

# SLOVENIA - CURRENT ECONOMIC TRENDS 2003 - 2005

## General Overview

Slovenia joining the EU – a historical event that took place this May – was the most important impetus and challenge to the economic and political activities not only in 2004 and 2005 but throughout the whole decade. Its short-term impacts on economic activity and GDP growth are expected to be prevailingly positive already in 2004 and 2005. According to the first announcements of the National Statistical Office of March 2004, **GDP growth** reached 2.3 percent in 2003, which was below the expectations and can be attributed to Slovenia sharing some less positive impulses with the weak European business cycle in 2003 and thus recording somewhat lower GDP results in the 3rd and 4th quarter of the year. In 2004, GDP could rise by 3.5 percent again and in 2005 by 3.7, with strengthening exports and imports.

**Exports and investments** are confirmed to remain the main driving forces behind Slovenia's economic growth in this period. In domestic demand, especially the **investments'** growth has soared (from 1.3 percent in 2002 to around 8 percent in 2004), followed by public and private consumption. The wage rise as the most important source of households' incomes has been moder-

ate in 2003. Some more expressed demands of trade unions for wage rises appeared in the spring of 2004, with the elections in autumn 2004 already affecting the overall climate.

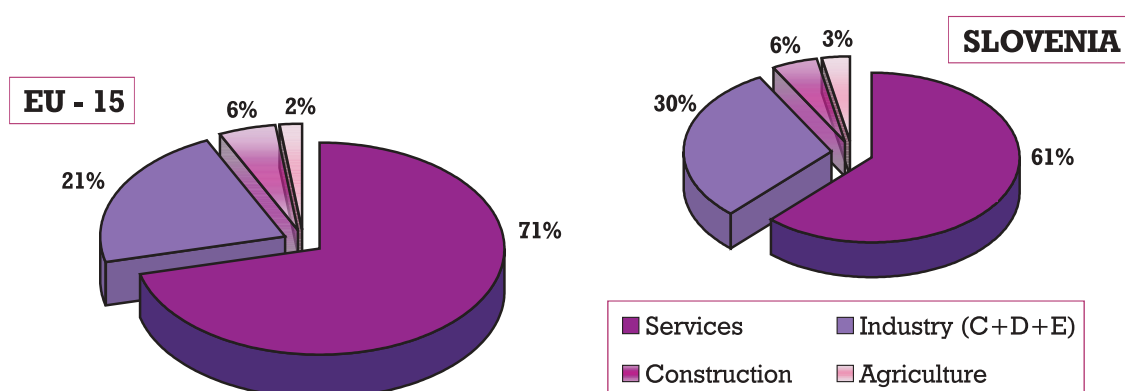
**Inflation** has been slowing down and the fall to around 3 - 3.5 percent of inflation in the first quarter of 2004 is quite an achievement in comparison to the past years. The downward trend is expected to continue in 2004 in line with the Programme for the entry to the ERM2. **Labour market** saw a decrease in employment (-0.8%) in 2003, with moderation being the most pronounced in the small private sector. This year's negative labour market trend is expected to soften.

### PURCHASING POWER PER CAPITA - SLOVENIA AND NEIGHBOURING COUNTRIES COMPARED TO THE EU-15=100, 2003

• SLOVENIA	71
• HUNGARY	56
• ITALY	98
• AUSTRIA	111

Purchasing power is currently on the level of 71 percent of EU-15 average. Domestic demand trends stimulate not only the domes-

### GDP COMPOSITION - COMPARISON, EU & SLOVENIA



Source: Eurostat, May 2004

SKEP GZS

### MAIN BUSINESS CYCLE INDICATORS FOR SLOVENIA 2003 - 2005

	2003 Estimates	2004 Forecasts	2005 Forecasts
GDP, real growth rate in % (*)	2.3	3.5	3.7
• Private consumption, real growth rate in %	3.0	3.0	3.0
• Public consumption, real growth rate in %	2.8	3.3	3.0
• Gross fixed investment, real growth rate in %	5.5	8.0	8.0
• Exports of goods and services, real growth rate in %	3.4	5.3	5.7
• Imports of goods and services, real growth rate in %	6.3	6.7	6.4
Employment, growth rate in %	-0.8	0	0.3
Unemployment rate (standardised by ILO definition), in %	6.7	6.6	6.5
Consumer prices - annual average, growth rate in %	5.6	3.7	3.2
Compensation per employee - average, real growth rate in %	1.8	2.4	2.4
Short-term interest rates, 3m - nominal (estimate)	10.8	8.4	8.4
Long-term interest rates, on banking loans, nominal (estimate)	12.6	9.7	9.2
Exchange rate, SIT per EUR, annual average (estimate)	234	239	242
Exchange rate, USD per EUR, assumption	1.13	1.25	1.23

Sources: Konjunkturna gibanja, No.2, May 2004, SKEP GZS, based on different domestic and international sources (SURS, BS, etc.)

