

# Slovak perspective

CEOs' view of the Slovak business environment

June 2010

# Our CEO's view



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We have learned so much in the last 18 months where huge challenges have required a fundamentally different approach and view of the world. The big question is where to we go from here?

In fact, Slovak CEO's are currently asking two key questions:

1. Is the crisis finally over?
2. What do I have to do to protect my business and ensure that my company will grow again?

Following the thirteenth global CEO survey conducted in November 2009, we decided to survey CEO's of companies operating in the Slovak market. We asked them how they managed to deal with the recession, and what lessons they learned for the future. We then compared their opinions to the global survey results.

There is a feeling that the business environment has improved this year. The majority of companies were forced to reduce staff, cut costs, and even close product and service lines in many cases. While there are still some bumps on the road to recovery, there is a large sense of relief that the worst is over.

While there is still a strong focus on controlling costs and monitoring cash flow, Slovak CEO's have bravely started talking about developing new products and making investments. They know that if you fail to win and keep clients, you are out of business. However, this is only part of the picture, with almost 90% of Slovak CEOs recognising the need to focus on better managing their internal talent.

I am sure that it is a relief to everybody to see some rays of optimism confirmed by this year's CEO survey. I am convinced that you will find some valuable insights and inspiring ideas for making strategic decisions in this survey.

A handwritten signature in black ink that reads "Todd Bradshaw". The signature is fluid and cursive, with a long horizontal stroke at the end.

Slovakia has been badly hit by the global recession. This has been the most serious recession that many have ever experienced, and the past 18 months could serve as the defining period for many CEOs. Slovakia has a lot going for it domestically, as it benefits from some solid fundamentals. Public debt was 30% of GDP in 2008 and is now still only a manageable 40%. The pace of Slovak GDP decline started to slow in the third quarter of 2009 and took a turn for the better in the first quarter of 2010. GDP fell in 2009 in comparison to the Czech Republic, but recovered in 2010 stronger than its neighbour.

Despite the economic downturn, 21% of Slovak CEOs confirmed that revenues grew compared to the previous year. However, 2009 revenues fell for most of the respondents.

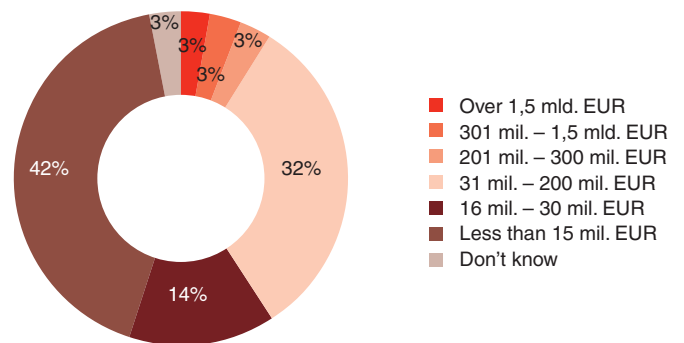
## Who we asked and where

The PricewaterhouseCoopers thirteenth Annual Global CEO Survey looked at what measures CEOs have been taking in response to the recession, how they view the post-crisis business environment, and what changes they are making to adapt their organizations. PwC surveyed 1,198 business leaders from around the globe between September and November 2009.

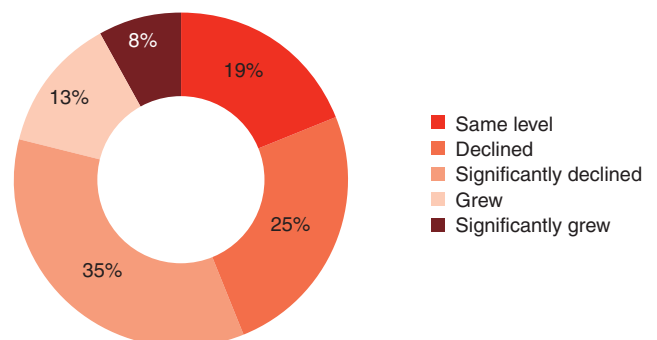
We then conducted a follow-up survey among CEOs of major companies operating in Slovakia. We have analysed 80 responses from leaders of large companies across all industries.

In terms of size, 32% of Slovak CEOs listed 2009 revenues of between EUR 31 million – EUR 200 million, and 42% of the companies that responded had 2009 revenues of less than EUR 15 million.

Please indicate your organization's revenue in the last fiscal year (in Euros)



How have 2009 revenues of your company changed compared to 2008?



# How do CEOs in Slovakia see our future?

## We're very confident

Although there are still strong concerns about a protracted global recession, some positive signs for the future have already appeared. Slovak CEOs are more confident of revenue growth than global CEOs. A total of 49% of participating Slovak CEOs reported being very confident about revenue growth over the next 12 months, compared to 31% of global CEOs. Their long-term view is even more optimistic, because 74% of participating CEOs reported that they are very confident of achieving revenue growth over the next three years.

