REPUBLIC OF SLOVENIA
FISCAL COUNCIL

IMAD
Institute of Macroeconomic Analysis and Development

Slovenia

Country note, July 2018

Key messages:

- **Broad based GDP growth continues.**
- **Renewed deterioration of the structural balance projected for 2018 and 2019 in the absence of new measures.**
- **New tasks assigned to the Fiscal Council.**

Macroeconomic outlook (prepared by IMAD)

Broad based economic growth continues into 2018. Strong growth of export oriented sectors stabilized at high y-o-y levels, with its pace slowing down. Domestic demand growth continues, especially private investments in machinery and equipment in light of high capacity utilization. Apart from weak first quarter, due to bad weather, construction activity is also strengthening. Household consumption growth continues, driven by favourable labour market developments and consumer confidence. The latest macroeconomic forecasts, prepared by IMAD (March 2018) predict 5.1% GDP growth for 2018, while in the next two years it will gradually decline to around 3%. Output gap closed in 2017 and is expected to hover around 2% in 2018 and 2019, according to estimates of various institutions. Although output gap is positive, several indicators, including wage growth, credit developments, inflationary expectations and current account surplus, point to sustained growth without overheating.

Short-term fiscal outlook (Fiscal Council)

Public finances improved substantially in 2017. Budget balance was recorded in both nominal and structural terms. The government resigned in March and the Stability Programme Update 2018 was adequately prepared according to no-policy change scenario. It shows no significant further improvement in the nominal balance and a renewed worsening of the structural balance in 2018 and 2019 despite assumed continuation of favourable economic trends. Both revenue and expenditure growth are expected to accelerate compared to previous years. Revenue growth will be driven by taxes and social contributions, while drawing of EU funds is also expected to increase strongly. Expenditure growth will be driven by further elimination of austerity measures in compensation of employees and social transfers, while investment activity is also expected to pick-up in relation to drawing of EU funds. Public debt as share of GDP is expected to continue to decrease to 60 % GDP in 2020, while in nominal terms it will stabilise at current level.

Medium-term fiscal outlook (Fiscal Council)

Fiscal Council (FC) believes that the results of no-policy change scenario in the Stability Programme 2018 provide a proof that fiscal consolidation up to 2017 mainly relied on a gradual elimination of austerity measures introduced mainly in 2012 and that favourable economic conditions in previous years were not used properly for introducing structural measures that would eventually bring about more sustainable public finances. In view of FC, this is even more important in relation to longer-term fiscal pressures with Slovenia facing high fiscal risk related to aging.

Fiscal framework and national fiscal rules (Fiscal Council)

FC has repeatedly warned both in autumn last year (DBP 2018) and in spring this year (SP 2018) that favourable cyclical conditions call for an adequate structural effort, which if adhered to would imply that the MTO at 0.25 % of GDP could be achieved in 2018 already. The Government on the other hand follows a different fiscal target (structural balance in 2020), which in view of FC is not in line with Fiscal Rule Act. FC also believes that expenditure targets should be updated for 2018 and 2019 by the adoption of a new Framework for state budgets, but the Government's view is that this a job to be handled by the incoming government. FC believes that an update of expenditure targets for 2018 and 2019 would bring public finances on a more consistent consolidation path. In spring 2018 the Public Finance Act was amended, in which new tasks were assigned to the FC, mainly an ex-post assessment of macroeconomic forecasts, prepared by IMAD, and of fiscal projections, prepared by MoF.

Chart 1: Broad based GDP growth

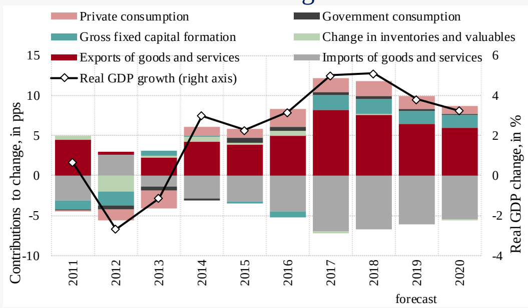
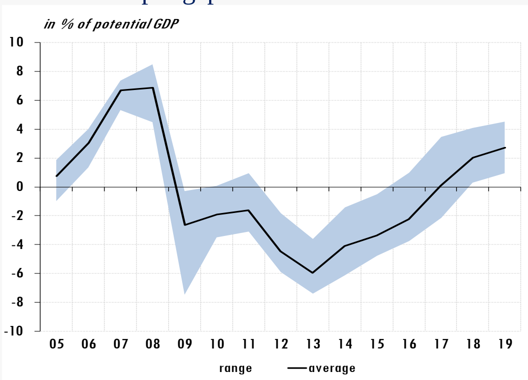
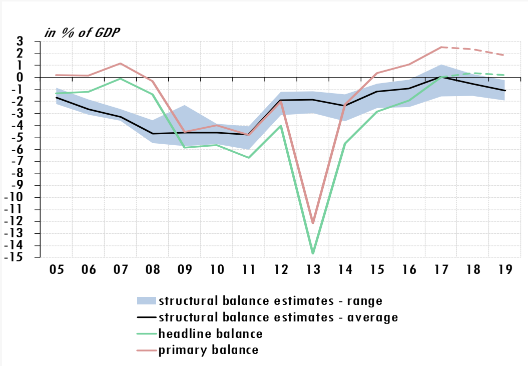


Chart 2: Output gap estimates



Source: IMAD, IMF, OECD, EC, MoF, FC calculations.

Chart 3: Public finance balances



Sources: SORS, IMAD, EC, OECD, IMF, MoF, Fiscal Council calculations.

Key indicator forecast

		2014	2015	2016	2017	2018 f	2019 f	Source
Real GDP growth rate	[% y-to-y]	3.0	2.3	3.1	5.0	5.1	3.8	1
Output Gap	[%]	-4.1	-3.4	-2.2	0.1	2.0	2.7	2
GG balance - MoF target	[% of GDP]	-5.5	-2.9	-1.9	0.0	0.4	0.2	3
GG primary balance - MoF target	[% of GDP]	-2.3	0.4	1.1	2.5	2.4	1.9	3
GG structural balance - FC estimate	[% of GDP]	-2.4	-1.2	-0.9	0.0	-0.5	-1.1	4
GG debt - MoF estimate	[% of GDP]	80.3	82.6	78.6	73.6	69.3	65.2	3

Sources: 1 – Statistical Office of the Republic of Slovenia; forecast: IMAD

2 – Fiscal Council: average and range (Chart 2 and base for Chart 3) of estimates of institutions (IMF, OECD, EC, IMAD, MoF) and of statistical estimates

3 – Ministry of Finance (SP 2018)

4 – Fiscal Council

f - forecast

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