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Slovenia:
Political mess reduces ability to act

GDP which is driven primarily by foreign demand will grow by 2% in 2011. The enterprise sector is currently facing liquidity problems and needs to deleverage, thus there is little room for investments. Somewhat faster growth can only be expected in the years to come, as long as investment enjoys a recovery and private consumption registers some improvement. For the latter to happen, however, the labour market will have to improve as well. Given the ongoing fiscal consolidation, public investment will need time to recover. Solving the political problems will be one of the main prerequisites for a return to a sustainable growth path.

Slovenia's GDP continued to grow at a moderate pace in the first quarter of 2011. The modest increase was backed by rising foreign demand and a resumption of growth in household consumption, while investment continued to shrink (already for the tenth consecutive quarter). Gross fixed capital formation fell by another 6%, affecting primarily construction. Government consumption on the other hand reported a modest increase. Apart from economic problems, the country's centre-left coalition led by Prime Minister Borut Pahor lost its majority in the parliament when the pensioners' party DeSUS left the coalition in May over a dispute on the pension reform, which it strongly opposed. In late June also ZARES, another coalition party, withdrew from the cabinet.

The positive tendencies in industrial production that had prevailed in 2010 continued and even strengthened during the first months of 2011, with output up by nearly 10%; above-average growth is reported for the production of capital goods and intermediate goods. Almost all industrial branches within manufacturing increased their output. In the construction sector, contracting significantly in both 2009 and 2010, the negative tendencies continued particularly in residential building; output dropped by 24% in the first quarter of 2011. There is still a huge number of unsold apartments, and public works – motorway construction in particular – have been phasing out. The construction sector has not recovered from the crisis yet and is still in a critical financial situation; only recently the Court of Ljubljana ended the compulsory settlement procedure in Slovenia's biggest construction company SCT, and started the bankruptcy procedure.

In external trade, during the first four months both goods exports and imports expanded, by 18% and 20% respectively in nominal terms. Though increasing, the trade deficit remained low as compared to a year earlier. Also in services trade, exports and imports accelerated, rising by 16% and 9% respectively; hence, the services trade surplus grew by about one third. Owing to the improvement in services trade and a surplus in the current transfer balance, the current account deficit was negligible (EUR 48 million). As opposed to the pre-crisis years, when Slovenia was a net exporter of FDI, inward foreign investments exceeded Slovenian investments abroad during the first months of 2011.

The situation on the labour market continued to deteriorate. Labour Force Survey data indicate that the number of employed fell remarkably in the first quarter of 2011, by 3.8%; the unemployment rate rose to 8.5%, which is still below the EU-27 average but high by Slovenian standards. In comparison, unemployment based on registration data has shown a steady increase since September 2008, putting the unemployment rate at 12.2% by the end of March 2011. Unemployment may further increase in the coming months due to the possible closing-down of enterprises. The crisis has hit first of all labour-intensive sectors such as the textile industry, employing females with low or no qualification, and the construction sector where older low-qualified workers were affected most.

After the European Commission’s approval of a recapitalization of the country’s two largest banks, the Slovenian government has subscribed almost all shares (worth EUR 250 million) issued by Nova Ljubljanska Banka (NLB), raising its ownership in the bank to over 50%, while the state’s share in Nova Kreditna Banka Maribor (NKMB) remained unchanged. The recapitalization had become necessary because of deteriorating capital adequacy ratios. In 2010 the Slovenian banking sector posted close to EUR 50 million losses. Slovenian banks are very exposed to highly indebted companies in the construction and real estate sectors, but also in leveraged buy-out holding companies. Given the poor situation of these companies further bank losses are to be expected. According to the IMF financial soundness indicator measure, non-performing loans increased to 8.2% of the banks’ total gross loans in the fourth quarter of 2010. A strategy discussed recently by the minister of finance envisages that the state remains the key owner not only of NLB but also of NKMB and the country’s biggest insurance company Zavarovalnica Triglav. Provided that the state remains the single largest owner, a reduction of its stakes in these institutions to 25% plus one share would be an option. NLB and NKMB currently account for more than 40% of Slovenia’s banking assets and Triglav for 36% of the insurance market.