Their outlooks partly reflect unfolding macro-economic conditions. Despite the slow recovery in the Eurozone, where annual GDP growth of 0.9% is expected in 2010, increasing to 1.6% in 2012, and then to around 1.8% by 2015, the Slovak economy should outperform this forecast by 2.3% this year, a more solid increase to 3.4% next year, and then annual growth in 2012 through 2014 of 4.5%.

## New product development will be the focus for future growth

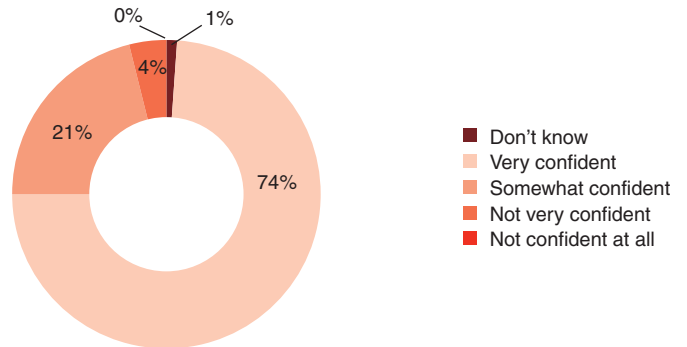
CEOs are less likely to explore new markets or go for strategic alliances and M&A. The largest proportion of CEOs (45%) is positioning companies for new product development. Early on, the same proportion (42%) will be focusing on better penetration of existing markets as the best bet for growth over the coming years.

New ways of cooperating could also help companies survive and grow, as almost half of CEOs expect to focus on their existing market and do not see much room for expansion abroad or for new acquisitions. This "inward" focus and cautious approach can also be linked to the concern of Slovak CEOs about shifts in consumer behaviour and low-cost competition.

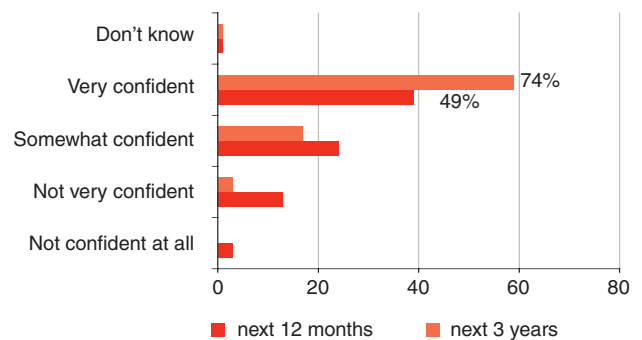
Product development and related R&D activities to achieve these goals are among the priorities of the Slovak government and the European Union. Thus, it is advisable to consider the utilization of state aid from EU funds to contribute to the growth of the company and increased profits, as well as to strengthen awareness of the importance of R&D in general.

There are several areas which the company might focus on when looking for its own way to develop - fundamental research, applied research, experimental development, and feasibility studies. All of them are being supported and represent an internal strength and source of the company for future long-term growth. Innovation and application of new technologies and procedures are aspects that should differentiate a company of the future from the stagnating entities of the pre-crisis period.

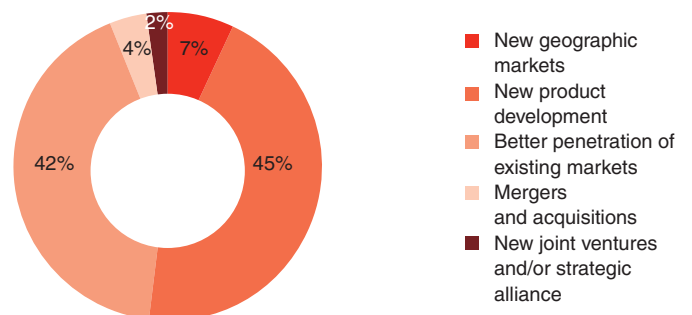
How do you assess your level of confidence in prospects for the revenue growth of your company over the next three years?



How do you assess your level of confidence in prospects for the revenue growth of your company over the next 12 months / 3 years?



Which one of the following potential opportunities for business growth you see as the main opportunity to grow your business in the next 12 months?



The most important lesson you've learned as a consequence of the economic crisis

The crisis made us much more focus on using our own reserves and the company's internal potential.

Luboš Lesay  
Managing Director, IKEA Components s. r. o.

Adapt fast to the changed market and business conditions.

Robert Grozdanovski  
Managing Director, Volvo Truck Slovak, s. r. o.

