financial sector and their corporate clients.

4. ACTIVITIES OF OTHER IFIs AND CO-OPERATION WITH EBRD

- **European Union (EU):** Structural funds for the countries of European Union are programmed in 7 year periods. Slovakia has become a member of EU in 2004 and for the shortened period 2004-2006 Slovakia received EUR 1.05 billion from European Regional Development Fund (ERDF) and European Social Fund (ESF) and EUR 509 million from Cohesion Fund (CF). For the 2007-2013 period Slovakia is eligible for drawdown of EUR 6.18 billion from ERDF and EUR 1.5 billion from ESF. As Slovakia still satisfies criteria for receiving funds from CF for the 2007-2013 period, the country is scheduled to receive EUR 2.3 billion for transport infrastructure and EUR 1.6 billion for environment purposes from CF.

- **European Investment Bank (EIB):** Since 2006, the EIB has signed 13 projects in Slovakia for a total of EUR 314 million. The EIB has focussed its activities in the financial sector, with 73% of its funding in the form of global loans to banks or leasing companies. The EIB also made three infrastructure loans to the Presov region totalling EUR 33 million as well as a EUR 50 million loan to the Slovak Motorway Agency.

- **International Monetary Fund (IMF):** The Slovak Republic joined the IMF in January 1993. The latest stand-by facility expired in March 1996. The Article IV consultations are held on the standard 12-month cycle.

- **World Bank (WB):** The World Bank has supported the Slovak Republic since 1993. World Bank commitments to the country have totalled USD 566.3 million for eight operations. The main priorities under the last Country Partnership Strategy for the Slovak Republic for 2005-2007 were (i) fiscal consolidation, (ii) the implementation of structural reforms to enhance competitiveness of the economy, (iii) poverty reduction and social inclusion (labour market reform; SME development, education and improvements of basic communal services and community infrastructure). Slovakia will graduate from the World Bank at the end of 2008. In this context, the World Bank closed its office in Bratislava in June 2008.

- **International Finance Corporation (IFC):** By 2002, when the IFC closed its office, it had financed four projects including a pre-privatisation equity stake in VUB, together with EBRD. The IFC re-opened its office in 2003 mainly to roll out a regional energy efficiency credit and risk sharing line for local banks.

ANNEX 1: COMMITTED PROJECTS PER YEAR

As of 31 December 2008 – EUR million

Year	Op ID	Op Name	Regional/Direct	EBRD Finance	Debt	Equity
1992	346	Czech & Slovak Investment Corp	Regional	3.6	0.0	3.6
1992	171	Eurotel Bratislava Spol s.r.o.	Direct	5.7	5.7	0.0
			2	**9.3**	**5.7**	**3.6**
1993	139	Slovak Telecom Project	Direct	44.0	44.0	0.0
1993	648	International Road Corridor	Direct	15.0	15.0	0.0
1993	44	Renaissance Fund	Regional	0.9	0.0	0.9
1993	43	Slovenska Pol'Nohospordarska Banka	Direct	3.6	0.0	3.6
1993	25178	Unibanka (equity)	Direct	2.4	0.0	2.4
			5	**65.8**	**59.0**	**6.9**
1994	684	Sloveca	Direct	7.7	7.7	0.0
1994	638	ZSNP Tranche A	Direct	27.6	27.6	0.0
1994	1309	Advent Private Equity Fund - Central Europe LP	Regional	0.8	0.0	0.8
1994	37668	Advent - Czech and Slovak PEF	Regional	1.2	0.0	1.2
1994	2177	Slovalco - ZSNP Tranche B & C	Direct	90.1	78.2	11.8
1994	1061	Slovnaft a.s	Direct	14.2	14.2	0.0
			6	**141.7**	**127.8**	**13.9**
1995	2148	MBA Loan Project (guarantee)	Regional	0.3	0.3	0.0
1995	1650	Tatra Bank Credit Line	Direct	15.3	15.3	0.0
1995	2486	Advent International (addition to Advent Private Equity)	Regional	4.9	0.0	4.9
1995	2161	Slovnaft a.s. Equity	Direct	44.2	0.0	44.2
1995	2551	Slovenska Pol'nohospodarska Banka ("SPB")	Direct	1.4	0.0	1.4
1995	3032	SPB Cofinancing Facility - Miva	Direct	0.5	0.5	0.0
1995	38104	MF Slovak PPF	Direct	23.5	0.0	23.5
1995	2559	Istrobanka Credit Line	Direct	5.8	5.8	0.0
			8	**95.9**	**21.9**	**74.0**
1996	3677	Pol'nobanka (Formerly Slovenska Pol'nohospordarska Banka)	Direct	2.3	0.0	2.3
1996	3594	Dalkia Termotech - Slovak Republic	Direct	1.9	1.5	0.3
1996	3620	FGG Municipal Services MPF: Heatco District Heating Project	Direct	3.1	3.1	0.0
1996	3300	Tatra Banka Subordinated Debt	Direct	12.8	12.8	0.0
1996	2407	PBK General Purpose and Energy Efficiency Credit Facility	Direct	11.8	11.8	0.0
1996	3851	SPB Cofinancing Facility - Mineralne Vody	Direct	0.8	0.8	0.0
			6	**32.8**	**30.1**	**2.6**
1997	3626	CGE MPF - Banska Bistrica Waste Management Project	Direct	1.0	1.0	0.0
1997	4390	SPB Co-financing Facility - Topolciansky	Direct	1.0	1.0	0.0
1997	3491	DBG Osteuropa Holding GmbH	Regional	2.6	0.0	2.6
1997	3813	Prva Komunalna Banka a.s. (credit line)	Direct	10.2	10.2	0.0
1997	4607	Advent Central & Eastern Europe II - Regional Fund	Regional	2.3	0.0	2.3
			5	**17.1**	**12.2**	**4.9**
1998	4465	PBK Equity Investment	Direct	3.7	0.0	3.7
1998	4681	L&G ESCO Slovakia	Direct	2.1	1.7	0.4
1998	5024	Innova/98 LP	Regional	0.4	0.0	0.4
1998	2460	Bucina Zvolen, a.s.	Direct	7.3	7.3	0.0
1998	5600	Slovak Grain Receipt Program - Pol'nobanka	Direct	3.1	3.1	0.0
1998	6176	MBA Loan Project II (guarantee)	Regional	0.0	0.0	0.0
			6	**16.7**	**12.2**	**4.5**

