Milan Martin **Cvikl**

SLOVENIA

Milan Martin Cvikl is a Slovenian central banker and technocrat in the area of public finance and public administration management. Since 2017 he has been Alternate Director on the EBRD Board of Directors, in the constituency of Belgium, Slovenia and Luxembourg. Between 2010-2016 he was a Member of the European Court of Auditors: responsible first for the audit of EU revenues and later, as Dean, presiding over deliberations on audits of EU financial and economic governance. Other notable past positions include Minister for European Affairs, Member of Parliament of the Republic of Slovenia, Chairman of its Parliamentary Committee on Public Finance Control and Secretary General of the Slovenian Government. He also worked as an economist for the World Bank and was CFO of NLB d.d. He has a Masters in Macroeconomics from the University of Ljubljana.

The views expressed here are those of the author and do not necessarily represent the official views of his current or past employers.

Slovene EU Convergence came in three phases. The first was the process of achieving independence, when on economic and political grounds, Yugoslavia ceased to exist. The second was the pre-accession drive in the period between 1996 and 2004. This continued with entrance into the euro-zone as the first among the new EU Member states.

However, convergence was stopped in the third phase by a most difficult financial, economic and sovereign crisis. In response, major financial and economic governance reforms were implemented within the EU, and this also enabled Slovenia to continue its convergence path.

I contributed to the first two phases in different inside roles and observed the last part from my post as Member of the European Court of Auditors (ECA).

Independence Drive

The Slovene economic convergence towards the most advanced EU Member States started during the opening of ex-Yugoslavian economy in the late 1950s and 1960s and the push towards Slovene polycentric developments and tensions with the centralized powers in the early 1970s. Exports to the West, to the rest of the Yugoslav market and countries of COMECON, together making up more than 60% of Slovene GDP, were the basis of high economic growth.

However, the instruments utilized to support growth and the Yugoslav foreign debt crisis had both erupted by the end the 1970s. They were coupled in the 1980s with the lack of confidence and "quasi fiscal deficits" created by the central bank's monetization of commercial banking losses, resulting in increasingly higher inflation.

By 1989, reforms were taken over by a hyperinflationary environment and by December 1989, monthly inflation had reached above 50%. Similar to the Polish "Balcerowicz" reform, Yugoslavia issued the new dinar with a fixed exchange rate of 1 Deutsche Mark for 7 Yugoslav New Dinars. The new fixed exchange rate policy would have been disastrous for the Slovene export industry if macroeconomic balances had not been preserved. When, on July 1st 1990, the Federal Government decided to keep the fixed exchange rate, while lax monetary and fiscal policies were re-established, Slovenia had practically decided for economic independence.

Slovenia didn't want to be bound by the slow speed and wrong directions of the Yugoslav "convoy of republics". The leanest and fastest growing parts of ex-Yugoslavia demanded political independence to ensue quicker convergence.

With independence, Slovenia immediately lost the Yugoslav market - some 40% of GDP. However, the flexible exchange rate, sound fiscal policies and efficient Government that, together with the central bank, immediately undertook a rehabilitation of the banking sector were all conducive for export growth.

Second Phase – The Process towards EU Membership and Entrance into the EU

In the second phase of Slovene convergence, Slovenia had to fast forward economic, social and political reforms in order to catch up with the rest of the EU10. If, up to the mid-1990s, Slovenia had been nicknamed SLOWenia when compared to other CEE countries, reforms were now being pushed from the outside and adopted inside as part of the drive towards EU Membership. The grand coalition Government of Slovene ALDE members, the Liberal Democracy of Slovenia and Slovene EPP members and the Slovene People's Party was bound to undertake most of these efforts. They were led by teams of line ministries on all Chapters of the negotiations under the coordination of the EU minister for EU affairs.

I was, following my World Bank tenure, appointed as State Secretary for public finance issues at the Ministry of Finance during the period 1998-2000. With the help of the IMF fiscal department, we developed the legislation for budget preparations and implementation, internal and external audit issues, EU funds implementation, as well as public procurement and further local finance reforms.

