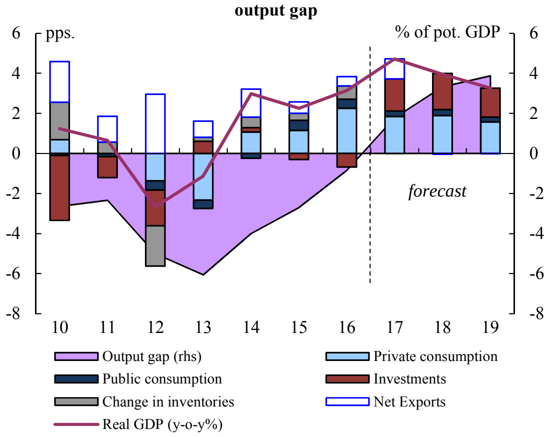
24. SLOVENIA
Broad-based expansion

Economic growth reached 3.1% in 2016 and has further accelerated in 2017, driven by exports, private consumption and investment. The economic expansion has been accompanied by rising employment and wage growth. Companies have continued to invest to meet growing demand from both domestic and international markets. Public finances are projected to continue to improve, reflecting the favourable macroeconomic outlook.

Solid growth in the first half of 2017

Slovenia's economy continued to grow at a strong pace in the first half of 2017, as real GDP increased by 4.8%, surpassing its pre-crisis peak. Domestic demand continued to expand. Investment increased by 10% in the first half of 2017, driven by a rebound in public investment, supported by the start of the new EU financing cycle. At the same time, private consumption grew by 3.4%, boosted by growing disposable income and upbeat consumer confidence. Export growth remained strong and outpaced import growth, further contributing to the current account surplus. Solid growth is set to continue in the second half of the year, leading to a real GDP increase of 4.7% in 2017.

Graph II.24.1: **Slovenia - Real GDP growth and contributions, output gap**



Expansion to continue in 2018 and 2019

Real GDP growth is forecast to reach 4% in 2018 and 3.3% in 2019, driven mainly by domestic demand. Private consumption is expected to remain strong over the forecast horizon, supported by growing employment, wages and bank lending. Similarly, investment is expected to grow at a high rate due to the combination of strong external and domestic demand with improving financing conditions and stronger corporate balance sheets. High growth in industrial production, very high capacity utilisation in the export sector, and growing export markets are creating room for further investment in production capacity. At the same time, demand for construction work is gradually strengthening and growth in construction investment is expected to accelerate. In addition, the improved take-up of EU funds is set to boost investment further in 2018 and 2019. Export performance is expected to remain robust, supported by stable unit labour costs and continued gains in price competitiveness. Imports are forecast to grow in line with domestic demand, gradually neutralising the growth contribution of net exports. Slovenia's current account surplus is expected to decrease moderately in both 2018 and 2019.

Risks to the growth outlook are tilted to the upside. These are primarily domestic in nature, as improving sentiment and better access to credit could further support investment, particularly in residential properties. Downside risks are mainly external and relate to the future development of energy and raw material prices.

Inflation set to remain moderate while wage growth accelerates

Employment growth remains high in most sectors as increasing exports, consumption and investment boost labour demand in the economy. Employment is expected to continue to grow by 1%-2% over the forecast horizon, but decelerate as labour shortages increase in the tightening labour market. As a result, the unemployment rate is expected to decline from 8% in 2016 to 5.2% in 2019. As the forecast unemployment rate approaches its natural rate, wage pressures are set to rise. Compensation per employee is expected to grow by 2.8% in 2017 and by around 3.2% in 2018 and 2019.

HICP inflation accelerated towards 2% (y-o-y) in the first quarter of 2017 but slowed thereafter, largely driven by base effects. Overall, consumer prices are projected to increase by 1.6% in 2017. Both headline and core inflation are expected to remain moderate over the forecast horizon. HICP inflation is forecast to reach 1.5% in 2018 and 1.8% in 2019.

General government balance continues to improve

In 2016, the general government deficit decreased to 1.9% of GDP from 2.9% in 2015, mainly due to higher revenues and a drop in public investment linked to the ending of the previous EU funding period.

In 2017, the government deficit is expected to decline to 0.8% of GDP as a result of strong tax revenues and social contributions. Public investment is expected to increase after a plunge of nearly 30% in 2016. Both the compensation of public employees and pensions are expected to continue rising.