## We're funding our growth

Our study has confirmed that, these days, senior executives may be loath to tap the volatile financial markets for acquisitions, and they are focusing more on internal funding. More than half (61%) of CEOs expect to fund growth through internally-generated cash flow. Only 2% of Slovak CEOs trust government sources, and 23% put their hope in bank lending.

As banks' insatiable thirst for balance sheet growth was replaced by a headache from distressed debt management, CEOs have been forced to resort to internal funding when seeking cash to fund growth. To finance growth from external sources, in this climate, is an exercise not all are willing to undergo, as the ever-more-vigilant eye of the audience can find many contestants out of shape. Bankers are setting their new ambitious plans and budgets for next year, and will look to CEOs with well prepared business plans to help them reach their end-year bonuses. This will alleviate some of the barriers in external financing introduced during these difficult yet interesting times.

## We are concerned about a protracted global recession

Slovak CEOs are concerned about a continued downturn, low-cost competition and over-regulation more than any other threat to growth, the same threats that global CEOs fear. Despite the decline in concern of global CEOs from last year (85%), most of them (65%) are still concerned about a protracted global recession as well. There is a strong indication that the recession and subsequent recovery may have accelerated trends favouring growth in some emerging markets, particularly as growth returns to emerging markets earlier.

Least important for them are terrorism, pandemics and the scarcity of natural resources. For 66.3 % of respondents, inflation is not a major threat to their growth.

The most important lesson you've learned as a consequence of the economic crisis

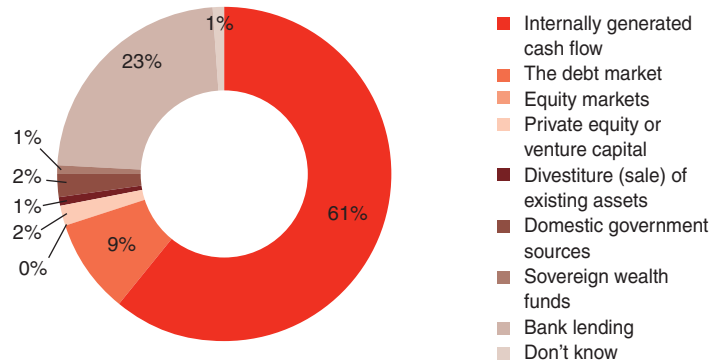
Investment and revenue check performed on a more regular basis. Open communication with all staff about the company's current position and the resulting consequences.

Marián Dubjel  
Country Manager, Krauthammer Slovakia, s. r. o.

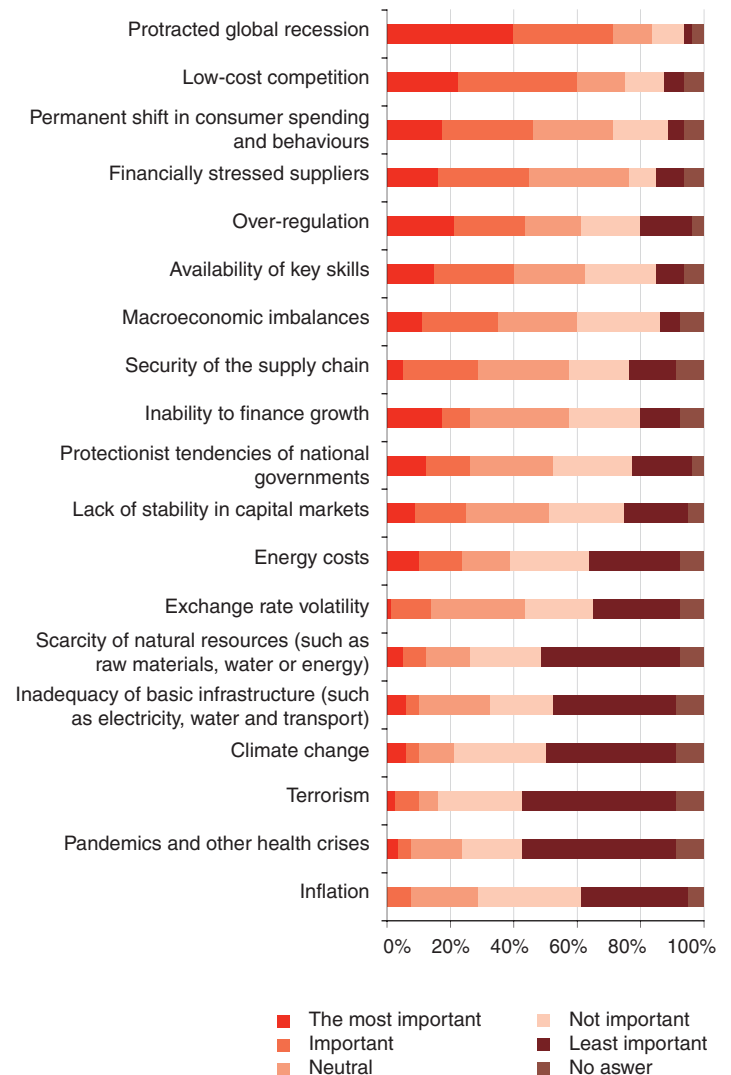
It is very easy to get into trouble. Even in the biggest economic boom, companies should behave economically and save money for a rainy day.