Slovenia introduced the necessary tax reforms, such as the implementation of VAT and reformed tax administration. We prepared a new Public Finance Act, as well as a Decree on the Preparations of the Budget. Some twenty years later, with some minor modifications, they are still effectively used in the preparation and implementation of budgets. This, together with the Program for the adoption of the Euro, jointly prepared by the Bank of Slovenia and the Ministry of Finance (As explained in the parallel paper by Mr. Dušan Mramor.), enabled Slovenia's soft landing and adoption of the euro, the first country among the EU10.

In 2004, I was invited to join the Government as Minister for EU Affairs. This was an interesting convergence period: celebrations of the EU's "ever closer Union". I will never forget how, while driving on April 30th to the tri-state border between Slovenia, Austria and Italy, where we wanted to start the celebrations of that very day, I received an SMS. The Slovene manager had written: "Dear Milan, congratulations to Slovenia for entering the European Union. We, Slovene exporters and businessmen, have been there for the last four decades". This synthesised our pre-EU convergence.

In June 2004, the last round of negotiations on the EU Treaty were to be concluded. There, like-minded countries, all very much defined by a similar economic structure, quickly found a common ground for a compromise with the rest of the EU on how to ensure the chances for equal development, under the new EU Treaty motto of "Unity in Diversity". The Treaty was agreed on, signed in Rome in October later that year, but fell flat at the Dutch and French referendum. This was the first sign that convergence wasn't a default option.

My last ministerial task was to receive an invitation from the European Council – would Slovenia be willing to preside over the EU Council in 2008, as the first among the EU10. As the caretaking Government, we brought the news to the Parliament and to the new Coalition and the offer was accepted.

Financial Crisis and the New EU Governance

Slovenia, being a member of the EU and NATO, with convergence in place, should have found the years between 2004 and 2008 easy sailing. However, the new Government had changed the course of the Slovene ship. Instead of staying close to the shores of low foreign indebtedness and using the export industry as the driver of growth, the course had changed to the high seas of huge external borrowing and increasing imports. When the financial crisis hit the EU, Slovenia was not prepared for it.

It took five years, three Governments and major fiscal effort of some 15% of GDP to get out trouble. However, the Slovene efforts would not have been enough, without the unprecedented fiscal and structural reforms that changed EU financial and economic governance. They were designed to protect sovereign states from the banking sector crisis and enabled solutions to the Greek and Cyprus crises.

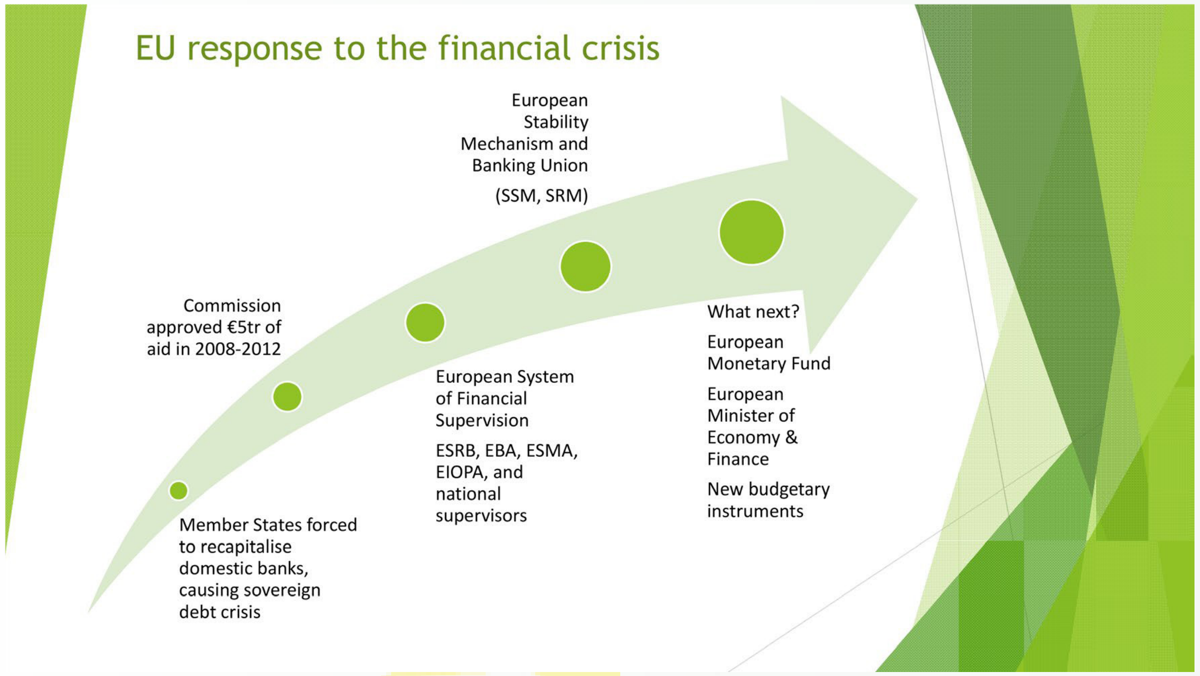
With entrance to the EU, Slovenia and the EU10, later the EU12 countries, hoped for a faster convergence to higher levels. These dreams were abruptly halted with the aftermath of the 2008 financial crisis. We all muddled through together, all the way up to the EU level efforts, that were ultimately strengthened in 2012 by the ECB's resolve and the creation of banking union.

