Hermine Vidovic

Slovenia: fundamental changes ahead

Driven by both domestic demand and an upswing in foreign demand, GDP grew by 3.8% in 2005, at a slightly lower rate than a year earlier. Domestic demand was mainly supported by rising private consumption backed by increased household lending. Investment growth decelerated to about 2%, from 6% in 2004, caused by a decline in machinery and equipment investments. Construction activities recovered from month to month, particularly those pertaining to buildings. The disinflation process continued, with consumer price inflation averaging 2.5% in 2005.

Industrial output growth gained momentum from the second quarter of the year and was up by about 3% in 2005. However, this increase was the result of methodological changes in data compilation starting from July rather than an 'actual' improvement. Capital goods production increased most (8%), while the production of intermediate and consumer goods performed below average. Output growth of manufacturing exceeded the average industrial growth, with the most outstanding result reported for the manufacture of transport equipment – car production (19%). On the negative side, the country's textile industry continued its downward trend with production contracting by another 10% in 2005.

Foreign trade developed dynamically in 2005, with exports and imports expanding by 12% and 10% respectively, resulting in a cut of the trade deficit compared to 2004. Detailed data obtained from the customs statistics for the period January to October point to an above-average export increase to the EU, particularly to France, where Slovenia exported 50% more than in the same period a year earlier. Slovenia's main export item to France are cars produced by the Revoz factory in Novo mesto. In contrast to the past few years when Slovenia recorded a remarkable expansion of exports to the successor states of the former Yugoslavia, deliveries to this area grew below average in 2005, with even declining exports to Bosnia and Herzegovina and Macedonia. The current account improved as against 2004 when the deficit to GDP ratio had posted an all time high (-2.1%) since the country's independence. In 2005 the deficit fell to some EUR 200 million or 0.7% of the GDP, which was mainly made possible through the reduction of the trade deficit and increasing net revenues from services, particularly from travel and transport. As in 2003, Slovenia was again a net exporter of FDI in 2005: the outflow of FDI was mainly targeting the successor states of the former Yugoslavia, but also Bulgaria and Romania, e.g. in banking (Nova Ljubljanska Banka) or retail trade. According to the Bank of Slovenia, in 2004 the highest Slovenian outward FDI stock was registered in Croatia, followed by Serbia and Montenegro, the Netherlands and Bosnia and Herzegovina.

Despite sizable GDP growth, the impact on employment remained weak. Overall, the number of employed rose by less than 1%, with a further decline in agriculture and manufacturing but an increase in the construction and services sector employment. Unemployment, at 6.3% according to the labour force survey and 10.3% based on registration data, remained unchanged as compared to a year earlier.

By mid-December the Slovenian parliament passed the (state) budgets for 2006 and 2007, envisaging budget deficits of 1.4% and 1.2% respectively of the estimated GDP (the respective values for the general government deficits are 1.7% and 1.4%, slightly lower than the EU forecasts). Altogether, Slovenia meets the Maastricht criteria for long-term interest rates, the fiscal deficit and the public debt to GDP ratio. Since the entry of the Slovenian tolar into the ERM II as of the end of June 2004, the exchange rate of the tolar against the euro has remained close to the central band.

In contrast to former governments that pursued a gradualist approach in implementing economic reforms, Slovenia's new centre-right government – in office since December 2004 – has come up with a package of radical reform measures. The centrepiece is a 20% flat tax to be introduced after Slovenia's admission to the euro zone in 2007; in addition, significant cuts in the social benefit system are envisaged. The privatization of state-owned enterprises and banks should be speeded up: proposals for the privatization of Nova Ljubljanska Banka (the country's biggest bank) and Nova Kreditna Banka Maribor, the privatization of telco, the Slovenian Telecom company, and the energy sector have already been submitted to the government. The privatization programme for the Slovenian Steel Group was adopted in late December, envisaging a reduction of the state's stake in the group to 25% plus one share over the next two years. The group, consisting of six steel producers, is intended to be sold as a whole and not piece by piece as foreseen in the original privatization programme. In addition, the government plans to sell all its minority stakes that it holds in Slovenian companies by the end of 2007.