Year	Op ID	Op Name	Regional/Direct	EBRD Finance	Debt	Equity
1999	4442	Info. and Comm. Tech & Industrial Electronic Fund Ltd.	Regional	2.4	0.0	2.4
1999	5049	AIG New Europe Fund	Regional	6.9	0.0	6.9
1999	6374	Slovak Grain Receipt Program - Pol'nobanka (1999/00)	Direct	4.2	4.2	0.0
1999	6326	Polus Center	Direct	23.0	23.0	0.0
1999	7693	SPP Bond Issue	Direct	29.8	29.8	0.0
1999	9144	Regional/Private Equity Fund Facility - Trigranit	Regional	3.4	0.0	3.4
1999	5058	Central & Eastern Europe Power Fund	Regional	0.9	0.0	0.9
1999	5422	Energy Efficiency and Emissions Reduction Fund	Regional	3.0	0.0	3.0
			8	**73.7**	**57.1**	**16.6**
2000	9620	EU/EBRD Phase I - GIMV Czech and Slovak SME Fund	Regional	0.5	0.0	0.5
2000	10492	Slovak/Grain Receipt Program - Pol'nobanka (2000/01)	Direct	10.2	10.2	0.0
2000	13828	TBIH Financial Services Group N.V. (debt & equity)	Regional	2.9	0.3	2.6
			3	**13.6**	**10.6**	**3.0**
2001	14807	Vseobecna Uverova Banka Pre-Privatisation (debt & equity)	Direct	23.5	0.0	23.5
2001	13120	EU/EBRD Phase I - Euroventures Danube BV	Regional	0.0	0.0	0.0
2001	7587	Slovalco Expansion - Equity	Direct	47.1	47.1	0.0
2001	18490	Slovalco Expansion - Debt	Direct	15.2	15.2	0.0
2001	16908	Unibanka (equity)	Direct	10.1	0.0	10.1
2001	15213	Orange Slovensko, A.S.	Direct	23.5	0.0	23.5
2001	19234	EU/EBRD Phase I - VUB	Direct	20.0	20.0	0.0
2001	18190	SLSP (portage equity)	Direct	97.5	97.5	0.0
2001	13199	Raiffeisen EU Enlargement Fund	Regional	0.8	0.0	0.8
2001	18283	Slovak/Grain Receipt Program - Pol'nobanka (2001/02)	Direct	10.0	10.0	0.0
2001	17767	Regional Europolis Portfolio	Regional	28.9	13.6	15.3
2001	10653	Aquachemia	Direct	8.1	8.1	0.0
			12	**284.7**	**211.4**	**73.2**
2002	8902	Accession Mezzanine Capital LP	Regional	3.0	0.0	3.0
2002	14644	Slovenske Elektrarne - Sector Restructuring Loan	Direct	120.4	120.4	0.0
2002	29935	UniBanka capital increase 2002	Direct	3.6	0.0	3.6
2002	27587	Heitman Central Europe Property Partners Fund II	Regional	2.1	0.0	2.1
2002	24838	Value Growth Fund	Direct	1.2	0.0	1.2
2002	29892	EU/EBRD Phase II - CAC Leasing Slovakia	Direct	5.0	5.0	0.0
			6	**135.3**	**125.4**	**9.9**
2003	29308	EU/EBRD Extension 3 - Tatra Leasing (RZB)	Direct	5.0	5.0	0.0
2003	32349	EU/EBRD Extension 3 - VUB II	Direct	10.0	10.0	0.0
2003	29124	ORCO APARTHOTELS	Regional	1.8	0.4	1.4
2003	23930	Project Bridge	Direct	49.2	0.0	49.2
2003	35084	Bucina ddd	Direct	8.0	8.0	0.0
2003	26969	ZSE Electricity Distribution Privatisation	Direct	60.5	60.5	0.0
2003	32514	EU/EBRD Extension 3 - SG Equipment Finance Czech R.	Regional	3.2	3.2	0.0
			7	**137.7**	**87.1**	**50.5**
2004	29307	EU/EBRD Extension 3 - Ludova banka	Direct	6.3	6.3	0.0
2004	34551	Polish Enterprise Fund V	Regional	1.9	0.0	1.9
2004	35037	Slovenske Elektrarne Restructuring Loan II	Direct	30.0	30.0	0.0
2004	32904	EU/EBRD Extension 3 - VB Leasing Slovakia	Direct	10.4	10.4	0.0
2004	33187	TriGranit III	Regional	0.5	0.0	0.5
2004	34722	EU/EBRD Extension 3 - Unibanka	Direct	8.0	8.0	0.0
2004	34563	Advent Central & Eastern Europe Successor Fund	Regional	5.0	0.0	5.0
2004	33058	Raiffeisen International	Regional	2.0	0.0	2.0
2004	35257	EU/EBRD MFF (Risk sharing) - Dexia Slovensko MFF	Direct	8.0	8.0	0.0
2004	35120	Europolis II	Regional	4.5	3.1	1.4
2004	35159	EU/EBRD Extension 5 - CAC Leasing II	Direct	21.4	21.4	0.0
2004	34930	EU/EBRD Extension 5 - OTP Bank Slovensko	Direct	10.0	10.0	0.0
			12	**107.9**	**97.2**	**10.8**

Year	Op ID	Op Name	Regional/Direct	EBRD Finance	Debt	Equity
2005	36167	Emerging Europe Convergence Fund II	Regional	3.6	0.0	3.6
2005	36262	EU/EBRD Ext. 5 Rural - UniBanka	Direct	5.0	5.0	0.0
2005	35813	EU/EBRD PA - Istrobanka	Direct	10.0	10.0	0.0
2005	36260	Connex Equity Investment	Regional	15.3	0.0	15.3
2005	35987	Argus Capital Partners II	Regional	0.4	0.0	0.4
2005	36617	SG AM Eastern Europe L.P.	Regional	3.3	0.0	3.3
			6	**37.6**	**15.0**	**22.6**
2006	36371	Capital Media	Regional	4.0	4.0	0.0
2006	36885	Alpha CEE II, L.P.	Regional	5.0	0.0	5.0
2006	36448	EU/EBRD Ext. 5 Rural - SG Equipment Finance CR	Regional	1.0	1.0	0.0
			3	**10.0**	**5.0**	**5.0**
2007	37269	Syntaxis Mezzanine Fund	Regional	2.5	0.0	2.5
2007	38237	Capital Media - Extension Facility	Regional	2.0	2.0	0.0
2007	35913	Véolia Voda Equity Investment	Regional	7.3	0.0	7.3
2007	38396	EnerCap renewable energy financing vehicle	Regional	2.5	0.0	2.5
2007	38357	SLOVSEFF - Dexia Banka	Direct	15.0	15.0	0.0
2007	38356	SLOVSEFF - Slovenska sporitelna	Direct	15.0	15.0	0.0
2007	36698	SLOVSEFF - Tatra Bank	Direct	15.0	15.0	0.0
2007	38358	SLOVSEFF - VUB (Vseobecna Uverova Banka)	Direct	15.0	15.0	0.0
			8	**74.3**	**62.0**	**12.3**
2008	37877	Arka Property Fund II	Regional	2.3	0.0	2.3
2008	38658	ViaOne	Regional	0.5	0.0	0.5
			2	**2.8**	**0.0**	**2.8**
	SLOVAK REPUBLIC TOTAL			**1,256.9**	**939.7**	**317.2**

