



## SLOVENIA: Unexpectedly high GDP growth

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**Increased foreign demand and rising investments supported by EU funds helped Slovenia to return to a growth path, at least temporarily, after the crisis. GDP growth in 2014 could come close to 2%, but will weaken again in the two years thereafter on account of dwindling investment activities and subdued economic growth being registered by its main trading partners. The newly elected government will have to continue its fiscal consolidation policy, including speeding up privatisation. Company deleveraging will also continue in the foreseeable future and remain an impediment to growth.**

The economic recovery starting in the last quarter of 2013 continued in 2014. Slovenia's GDP grew by an unexpected 2.5% in the first half of the year, backed primarily by foreign demand and an upswing in gross fixed capital formation (rising by close to 5%). Household consumption remained nearly stagnant, while government consumption continued to fall for the fourth consecutive year. Also the change in inventories contributed negatively to GDP growth. Rising investment translated first of all into a remarkably strong increase in construction activities, municipal infrastructure in particular, co-financed by EU funds at the end of the financial perspective. By contrast, investment in machinery and equipment dropped by 13%. Industrial production recovered after two years of contraction, largely on account of low- and medium-technology industries, while high-tech industries remained slow in picking up again. The labour market situation has somewhat improved: based on Labour Force Survey data, employment increased by 2% in the first half of 2014 (year-on-year), which is mainly due to rising employment of temporary workers; the unemployment rate stood at 10%, slightly lower than in the first half of 2013. In September the consumer confidence indicator reached the highest level since 2008, which was due to a more optimistic outlook on unemployment, the improved financial situation of households and heightened expectations concerning the general economic situation over the next 12 months.

In foreign trade, goods exports rose by 5% and imports by 3% in the first half of 2014, resulting in a significantly higher trade surplus than in the same period of 2013. By contrast, the surplus in services trade fell owing to modest exports growth (1.5%) and rapidly rising imports (14%) particularly in business and technical services and construction services. Also the deficit in factor income has increased because of higher net interest payments on general government debt and debt repayments by the private sector. On the other hand, the net inflow of income from labour increased, because of a rising number of labour migrants abroad. Overall, the current account closed with a surplus of EUR 970 million in the first half of 2014, which was by EUR 140 million less than in the corresponding 2013 period.

After years of dragging inflows, FDI gained momentum in 2014 owing primarily to the sale of state-owned companies to Austrian and Croatian investors.<sup>1</sup> As for the whole year, the inflow of FDI is expected to rise to EUR 1 billion due to further privatisations. Slovenia's gross foreign debt amounted to EUR 44 billion by the end of June and was by EUR 4.1 billion higher than at the end of 2013. This increase is mainly attributable to government borrowing by selling bonds. Debts of the Bank of Slovenia to the eurosystem and private sector debt decreased.

Thanks to the improved economic situation, growth in general government revenues outpaced growth of expenditures in the first seven months of 2014, resulting in a lowering of the general government deficit. Revenues improved in all categories (taxes and a one-off inflow from concession fees for the mobile telephony radio spectrum), while expenditures rose mainly due to increased interest payments and rising investment outlays. However, despite the reduction, the target deficit for this year has already been exceeded. As a consequence the Minister of Finance announced the adoption of a supplementary budget (spending cuts across several ministries) in the autumn months as well as amendments to the 2015 budget which should be approved at the beginning of 2015. After having injected EUR 3.3 billion in the ailing banking sector in late 2013, the yield on ten-year government bonds fell significantly, from 6.8% in autumn 2013 to 2.7% by the end of September 2014.

