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EUROSYSTEM



SUMMARY OF MACROECONOMIC DEVELOPMENTS

JANUARY 2018

Summary of macroeconomic developments, January 2018

The economic situation in the international environment is favourable. Forecasts of global economic growth are continuing to be gradually raised, and GDP growth is strengthening in the euro area, where the economic sentiment remains strongly above its long-term average. The conditions for growth in Slovenian exports are also expected to be very good this year as weighted economic growth of Slovenia's major trading partners based on Consensus forecasts for 2018 has increased again. In the final quarter of last year, the divergence between the monetary policies of the ECB and the Fed increased further. Despite this, the euro's year-on-year appreciation against the US dollar stood at approximately 14% in the first half of January at 1.20 dollars per euro. This is comparable to the average exchange rate between 1999 and 2017. The price of Brent crude is continuing to rise. It approached USD 70 per barrel in the first half of January, its highest level of the last three years, which will also have an impact on global inflation this year.

In the third quarter of last year, the high growth in the Slovenian economy was largely the result of the exploitation of the economic climate in the euro area. The contribution made to GDP growth by the export sector increased to its highest level since 2010, albeit from a significantly higher starting point than after the crisis year of 2009. In the third quarter, the manufacturing sector's turnover on euro area markets was up almost 16% in year-on-year terms. Exports thus compensated for the slowdown in domestic private consumption, and even more for the slowdown in investment. Growth in investment was surprisingly low compared with economic growth, although the slowdown was most probably merely temporary, given that conditions for investment are extremely favourable. A particular highlight is the record operating surplus in the corporate sector, which is continuing to allow firms to finance themselves with internal resources and is reducing the need for bank financing. With rapid employment growth, the situation on the labour market is also providing for faster growth in private consumption than was realised in the third quarter. According to survey data on the economic sentiment and new orders, the climate is not letting up.

Although structural imbalances are increasing on the labour market, and growth in demand for labour is outpacing growth in supply, labour availability remains higher than in the pre-crisis years of an overheating economy. In the third quarter of last year, employment growth remained high and was additionally strengthened by foreign workers. Firms again primarily demanded lower-skilled labour, and hiring was predominantly in sectors with below-average pay. Although the proportion of firms facing a shortage of workers increased further, the supply of labour for now remains higher than it was before the crisis. Unemployment according to the broader definition, which includes employees on reduced work hours, was significantly lower at that time than in the third quarter of last year. The increase in wage growth over the first ten months of the year was small, and did not entirely track the rise in inflation. In the wake of the sharp growth in employment, growth in the nominal wage bill increased further, averaging 5.9% over the first ten months of the year, which is strengthening consumer purchasing power.

The structure of employment reflects the structure of the Slovenian economy, which is also being reflected in complexity of Slovenia's merchandise exports. Last autumn nominal export growth reached its pre-crisis level although the climate in the international environment was less strong than at that time and the actual volume of exports was at a significantly higher level than a decade ago. In the wake of slightly weaker growth in domestic demand and an improvement in the terms of trade, the trade surplus strengthened again, and was approaching fully 10% of GDP over the 12 months to October. Despite the rapid growth in exports and market shares over the last few years, which reflect the improved competitiveness of Slovenian exporters, analysis of the labour intensity of production reveals that exporters in industry have only

slightly increased their use of highly skilled labour, and retained their competitive advantage over the EU primarily in sectors with a medium-skilled labour force. Analysis of Slovenia's integration into global production chains further reveals that the pronounced specialisation in manufacturing with a low share of value-added in exports and the positioning in the lower part of production chains are concentrating Slovenian exports in labour-intensive sectors with relatively low labour costs. The non-price competitiveness and technological intensity of Slovenian exports will thus largely be dependent on the positioning in international production chains. Production in final stages will have a greater share of foreign value-added, although this will not necessarily lead to more significant growth in value-added per employee.

The fiscal position is improving, as a result of the favourable cycle and a decline in interest payments on general government debt as a share of GDP. Growth in general government expenditure remained moderate last year, primarily owing to low government investment as a result of the very weak disbursement of EU funds, which was down significantly on the government's original plans. The financing conditions were also extremely favourable: the current spreads on long-term bonds are merely around 40 basis points over the German benchmarks of comparable maturities. According to Ministry of Finance forecasts, last year's general government deficit was expected to stand at 0.8% of GDP, down just over 1 percentage point on 2016, while the government is forecasting a surplus of 0.4% of GDP for this year. Despite the favourable GDP forecasts and the anticipated high growth in general government revenues, the government must actively endeavour to achieve the planned surplus, as pressures for a more significant rise in expenditures, particularly on wages, have recently strengthened sharply.