ANNEX 2: NET CUMULATIVE BUSINESS BY INDUSTRY

As of 31 December 2008 – EUR million

Sector Team (SIC)	EBRD Finance	Debt	Equity	Private	State	Portfolio Ratio*	% Share of Commitments	Total Project Value
Corporate								
Agribusiness	30	30	0	30	0	100%	2%	128
General Industry	205	193	12	205	0	100%	16%	535
Property and Tourism	66	40	26	66	0	100%	5%	248
Telecoms Informatics & Media	82	56	26	38	44	46%	7%	515
Sub-total Corporate	**384**	**319**	**65**	**340**	**44**	**89%**	**31%**	
Energy								**1,426**
Natural Resources	96	52	44	66	30	69%	8%	579
Power and Energy	217	211	6	97	120	45%	17%	963
Sub-total Energy	**313**	**263**	**51**	**163**	**150**	**52%**	**25%**	
Financial Institutions								**1,542**
Bank Equity	150	97	53	150	0	100%	12%	527
Bank Lending	186	186	0	186	0	100%	15%	213
Equity Funds	74	0	74	74	0	100%	6%	241
Non Bank Financial Institutions	98	46	52	98	0	100%	8%	110
Sub-total Financial Institutions	**508**	**329**	**179**	**508**	**0**	**100%**	**40%**	
Infrastructure								**1,092**
Municipal & Env Inf	37	14	23	37	0	100%	3%	165
Transport	15	15	0	0	15	0%	1%	42
Sub-total Infrastructure	**52**	**29**	**23**	**37**	**15**	**71%**	**4%**	**207**
SLOVAK REPUBLIC TOTAL	**1,257**	**940**	**317**	**1,048**	**209**	**83%**	**100%**	**4,266**

DEBT	790	790	0	164	89
EQUITY	317	0	317	109	0
GUARANTEE	149	149	0	8	120

PRIVATE	1,048	730	317	281	0
STATE	209	209	0	0	209

Direct	1,116	912	205	200	209
Regional	141	28	113	81	0

Non-Sovereign	1,170	853	317	281	150
Sovereign	87	87	0	0	59

ANNEX 3: SELECTED ECONOMIC INDICATORS

	2003	2004	2005	2006	2007	2008	2009
						Estimate	*Projection*
Output and expenditure			*(Percentage change in real terms)*				
GDP	4.7	5.2	6.5	8.5	10.4	6.4	-1.0
Private consumption	1.7	4.6	6.5	5.8	7.0	6.1	na
Public consumption	4.1	-2.2	3.3	10.2	-1.4	4.3	na
Gross fixed capital formation	-2.7	4.8	17.6	9.3	8.7	6.8	na
Exports of goods and services	15.9	7.4	10.0	21.0	13.8	3.2	na
Imports of goods and services	7.4	8.3	12.4	17.7	8.9	3.3	na
Industrial gross output	5.0	4.1	3.2	10.1	12.7	8.0	na
Agricultural gross output	-9.6	1.5	-10.7	-2.4	5.6	4.3	na
Employment			*(Percentage change)*				
Labour force (end-year)	0.2	0.9	-0.5	0.3	-0.2	na	na
Employment (end-year)	1.8	0.3	2.1	3.8	2.4	na	na
			(In per cent of labour force)				
Unemployment (end-year)	17.4	18.1	16.2	13.3	11.0	na	na
Prices and wages			*(Percentage change)*				
Consumer prices (annual average)	8.5	7.5	2.5	4.5	2.8	4.6	2.0
Consumer prices (end-year)	9.3	5.9	3.4	4.3	3.4	4.4	2.0
Producer prices (annual average)	8.9	3.4	3.9	8.0	2.2	5.8	na
Producer prices (end-year)	9.5	3.5	6.2	5.6	2.5	6.4	na
Gross average monthly earnings in economy (annual average)	6.3	10.2	9.2	8.6	7.4	na	na
Government sector[1]			*(In per cent of GDP)*				
General government balance[2]	-2.7	-2.3	-2.8	-3.5	-1.9	-2.2	-3.5
General government expenditure	40.1	37.7	38.1	37.1	34.6	na	na
General government debt	42.4	41.4	34.2	30.4	29.4	28.8	na
Monetary sector[3]			*(Percentage change)*				
Broad money (M2, end-year)	5.2	5.7	5.8	8.2	11.8	5.5	na
Domestic credit (end-year)	10.2	14.1	14.9	23.3	20.3	25.5	na
			(In per cent of GDP)				
Broad money (M2, end-year)	61.3	58.2	56.5	54.7	54.8	51.9	na
Interest and exchange rates			*(In per cent per annum, end-year)*				
Refinancing rate	6.0	4.0	3.0	4.8	4.3	2.5	na
3-month BRIBOR	6.0	3.7	3.1	4.8	4.3	3.2	na
Deposit rate[4]	5.3	4.1	2.4	3.6	3.7	na	na
Lending rate[4]	8.5	9.1	6.7	7.7	8.0	na	na
			(Korunas per US dollar)				
Exchange rate (end-year)	32.9	29.1	31.9	26.2	22.9	21.4	na
Exchange rate (annual average)	36.8	32.3	31.0	29.7	24.7	21.4	na
External sector							
			(In millions of US dollars)				
Current account	-1,971.6	-3,297.4	-4,065.0	-3,919.1	-3,994.5	-5,900.0	-5,520.0
Trade balance	-637.3	-1,536.2	-2,385.2	-2,531.8	-865.3	-1,000.0	-1,020.0
Merchandise exports	21,843.2	27,621.2	31,914.8	41,477.8	57,489.5	70,000.0	71,400.0
Merchandise imports	22,480.4	29,157.4	34,299.9	44,009.7	58,354.8	71,000.0	72,420.0
Foreign direct investment, net	1,913.4	3,051.8	2,278.8	3,797.1	2,881.0	2,100.0	1,000.0
Gross reserves, excluding gold (end-year)	11,678.1	14,418.8	14,924.0	12,684.8	17,674.8	17,854.1	na
External debt stock	18,090.2	23,763.6	27,052.5	32,206.0	44,308.7	50,000.0	na
			(In months of imports of goods and services)				
Gross reserves, excluding gold (end-year)	5.3	5.3	4.6	3.1	3.3	2.7	na
			(In per cent of exports of goods and services)				
Debt service due	14.3	10.8	11.7	4.7	4.2	4.4	na
Memorandum items			*(Denominations as indicated)*				
Population (end-year, million)	5.4	5.4	5.4	5.4	5.4	5.4	na
GDP (in billions of korunas)	40.6	45.2	49.3	55.1	61.5	68.4	69.1
GDP per capita (in US dollars)	8,520.8	10,428.4	11,574.2	12,827.5	15,562.3	18,549.7	na
Share of industry in GDP (in per cent)	25.9	27.1	26.4	28.2	28.2	na	na
Share of agriculture in GDP (in per cent)	4.0	3.6	3.2	3.2	3.2	na	na
Current account/GDP (in per cent)	-4.3	-5.9	-6.5	-5.7	-4.8	-5.9	-6.4
External debt - reserves (in US$ million)	6,412.1	9,344.8	12,128.5	19,521.2	26,633.9	32,145.9	na
External debt/GDP (in per cent)	39.5	42.3	43.4	46.5	52.7	49.9	na
External debt/exports of goods and services (in per cent)	72.0	75.8	74.5	68.7	68.7	64.1	na

[1] General government includes central government, municipalities and extra-budgetary funds.