At the beginning of May this year Slovenia's Prime Minister Alenka Bratusek resigned after losing the leadership of her party 'Positive Slovenia' to the mayor of Ljubljana, Zoran Jankovic. Early elections were held on 13 July and a new coalition government consisting of the newly founded party SMC of Miro Cerar (a lawyer), the Pensioners Party DeSUS and the Social Democrats took office in mid-September. Most of the new ministers from the SMC party are political newcomers, the only exception being the new Minister of Finance, Dusan Mramor (a professor of economics) who served already as a finance minister between 2002 and 2004. The coalition agreement stipulates that the new government will 'strive to take Slovenia out of the political, social, economic and ethical crisis by securing economic growth, protecting existing jobs and creating new jobs'. Prime Minister Cerar announced that the newly elected government aims to cut the budget deficit from an expected 4.2% of the GDP this year to 3% in 2015 as agreed with the European Commission. Fiscal policy will remain restrictive, public spending is to be reduced and the efficiency of tax collection should be increased. Reforms of the health and pension systems are envisaged as well. Plans for the introduction of a real estate tax were dropped (the attempt to introduce such a tax was rejected by the constitutional court at the beginning of the year). Despite some initial resistance from coalition parties, the privatisation of state-owned enterprises will be continued as planned by the outgoing government. The prime minister announced to draw up a list of additional companies to be sold.

Out of the 15 enterprises earmarked for privatisation in 2013, the coatings maker Helios, the laser producer Fotona and recently also a 75.5% stake in the airport operator Aerodrom Ljubljana have been sold. The latter went to the German airport operator Fraport. In mid-September the privatisation of a 51.1% stake in Žito, one of Slovenia's biggest food companies, has been officially launched. The privatisation process of the biggest company, Telekom Slovenije, which was put on hold prior to the formation of the new government, should be continued and completed by the beginning of 2015. The government expects to receive some EUR 700 million from the sale of the telecom company. Deutsche Telekom and Turkcell were mentioned repeatedly as potential investors.

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<sup>1</sup> The Austrian Ring International Holding (RIH) took over the majority of the coating maker Helios in April. Regarding the Croatian investment, part of Agrokor's payment for Mercator was made in the first half of 2014.

Deleveraging of Slovenia's highly indebted companies continued in 2014 at the same pace as in 2013, while household and government deleveraging slowed down. In the first seven months of 2014 loans to the domestic non-banking sector declined by about 15% as compared to the same period a year earlier. It is expected that company deleveraging will continue also in the foreseeable future and remain an impediment to growth.

Based on available results for the first half of 2014, wiiw has revised the forecast for Slovenia's GDP growth for 2014 from minus 0.5% (March forecast) to plus 1.8%, backed by rising exports and stronger than expected investment. The foreign trade performance suggests that the current account will remain in positive territory in 2014 and probably also in 2015. GDP growth will continue in 2015 and 2016, but at a slower pace than in 2014 due to a weakening of investment activities, and it will very much depend on a further rise in exports. Household demand is bound to start slowly recovering due to an improvement of the labour market situation along with growing GDP. Uncertainties remain regarding the policy that will be pursued by the (politically highly inexperienced) new government.

