

Yves Mersch: Tenth anniversary of the Euro in Slovakia

Speech by Yves Mersch, Member of the Executive Board of the ECB, at the International Conference to mark the tenth anniversary of the introduction of the euro in Slovakia, Bratislava, 11 January 2019

Charts

I am honoured to be in Bratislava today and to speak before such a distinguished audience. This conference marks the tenth anniversary of the euro in Slovakia, which in fact is a double anniversary as it coincides with twenty years of the euro.

What could be a better anniversary gift, or a clearer symbol of the vitality of our single currency, than Slovakia's success since the introduction of the euro on 1 January 2009?

Slovakia has achieved an impressive real convergence of living standards towards the EU average. The key ingredients of this success have been the country's willingness to grasp the opportunities offered by EU membership and the adoption of the euro.

Indeed, on the economic side fundamental institutional reforms allowed Slovakia to transition to a vibrant market economy and adopt a highly successful export-led growth model, which underpinned real convergence. Reforms rather than continued devaluation or requests for financial assistance is the recipe for success.

Nevertheless, this should be no reason for complacency, as the next stage of convergence is bound to be harder. Neither EU membership nor the single currency offer an "autopilot" for strong economic growth.

I will therefore argue that relentless efforts in the pursuit of institutional quality and good governance are essential in order to raise the country's long-term growth capacity.

The drivers of Slovakia's success

Within just three decades, Slovakia has made a remarkable economic transition from a centrally planned economy to a market economy that is closely integrated into the Single Market. The significant efforts made during the transition have clearly paid off.

Having all but doubled since the early 1990s, Slovakia's real GDP per capita

stands at just over 80% of the EU average.^[1]

Equally impressive has been the pace of economic convergence, which exceeded expectations based on the initial level of Slovak national income.^[2] Slovakia has managed to achieve a per capita GDP level above that of most other countries in central and eastern Europe (CEE), and close to catching up with that of Slovenia and the Czech Republic (Chart 1).

Much of this success is rooted in the country's remarkable institutional transformation in the context of joining the EU.

Slovakia's accession to the EU gave momentum to its convergence efforts and provided it with an external institutional anchor.

Fundamental reforms such as the establishment of a clearly defined system of property rights, effective economic law enforcement and institutions to curb fraud and anticompetitive behaviour were crucial in allowing Slovakia to operate in a market economy and to cope with competition and market forces.

Access to the Single Market and adoption of the *acquis communautaire* have contributed to Slovakia's success in two ways.

First, the removal of trade barriers and application of European-wide standards considerably reduced the cost of doing business across borders, fostering trade and encouraging the country's participation in European value chains.^[3]

Second, a more stable and predictable legal and regulatory environment improved investor security and contributed to a rapid inflow of foreign investment, providing the economy with the necessary foreign capital, know-how and technology to increase its competitiveness.

The Slovak economy became deeply integrated into the Single Market, with an export share of almost 100% of GDP, well above that of other CEE economies (Chart 2), and almost 20% of jobs depending on EU exports to the rest of the world.^[4]

The resulting significant economic convergence eventually paved the way for the introduction of the euro.

Many saw the loss of an independent monetary policy and the inability to respond to external shocks as the most significant cost of joining the euro area.

However, Slovakia's high degree of openness had made it difficult for its national central bank to manage the business cycle in the face of volatile capital flows. The exchange rate had more often become a source of shocks rather than a shock absorber.^[5]

So the benefits of adopting the euro were compelling.

One immediate benefit was the stabilisation of Slovakia's exchange rate with key trading partners and the elimination of currency conversion costs.

Research shows that euro adoption thereby contributed to a 12% increase in Slovakia's exports to the euro area.^[6]

A further advantage of the introduction of the euro was the strengthening of Slovakia's macroeconomic institutions. Adopting the euro gave further impetus to institutional convergence and allowed Slovakia to anchor its macroeconomic institutions in a stronger European framework.

In the run-up to euro adoption, numerous amendments to the Slovak institutional framework were made to ensure convergence with EU requirements, which were closely monitored by the European institutions as in the ECB Convergence Report.^[7]

High standards were required for the independence of the central bank, particularly for the personal independence of executive board members.^[8] Safeguarding institutional independence is crucial when European monetary policy coexists with national financial and labour market policies and where interests may not always be aligned.

