

17. SLOVENIA

Growth cooling down but remaining robust

Economic growth in Slovenia slowed down in the first half of 2019 on the back of weakening foreign demand, and it is expected to remain broadly stable over the forecast horizon. Domestic demand is expected to remain strong. Inflation is projected to increase slightly in 2020 and 2021. The government budget balance is forecast to remain in surplus, with a slightly improving structural balance position in the coming years.

Slowdown in the first half of 2019

In the first half of 2019, Slovenia's economy grew by 3.0% compared to the first half of 2018 (or 0.9% compared to the previous six months). This compares with a (revised) growth of 4.1% in 2018. Domestic demand growth was driven by investment spending, while private consumption grew somewhat slower. Residential construction grew at a strong pace (13.8%) while investment in machinery and equipment grew more modestly (3.6% on half year-on-half year). Exports grew by 8.6%, slightly below import growth, which stood at 9.9%.

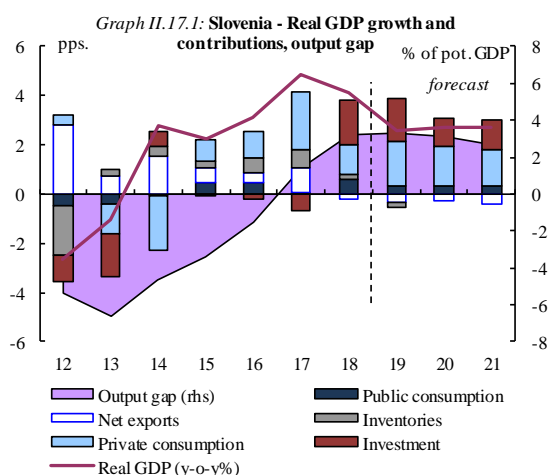
Economic sentiment worsened over the first nine months of 2019. Taking into account the slowdown in Slovenia's main export markets, economic growth in the second half of the year is projected to lose further momentum. Real GDP growth is now forecast to fall to 2.6% in 2019, compared to 3.1% in the spring forecast.

Growth expectations lower for 2020 and 2021

GDP growth is forecast to average 2.7% in both 2020 and 2021. Growth is expected to continue to be driven by domestic demand, with a negative contribution from net exports over the forecast horizon. Domestic demand is expected to be supported by continued increases in employment and wages, as well as favourable bank lending conditions. Investment growth is projected to continue at around the same pace as this year, mainly driven by construction investment. Housing prices have risen rapidly and supply has been constrained so far, further supporting the expected pick-up in housing construction. In the public sector, the uptake of EU funds is forecast to increase further as the programming period draws to a close.

While export growth was boosted by one-off factors in 2019, it is expected to be significantly lower in 2020 and 2021, at 4.9% and 4.6%, respectively. This lower growth path is explained

by lower demand from export markets, while Slovenia's price competitiveness is expected to remain strong with labour cost growth relatively moderate compared to its trading partners. Imports are expected to continue growing more quickly than exports. Slovenia's current account surplus is projected to decline to 5.1% of GDP in 2021 after reaching 5.8% in 2019.



Negative risks to the growth mainly stem from the external outlook. A sharper-than-expected slowdown in export demand growth would not only affect exports but also business investment. On the upside, household consumption could increase faster than currently projected as the saving rate remains high.

Labour market still strong

In 2019, employment is expected to grow by 2.3% and to slow down somewhat over the forecast period. An inflow of foreign workers and a rising participation rate should help alleviate labour supply constraints to some extent. The unemployment rate is projected to fall to 4.4% in 2019 and to stabilise at 4.2% in the following years. Growth of compensation per employee is expected to average 3.6% over the forecast horizon.

At 1.8%, HICP inflation is projected to be lower in 2019 than it was in 2018, mainly due to the slowdown in energy and food price inflation. Inflation is expected to modestly increase – to 1.9% in 2020 and 2.0% in 2021.

General government budget remains in surplus

In 2018, Slovenia's general government surplus increased to 0.8% of GDP from a balanced budget in 2017, driven by particularly strong revenue growth. A widening positive output gap led to a small deterioration in the structural deficit to about 2/3% of GDP. Over the forecast horizon, the headline surplus is expected to be at around 0.5% of GDP, while the structural deficit is projected to deteriorate in 2019 and to gradually improve thereafter.