After two years of deflation, inflation had risen to 1.9% by December of last year, thereby exceeding the euro area average. All of last year's main movements in headline inflation were primarily caused by movements in global oil prices. The core inflation indicators only increased minimally, and remained between 0.7% and 1.1%, below the euro area average. Core inflation was raised by food prices, while prices of non-energy industrial goods continued to fall, most likely as a result of falling import prices and strong competition in the retail sector. Growth in services prices remained unchanged, despite strong domestic economic activity. Inflation thus remains primarily determined by external factors. In December, consumers' inflation expectations remained significantly above the euro area average, while firms' inflation expectations were comparable to the euro area average.

Main macroeconomic indicators

| | 2014 | 2015 | 2016 | 17Q1 | 17Q2 | 17Q3 | 2014 | 2015 | 2016 | 17Q1 | 17Q2 | 17Q3 |
|--|--------------------------------|-------|------|------|------|------|------------------|-------|-------|-------|-------|-------|
| | Slovenia | | | | | | euro area | | | | | |
| Economic developments | <i>y-o-y growth rates in %</i> | | | | | | | | | | | |
| GDP | 3.0 | 2.3 | 3.1 | 5.1 | 4.6 | 4.5 | 1.3 | 2.1 | 1.8 | 2.7 | 1.8 | 2.5 |
| - industry | 4.6 | 1.4 | 4.4 | 6.9 | 6.5 | 8.2 | 2.7 | 4.0 | 2.0 | 3.7 | 1.0 | 3.3 |
| - construction | 10.5 | -1.6 | -4.4 | 13.0 | 11.4 | 5.5 | -1.0 | 0.4 | 1.6 | 3.8 | 2.3 | 2.9 |
| - mainly public sector services | -0.1 | 1.4 | 2.9 | 2.5 | 2.1 | 1.4 | 0.5 | 0.9 | 1.3 | 1.6 | 1.3 | 1.5 |
| - mainly private sector services | 4.6 | 2.4 | 3.2 | 6.1 | 5.7 | 5.4 | 1.5 | 2.1 | 1.8 | 2.9 | 1.8 | 2.8 |
| Domestic expenditure | 1.7 | 1.8 | 2.9 | 5.3 | 3.5 | 2.4 | 1.3 | 2.0 | 2.3 | 2.4 | 1.9 | 1.8 |
| - general government | -1.2 | 2.7 | 2.5 | 0.9 | 1.3 | 1.8 | 0.7 | 1.3 | 1.8 | 1.2 | 1.0 | 1.2 |
| - households and NPISH | 1.9 | 2.1 | 4.2 | 3.8 | 2.8 | 2.7 | 0.8 | 1.8 | 2.0 | 1.7 | 1.7 | 1.8 |
| - gross capital formation | 3.8 | 0.2 | -0.1 | 14.0 | 7.5 | 1.9 | 3.3 | 3.4 | 3.8 | 5.8 | 3.3 | 2.5 |
| - gross fixed capital formation | 1.1 | -1.6 | -3.6 | 13.0 | 8.7 | 6.1 | 1.9 | 3.3 | 4.5 | 5.5 | 2.3 | 2.0 |
| - inventories and valuables, contr. to GDP growth in pp | 0.5 | 0.3 | 0.7 | 0.4 | -0.1 | -0.7 | 0.3 | 0.0 | -0.2 | 0.1 | 0.2 | 0.1 |
| Labour market | | | | | | | | | | | | |
| Employment | 0.4 | 1.2 | 1.9 | 2.9 | 2.8 | 2.7 | 0.6 | 1.0 | 1.3 | 1.6 | 1.6 | 1.7 |
| - mainly private sector services | 0.4 | 1.4 | 1.9 | 2.9 | 2.9 | 2.8 | 0.5 | 1.0 | 1.4 | 1.7 | 1.8 | 1.9 |
| - mainly public sector services | 0.4 | 0.8 | 2.2 | 3.0 | 2.5 | 2.2 | 1.0 | 1.0 | 1.3 | 1.2 | 1.1 | 1.1 |