Estimates and forecasts: SKEP - Economic Outlook and Policy Services, Chamber of Commerce and Industry of Slovenia, April/May 2004.

tic trade but also the **import** rises in 2004 and in 2005. Slovenian **exports** of goods and services should rise by 5.3 percent in 2004 and 5.7 percent in 2005. The **current account**, positive in previous years, could see a minor deficit relative to GDP over the whole year 2004. The **degree of openness** of the Slovenian economy (trade in goods and services relative to GDP) reached 114 percent in 2003, which is considerably above the average in the EU-15 where this proportion amounted to 68 percent. Slovenia thus reaches an openness level close to Ireland and the Netherlands.

## Foreign Trade, Balance of Payment, FDI

In the course of 2003, in less favourable market environment, moderate growth in exports was attained, with improvement in **foreign trade trends** towards the end-year. Exports of goods were up by 4 percent and imports by 6.5 percent in real terms. In 2003, Slovenia increased its market share with most EU-15 countries except for France and Germany, although the trade continued to rise at a somewhat slower pace than trade in general. In the case of Germany the market share has been decreasing since 1995.

At the beginning of **2004** further positive foreign trade trends have been maintained, this time with exports growing faster than imports. In the first quarter of the year, exports of goods grew by 6.8 percent, while imports grew by 6.2 percent in real terms over 2003. Trade in capital goods increased the most, but on the imports side, the consumption goods imports augmented the most.

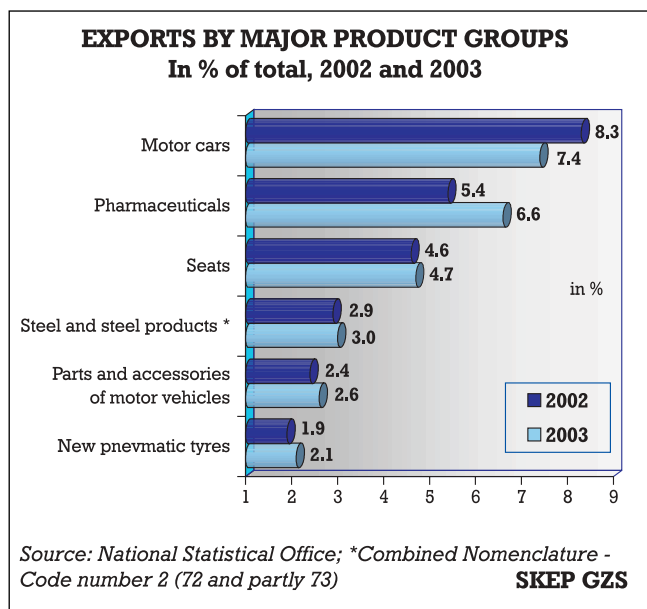
SLOVENIAN EXPORTS AND IMPORTS, in EUR				
	2003	I-III 2004	2003	I-III 2004
	EUR million		Growth rates in %	
<b>Exports total - goods</b>	<b>11,285</b>	<b>2,962</b>	<b>2.9</b>	<b>8.1</b>
EU-15	6,595	1,809	1.3	6.2
EU-10 new countries *	956	251	7.1	15.5
Countries of former Yugoslavia	1,967	459	0.8	10.0
Countries of former Soviet Union	550	131	8.0	20.1
<b>Imports total - goods</b>	<b>12,237</b>	<b>3,168</b>	<b>5.7</b>	<b>5.9</b>
EU-15	8,231	2,127	4.6	6.4
EU-10 new countries *	1,023	246	5.6	-3.2
Countries of former Yugoslavia	613	141	6.7	-3.1
Countries of former Soviet Union	381	117	11.5	5.0

Source: National Statistical Office;

Note: \* EU-10 new countries Czech Republic, Hungary, Poland, Slovakia, Estonia, Latvia, Lithuania, Malta, Cyprus. Excluding export/import data for Slovenia.