Ivan Novák  
General Director, PPA CONTROLL, a. s.

How do you expect to finance this growth?



Which of the following potential threats to your growth prospects are you concerned about?



# What do CEOs in Slovakia want to change?

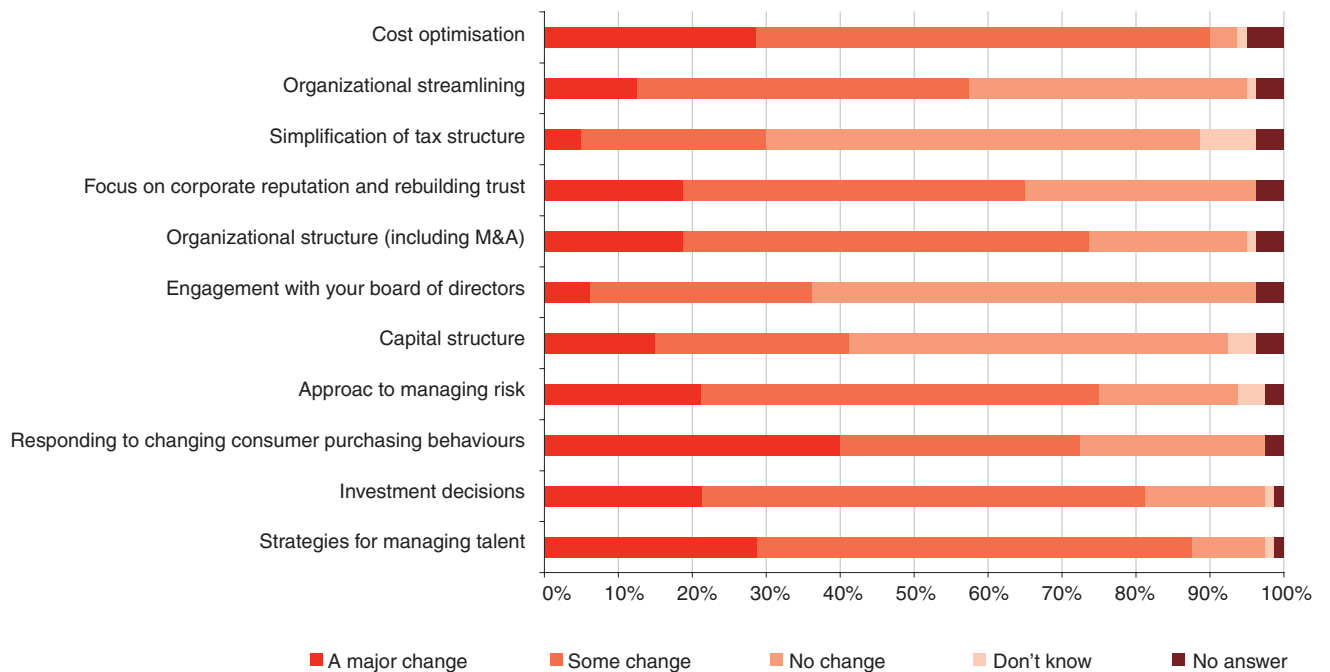
## We will optimise costs

Most (81%) Slovak CEOs plan to make changes in investment procedures. Our CEOs are satisfied with our tax system because the majority of them (59%) prefer no change in the simplification of the tax structure.

Slovak CEOs will be continuing to look for strategic approaches to optimize costs, followed by strategic changes focusing on their company's strategies for managing key people.

The nature of the action required depends on the magnitude of the cost challenge. Immediate cost savings of up to 10% of the cost base can be achieved by tightening budget controls and focusing on quick-win initiatives. If company aims at reductions in the range of 10% to 20%, then changes in business processes are essential. For those who wish to exceed 20%, this means restructuring initiatives requiring fundamental changes in the company's operating model or system infrastructure.

Are you planning any changes in your business model (in terms of strategy, organization or operations)?



## We want to manage our talents

The second biggest change that CEOs are planning to make are changes in strategies for managing talent, where almost 90% of Slovak CEOs said they would do so.