Slovenia's fiscal deficit has increased quite significantly during the crisis period caused primarily by stimulus packages initiated by the government in order to cushion the impact of the crisis. In 2009 and 2010 some 1.8% and 0.2% of the GDP were used, among other things, for short-term working arrangements, the reduction of the corporate income tax or R&D subsidies for companies. Thus, the general government deficit rose from 1.8% in 2008 to almost 6% thereafter – a huge jump especially in the Slovenian context. In 2010 the general government deficit declined to 5.6% thanks to growing revenues. As for 2011 the deficit is expected to increase again to slightly less than 6%, mainly because of the government recapitalization of banks. Public debt grew in line with rising budget deficits from 22% of the GDP in 2008 to 38% in 2010, and is likely to increase to 43% in 2011 – which is still very low by current European standards.

In order to reduce the fiscal deficit the Slovenian government envisages postponing the elimination of wage disparities in the public sector (and implementing the measure only when economic conditions allow), not to index wages to inflation in 2011 and 2012, reducing public sector employment and a number of structural reforms. The most debated among these reforms is the pension reform which was adopted by the government in November 2010. It includes a gradual increase of the statutory retirement age to 65 years for both males and females until 2020, an extension of the period for calculating the pension base and incentives for employers to employ older workers. As elsewhere, however, trade unions opposed this reform. In Slovenia, they pushed for a referendum on the issue, which was eventually held on 5 June. According to the vote, over 70% of the electorate not surprisingly rejected the pension reform. So far Prime Minister Pahor, whose government lost the majority in parliament in May, has refused to resign, because 'his resignation would not lead automatically to new elections' (according to the constitution the Slovenian president can call early elections only if the parliament has failed to elect a new prime minister in three attempts). The next regular parliamentary elections are scheduled for autumn 2012. As an immediate consequence of the lost referendum, the prime minister announced additional saving measures to ensure the stability of the budget: accordingly a revision of the budget should be adopted by the parliament in July, envisaging a cut in expenditures for merchandise, services and investments.

wiiw still adheres to its earlier GDP forecast of 2% in 2011, driven primarily by foreign demand and to a lesser extent by domestic demand. Somewhat higher growth (2.5%) can only be expected in 2012, provided a recovery of investment and a further improvement in private consumption. Given the moderate growth prospects, employment will continue to decrease in 2011 and increase slightly, if at all, only from 2012 onwards. Unemployment (LFS) is expected to come down only gradually. The recovery of household consumption is, however, conditioned on an improvement on the labour market. Given fiscal consolidation, public investment will need some time to recover and will regain strength only in 2012. Solving the political problems would be one of the main preconditions for further action and the return to a sustainable growth path.