[2] The general government balance excludes privatisation revenues and is calculated according to Eurostat methodology (ESA95). In line with the Eurostat derogation the second pillar pension funds are included from 2005.

[3] Until 2002 monetary data are compiled in national methodology. From 2003 they are compiled in the harmonised ECB methodology.

[4] Weighted average over all maturities.

ANNEX 4: STRUCTURAL CHANGE INDICATORS

Structural and institutional change indicators (latest available data 2007/2008)

	Czech Republic	Estonia	Hungary	Latvia	Lithuania	Poland	Slovak Republic	Slovenia
Enterprises								
Private sector share in GDP (in per cent)	80.0	80.0	80.0	70.0	75.0	75.0	80.0	70.0
Private sector share in employment (in per cent)	na	75.9	na	76.0	na	72.2	75.0	71.0
Share of industry in total employment (in per cent)	40.0	22.9	32.6	17.2	na	30.1	28.4	35.5
Change in labour productivity in industry (in per cent)	8.3	10.7	2.5	7.3	na	na	12.4	2.3
Investment/GDP (in per cent)	26.9	37.9	na	37.2	29.4	0.0	27.2	31.4
EBRD index of small-scale privatisation	4.3	4.3	4.3	4.3	4.3	4.3	4.3	4.3
EBRD index of large-scale privatisation	4.0	4.0	4.0	3.7	4.0	3.3	4.0	3.0
EBRD index of enterprise reform	3.3	3.7	3.7	3.0	3.0	3.7	3.7	3.0
Markets and trade								
Share of administered prices in CPI (in per cent)	12.2	23.3	15.1	12.9	13.5	1.0	24.1	15.0
Number of goods with administered prices in EBRD-15 basket	2.0	2.0	1.0	2.0	1.0	2.0	2.0	1.0
Share of trade with non-transition countries (in per cent)	75.8	66.9	73.5	51.6	52.1	76.3	62.7	71.2
Share of trade in GDP (in per cent)	136.9	123.6	134.7	86.0	104.3	73.2	154.5	120.0
Tariff revenues (in per cent of imports)	na	0.3	na	na	na	na	0.0	0.2
EBRD index of price liberalisation	4.3	4.3	4.3	4.3	4.3	4.3	4.3	4.0
EBRD index of forex and trade liberalisation	4.3	4.3	4.3	4.3	4.3	4.3	4.3	4.3
EBRD index of competition policy	3.0	3.7	3.3	3.0	3.3	3.3	3.3	2.7
Financial sector								
Number of banks (foreign-owned)	37 (15)	15 (13)	40 (27)	25 (14)	14 (6)	64 (54)	26 (15)	27 (11)
Asset share of state-owned banks (in per cent)	2.4	0.0	3.7	4.2	0.0	19.5	1.0	14.4
Asset share of foreign-owned banks (in per cent)	84.8	98.7	64.2	63.8	91.7	75.5	99.0	28.8
Non-performing loans (in per cent of total loans)	2.8	0.5	2.8	0.4	1.1	5.4	2.6	3.9
Domestic credit to private sector (in per cent of GDP)	45.0	89.3	59.2	93.9	61.2	na	42.3	79.0
Domestic credit to households (in per cent of GDP)	20.0	43.3	21.7	42.7	24.4	20.0	16.3	19.2
Of which mortgage lending (in per cent of GDP)	12.5	37.7	16.4	33.7	17.2	9.9	4.5	6.2
Stock market capitalisation (in per cent of GDP)	37.4	26.9	32.4	10.8	24.7	44.1	8.6	57.2
Stock trading volume (in per cent of market capitalisation)	68.7	34.9	106.0	4.8	10.1	47.5	0.5	12.3
Eurobond issuance (in per cent of GDP)	0.9	0.2	2.7	na	3.9	1.0	na	6.5
EBRD index of banking sector reform	4.0	4.0	4.0	4.0	3.7	3.7	3.7	3.3
EBRD index of reform of non-bank financial institutions	3.7	3.7	4.0	3.0	3.3	3.7	3.0	3.0
Infrastructure								
Fixed-line (mobile) penetration rate (per 100 inhabitants)	28.3 (128.4)	37.1 (148.4)	32.4 (110.0)	28.3 (97.4)	23.6 (144.9)	27.1 (108.7)	21.4 (112.6)	42.8 (96.4)
Internet users (per 100 inhabitants)	43.2	58.4	41.9	51.7	39.3	42.0	43.6	65.0
Railway labour productivity (1989=100)	109.1	285.2	173.2	116.9	91.1	102.6	70.1	186.5
Residential electricity tariffs (USc kWh) [4]	16.2	10.2	18.8	9.9	10.9	12.3	15.4	14.0
Average collection rate, electricity (in per cent)	100	99	99	100	99	na	na	99
EBRD index of infrastructure reform	3.3	3.3	3.7	3.0	3.0	3.3	3.0	3.0
Electric power	3.3	3.3	4.0	3.3	3.3	3.3	4.0	3.0
Railways	3.0	4.0	3.7	3.7	2.3	4.0	3.0	3.0
Roads	3.0	2.3	3.7	2.3	2.3	3.0	2.3	3.0
Telecommunications	4.3	4.0	4.0	3.0	3.7	4.0	3.7	3.0
Water and waste water	4.0	4.0	4.0	3.3	3.3	3.3	3.3	3.3

[1] There are controls in the air-transport sector for non-resident investors.
[2] The Czech Republic has no specific concession law but largely
with internationally accepted principles on concession laws.

ANNEX 5: POLITICAL AND SOCIAL ASSESSMENT

Section 1. Political Issues In The Context Of Article 1 Of The Agreement Establishing The Bank

The Slovak Republic is committed to, and applying, the principles of multiparty democracy, pluralism and market economics in accordance with the conditions specified in Article1 of the Agreement establishing the Bank.

Political developments

The Slovak Republic came into being on 1 January 1993 following the break-up of the Czechoslovak Federation. Much of its progress in the late 1990s-early 2000s was geared towards accession to the European Union. Once the country achieved harmonization with the *acquis communautaire* and fulfilled all the necessary criteria, it joined the EU in May 2004.