Becoming a Member State of the enlarged European Union in May 2004, Slovenia anticipates broadening of trade with EU-15 and also with the new EU-10 member states. Already today intra EU-25 trade accounts for some to three-quarters of total trade in goods. The trade with **EU-15 markets** remains the most important for Slovenian companies, with 61 percent share in the total value of exports and 67 percent in imports in the **first quarter 2004**. Exports and imports of goods in EUR terms grew by 6.2 percent and 6.4 percent respectively. An increase was in exports with Germany, Austria, Belgium, Denmark, Greece, Ireland, Spain and some Scandinavian countries, while the exports lowered with Italy, Netherlands, France and Great Britain. Imports from France, Austria, Germany, Netherlands, GB, Spain and Portugal rose the most, and although the imports from Italy, Greece and Finland went down, the trade deficit with EU countries climbed up to EUR

318 million in the first quarter of 2004.



Like in the last few years, trade with **CEFTA** and other **new EU member states** grew faster in 2003, in particular exports. In early 2004, continuous upward trend has been perceived, with export boosting the most to Poland, Slovakia, Czech Republic and Hungary. In the same period imports from these countries were down, except with Poland, Estonia and Lithuania. 8.5 percent share in the total value of exports and 7.8 percent share of imports were achieved with the new member states in the first quarter 2004.

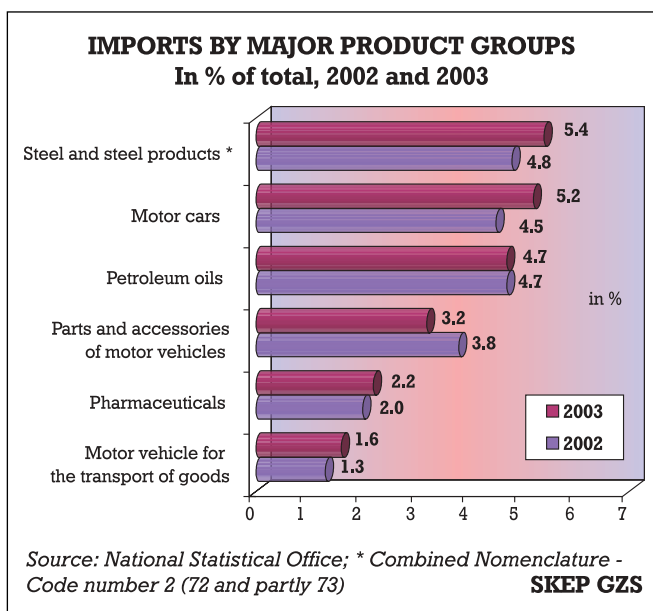
SLOVENIAN EXPORTS AND IMPORTS IN GOODS				
Shares of total in %				
	2003		I-III 2004	
	Exports	Imports	Exports	Imports
EU-15	58.4	67.3	61.1	67.1
EU-10	8.5	8.4	8.5	7.8
<b>EU-25</b>	<b>66.9</b>	<b>75.6</b>	<b>69.5</b>	<b>74.9</b>
Other countries	33.1	24.4	30.5	25.1

Source: National Statistical Office

After entering the European Union in May 2004, Slovenia's trading conditions with the **South Eastern European countries** have worsened. Exports are expected to dwindle, as previous bilateral agreements with these countries were more advantageous for Slovenia. However, exports to these countries were up by 10 percent in the first quarter this year, to Croatia even by 13 percent. Generally, imports of goods from these countries were down by 3 percent, except for the imports from Bosnia and Herzegovina, which boosted.

The trade balance with **Russia** and other **CIS-countries** saw some deterioration in the course of 2003 even though exports were up by 8 percent. The exports have been again picking up this year, this time faster than imports. With Russia, the major trade partner in CIS group, exports rose by 30.3 percent and imports by 9.4 percent in the first quarter of the year. Slovenia also increased its market share in the Russian imports to 0.48 percentage points. Also trade with **non-European OECD** member states has been on rise again in 2004. Following a very successful year, the exports are in the first months this year still increasing, although at a slower pace. The highest export

growth was achieved with Turkey, Mexico and Canada, but Slovenian exports to USA and Japan went down.