Table SI

Slovenia: Selected Economic Indicators

	2007	2008	2009	2010 1)	2010	2011	2011	2012	2013
					1st quarter			Forecast	
Population, th pers., average	2018.1	2021.3	2039.7	2047.0	2047.0	2050.2	2050	2050	2050
Gross domestic product, EUR mn, nom.	34568.2	37304.7	35384.4	36061.0	8239.2	8504.9	37700	39610	41820
annual change in % (real)	6.9	3.7	-8.1	1.2	-1.1	2.0	2	2.5	3
GDP/capita (EUR at exchange rate)	17100	18400	17300	17600	4000	4100	18400	19300	20400
GDP/capita (EUR at PPP)	22100	22800	20800	21300	.	.	.	.	.
Consumption of households, EUR mn, nom.	17944.2	19477.5	19355.9	20016.7	4485.5	4676.8	.	.	.
annual change in % (real)	6.7	2.9	-0.5	0.5	-0.9	1.2	1.5	1.5	2
Gross fixed capital form., EUR mn, nom.	9571.3	10743.4	8471.6	8027.7	1765.9	1706.1	.	.	.
annual change in % (real)	13.0	8.5	-21.6	-6.7	-10.5	-6.1	-3.5	3	4
Gross industrial production									
annual change in % (real)	7.1	2.4	-17.3	6.8	-0.3	9.7	8	6	6
Gross agricultural production									
annual change in % (real)	3.9	-1.3	-1.3	1.0	.	.	.	.	.
Construction industry									
annual change in % (real)	18.5	15.5	-20.9	-16.9	-18.9	-24.1	.	.	.
Employed persons - LFS, th, average	985	996	981	966	965	928	940	950	960
annual change in %	2.5	1.1	-1.5	-1.5	0.3	-3.8	-3	1	1
Unemployed persons - LFS, th, average	50	46	61	75	74	86	.	.	.
Unemployment rate - LFS, in %, average	4.8	4.4	5.9	7.3	7.1	8.5	8	7.5	7
Reg. unemployment rate, in %, end of period	7.3	7.0	10.3	11.8	10.6	12.2	11.5	10.5	10
Average gross monthly wages, EUR	1285	1391	1439	1495	1460	1505	.	.	.
annual change in % (real, net)	4.2	2.0	2.5	2.1	2.1	1.6	.	.	.
Consumer prices (HICP), % p.a.	3.8	5.5	0.9	2.1	1.7	2.2	2.5	2.5	2.5
Producer prices in industry, % p.a.	4.4	3.9	-1.4	2.0	-1.2	5.7	4	2.5	2
General governm.budget, EU-def., % GDP									
Revenues	42.4	42.3	43.1	43.4	.	.	43.3	43.1	43
Expenditures	42.5	44.1	49.0	49.0	.	.	49.1	48.1	47.5
Net lending (+) / net borrowing (-)	-0.1	-1.8	-6.0	-5.6	.	.	-5.8	-5.0	-4.5
Public debt, EU-def., in % of GDP	23.1	21.9	35.2	38.0	.	.	42.8	46	50
Central bank policy rate, % p.a., end of period 2)	4.0	2.5	1.0	1.0	1.0	1.0	.	.	.
Current account, EUR mn	-1646	-2490	-526	-409	-107	-87	-450	-600	-720
Current account in % of GDP	-4.8	-6.7	-1.5	-1.1	-1.3	-1.0	-1.2	-1.5	-1.7
Exports of goods, BOP, EUR mn	19799	20048	16167	18380	4203	5021	21300	24100	27200
annual growth rate in %	16.3	1.3	-19.4	13.7	6.8	19.5	16	13	13
Imports of goods, BOP, EUR mn	21465	22699	16866	19354	4338	5304	23000	26200	29600
annual growth rate in %	18.1	5.7	-25.7	14.8	6.1	22.3	19	14	13
Exports of services, BOP, EUR mn	4146	5043	4300	4363	925	1076	5000	5600	6200
annual growth rate in %	16.0	21.6	-14.7	1.5	0.7	16.3	15	11	10
Imports of services, BOP, EUR mn	3098	3549	3187	3307	692	769	3700	4100	4600
annual growth rate in %	20.1	14.6	-10.2	3.8	1.8	11.3	11	11	12
FDI inflow, EUR mn	1106	1330	-418	628	82	86	500	.	.
FDI outflow, EUR mn	1316	948	120	129	121	-4	.	.	.
Gross reserves of NB excl. gold, EUR mn	666	623	671	695	639	656	.	.	.
Gross external debt, EUR mn	34783	39234	40276	40897	40977	42884	.	.	.
Gross external debt in % of GDP	100.6	105.2	113.8	113.4	113.6	113.8	.	.	.
Average exchange rate EUR/EUR	1.0000	1.0000	1.0000	1.0000	1.0000	1.0000	1	1	1
Purchasing power parity EUR/EUR	0.7749	0.8087	0.8356	0.8265	.	.	.	.	.

Note: Gross industrial production, construction output and producer prices refer to NACE Rev. 2.
1) Preliminary. - 2) From 2007 official refinancing operation rates for euro area (ECB), main refinancing rate of NB before.

Source: wiiw Database incorporating Eurostat and national statistics. Forecasts by wiiw.