Early parliamentary elections held on 17 June 2006 led to the replacement of the reform-oriented government of Prime Minister Mikulas Dzurinda, who held that position for eight years, by a new coalition government led by Prime Minister Robert Fico's centre-left Smer-Social Democracy (Smer-SD) and comprising also the Movement for a Democratic Slovakia (LS-HZDS) and the Slovak National Party (SNS). A shift of priorities projected by the new Government was highlighted by the emphasis on social policy. After two years in power, the ruling Smer enjoys a record-high level of popular support. The next test for the balance of power will be elections to the European Parliament due in 2009.

Rule of Law and Human Rights

The legal system, which has undergone comprehensive reforms, provides a framework safeguarding fundamental rights and freedoms.

<u>Elections</u>

The Slovak electoral system provides for the free succession of power among political parties and provides the basis for a transparent, accountable, fair and equal process. All previous elections (ODIHR OSCE stopped monitoring Slovak elections in 2004), were assessed by international observers as conducted in a manner consistent with international standards and commitments for democratic elections. Although past elections demonstrated a trend of growing voter apathy, highlighted by the lowest turnout in EU at the first elections to the European Parliament, and by 11 per cent turnout at the second round of municipal elections in 2005, the latest general elections provided an impressive 55 per cent turn out.

<u>Integrity issues</u>

The Slovak Republic was ranked 52 out of 180 countries in the latest Corruption Perceptions Index by Transparency International published in September 2008, which places it among the five best countries in this respect among all countries of operation. However, some corruption issues remain. A handful of corruption scandals in the last years involved cabinet members, members of regional parliaments and local councils and representatives of political parties. Corruption ranks high in opinion polls as one of the issues of concern to citizens. The recent Life in Transition Survey, conducted by EBRD in cooperation with the World Bank, revealed that 'irregular payments' to public officials are believed to be more frequent on average than in many other countries of CEB.

Media

Freedom of speech is respected, and independent media operate freely in the Slovak Republic. The legislation in place and wide selection of media prevent control over access to information. The latest global press freedom ranking by Freedom house placed Slovakia among the best 50 countries in its 195-long list.

Religious freedoms

The government respects religious freedom. The Roman Catholic Church is the largest denomination in the country. Registered churches and religious organizations are eligible for tax exemptions and government subsidies.

Human trafficking

The Slovak Republic is a source, transit, and, to a lesser extent, a destination for women from Moldova, Ukraine, Bulgaria, and the Western Balkans, trafficked to Western Europe for the purpose of commercial sexual exploitation. According to regular reports issued by the US State Department on the state of affairs in fighting human trafficking world-wide, the Slovak authorities do not fully comply with the international standards for the elimination of trafficking, but are making significant efforts to do so. The Slovak Republic prohibits all forms of trafficking through its criminal code, which prescribes penalties which are sufficiently stringent. The government has made efforts to improve victim identification and assistance referral. It has demonstrated increased law enforcement efforts.

In 2007, Slovakia became one of two initial signatories to the Council of Europe's Convention on Action against Trafficking in Human Beings.

Ethnic minorities

There are more than ten recognized ethnic minorities in Slovakia, which represent about 15 percent of population. Ethnic Hungarians, who, according to the census, are about 10 per cent of the population, form the largest minority. Traditionally, ethnic Hungarians have a high rate of political mobilization; they are represented, in particular, through the Party of Hungarian Coalition (SMK), which enjoys a solid position in some regional and local self-governance organs.

While the official census places the Roma population at about 90,000, it is generally believed that the actual figure for this vulnerable minority is substantially higher. The government began a program to improve education and housing for Roma and established an informal advisory board to widen dialogue with the Roman community.

External relations

The Slovak Republic's top foreign policy priority is further integration into EU and Euro-Atlantic institutions. It is a member of the EU and NATO and it has ratified the EU Reform Treaty. The Slovak Republic participates in a number of regional organizations, including Central European Initiative. It also participates in the Western Balkans Fund of Donors initiated by the EBRD.

Section 2. Social Issues

Health

Compared to the average in EU and OECD countries, and similar to other new EU member states, Slovakia is characterised by relatively low health outcomes. According to the World Bank's World Development Indicators database, health adjusted life expectancy (HALE) is only 66 years, or five less than the average in the EU and OECD. Death rates, infant and child mortality rates and the incidence of tuberculosis are also worse.

Total expenditure on health accounted for around 7 per cent of GDP in 2005. Given the government's medium-term public finance consolidation objectives, the challenge for the health care sector will be to improve outcomes while containing already high health expenditures.[7] This requires increasing the efficiency of health spending. Reforms in the healthcare sector are still needed to rationalise excess facilities, reduce pharmaceutical costs, decrease rising demand pressures and ensure sustainable financing going forward. The current government has recently reversed some of the reforms introduced by the previous government in 2003-2004; for example, fees to visit to the doctor have been scrapped, prescription charges have been lowered, VAT on medicines and medical services reduced and limits on operating costs for insurance companies introduced. Moreover, the transformation of hospitals into private companies has been halted and is contributing to a rapid increase in arrears of public healthcare facilities. In addition, the government in 2007 passed a new Health Insurance Law which prohibits private health insurers from paying out dividends and forces them to reinvest their profits in healthcare services. The private health insurers have announced their intention to seek international arbitration to protect their investments or obtain compensation. In June 2008 the smallest of the four private health insurers operating in Slovakia – Europska ZP- announced its intention of leaving the market.

Education

Education outcomes are also low in international comparison. Educational achievement is below the OECD average according to the 2003 PISA study and is strongly influenced by socio-economic background.[8] Outcomes of secondary vocational programmes are poor and tertiary attainment is low (14 per cent of 25-34 year olds, compared to the OECD average of 31 per cent). To improve the situation, the OECD

[7] For a more thorough analysis of this subject, please refer to IMF Working Paper, " The Health Sector in the Slovak Republic: Efficiency and Reform", WP/07?226, September 2007.
[8] For a detailed analysis, see OECD, "Economic Survey: Slovak Republic", 2007.

has suggested that the government should expand participation in pre-school education, reduce stratification in the system, improve teaching quality, and make secondary vocation education more relevant to labour market requirements. Over the past year some improvements have been made. For example, the government has decided to make kindergarten free of charge for five-year-olds from 2008 onwards. Some reduction in segregation is being achieved by encouraging the integration of technical and vocational secondary schools.