In 2019, tax revenues are expected to grow more slowly than in the year before due to weaker domestic demand growth and a tax exemption on the annual holiday allowance. Expenditure is expected to grow faster than revenues. Next to the significant public sector pay rise negotiated with labour unions at the end of 2018, social transfers are forecast to be among the main drivers of expenditure growth. Public investment is also

projected to increase, although at a lower pace than in 2018.

In 2020, tax revenue growth is forecast to remain moderate, due to changes adopted to reduce the tax burden on labour. Higher social transfers, further public sector pay rises and higher absorption of EU funds will drive expenditure growth. In 2021, somewhat strengthening private consumption and higher wages should continue to support the surplus.

The downside risks to public finances stem from expenditure pressures, particularly on wages and social benefits, and the possibility of unexpected one-offs due to unfavourable court rulings. Lower-than-projected economic growth could put downward pressure on revenues.

Slovenia's debt-to-GDP ratio has been on a declining path since its peak at 82.6% in 2015. Supported by the low interest rate environment, active public debt management, the general government surplus and privatisation proceeds, the ratio is expected to decrease significantly from 70.4% in 2018 to 63.1% in 2020 and to fall below the 60% threshold in 2021.

Table II.17.1:

Main features of country forecast - SLOVENIA

	2018			Annual percentage change						
	bn EUR	Curr. prices	% GDP	00-15	2016	2017	2018	2019	2020	2021
GDP	45.8	100.0		2.0	3.1	4.8	4.1	2.6	2.7	2.7
Private Consumption	23.9	52.3		1.6	4.4	2.3	3.4	3.0	2.9	3.0
Public Consumption	8.4	18.3		1.8	2.5	0.3	3.2	2.0	1.9	1.8
Gross fixed capital formation	8.8	19.2		-0.3	-3.7	10.4	9.4	6.1	6.0	5.9
of which: equipment	3.8	8.2		1.4	7.4	12.5	10.7	2.5	2.1	2.1
Exports (goods and services)	39.1	85.4		6.1	6.5	10.8	6.6	7.9	4.9	4.6
Imports (goods and services)	35.3	77.1		4.6	6.7	10.7	7.7	9.2	5.8	5.5
GNI (GDP deflator)	45.0	98.4		1.9	3.7	5.6	4.4	2.9	3.0	2.9
Contribution to GDP growth:		Domestic demand		1.2	2.1	3.1	4.1	3.1	3.0	3.1
		Inventories		0.0	0.6	0.7	0.2	-0.2	0.0	0.0
		Net exports		0.9	0.4	1.0	-0.2	-0.3	-0.3	-0.4
Employment				0.3	1.8	3.0	3.2	2.3	1.5	1.3
Unemployment rate (a)				7.1	8.0	6.6	5.1	4.4	4.2	4.2
Compensation of employees / head				4.9	3.1	3.0	3.9	3.6	3.6	3.6
Unit labour costs whole economy				3.1	1.8	1.2	3.0	3.3	2.4	2.2
Real unit labour cost				0.0	1.1	-0.4	0.7	0.7	0.0	-0.2
Saving rate of households (b)				13.1	11.5	12.4	12.6	13.7	14.2	14.0
GDP deflator				3.1	0.8	1.6	2.2	2.7	2.4	2.3
Harmonised index of consumer prices				3.6	-0.2	1.6	1.9	1.8	1.9	2.0
Terms of trade goods				-0.4	0.8	-0.6	-0.1	0.4	0.0	-0.1
Trade balance (goods) (c)				-2.0	3.8	3.7	2.5	1.8	1.0	0.1
Current-account balance (c)				-1.0	4.9	6.3	5.8	5.8	5.5	5.1
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-0.8	4.1	5.4	5.3	5.3	5.0	4.6
General government balance (c)				-4.0	-1.9	0.0	0.8	0.5	0.5	0.6
Cyclically-adjusted budget balance (d)				-3.7	-1.2	-0.7	-0.7	-1.0	-1.0	-0.7
Structural budget balance (d)				-	-1.1	-0.6	-0.7	-1.0	-0.9	-0.7
General government gross debt (c)				39.7	78.7	74.1	70.4	66.7	63.1	59.5

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.