CEOs stated that most important part of a competitive advantage is high quality customer service, and that can be secured by the right product or services and skilled employees. CEOs are aware that the availability of key skills are needed for the sustainability of growth. Businesses appreciate a real long-term partnership with clients as the key factor for overcoming the crisis, and they acknowledge the need for both a long-term management strategy and an ongoing dialogue with key talents.

Both these factors confirm that it is essential to set the corporate performance management process correctly.

Based on the brief crisis survey we conducted in autumn 2009, the companies surveyed became aware of the importance of key talents in difficult times and, despite the freeze on salary increases, key talents were one of the few employee categories where a salary increase was noted.

Similar steps were taken in the field of learning and development. The overall expenditures for Learning & Development activities were shrinking, whilst the system of education for key talent was comparable with previous years.

## What, and how, we restructure

Despite widespread restructuring last year, many businesses remain committed to further cost-cutting. In an indication of the cost pressure they continue to face, 65% of CEOs we surveyed plan cost-reduction initiatives in the next 12 months, compared with the 81% who made cuts over the past year.

These activities are most often a response to the decrease in the volume of sales and prices, performed with the aim to keep desired profitability (or minimize losses). However, several factors need to be considered. Is the cost reduction in line with the company's strategy? For example, a reduction in headcount in sales and marketing departments may influence your S&M initiatives and subsequent presence on the market. Does cost reduction really cover all major supplies? Non-core spending is an obvious area to focus on (and usually the first), but a company needs to be sure that all core contracts are under a CEO's review and subsequent renegotiation.

Significant headcount reductions reflecting the impact of the financial crisis have already taken place over the past 12 months, as almost 60% of CEOs confirm headcount reductions. CEOs continue to decrease headcount, as 18.8% of CEOs we surveyed will lay off people in the next 12 months. Certain positive expectations were noted in regard to headcount changes, as 40% of CEOs are planning to increase headcount over the next 12 months.

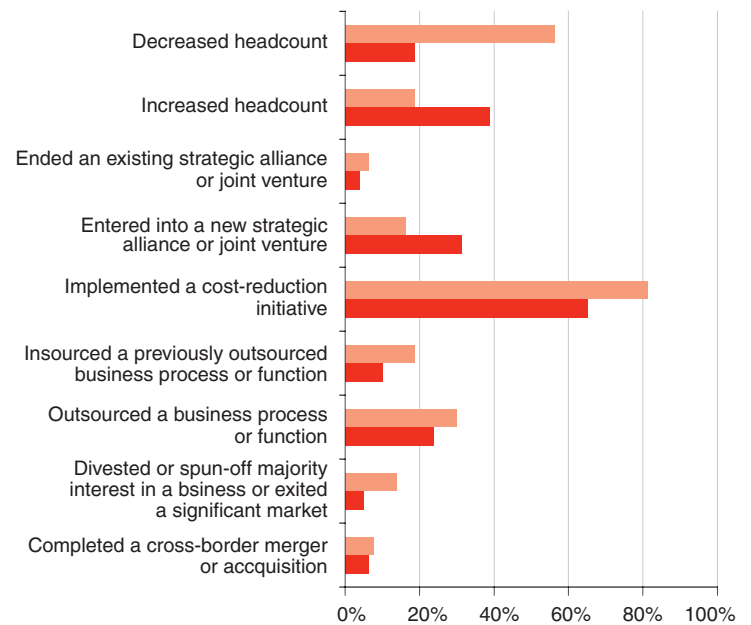
Costs of headcount reduction and subsequent hiring may increase your costs base (the yoyo effect). And, of course, all cost reduction initiatives may need to be considered from the aspect of the quality of products and services delivered.

While cross-border mergers and acquisitions are still waiting to make a come back, we can see strong tendencies for companies to find other ways to interconnect or cooperate that could provide reasonable benefits on all sides, such as reduced costs on a distribution network or Research & Development.

In the coming months and years, we will be able to see strategic alliances or joint ventures that would have been unimaginable in the past.

Which, if any, of the following restructuring activities

- have you initiated in past 12 months
- do you plan to initiate in coming 12 months



The most important lesson you've learned as a consequence of the economic crisis

**Need a more flexible cost structure.**

George F. Babcoke  
General Manager, U. S. Steel Košice, s. r. o.

**By managing the portfolio risk optimally and by setting fair price conditions for services provided, you can generate a profit even when sales are falling.**

Namina Koussahova  
General Director, ČSOB Factoring a. s.

**Long-term planning strategy versus flexibility to the quickly changing business environment.**

Jaroslav Kollar  
Country Manager, Nestlé Slovensko s. r. o.

# How will CEOs in Slovakia set themselves up for growth?

## Keep effective control

Tax compliance, maintaining efficiency in an environment with cost pressures, and transparent public procurement are the most important topics for Slovak CEOs in 2010. They think that cross-border restructuring is one of the least important issues for next year.