Labour

Real wage growth is estimated to have accelerated to 4.5 per cent in 2007, from 3.95 per cent the previous year. In 2007, as a whole, the average monthly wage reached 20,146 koruna, up 7.4 per cent over the previous year's level in nominal terms. The unemployment rate fell by around three percentage points in 2007 (from 13.3 per cent end-2006 to 10 per cent end-2007). However, there remain large regional differences in labour market conditions, with regions such as Bratislava experiencing skill shortages and particularly acute wage pressures and some of the eastern regions still recording unemployment rates of over 20 per cent. The largest trade union body, the confederation of Trade Unions (KOZ), has 464,000 members in its 35 constituent unions. KOZ represents the trade union at the national level in tripartite bodies also including the government and the employers. Trade Unions are widely considered as weak and lacking in influence.

ANNEX 6: COMMERCIAL LAWS OF THE SLOVAK REPUBLIC

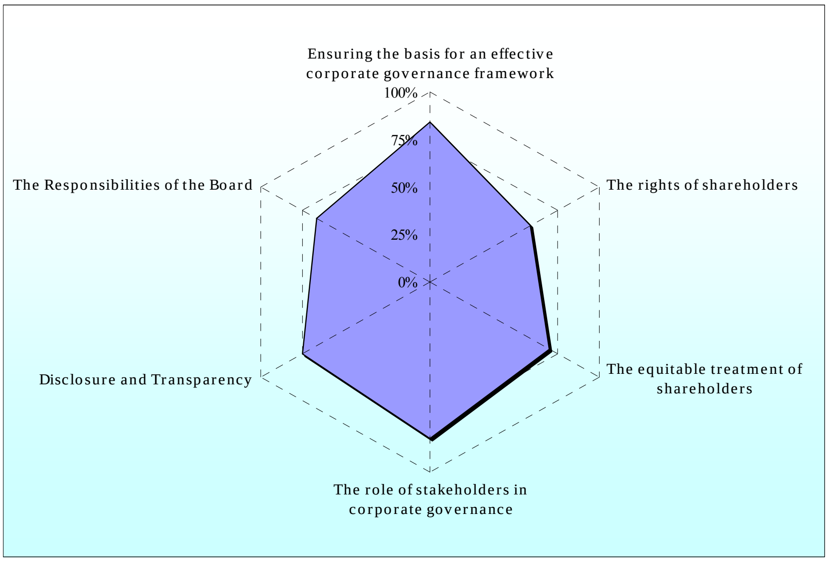
The EBRD has developed and regularly updates a series of assessments of legal transition in its countries of operations, with a focus on selected areas relevant to investment activities: capital markets, company law and corporate governance, concessions, insolvency, secured transactions and telecommunications. The existing tools assess both the quality of the laws "on the books" (also referred to as "extensiveness") and the actual implementation of such laws (also referred to as "effectiveness"). All available results of these assessments can be found at www.ebrd.com/law. This annex presents a summary of the results for the Slovak Republic, accompanied by critical comments of the Bank's legal experts who have conducted the assessments.

Company Law and Corporate Governance

The principal legislation concerning corporate governance is essentially included in the 1991 Commercial Code, in the 2001 Act on Securities and Investment Services and in the 2002 Act on the Stock Exchange, all as amended.

In September 2002, the Bratislava Stock Exchange, in collaboration with the market regulator, enacted a Code of Corporate Governance.[9] Since 2003, the Listing Rules of the Bratislava Stock Exchange require companies to report their compliance with the Code - under the so-called "comply or explain" rule.

Quality of corporate governance legislation – Slovak Republic (2008)



Note: The extremity of each axis represents an ideal score, *i.e.,* corresponding to OECD Principles of Corporate Governance. The fuller the 'web', the more closely the corporate governance laws of the country approximate these principles

[9] The Code is available on the EBRD website at: http://www.ebrd.com/country/sector/law/corpgov/codes/index.htm

According to preliminary results of the latest EBRD Corporate Governance Sector Assessment, which assessed the quality of corporate governance legislation in force as of November 2007, the Slovak Republic showed a high level of compliance with the OECD Principles of Corporate Governance, with only minor shortcomings in the sections on “the rights of shareholders” and “the responsibilities of the board” (see chart above).

In 2005, the EBRD launched a survey to test how well the corporate governance legislation works in practice. A case study dealing with related-party transactions was designed. The case study investigated the position of a minority shareholder seeking to access corporate information in order to understand if (1) a related-party transaction was indeed entered into by the company, and (2) whether it was possible to obtain compensation if damage was suffered. Effectiveness of the legislation was then measured according to four principal variables: institutional environment, enforceability, complexity and speed.

The survey revealed that the corporate governance legislation is relatively effective, although it contains some weaknesses. In particular, it might be difficult for a minority shareholder to obtain disclosure from the company in case of obstruction by the controlling shareholders; the legal framework detailing related party transactions needs to be improved; prosecutors are not sufficiently experienced in corporate law cases; and the availability and use of case law by judges and lawyers is very limited.

Concessions

A solid policy framework promoting private sector participation in public works and services and vouching for improvements in the legal environment has been developed by the Ministry of Finance of the Slovak Republic and approved by the Government. In addition, methodological Guidelines for the implementation of PPP have recently been published.

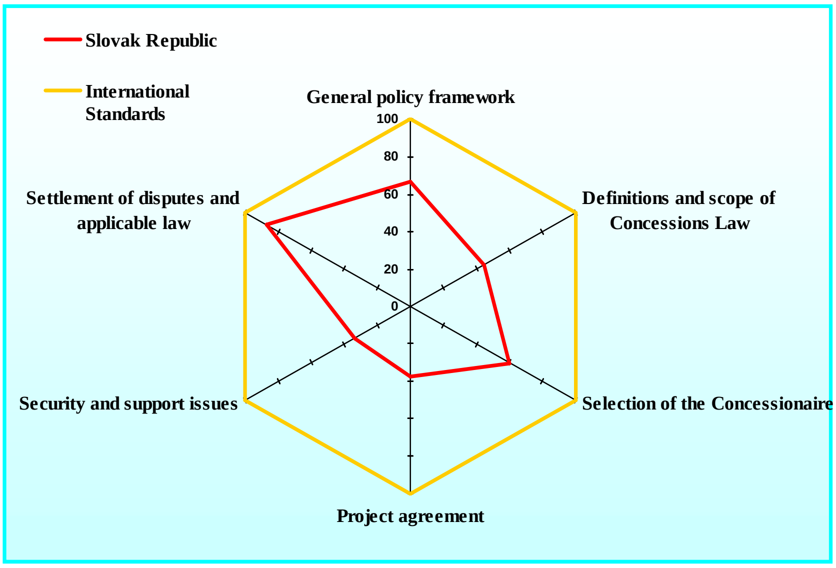
The Slovak Republic does not have a specific Concession or PPP Law. The Public Procurement Law dated 2004 that contained provisions regulating concessions has now been repealed and replaced by the Act No. 25/2006 Coll. on Public Procurement, as amended, effective as of February 2006 (“Public Procurement Act”). Several sources of public law, including the Public Procurement Act, laws governing the administration of property owned by the state or self-administration, the Budgeting Act, the Road Traffic Act and the Act on Electronic Toll Collection, and private law - the Commercial Code and Civil Code - are applicable to PPP.