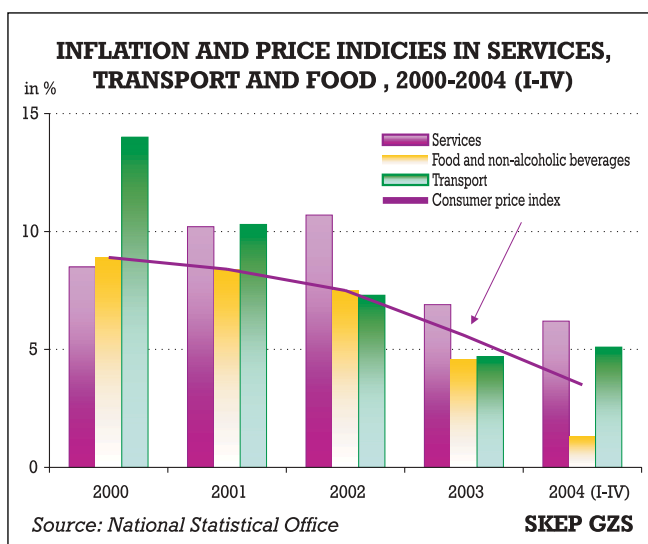
In 2003, Slovenia's **balance of payment** was close to equilibrium. After a high surplus of EUR 330 million in 2002, the current account surplus narrowed owing to widened trade deficit and smaller surplus in services. Services generated a surplus of EUR 541 million, with export growing by only 0.6 percent in nominal terms and imports by 5.5 percent. Travel expanded faster. In the first quarter of 2004, the balance of payments again saw a surplus of EUR 44 million, as a result of positive trade developments. There was no special change in the terms of trade. Compared to 2002 export and import prices were up by 2.5 percent.

Regarding **foreign direct investments** Slovenia turned out a **net exporter** of direct investment in 2003. Domestic investments abroad surpassed even 1.7 times the inward net investment. The outward investment reached EUR 269 million, most of it in ownership capital in the South-Eastern European countries Bosnia and Herzegovina, Serbia and Montenegro, Croatia and Bulgaria, as well as in the new EU Member States (Poland), Luxembourg, etc. There was a net inflow of inward investment of EUR 160 million in 2003 and year-end stock was close to EUR 4 billion. In the first quarter of 2004, the net inflow of direct investment from abroad amounted to EUR 48 million, thus being substantially higher than in the same period of the previous year, and the net outward investment again stood at EUR 69 million.

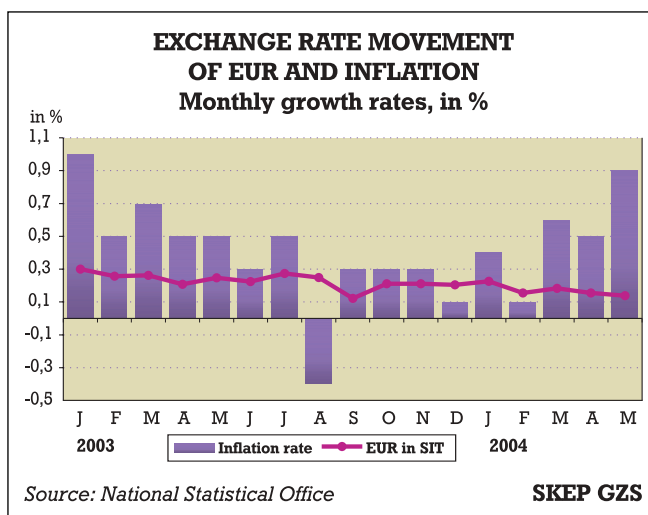
## Prices, Interest Rates, Exchange Rates & Policy

With a promising slowdown of **inflation** towards the end of 2003 and in the first months of 2004, Slovenia made an important step forward to establishing **price stability**. Inflation at the end of 2003 was 4.6 percent, while the average price rise reached 5.6 percent last year. In April 2004, inflation was 3.5 percent at an annual level, thus bringing the four months average rate to 3.6 percent, 2.5 percentage points down compared to the a year ago. Nevertheless, some threats to further easing

of inflation are still present. The pressure of high oil prices on world markets has raised domestic fuel prices and together with major raw materials price pushed up the **producer prices** to 4 percent on an annual level in April. In the field of administered prices some increases could not be avoided despite the joint efforts of the Government and the Bank of Slovenia in this area. With the entering to EU in May, also some other price adjustments took place, especially in services sector. Our forecast for inflation for the whole 2004 stands at 3.7 percent, with a possibility of lower average rate, if seasonally lower prices in the summer months bring about some deflation.



With lower inflation and several interest rate cuts by the Bank of Slovenia, **interest rates** have dropped markedly over the last one-year period. For companies, the average nominal interest rate for short-term loans in banks were reported at 9.1 percent on average in April, around 2 percentage points lower than a year ago. Besides lowering of interest rates, the access to bank loans has been eased. Long-term interest rates already correspond to the Maastricht requirements.