**Table 1 / Slovenia: Selected Economic Indicators**

	2010	2011	2012	2013 <sup>1)</sup>	2013 January-June	2014	2014 Forecast	2015 Forecast	2016
Population, th pers., average <sup>2)</sup>	2,049	2,053	2,057	2,060	2,059	2,061	2,058	2,058	2,058
Gross domestic product, EUR mn, nom. <sup>3)</sup>	36,220	36,868	36,006	36,144	17,568	18,154	37,050	37,980	38,940
annual change in % (real) <sup>3)</sup>	1.2	0.6	-2.6	-1.0	-2.9	2.5	1.8	1.5	1.5
GDP/capita (EUR at exchange rate)	17,700	18,000	17,500	17,500	.	.	18,000	18,500	18,900
GDP/capita (EUR at PPP)	21,000	21,600	21,800	21,800	.	.	.	.	.
Consumption of households, EUR mn, nom. <sup>3)</sup>	19,960	20,299	19,981	19,301	9,254	9,366	.	.	.
annual change in % (real) <sup>3)</sup>	1.0	0.0	-2.9	-4.0	-4.9	0.6	0.4	0.8	1.0
Gross fixed capital form., EUR mn, nom. <sup>3)</sup>	7,694	7,445	6,927	7,127	3,451	3,632	.	.	.
annual change in % (real) <sup>3)</sup>	-13.7	-4.6	-8.9	1.9	-0.5	4.9	4.5	2.5	2.0
Gross industrial production									
annual change in % (real)	7.2	1.3	-1.1	-0.9	-2.1	3.5	3.0	2.5	3.0
Gross agricultural production									
annual change in % (real)	0.1	0.3	-10.5	-4.0	.	.	.	.	.
Construction industry <sup>4)</sup>									
annual change in % (real)	-16.9	-24.9	-16.9	-2.4	-16.7	37.6	.	.	.
Employed persons, LFS, th, average	966	936	924	906	896	914	920	930	940
annual change in %	-1.5	-3.1	-1.3	-1.9	-3.0	2.0	2.0	1.0	1.0
Unemployed persons, LFS, th, average	75	83	90	102	107	102	.	.	.
Unemployment rate, LFS, in %, average	7.3	8.2	8.9	10.1	10.8	10.1	10.0	9.8	9.6
Reg. unemployment rate, in %, end of period	11.8	12.1	13.0	13.5	12.8	12.8	13.2	13.0	12.9
Average monthly gross wages, EUR	1,495	1,525	1,525	1,523	1,513	1,528	.	.	.
annual change in % (real, gross)	2.1	0.2	-2.4	-2.0	-2.9	0.3	.	.	.
Average monthly net wages, EUR	967	987	991	997	991	999	.	.	.
annual change in % (real, net)	2.1	0.3	-2.1	-1.2	-2.1	0.1	.	.	.
Consumer prices (HICP), % p.a.	2.1	2.1	2.8	1.9	2.2	0.7	0.7	1.0	1.0
Producer prices in industry, % p.a.	2.0	4.6	0.9	0.0	0.5	-1.0	0.0	0.5	1.0
General governm.budget, EU-def., % of GDP									
Revenues	42.7	42.7	43.5	43.6	.	.	.	.	.
Expenditures	48.5	48.9	47.5	58.0	.	.	.	.	.
Net lending (+) / net borrowing (-)	-5.7	-6.3	-3.9	-14.4	.	.	-5.0	-4.0	-3.5
Public debt, EU-def., % of GDP	37.9	46.2	53.3	70.0	.	.	82.0	84.0	85.0
Central bank policy rate, % p.a., end of period <sup>5)</sup>	1.00	1.00	0.75	0.25	0.50	0.15	.	.	.
Current account, EUR mn	-50	145	1,026	2,102	1,106	969	1,950	1,800	1,700
Current account, % of GDP	-0.1	0.4	2.8	5.8	6.3	5.3	5.3	4.7	4.4
Exports of goods, BOP, EUR mn	18,973	21,450	21,630	22,025	11,003	11,575	23,100	24,400	25,900
annual change in %	14.4	13.1	0.8	1.8	0.7	5.2	5.0	5.5	6.0
Imports of goods, BOP, EUR mn	19,803	22,406	21,802	21,380	10,632	10,938	22,000	23,100	24,700
annual change in %	16.3	13.1	-2.7	-1.9	-4.9	2.9	3.0	5.0	7.0
Exports of services, BOP, EUR mn	4,593	4,842	5,081	5,367	2,512	2,548	5,500	5,800	6,100
annual change in %	6.0	5.4	4.9	5.6	8.5	1.5	2.0	6.0	6.0
Imports of services, BOP, EUR mn	3,313	3,366	3,360	3,406	1,489	1,702	3,800	4,200	4,500
annual change in %	4.5	1.6	-0.2	1.4	-0.1	14.3	13.0	10.0	7.0
FDI inflow (liabilities), EUR mn	272	718	-59	-786	-843	668	1,000	.	.
FDI outflow (assets), EUR mn	-156	84	-226	-187	-93	78	.	.	.
Gross reserves of NB excl. gold, EUR mn	695	642	593	580	552	767	.	.	.
Gross external debt, EUR mn	40,723	40,100	41,264	39,930	40,867	44,004	.	.	.
Gross external debt, % of GDP	112.4	108.8	114.6	110.5	113.1	118.8	.	.	.
Purchasing power parity EUR/EUR	0.8412	0.8315	0.8030	0.8056	.	.	.	.	.

1) Preliminary. - 2) From 2011 according to register-based census 2011. - 3) According to ESA'10. - 4) Enterprises with 20 and more employees and output of some non-construction enterprises. - 5) Official refinancing operation rates for euro area (ECB).

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