In addition to the general provisions on procurement, the Public Procurement Act also introduced provisions regarding concessions for the procurement of building works, enabling contractual relationships between public and private parties, such as PPP projects. The contracting authority is obliged to follow these provisions where the estimated value of a building works concession contract equals or exceeds €5,923,000.

It seems, however, the objective of this new Public Procurement Act has been to comply with the EU harmonisation requirement by copying parts of relevant Directives rather than to promote PPP or concession in any way. Concessions are defined by reference to work or service contracts. The Public Procurement Act does not regulate project agreements in any way (apart from specifying duration) and makes no reference to possible government support measures or much needed security issues. The selection procedure may not be suitable for certain PPP projects (for example there is no reference to unsolicited proposals). These shortcomings undermine concessions as an important type of private sector participation in infrastructure projects and public works and services and might limit investors' options and thus interest. Therefore, in order to facilitate PPP in the country, a specific concession law or substantial expansion of the existing part of the Public Procurement Act is required. However, a specific Concession Law is not currently being considered.

The recent EBRD Concession Laws Assessment, undertaken to evaluate applicable regimes throughout the EBRD's countries of operations (the laws on the books only rather than how they work in practice), concluded that Slovak laws had "medium compliance" with internationally accepted standards in the sector (see graph below).

Quality of concession legislation – Slovak Republic (2007/8)



Note: the extremity of each axis represents an ideal score in line with international standards such as the UNCITRAL Legislative Guide for Privately Financed Infrastructure projects. The fuller the 'web', the more closely concessions laws of the country approximate these standards.

Source: EBRD Concessions Sector Assessment 2007/8.

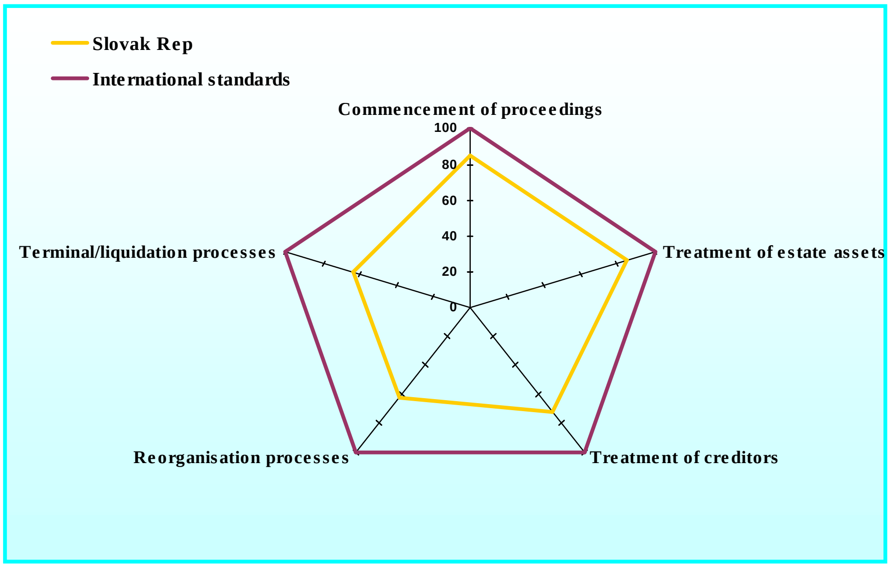
Insolvency

The Act on Bankruptcy and Insolvency ("Insolvency Act") became effective on 1 January 2006, completely reforming the bankruptcy system and repealing the Act on Bankruptcy and Composition of 1991. The goal of the reform was to create a quicker, more creditor-friendly regime that emphasises restructuring rather than liquidation.

It appears that the Insolvency Act largely achieves these goals, although some deficiencies from the old law remain. An update to the EBRD Insolvency Sector Assessment, completed in 2006, found that the Insolvency Act is of a generally acceptable standard and is in "medium compliance" with international standards. The assessment based this rating on the fact that the law "on the books" features reasonable commencement criteria and processes, provides for interim protection, requires delivery of assets and disclosure of relevant information and provides reasonably strong provisions relating to the avoidance of pre-bankruptcy transactions.[10]

The graph below displays the results of the EBRD assessment of the Insolvency Act's level of compliance with international standards in five key areas.

Quality of insolvency legislation – Slovak Republic (2006)



Note: The extremity of each axis represents an ideal score, *i.e.*, corresponding to the international standards such as the World Bank's Principles and guidelines for Effective Insolvency and Creditor Rights Systems, the UNCITRAL Working Group on "Legislative Guidelines for Insolvency Law" and others. The fuller the 'web', the more closely insolvency laws of the country approximate these standards.

Source: EBRD Insolvency Sector Assessment 2006

One of the improvements in the Insolvency Act over the prior law is the speed with which an insolvency proceeding may be completed. In addition, the Insolvency Act contains provisions that make reorganisation easier to achieve. Another feature of the Insolvency Act is that it emphasises, and gives creditors more say in choosing, the administrator.

Although the Insolvency Act is an improvement over the prior law, some defects still remain that should be remedied. For example, the Insolvency Act's protections for creditors during the reorganisation process should be strengthened to provide for, among other things, an independent analysis of the plan to be made available to creditors and modification or amendment of the plan with creditor consent. In addition, the Insolvency Act does not provide for a specialised bankruptcy court, and instead provides for a court of general jurisdiction to preside over bankruptcy cases. There is also no automatic conversion to liquidation in the event a reorganisation fails, and the law's provisions regarding sanctions for breach of the terms of a reorganisation plan are weak. If the Insolvency Act is amended to address these weaknesses, the law's compliance rating may improve in subsequent assessments.

[10] A bill has been proposed to amend the Insolvency Act, but consideration of the bill has been suspended. When, and if, any amendments are made, the EBRD will perform an assessment of the amended law.

Secured Transactions

In 2000, the Slovak Republic undertook, with EBRD technical assistance, a thorough revision of Civil Code provisions relating to secured transactions (covering pledges and mortgages). Both quantitative and qualitative evidence shows that the new regime, which entered into force on 1 January 2003, is working well and enables creditors and lenders to secure their claims simply and efficiently. This gives the Slovak Republic one of the most advanced frameworks for secured credit in Europe.

Security can be taken over any asset that is capable of being transferred. The law covers security over real property, movable assets and intangibles (such as rights and receivables). The assets may be identified by general description and may include assets to be acquired by the debtor at a future date. It is possible to take security over a group of assets even where the group is constantly changing, such as inventory or trade receivables or even an enterprise. All types of claim may be secured. The secured debt may be denominated in any currency, may be of fixed or varying amount and may include claims that will arise in the future. The law is not restricted to bank lending but covers credit given by any person.