I was appointed Member of the European Court of Auditors in May 2010, when measures to use the EFSM were undertaken and supported by the creation of EFSF by the euro area Member States. This was the predecessor of today's ESM instrumental to assure a "fiscal fall-back" recourse. I remember my first dinner with the European Commission (EC) in June 2010, when President Jose Manuel Barroso mentioned in his speech how the EC was pleased that MSs had undertaken the necessary efforts to resolve the crisis. And I said to my colleagues it would not be long before the ECA would be called to audit these new economic and financial tools.

As presented in Picture 1 below, the EU reacted to the crisis step by step. It couldn't immediately activate the arsenal of prudential regulation, supervisory measures, supported by fiscal resources (like in Canada or the USA) as it didn't have such structures and did not possess sufficient resources.

The initial funds to deal with the crisis were the Balance of Payment Assistance and the European Financial Stability Mechanism. They were linked to the EU budget and thus limited in amount. It was logical that later, in May 2010, the Member States would create a separate facility, which is today linked with the European Stability Mechanism, in which the ECA has a role to play.

Picture 1 – EU response to financial crisis 2008-16, Source ECA



The EU eventually put in place all elements of a banking union, first by establishing the European System of Financial supervision, with the ESRB, and then by establishing three financial authorities (EBA, ESMA and EIOPA). Later the ECB took on the role of the Single Supervisory Mechanism for the systemic banks. With all these, and the Single Resolution Mechanism and the Single Resolution Board, the EU should be able to contain the problem of a particular financial institution which is too big to fail for one sovereign state.

By 2016 at the ECA, we had carried out some very important audits on how the European institutions and the Member States have reacted to the crisis. As our first economic and financial governance audit, I presented the report on EBA and later the audit on the excessive deficit procedure. Both highlight what still needs to be improved in the areas of prudential regulation and preventive arm of Stability and Growth pact, respectively. As was well described in the earlier ECA report on the financial assistance to countries in difficulty before 2008, the economic governance mechanisms at the EU level were not effective enough. For macroeconomists, the lack of funds and a lack of the coordination of fiscal policy had not yet proved the eurozone to be an optimum currency area.

On the fiscal front, the EU has also developed new initiatives that will further improve the economic governance of the EU: alongside the European Semester and the MIP procedure, the advisory European Fiscal Board, and a system of national competitiveness boards have been set up. New initiatives need to respect that there are sovereign Member States and there are European institutions and we have a common currency to be protected with sound policies. That is, in essence, what we found in the excessive deficit procedure audit. Both sides need to be respected. We need more transparency and consistency. A debate about the further fiscal policy coordination of the

Member States is simply needed for the euro zone and EU MSs to further converge.

Concluding Remarks

Over the last 30 years, starting with the Slovene Spring in 1988-89, there have been efforts to undertake first, independence, and second (in order to ensure independence), to undertake the accession efforts to become a Member of the EU. We hoped that we would land in an economically ever-progressive group of nations. The financial, economic and sovereign crisis showed us that convergence is not a default option. Nevertheless, Slovenia, also with the help of the EU and by the presence on EU and global markets, has relatively successfully managed its economic development over the last three decades. I am proud to be part of these endeavours.