Some of the intended measures, particularly the introduction of the flat tax and the cuts in social welfare, come with some surprise as similar measures have so far been implemented only in less developed CEE countries facing severe economic problems at the outset of reforms. Within the country the announced reforms meet with strong opposition from trade unions, pensioners and students as well as some opposition parties.

In order to coordinate the implementation of the announced reforms (formulated in Slovenia's Development Strategy) a Reform Coordination Office was established at the beginning of January 2006, headed by Jože Damijan, an economist and minister without portfolio. The main objectives of the office's activities are to enhance economic competitiveness, raise economic growth and curb unemployment, while maintaining social security. The office is divided into two divisions: on economic and on social reforms.

The general outlook for the next two years is favourable. GDP growth rates at close to 4% will be backed by both domestic and foreign demand. Taking into account the Slovenian authorities' declared intention to fulfil and maintain the Maastricht criteria, the introduction of the euro at the beginning of 2007 is realistic and feasible. A further lowering of inflation may be jeopardized by increasing oil prices. The situation in mid-2006 will be crucial for assessing Slovenia's readiness for the adoption of the euro.

Table SI

Slovenia: Selected Economic Indicators

	1999	2000	2001	2002	2003	2004	2005 [1]	2006	2007
								forecast	
Population, th pers., mid-year	1985.6	1990.3	1992.0	1995.7	1996.8	1997.0	2001.1	.	.
Gross domestic product, SIT bn, nom. [2]	3919.0	4300.4	4799.6	5355.4	5813.5	6251.2	6650	7080	7530
annual change in % (real) [2]	5.4	4.1	2.7	3.5	2.7	4.2	3.8	3.9	3.9
GDP/capita (EUR at exchange rate) [2]	10194	10538	11094	11862	12458	13105	13870	.	.
GDP/capita (EUR at PPP - wiiw) [2]	13870	14640	15400	16040	16510	17930	18900	.	.
Gross industrial production									
annual change in % (real) [3]	-0.5	6.2	2.9	2.4	1.4	4.8	2.8	2.5	2
Gross agricultural production									
annual change in % (real)	-1.7	1.0	-4.3	13.4	-12.7	19.3	.	.	.
Construction output, in effect. working time									
annual change in % (real) [4]	10.2	-1.2	-2.1	-3.4	-1.7	2.5	2.1 I-XI	.	.
Consumption of households, SIT bn,nom. [2]	2225.6	2415.1	2657.8	2903.4	3167.4	3386.2	.	.	.
annual change in % (real) [2]	6.0	0.7	2.3	1.3	3.5	3.3	3.5	3	3
Gross fixed capital form., SIT bn, nom. [2]	1033.2	1098.9	1158.7	1211.5	1353.1	1506.0	.	.	.
annual change in % (real) [2]	18.2	1.8	0.4	0.9	7.1	5.9	2.0	3	3.5
LFS - employed persons, th, avg.	886	901	916	910	897	943	950	.	.
annual change in %	-1.7	1.7	1.7	-0.7	-1.4	5.1	0.7	.	.
Reg. employees in industry, th pers., avg. [5]	242.8	241.6	243.5	246.1	242.2	239.7	240.0 I-IX	.	.
annual change in %	-1.4	-0.5	0.8	1.1	-1.6	-1.0	.	.	.