Creation of security is simple, cheap and rapid. The requirements are a written agreement and publication of the security by registration. If the agreement is in notarial form, subsequent enforcement of the security is facilitated. A caveat on this exists for mortgages, however, which require registration in the Land Register. Despite ongoing efforts to modernise the register, the process is still very lengthy (on average between 2 and 4 weeks). Another concern stems from the fact that Slovak law dissociates land and buildings and so a mortgage over land would not automatically apply to future constructions over the land. This legal approach is causing difficulties for the financing of new constructions.

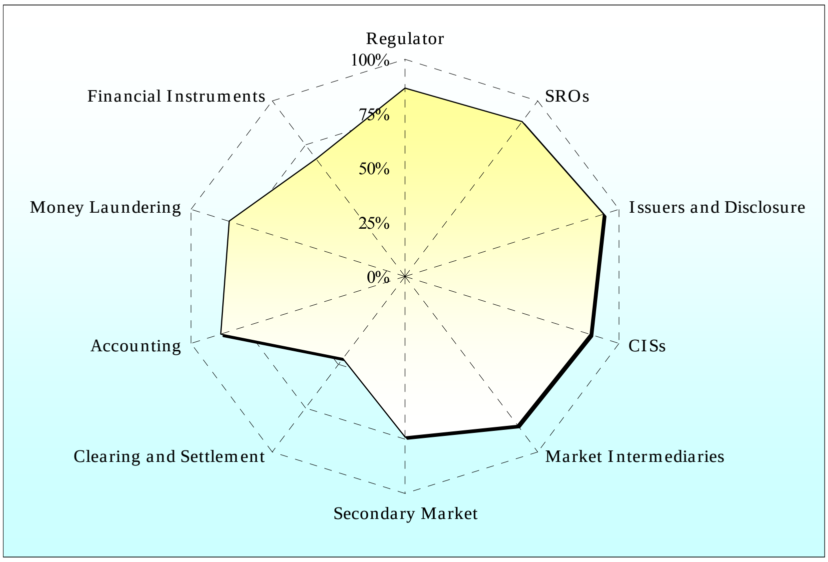
The secured creditor has a first right in the assets taken as security, subject to any prior security given to other creditors. Other persons dealing with the debtor are able to ascertain whether assets are subject to security by consulting the register. Normal rules are included to protect ordinary course of business transactions. Tax claims are no longer paid ahead of secured creditors. Reform of the Insolvency Law has also strengthened the rights of secured creditors in case of debtor’s insolvency.

If the debtor fails to pay the secured debt when due, the secured creditor has the right to take possession, sell the assets given as security and use the proceeds to repay the debt. Sale may be through a court procedure, or by auction or private sale organised by the creditor. A Law on voluntary private-held auctions also provides the framework for realisation to be achieved rapidly and efficiently through auction. Here again, EBRD-led surveys have shown that the process works well and creditors can quickly and efficiently enforce their rights over the secured assets (be they movable or immovable).

Securities Markets

The primary legislation governing securities markets in the Slovak Republic includes the 2001 Act on Securities and Investment Services, the 2003 Act on Collective Investment, the 2002 Act on Stock Exchange, the 1990 Act on Bonds and the 2004 Act on Financial Market Supervision, all as amended. Starting from 1 January 2006, the securities markets regulator is the National Bank of Slovakia (NBS), which is competent for banking, insurance and pension funds.

Quality of securities markets legislation – Slovak Republic (2007)



Note: The extremity of each axis represents an ideal score, *i.e.*, corresponding to the standards set forth in IOSCO's *Objectives and Principles for Securities Regulations*. The fuller the 'web', the closer the relevant securities market legislation of the country approximates these principles.

Source: EBRD Securities Market Legislation Assessment 2007

The 2007 EBRD Securities Markets Legislation Assessment (see chart above), found the Slovak Republic in "high compliance" with the Objectives and Principles of Securities Regulation published by the International Organization of Securities Commissions (IOSCO), showing only minor weaknesses in the legislation on clearing and settlement. To understand how securities markets legislation works in practice, the EBRD recently concluded the 2007 Legal Indicator Survey ("the LIS"). Practitioners in the region were asked to comment on a hypothetical case study, advising an investor who lost his savings after buying shares in a national company's Initial Public Offering (IPO), misled by erroneous information in the prospectus. In particular, the Survey concentrated on effectiveness of prospectus disclosure requirements, private and public enforcement mechanisms and authority of the market regulator.

The LIS revealed that, although IPOs in the Slovak Republic are seldom used as a source of funding, disclosure practice follows good standards. The prospectus is considered reliable and financial reporting practices are sound: EC Regulation 809/2004 directly applies detailed disclosure requirements and is well implemented. Courts and the regulator are developing expertise in investigating complex securities cases but the corresponding capacity of prosecutor needs to be improved. Private enforcement mechanisms (*i.e.*, legal action before a court) can be lengthy and characterised by heavy burdens of proof, which can diminish the effectiveness of the action.

Telecommunications

The communications sector in the Slovak Republic is currently regulated by the Telecommunications Office of the Slovak Republic ('TUSR') and is governed, primarily, by the Electronic Communications Law, 2003 (the '2003 Law'), as amended. TUSR's responsibilities include licensing, equipment approval, interconnection administration, dispute resolution, tariff regulation and spectrum administration. The Ministry of Transport, Post and Telecommunications (the "Ministry") is responsible for policy development. The 2003 Law formally transposes all the key features of the European Union (EU) communications regulatory framework into domestic law.

While the formal framework necessary for a competitive marketplace is in place and first round market reviews complete and acted upon where relevant by TUSR, practical implementation remains challenging and a number of areas give cause for concern. Of particular concern is the dominant position maintained by Slovakia Telecoms (ST), the incumbent operator in the fixed sub-sector, a dominance which appears to have in fact grown recently and remains one of the highest in the EU. While TUSR has imposed remedies arising from the first round of market reviews, these appear to have been insufficient in certain respects. Local Loop Unbundling (LLU) and interconnection generally remains challenging, with alternative operators refusing to avail of interconnection offers of ST, complaining that the terms are too commercially unattractive. As a result the European Commission (EC) has advised TUSR to re-assess the conditions in the relevant interconnection reference offer to ensure an effective compliance with the obligations imposed. EC has also pointed to the continuing difficulties faced by TUSR itself due to lack of resources, in the areas of both personnel and finance; together with the negative impact caused by an administrative appeal system which sees the automatic suspension of a decision of TUSR upon appeal by an aggrieved party. Implementation of modern electronic communications regulation can be complex and demanding in terms of resources, but doubtlessly beneficial in terms of positive impact overall on the economy. Accordingly, government should ensure that TÚSR is provided will all appropriate resources (human, financial and otherwise) and mechanisms to achieve their mandate.