The embedding of Slovak institutions in a stable European institutional framework therefore contributed to macroeconomic stability during the crisis and increased investment and trade.

Indeed, in comparison with the Czech Republic, which has very similar economic structures, Slovakia has experienced faster economic growth since 2009. Although the Czech Republic was able to pursue an independent monetary policy during the crisis, Slovakia managed to maintain a 0.9 percentage point advantage over that country in terms of average annual GDP growth between 2009 and 2016.^[9]

As a result, the gap between Slovak and Czech GDP per capita narrowed from 21% in 2008 to 13.8% in 2017.

The importance of institutional quality for long-term convergence

May Slovakia's success continue for many years to come. In the long run, though, it cannot be taken for granted that Slovakia's growth model will continue to deliver strong growth; convergence with EU countries could slow. Slovakia risks falling into the so-called middle-income trap, whereby middle-income economies tend to follow a lower growth trajectory.

Much of the country's growth depends on its ability to attract foreign investment, skills and technology to raise productivity. However, the country has now started to experience a slowdown in foreign investment, technology diffusion and labour productivity.^[10]

For Slovakia to avoid the middle-income trap, it could be useful to develop new strategies focused on domestic innovation. Above all, this would lead to more productive firms, more private capital and more skilled labour to spur long-term growth.

Such improvements, however, often depend on setting the right institutional conditions. Indeed, institutional quality has proved to be an important factor in achieving higher incomes in the long run.^[11] Factors such as inefficient public administration, weak control of rent seeking, tax evasion and corruption hamper competition and economic inclusion.

Slovakia ranks below the euro area average in some of these areas, as measured by the most commonly used institutional governance indicators. More importantly, while most other new euro area countries showed some improvement over the past decade, reform momentum in Slovakia appears to have slowed after the euro was adopted (Chart 3).

By improving in two key areas, Slovakia could help foster the right domestic conditions for businesses to thrive.

One area is improving the business environment. According to the World Bank's Doing Business Indicator, Slovakia ranks below the new euro area countries, in particular in areas such as starting a business, protecting minority investors or dealing with construction permits (Chart 4). Moreover, 55% of entrepreneurs perceived corruption as a problem for doing business in the country, according to the Eurobarometer in 2017.^[12]

Another area for potential improvement is the judicial system. According to the Organisation for Economic Co-Operation and Development (OECD), the integrity of the legal system and independence of the judiciary are perceived as insufficient (Chart 5).^[13] Improving the independence and transparency of the judicial system could help in the fight against corruption and increase public confidence in the state.

Addressing these issues would also create the conditions for national businesses to fully exploit the potential of the Single Market and contribute to sound and inclusive growth.

Conclusion

As we celebrate ten years of euro adoption, Slovakia has become a success story for the convergence process in the EU. The country can be proud of having achieved impressive economic and institutional convergence in such a short time.

Slovakia's success shows that EU accession and the adoption of the euro can create considerable opportunities – opportunities that can be seized, or wasted. Slovakia is a positive example of a country that has seized the opportunities of European integration through fundamental institutional reforms.

Nevertheless, continued efforts in the pursuit of institutional quality and good governance are needed in all euro area countries in order to reap lasting benefits from Monetary Union. This includes strict compliance with the doctrine of central bank independence.

For Slovakia, further improving the business environment and judicial system

would help promote continued economic success over the next ten years.

I'm confident that sound domestic and European institutions will support sustainable growth and contribute to maintaining confidence in the euro and the European project.

[First release for the third quarter of 2018 – Business investment rate up to 23.3% in the euro area – Business profit share down to 40.3%](#)

In the third quarter of 2018, the business investment rate was 23.3% in the **euro area**, compared with 23.0% in the previous quarter. The business profit share in the **euro area** was 40.3% in the third quarter of 2018, compared with 40.6% in the second quarter of 2018.