## Hope for asset price recovery

Most Slovak CEOs consider the sale or acquisition of distressed assets to be at the bottom of their priority list for 2010. This suggests that many CEOs will be passive in their approach, hoping to be lifted by the rising tide of asset price recovery. Only a few CEOs will benefit from the current market situation by taking an active approach in managing assets.

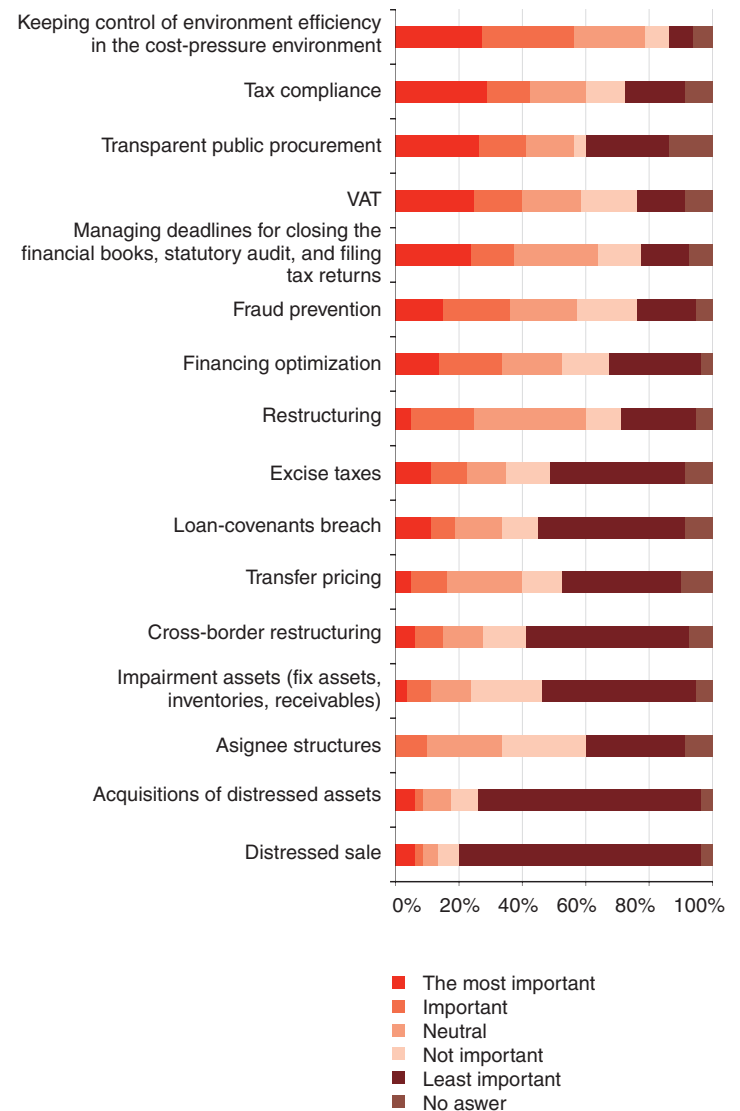
Most of the asset sales will be forced by banks, using covenant breaches to step in and guard their positions, creating little or no room to use the proceeds from asset sales for purposes other than debt repayment. An active approach to managing assets will separate the winners from the losers for the next decade.

## Fraud prevention

Fraud prevention, together with financing optimization, have also been identified by Slovak CEOs' as very important priorities for them. The financial crisis has brought an increased risk of fraud, as it puts greater pressure on individuals as well as companies, and has also created greater opportunities for committing fraud.

On the other hand, as companies started looking more closely at their costs, processes, and contracts, this has led to an increased opportunity to discover fraud. The results of the last two PwC Slovakia crime surveys show that approximately 30% of companies have been victims of fraud, and 70% of those say that the related damage has been higher than USD 100,000.

How important are the topics listed below for your business in 2010?