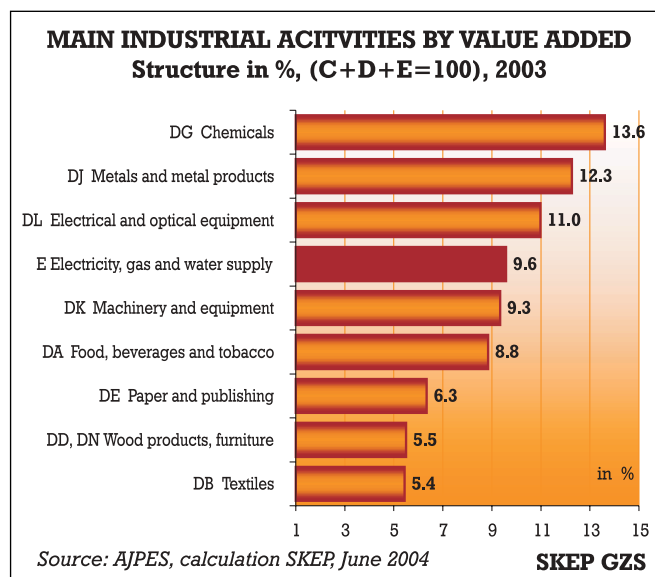


As Slovenia is likely to enter the **ERM2 regime** not later than at the year-end 2004, this spring the monetary authorities stated that no important corrections of **exchange rates** were needed. In the course of 2004 the tolar depreciation against the euro continued at a slower pace, which should enable a smooth transition to ERM2. The euro has been stabilizing at

SIT 237.8 average rate in the first five months 2004, while in 2003 the average rate of the euro was SIT 233.7. This was a rise by 3.3 percent in nominal terms, thus lagging behind the rise in domestic prices by 2.3 percentage points and indicating a continuation of trend from previous years. It also led to lower price competitiveness of Slovenian companies. In the first five months of 2004, the euro was up by 2.5 percent and domestic prices rose by 3.7 percent, compared to the same period last year. Exporters were loosing additionally because of the weak dollar, down by 9 percent in the first five months this year.

## Production and Services

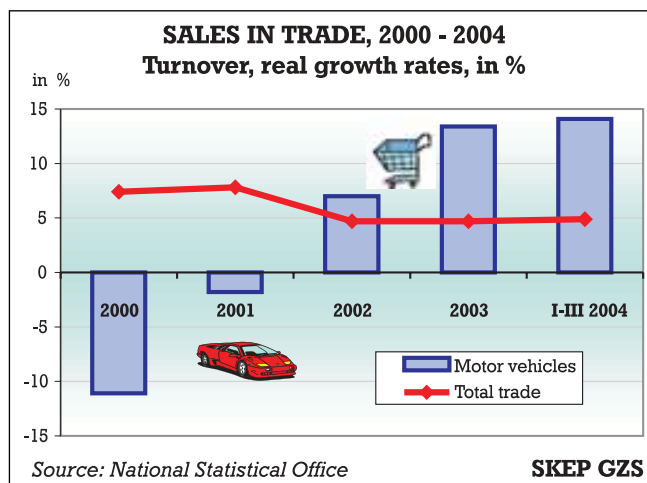
With the rate of 1.4 percent the industrial output growth was modest in 2003. The first quarter of 2004 showed some more dynamism, with **industrial production** rising by 4.2 percent compared to the same period in 2003. Capital goods industries recorded a rise by 7 percent and intermediate goods industries by 6.4 percent. On the other hand, the production of durable consumer goods industries was some 11.5 percent lower compared to the first quarter of 2003. In the breakdown by sectors in 2004, the highest rise was recorded by the manufacture of electrical and optical equipment (14.6 percent), and manufacture of chemicals (12.1). However, some activities could still not avoid a drop – most markedly the manufacture of leather products and textiles, which was down by 9 percent.



In **construction**, civil engineering with close to 16 percent real growth in the value of works indicated a strong expansion in 2003. Motorways, energy sector and municipal infrastructure investments as well as some equipment investment in manufacturing have been the main driving forces behind it. In 2004, the positive trends in construction continue, with buildings (business buildings, trade, tourism) and especially residential construction revival on the way. 27 percent growth in buildings and over 100 percent in residential construction already in the first quarter underlie this assessment.