| Labour costs per employee | 1.3 | 1.4 | 2.8 | 1.7 | 2.5 | 2.8 | 1.4 | 1.4 | 1.3 | 1.6 | 1.6 | 1.7 |
| - mainly private sector services | 2.4 | 1.6 | 2.2 | 1.9 | 2.4 | 2.4 | 1.5 | 1.5 | 1.3 | 1.6 | 1.5 | 1.7 |
| - mainly public sector services | -2.1 | 0.7 | 5.2 | 4.2 | 3.0 | 2.9 | 1.1 | 1.2 | 1.2 | 1.5 | 1.8 | 1.5 |
| Unit labour costs | -1.9 | 0.4 | 1.6 | -0.7 | 0.3 | 0.8 | 0.7 | 0.5 | 0.9 | 0.5 | 1.5 | 0.8 |
| - industry | -0.9 | 1.3 | 0.7 | -1.6 | -0.2 | -2.2 | -1.0 | -1.8 | 0.0 | -1.1 | 1.7 | -0.2 |
| | <i>in %</i> | | | | | | | | | | | |
| LFS unemployment rate | 9.8 | 9.0 | 8.0 | 7.8 | 6.4 | 6.3 | 11.7 | 10.9 | 10.0 | 9.9 | 9.0 | ... |
| Foreign trade | <i>y-o-y growth rates in %</i> | | | | | | | | | | | |
| Current account balance as % of GDP | 5.8 | 4.4 | 5.2 | 4.8 | 5.5 | 7.0 | 2.3 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| External trade balance as contr. to GDP growth in pp | 1.4 | 0.6 | 0.5 | 0.3 | 1.5 | 2.4 | 0.1 | 0.1 | -0.4 | 0.3 | 0.0 | 0.7 |
| Real export of goods and services | 5.7 | 5.0 | 6.4 | 9.8 | 8.6 | 12.0 | 4.7 | 6.4 | 3.3 | 6.2 | 3.1 | 4.9 |
| Real import of goods and services | 4.1 | 4.7 | 6.6 | 10.8 | 7.7 | 10.1 | 4.9 | 6.7 | 4.7 | 6.0 | 3.4 | 3.7 |
| Financing | <i>in % of GDP</i> | | | | | | | | | | | |
| Banking system's balance sheet | 115.7 | 107.0 | 99.2 | 99.0 | 96.2 | 94.5 | 297.4 | 281.8 | 276.3 | 277.9 | 272.7 | 268.3 |
| Loans to NFCs | 31.2 | 26.3 | 22.5 | 22.8 | 22.5 | 22.2 | 40.1 | 38.8 | 37.9 | 37.8 | 37.6 | 37.2 |
| Loans to households | 21.3 | 21.1 | 21.1 | 21.2 | 21.3 | 21.4 | 50.5 | 49.8 | 49.5 | 49.3 | 49.3 | 49.3 |
| Inflation | <i>in %</i> | | | | | | | | | | | |
| HICP | 0.4 | -0.8 | -0.2 | 2.0 | 1.4 | 1.3 | 0.4 | 0.0 | 0.2 | 1.8 | 1.5 | 1.4 |
| HICP excl. energy, food, alcohol and tobacco | 0.6 | 0.3 | 0.7 | 0.7 | 0.8 | 0.8 | 0.8 | 0.8 | 0.9 | 0.8 | 1.1 | 1.2 |
| Public finance | <i>in % of GDP</i> | | | | | | | | | | | |
| Debt of the general government | 80.3 | 82.6 | 78.5 | 80.2 | 79.8 | 78.4 | 91.8 | 89.9 | 88.9 | 89.2 | 89.0 | ... |
| One year net lending/net borrowing of the general government | -5.3 | -2.9 | -1.9 | -1.4 | -1.2 | -0.8 | -2.6 | -2.1 | -1.5 | -1.3 | -1.3 | ... |
| - interest payment | 3.2 | 3.2 | 3.0 | 3.0 | 2.9 | 2.9 | 2.6 | 2.4 | 2.2 | 2.2 | 2.1 | ... |
| balancedeficit | -2.1 | 0.3 | 1.2 | 1.5 | 1.8 | 2.1 | 0.1 | 0.3 | 0.6 | 0.8 | 0.9 | ... |
| - balance excl. bank recapitalisations | -4.4 | -2.9 | -1.9 | -1.4 | -1.2 | -0.8 | | | | | | |
| - primary balance excl. bank recapitalisations | -1.1 | 0.3 | 1.2 | 1.5 | 1.8 | 2.1 | | | | | | |

Source: SORS, Eurostat, Bank of Slovenia, ECB, Ministry of Finance.