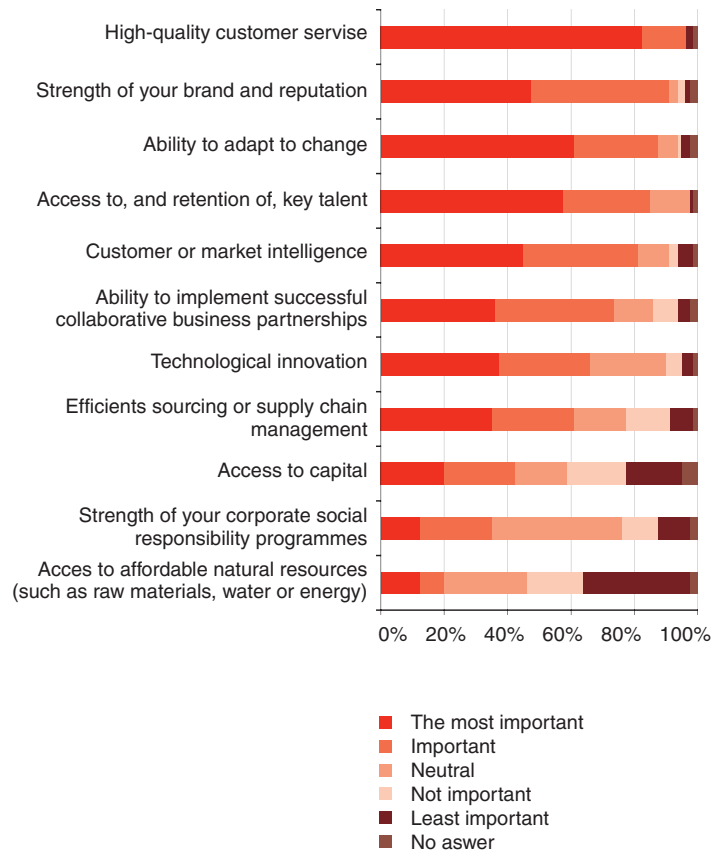
## Close to the customer

To sustain growth over the long term, the majority of Slovak CEOs will focus on customers. Putting the customer in first place in terms of importance is not just a proclamation but, according to more than half of CEOs, is a necessity for sustaining long-term growth. This means ensuring high-quality customer service, having the right information about customers and the market, and the right people to deliver what customers expect. Brand strength and reputation are two other key elements of sustainable growth.

Most Slovak CEOs (82.5%) have identified high-quality customer service as the single most important source of a competitive advantage. These days, it is becoming more and more difficult to differentiate among products, and even if the company successfully launches a new unique product, competitors will quickly respond to erase this advantage. In these conditions of very similar product offerings, a customer's experience matters most, and companies are focusing on building customer loyalty by delivering unique customer service.

It thus comes as no surprise that over half of CEOs plan changes in the way they manage talent and deal with consumers. Focusing on cost optimization and organizational streamlining should help businesses generate cash for future growth and balance the temporary shortage of external financing.

Which of these sources of competitive advantage are important to sustain your growth over the long term?




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The most important lesson you've learned as a consequence of the economic crisis

Keep close to your customer.

John McGuigan  
General Director, Telefónica O2 Slovakia s. r. o.

A proactive approach to face change and flexibility to adapt.

Paolo Ruzzini  
General Director, Slovenské elektrárne a. s.

Manage receivables, stay close to your customers in good and bad times.

Fulco van Lede  
Managing Director, Probugas a. s.

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# How do CEOs in Slovakia perceive the Slovak business environment?

## State aid

To improve the competitiveness of Slovak companies, nearly all CEOs require better access to EU funds (91%) and more transparent public procurement (87.2%).

From the perspective of Slovak companies, the state aid application process is considered administratively burdensome, time consuming, and insufficiently transparent. The process of applying for investment aid is very complex and is for bigger entities wishing to implement big investment projects exceeding EUR 3.32 million (EUR 6.64 million from 2011).

In spite of the fact that EU funds are intended for smaller projects, and that they should allow small and micro entities to apply for aid as well, the process of applying for EU funds is rather administratively burdensome, and the evaluation criteria are very strict. Thus, companies in Slovakia often avoid applying for state aid and make major efforts to obtain external sources or collect internal ones for investing or for expanding their businesses. Increasing transparency and simplifying the state aid application rules could maximize the benefit for both sides – companies would have more extensive sources of funding available, while the state would benefit from contributions to the public budget from investments made in Slovakia and increased competitiveness.