In **domestic trade**, the turnover was up by 4.9 percent in real terms in the first quarter 2004. Similar to 2003, when the trade of motor vehicles expanded the most - with over 13 percent real upsurge - the rise in trade of motor vehicles was again up, by

over 14 percent. On the other hand, sales of food, beverages and tobacco were up only by 2.2 percent and only modest sale has been seen in non-food stores. The latter generated some 2.9 percent growth, with increasing sales of furniture, household equipment and construction material, followed by retail sale via mail order houses and textile, clothing and leather products. The turnover in fuels trade has been down by 0.8 percent.



Also in **tourism** the trends remain promising in 2004. In 2003 Slovenia recorded 7.5 million total tourist overnights. 4.2 million were by foreign tourists, up by 36 percent from 1999. The foreign tourism receipts reached of EUR 1.18 billion, i.e. 31 percent more than in 1999. In the first third of 2004, foreign arrivals were up by 5 percent, and are expected to further expand over the whole year. The EU enlargement to "EU-25" is changing the traditional European tourist flows and is making new ones. Slovenian tourism should benefit from that as well. Some new air connections between Ljubljana and some European capitals were established in early 2004, already bringing new groups of tourists to Slovenia.

Growth in **banking sector's** total assets continued throughout the first four months of 2004. Credit increase remains relatively strong. Lending to enterprises began to grow back in the middle of last year, and household credits this year. The increased credit activity arises from several facts - economic growth, domestic private consumption, fall in domestic interest rates, and also complete lifting of restrictions on foreign currency lending, which is more extensive than local lending. Deposit growth remains weak, while bank borrowing through foreign institutions continued to grow strongly. In the first months of 2004 small banks in Slovenia increased their assets the most, while the largest banks (NLB, NKBM, SKB-Societe Generale are among biggest), increased their ROE.

## Labour Market, Wages, Labour Costs

The continued downward trend in small private business sector and modest employment in companies and organisations confirm the delay in the recovery of the Slovenian labour market in 2003. **Total employment** decreased by 0.8 percent and registered **unemployment rate** as well as standardised unemployment rate by ILO definition remained high (11.2 and 6.7 percent, respectively) despite the decline in registered unemployed persons. The supply of **job vacancies** has been



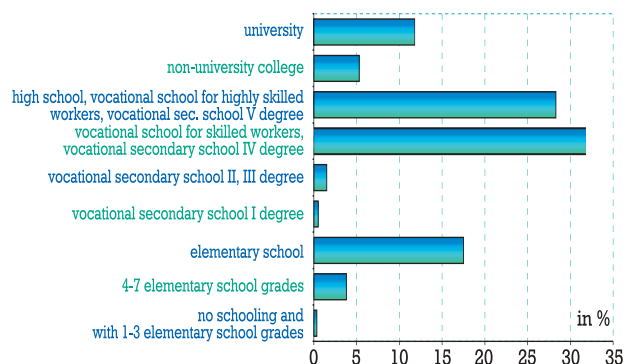
improving according to the National Employment Service. The trend has continued in the first quarter of 2004.

LABOUR FORCE, 2003 - 2004			
	Number 2003	Growth in %	
		2003	2004 I-III
<b>LABOUR FORCE</b>	874,921	-1.3	-0.4
<b>1. Total employment</b>	777,247	-0.8	-0.2
• in enterprises, companies	632,981	0.3	0.3
• by self-employed persons	66,164	-0.9	-0.8
• self-employment	78,101	-8.8	-3.0
- individual private entrepreneurs	43,308	-2.0	-1.9
<b>2. Registered unemployment</b>	97,674	-4.8	-2.4

Source: National Statistical Office

In 2004, the negative tendencies in the labour market are expected to soften, but precaution in employers' decisions regarding new hiring still remains. No growth in total employment and around 6.6 percent ILO unemployment rate on average is expected.