In 2018, the general government balance is expected to be 0.0% of GDP as tax revenues and social contributions continue to grow strongly and interest expenditure is expected to decrease significantly. At the same time, the compensation of public employees and expenditure on social benefits are projected to increase further due to wage increases and an extraordinary indexation of pensions. Public investment is expected to grow in line with the dynamics of the current EU multiannual financial framework. Under a no-policy-change assumption, the general government balance is expected to record a surplus of 0.4% of GDP in 2019, mainly due to economic growth and improved labour market conditions.

The main downside risks to public finances over the forecast horizon stem from building expenditure pressures, particularly on wages and pensions.

In structural terms, Slovenia's fiscal position is expected to be broadly unchanged between 2016 and 2018 and improve slightly in 2019. This takes place in a context where the output gap is projected to turn positive in 2017 and increase strongly thereafter.

The debt-to-GDP ratio peaked at 82.6% in 2015, but started to decrease in 2016 to 78.5% of GDP. Supported by the economic recovery and reduced precautionary cash buffers, public debt is forecast to decline steadily to 72.0% in 2019.

Table II.24.1:

Main features of country forecast - SLOVENIA

		2016		Annual percentage change						
		bn EUR Curr. prices	% GDP	98-13	2014	2015	2016	2017	2018	2019
GDP		40.4	100.0	2.2	3.0	2.3	3.1	**4.7**	**4.0**	**3.3**
Private Consumption		21.6	53.4	1.8	1.9	2.1	4.2	**3.4**	**3.6**	**3.0**
Public Consumption		7.6	18.7	2.0	-1.2	2.7	2.5	**1.5**	**1.6**	**1.3**
Gross fixed capital formation		7.1	17.6	1.1	1.1	-1.6	-3.6	**9.1**	**9.8**	**7.4**
of which: equipment		3.0	7.4	3.6	-8.5	3.8	7.5	**15.6**	**15.2**	**11.5**
Exports (goods and services)		31.4	77.7	6.0	5.7	5.0	6.4	**8.9**	**7.4**	**5.5**
Imports (goods and services)		27.7	68.5	5.1	4.1	4.7	6.6	**8.7**	**8.4**	**6.2**
GNI (GDP deflator)		39.3	97.2	2.2	3.4	0.1	3.4	**4.6**	**4.0**	**3.3**
Contribution to GDP growth:	Domestic demand			1.8	1.1	1.4	2.0	**3.7**	**4.0**	**3.3**
	Inventories			0.0	0.5	0.3	0.7	**0.0**	**0.0**	**0.0**
	Net exports			0.5	1.4	0.6	0.5	**1.0**	**0.0**	**0.0**
Employment				0.3	0.4	1.2	1.9	**2.3**	**1.6**	**1.0**
Unemployment rate (a)				6.8	9.7	9.0	8.0	**6.8**	**5.9**	**5.2**
Compensation of employees / head				5.8	1.3	1.4	2.8	**2.8**	**3.2**	**3.1**
Unit labour costs whole economy				3.8	-1.2	0.4	1.6	**0.4**	**0.9**	**0.9**
Real unit labour cost				-0.1	-2.0	-0.6	0.7	**-1.3**	**-0.8**	**-0.7**
Saving rate of households (b)				13.4	12.5	12.7	12.8	**11.3**	**10.1**	**10.0**
GDP deflator				3.9	0.8	1.0	0.9	**1.7**	**1.6**	**1.7**
Harmonised index of consumer prices				4.5	0.4	-0.8	-0.2	**1.6**	**1.5**	**1.8**
Terms of trade goods				-0.4	1.1	1.3	0.8	**-0.3**	**-0.3**	**-0.3**
Trade balance (goods) (c)				-3.1	2.9	3.8	3.8	**4.0**	**3.3**	**2.7**
Current-account balance (c)				-1.8	5.8	4.5	5.3	**5.9**	**5.4**	**4.9**
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-1.6	6.0	5.6	4.5	**5.5**	**5.2**	**4.8**
General government balance (c)				-3.8	-5.3	-2.9	-1.9	**-0.8**	**0.0**	**0.4**
Cyclically-adjusted budget balance (d)				-3.8	-3.4	-1.6	-1.5	**-1.7**	**-1.6**	**-1.4**
Structural budget balance (d)				-	-2.2	-1.6	-1.5	**-1.6**	**-1.6**	**-1.4**
General government gross debt (c)				32.5	80.3	82.6	78.5	**76.4**	**74.1**	**72.0**

(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.