LFS - unemployed, th pers., average	73.0	68.0	63.0	62.0	64.8	64.0	65	.	.
LFS - unemployment rate in %, average	7.6	7.0	6.4	6.4	6.7	6.3	6.3	6	5.8
Reg. unemployment rate in %, end of period	13.0	12.0	11.8	11.3	11.0	10.4	10.4	10	9.5
Average gross monthly wages, SIT [6]	173245	191669	214561	235436	253200	284281	276073 I-XI	.	.
annual change in % (real, net) [6]	3.0	1.4	3.1	2.1	1.8	2.1	4.1 I-XI	.	.
Consumer prices, % p.a.	6.1	8.9	8.4	7.5	5.6	3.6	2.5	2.4	2.3
Producer prices in industry, % p.a.	2.1	7.6	8.9	5.1	2.5	4.3	2.7	2.5	2.4
General governm.budget, EU-def., % GDP [7]									
Revenues	.	44.7	45.1	45.7	45.8	45.8	45.4	.	.
Expenditures	.	48.2	49.0	48.4	48.5	47.9	47.2	.	.
Deficit (-) / surplus (+), % GDP	.	-3.5	-3.9	-2.7	-2.7	-2.1	-1.7	-1.9	-1.6
Public debt in % of GDP [7]	24.9	27.4	28.4	29.8	29.4	29.8	29.3	29.5	29.2
Discount rate % p.a., end of period [8]	8.0	10.0	7.8	7.3	5.0	3.3	3.8	.	.
Current account, EUR mn	-664.2	-583.0	38.0	343.8	-81.2	-543.7	-200	-200	-100
Current account in % of GDP	-3.3	-2.8	0.2	1.5	-0.3	-2.1	-0.7	-0.7	-0.3
Gross reserves of NB excl. gold, EUR mn	3159.2	3435.8	4907.5	6701.5	6798.2	6464.0	6824.1	.	.
Gross external debt, EUR mn	8012	9490	10403	11484	13259	15278	18926 XI	.	.
FDI inflow, EUR mn	99.2	149.1	412.4	1700.2	300.3	662.1	270	.	.
FDI outflow, EUR mn	44.7	71.7	161.2	162.1	418.0	441.5	460	.	.
Exports of goods, BOP, EUR mn	8103.2	9574.2	10454.3	11081.6	11417.1	12932.8	14470	15700	16900
annual growth rate in %	0.2	18.2	9.2	6.0	3.0	13.3	12	9	8
Imports of goods, BOP, EUR mn	9267.3	10801.2	11138.7	11346.6	11959.9	13941.6	15390	16800	18300
annual growth rate in %	5.4	16.6	3.1	1.9	5.4	16.6	10	9	9
Exports of services, BOP, EUR mn	1763.5	2051.5	2177.6	2440.0	2464.8	2782.2	3200	.	.
annual growth rate in %	-2.3	16.3	6.1	12.0	1.0	12.9	15	.	.
Imports of services, BOP, EUR mn	1434.0	1562.3	1642.1	1819.9	1924.0	2096.2	2320	.	.
annual growth rate in %	5.7	8.9	5.1	10.8	5.7	9.0	11	.	.
Average exchange rate SIT/USD	181.77	222.68	242.75	240.24	207.11	192.38	192.70	.	.
Average exchange rate SIT/EUR (ECU)	193.63	205.03	217.19	226.22	233.70	238.86	239.64	239.9	240
Purchasing power parity SIT/USD	124.63	129.94	136.39	144.24	150.37	149.15	.	.	.
Purchasing power parity SIT/EUR	142.35	147.57	156.42	167.32	176.31	174.64	.	.	.

Notes: 1) Preliminary. - 2) Revised data (FISIM adjustment and previous year price introduction). - 3) From July 2005 new methodology. - 4) From 2004 construction put in place; units with at least 20 employees. - 5) From January 2005 data from Statistical Register of Employment, years before from Monthly Report on Earnings. - 6) From January 2005 legal persons with 1 or 2 employees in private sector are included. - 7) According to ESA'95, excessive deficit procedure. - 8) From 2001 main refinancing rate.

Source: wiiw Database incorporating national statistics; AMECO Database; wiiw forecasts.