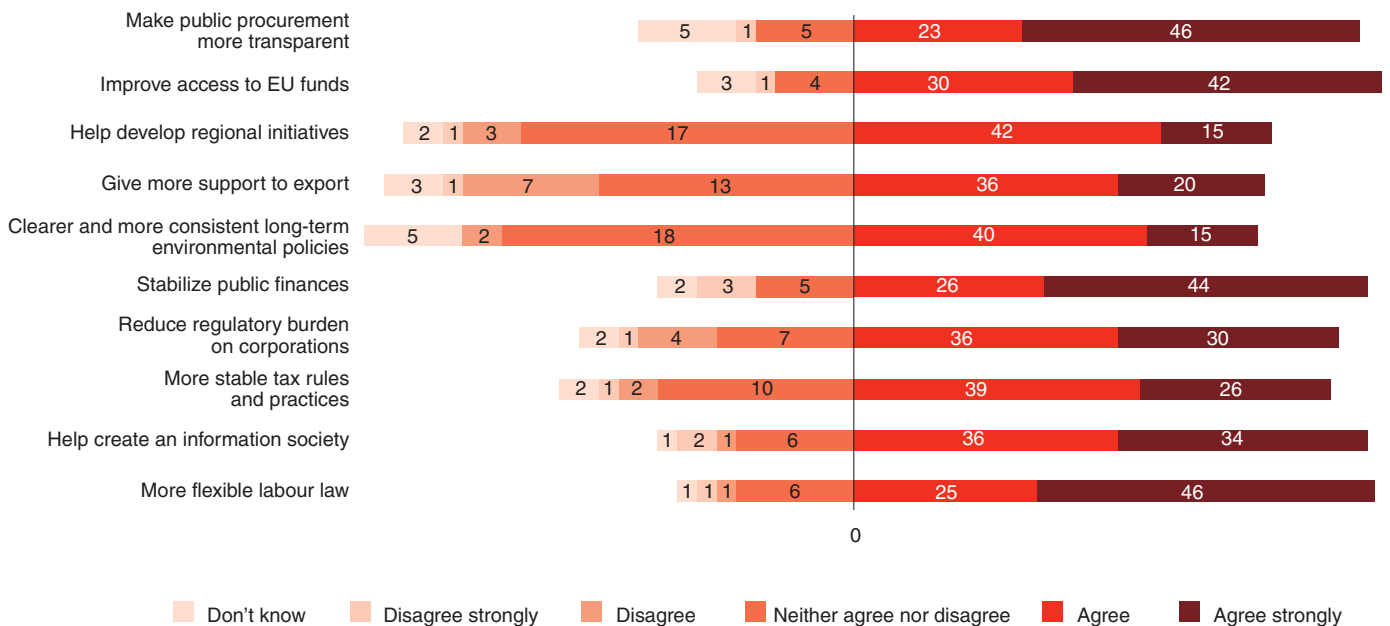
## Sustainable fiscal policies and less regulation

While the Global CEO Survey disclosed that company leaders appreciated the governments' measures to stabilize the financial system, CEOs also expressed concerns about over-regulation. Also, Slovak CEOs want regulatory clarity and stability more than direct support from their government.

Slovak CEOs see ensuring more stable tax rules, more flexible labour laws (89.7%), stable public finances (89.7%), as well as a reduction in the regulatory burden on corporations as the biggest challenges for government. CEOs find untying their hands to be more important than export supports or regional initiatives to improving the competitiveness of Slovak companies.

Governments all over the world are facing a conundrum – how to deal with ever more debt at a time when the needs of businesses and citizens for support are rising, with the economic downturn resulting in greater numbers of unemployed and disadvantaged people needing state assistance. However, CEOs need to hear clear commitments from the government that it will maintain fiscal stability and will not harm the business environment and the perception of the country abroad.

What should the Government do to improve the competitiveness of Slovak companies?



Compared to other EU countries, the 2009 figures of the Slovak public sector seemed fairly good. Public debt at 40% of GDP is less than the EU average (73.6% of GDP). However, in a year the figure increased by 10%, and his further increase is also expected for 2010.

The overall regulatory burden undermines the efforts of companies and entrepreneurs to focus on their businesses. In particular, small and mid-sized companies are faced with a situation in which a significant part of the time spent on their core business is swallowed up by regulatory burdens.

When it comes to improving regulations, there is still a desire for collaboration between business and government in order to achieve a more positive situation. Also, the global results of the CEO survey confirm that this is particularly critical at the current point in the economic cycle, when governments must beware of imposing regulations which stifle innovation, competitiveness, and the growth of jobs.

## A stable taxation system

While it might be difficult for governments to decrease tax rates, reducing the administrative burden can always be a positive action, delivering benefits to both government and business. According to the latest World Bank Group and PricewaterhouseCoopers report *Paying Taxes*, on average, across all of the 183 economies covered in the report, the standard case study company has to make 31 tax payments and spend 286 hours calculating and paying its taxes. In Slovakia, a company had to make 31 tax payments and spend 257 hours calculating and paying taxes. This means that the Slovak Republic has reduced the number of hours to comply with tax laws by 68 hours (down from 325 hours last year). It has moved up 26 places in the ranking for this indicator, from number 129 to number 103. The Slovak Republic's overall rank in terms of the ease of paying taxes has improved.

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Slovakia has a fairly low corporate income tax rate, which has helped the country remain attractive to investors during the economic downturn, as has the relative simplicity of the tax system. However, corporate tax is only one element of the total tax burden, and Slovakia's fairly low ranking in terms of total tax rate reflects the fact that its labour taxes are relatively high.

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For this survey, a "Slovak CEO" is a person who leads a company based in Slovakia. The term does not indicate the mother tongue or nationality of the person.

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