#### PERSONS IN EMPLOYMENT BY EDUCATION LEVEL, SLOVENIA, 3 years average, 1999-2002

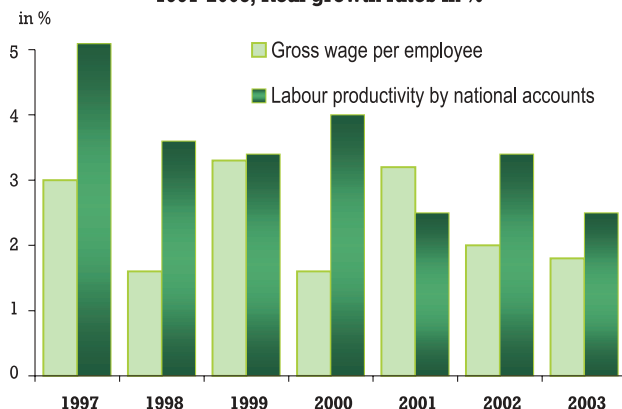


Source: National Statistical Office, March 2004

SKEP GZS

After a 1.8 percent real growth in 2003, **wages** started to rise faster in the first quarter of 2004. In 2003, the average monthly gross wage stood at SIT 253,200 - EUR 1,083- and in manufacturing SIT 211,060 (EUR 903) – by 40-hour week, which includes ½ hour meal break per day. Average monthly take-home wage in Slovenia was SIT 159,072 (EUR 680). The statutory **minimum wage**, including employee contributions and

#### GROSS WAGE PER EMPLOYEE AND LABOUR PRODUCTIVITY 1997-2003, Real growth rates in %



Source: National Statistical Office

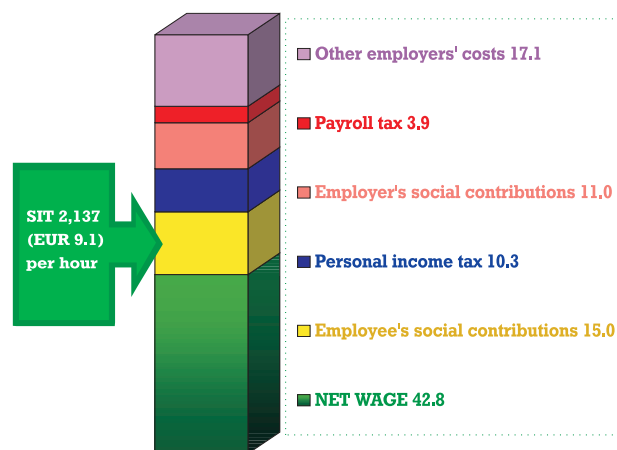
SKEP GZS

personal income tax, in force as from December 2003, is SIT 111,484 – EUR 471 - and from August 2004 on SIT 117,500.

In the **distribution of employees by wage levels** a gradual shift from low-wage earners towards average-wage earners has been perceived.

#### HOURLY LABOUR COST IN SLOVENIA, 2003

Structure in %



Source:

National Statistical Office, Calculation SKEP GZS

SKEP GZS

The average **labour cost** for employer, including additional labour costs, totalled SIT 2,137 (EUR 9.1) **per hour**, while in manufacturing SIT 1,816 (EUR 7.8) in 2003, with a gradual upward tendency in 2004.

In April 2004, a new **Wage Policy Agreement** for Private Sector 2004-2005 was signed by social partners - Trade Unions, Employers representatives and the Government. According to this Agreement, gross wages of employees paid by collective agreements should be adjusted by 3.2 percent in 2004 and by 2.7 percent in 2005, however an adjustment involves an agreed amount of wage supplement rather than a percentage increase. The main emphases of the new Slovenian Wage Agreement are:

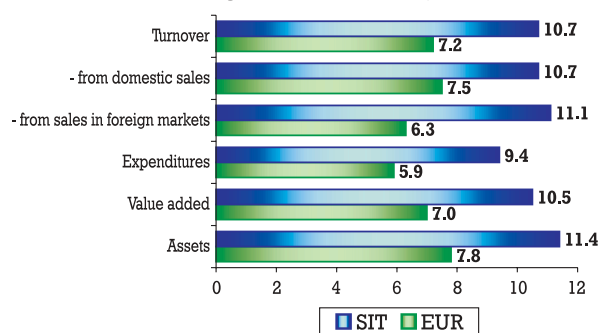
- real gross wage growth should lag behind productivity growth by at least 1 percentage point,
- gross wages are the object of adjustment, no more starting basic wages,
- sectoral collective agreements determine the amount of wage supplement,
- minimum adjustment amount must be SIT 5,000 for 2004 and SIT 5,100 for 2005,
- first wage adjustment is settled for August 2004,
- if productivity growth allows, the adjustment amount determined by sectoral collective agreements could be higher,
- minimum wage is defined as amount, SIT 117,600 as from August 2004 and SIT 122,600 as from August 2005.

In relation to the new private sector agreement and expected further moderate wage growth in public sector, the average **real gross wage** growth in Slovenia could reach around **2.4 percent** in the whole 2004. However, if the sectoral agreements' solutions discussing in the course of the year do not stay in line with productivity, the accelerated wage growth could threaten the macro-economic goals set out in the Social Agreement.