[Full text available on EUROSTAT website](#)

[First release for the third quarter of 2018 – Household saving rate up to 12.3% in the euro area – Household investment rate stable at 9.1%](#)

The household saving rate in the **euro area** was 12.3% in the third quarter of 2018, compared with 12.1% in the second quarter of 2018. The household investment rate in the **euro area** was 9.1% in the third quarter of 2018, stable compared with the previous quarter.

[Full text available on EUROSTAT website](#)

Roaming charges ended in the European Union on 15 June 2017. Europeans travelling within EU countries will 'Roam Like at Home' and pay domestic prices for roaming calls, SMS and data. ...

On 23 June 2016 citizens of the United Kingdom (UK) voted to leave the European Union (EU). On 29 March 2017 the UK formally notified the European Council of its intention to leave the EU by...

Over the past 20 years, the European Union has put in place some of the highest common asylum standards in the world. And in the past two years, European migration policy has advanced in leaps and...

'Europe will not be made all at once, or according to a single plan. It will be built through concrete achievements which first create a de facto solidarity.' Robert Schuman 9 May 1950 On 25 March 2017, ...

In response to the illegal annexation of Crimea and deliberate destabilisation of a neighbouring sovereign country, the EU has imposed restrictive measures against the Russian Federation. ...

Enlargement is the process whereby countries join the EU. Since it was founded in 1957, the EU has grown from 6 member countries to 28. Any European country that respects the principles of liberty, ...

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I am very proud and happy that in this first half of 2019 I will be managing our common, European matters together with you, as part of your first ever EU presidency. I am sure that you will be performing your own 'Romanian Rhapsody' with energy and wisdom during these six months. That your presidency will be as energetic, as Romanian and as European as the music of George Enescu. And I do not say this just because we are at the Athenaeum

tonight. But because I know how resilient and creative the Romanian nation is. I feel that you will do your very best in 'conducting' the orchestra, creating the right sound and working as a team with the European interest in mind.

You will be the hosts of Europe and I strongly believe that you will take the proverb, *a good farmer makes a good farm*, seriously. I also believe that you will play by the rules. In a fast-changing world, in which the future will surprise us every day, following the rules and being attached to principles will play a particular role. You will all remember the beautiful poem by Nichita Stănescu:

*The future is approaching, I can hear it, I can see it
The thoughts I send its way
return faster than ever.
And sparks keep shooting through my soul
broadcasting its arrival.*

To a large degree it will now be up to Romania, how, and if, Europe will overcome the challenges of the future. It depends only on you, whether, for Europe, Romanian politics will be a good example, or a dire warning. What is at stake during the Romanian Presidency, as well as the informal European Council in Sibiu, is nothing less than the way we envisage our European future together. To those in the European Union who might think that playing outside the agreed rules and cutting corners means strength, I say: you are wrong. It means weakness. To those working hard to defend European values, our freedoms and rights, I say: keep fighting. Remember that there will always be challenges and, sometimes, 'light does not come from light, but from darkness', as Mircea Eliade once put it. And when 'all obstacles seem like walls, the issue is to treat them as mirrors or windows', in the words of Andrei Pleșu.

Romania has the power to fascinate and enchant. The first car in our family was a grey Dacia 1300 of my father-in-law. Interestingly, today my son's father-in-law also drives a Dacia Duster. To me, however, Romanian cars have been less fascinating than Romanian intellectuals and sports personalities. Mircea Eliade, whom I quoted earlier, Emil Cioran, the Dadaist Tristan Tzara, Eugen Ionescu – they are all heroes of my imagination. And so are the athletes, who have delighted audiences around the globe, such as Nadia Comăneci and Simona Halep. But what has left the greatest imprint on my memory was the 1986 European Cup final in Sevilla, that is the victory of Steaua Bucharest over Barcelona. And I would like to appeal to all Romanians, to defend, at home and in Europe, the foundations of our political civilisation – freedom, integrity, the truth in public life, the rule of law and the constitution – with the same determination as Helmuth Duckadam when he defended penalty shots. Back then I also couldn't believe it possible to save 4 penalties in a row! But he made it. And also you will make it. I will help you with this as much as I can.

(The speech was delivered in Romanian)

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