## Business Results of Companies

Annual financial and accounting statements of Slovenian companies for the business year 2003 point to EUR 1.3 billion of **profits** after deduction of taxes. The total **sales revenues** of companies amounted to 51.4 EUR billion, up by 7.2 percent in euro nominal terms, and the average profit margin rising to 5.1 percent. In line with renewed accounting standards, the process of a more realistic evaluation of the assets, equity and financial issues was still present, resulting in some less favourable profits in some cases, despite quite higher EBDIT (earnings before depreciation, interest and taxes). According to new, specialized accounting standards for sole proprietors - **entrepreneurs**, the sales revenues of this group of businesses reached EUR 3.9 billion, up by 5.5 percent in euro nominal terms.

### COMPANIES - TURNOVER, EXPENDITURES, VALUE ADDED, ASSETS Annual growth rates in %, 2003



Source: AJPES, calculation SKEP, June 2004

SKEP GZS

By turnover and employment, **large** companies are the most important, with 50 percent of employees and 59 percent of turnover. Small **companies** on the other hand represent 95.3 percent of all companies, generate 25 percent of turnover and employ 32 percent of all employees, while medium-sized companies comprise some 16 percent of turnover. The proportion of sales revenues generated **in foreign markets** stood at 26.4 percent in total revenues. **Exporters** continued to be an important engine of Slovenian economy, in particular large exporters whose export revenues accounted for as much as 67.4 percent of total.

### OPERATING COMPANIES AND ENTREPRENEURS, 2003

<b>Number of companies:</b>	<b>39,838</b>
- SME's*	38,998
- Large companies:	840
<b>Number of exporters:</b>	<b>9,190</b>
<b>Number of entrepreneurs:</b>	<b>53,396</b>

\*Defined by 2 from 3 standards (0-250 employees, turnover, equities)  
Source: AJPES, June 2004

**Value added** per employee by our calculations stood at **EUR 26,211** on average, recording 5.2 percent growth over the previous year in euro terms and 8.7 in tolar. The **return on equity** was on average 4.6 percent and **return on assets** 2.1 per cent, whilst in manufacturing these figures were 5.7 and 3.1, respectively. Total equity of companies in 2003 in tolar nominal terms was 11.4 percent higher than a year before, thus increasing its real value.

## Expectations and Developments

Like throughout the last decade, Slovenia's GDP growth is expected to be above the EU average in the coming period. Higher exports and imports growth along with some domestic demand impulses remain to be the main drivers behind it. Domestic demand will be supported mostly by investments and to some extent also by private consumption. We do forecast GDP to grow at around 4 percent per year in the next years.

### COMPANIES: SHORT-TERM EXPECTATION ON EXPORT, 1996 - 2004



Source: SKEP quarterly Survey,  
December 1995 - March 2004

SKEP GZS

**Business expectations** of companies have been developing positively, even though the March 2004 evaluation of the current situation in companies still revealed some caution, especially in industry. The most positive expectations come from exporters and their business cycle expectations, encouraged by structural reasons and global market trends.

For Slovenia, the next step after joining the EU, should be to enter the ERM2 and latter introducing the Euro. This is expected to realize soon, as the Tolar/Euro exchange rate has recently seen relatively low volatility and meeting of Maastricht criteria seems realistic. Slovenian Development **Strategy to the year 2013**, i.e. in the first decade of EU membership, has been discussed during the year 2004. The development should be oriented particularly to achieving the real convergence and to exceeding the average level of development of the EU-25. This calls for Slovenia to achieve a high (4-5 percent) annual growth in the coming years and to efficiently address new structural challenges and innovations.

Ljubljana, June 2004

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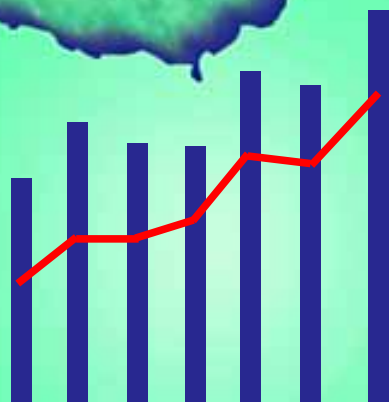


ECONOMIC OUTLOOK AND POLICY SERVICES

# - SLOVENIA - CURRENT ECONOMIC TRENDS

2003-2005

*Spring Issue 2004*



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