BANKA SLOVENIJE

EVROSISTEM

Review of macroeconomic developments

January 2023

Title: Review of macroeconomic developments

Issue: January 2023

Issued by:
Banka Slovenije
Slovenska 35, 1505 Ljubljana, Slovenia
www.bsi.si

Based on data available by 20 January 2023.

The material was discussed at the meeting of the Governing Board of Banka Slovenije of 24 January 2023.

ISSN 2820-4751

This publication is also available in Slovene.

Contents

Boxes

Summary

The economy continued to slow down in the final quarter of last year amid persistently high inflation and signs of weakening foreign demand, but an uptick in the confidence indicators slightly improves outlook for the early part of this year.

- **The euro area mainly saw signs of weaker economic activity in the final quarter of last year, but December's rise in confidence brought an improvement in the outlook for the early part of this year.** The PMI for the final quarter of last year was unfavourable, although the pace of decline in economic activity measured by the indicator slowed in December in both manufacturing and services. Rises in retail confidence, services confidence and consumer confidence improved the economic sentiment, which nevertheless remained below its long-term average. Inflation eased slightly in December as the contribution by energy prices declined, but it still remained above 9%. According to the World Bank's January forecasts, the euro area economy is expected to record zero growth this year, before growth strengthens to 1.6% next year. Low growth is also forecast this year for global economy. The rate of 1.7% would be the lowest of the last three decades outside the years of the global financial crisis and the pandemic.
- **In light of the sustained high inflation, major central banks have continued raising their key interest rates, and have signalled their intent to make further rises.** The mood among investors with regard to higher-risk assets has improved slightly over the last three months, amid the persistence of global economic growth, the mild winter in Europe, and the opening of the Chinese economy, which has driven a rise in the value of assets in this class.
- **In the final quarter of last year, Slovenia's export sector faced a difficult external environment, but domestic demand remained solid, and the economic sentiment improved.** The energy and manufacturing sectors faced uncertainties in the international environment and strong cost pressures. Domestic demand contrastingly remained solid according to our assessments. Of the sectors tied to the domestic market, the strongest year-on-year increase was recorded by construction. Year-on-year growth in the value of card payments also increased slightly, and the economic sentiment improved. Taking account of various data impulses, the nowcasts on average suggest quarterly GDP growth of 0.1%, which given the quarterly figures as currently released would entail annual GDP growth of 4.7% in 2022.
- **The labour market position remained highly robust.** The workforce in employment excluding self-employed farmers is at a record high, although its year-on-year rate of growth of 2.1% in November of last year was down just over 1 percentage point on the beginning of the year. According to the survey data, hiring will continue in the first half of this year. Registered unemployment did increase slightly in December because of a seasonal effect, but its average over the year of 56,665 was a record low. Wage growth is continuing to strengthen. Amid high inflation, tight labour market, increase in the minimum wage and rising wages in the public sector, wage pressures will escalate this year, something that will also be seen across the euro area.

- **The situation faced by the export sector worsened towards the end of the year, but the strong import-side inflationary pressures began to ease.** Nominal year-on-year growth in merchandise exports slowed to 11.7% in November, and exports were actually down on a year earlier in real terms. Demand weakened on EU markets in particular. Nominal growth in merchandise imports slowed significantly to 17.2%, driven in part by growth in import prices slowing to 14.3%, down 15.9 percentage points on its peak in May. Growth in services trade slowed, but net services exports remained positive. The 12-month current account deficit amounted to EUR 430 million in November, albeit primarily because of developments in merchandise trade over the first eight months of the year.
- **Domestic inflation remained at 10.8% in December, primarily because of rising services prices.** Evidence that inflation is broadly based comes from the extensive pass-through of higher input costs into final consumer prices, with solid domestic demand making this easier. Energy price inflation slowed slightly, thanks to government measures and falling fuel prices, while growth in food prices and prices of non-energy industrial goods did not pick up further pace in December. The external and, in particular, domestic price pressures remain strong, while measured year-on-year inflation is already being reduced slightly by a base effect, inflation having begun to rise in the autumn of 2021.
- **The general government position has deteriorated over recent months, and the deficit is expected to widen this year, driven primarily by measures in connection with the energy crisis.** The consolidated general government deficit amounted to EUR 750 million over the first eleven months of the year, significantly narrower in year-on-year terms because of developments in the first half of the year, when expenditure was mainly reduced by the decline in pandemic-related payments, and revenues saw high growth. There was a year-on-year deterioration in the position in October and November, and also in December according to the state budget figures. This was attributable in part to the measures to mitigate the impact of high energy prices, which are expected to be the key driver of this year's larger deficit. The general government debt measured as a ratio to GDP continued to decline last year, and had reached 72.3% by the end of September.

1 International Environment

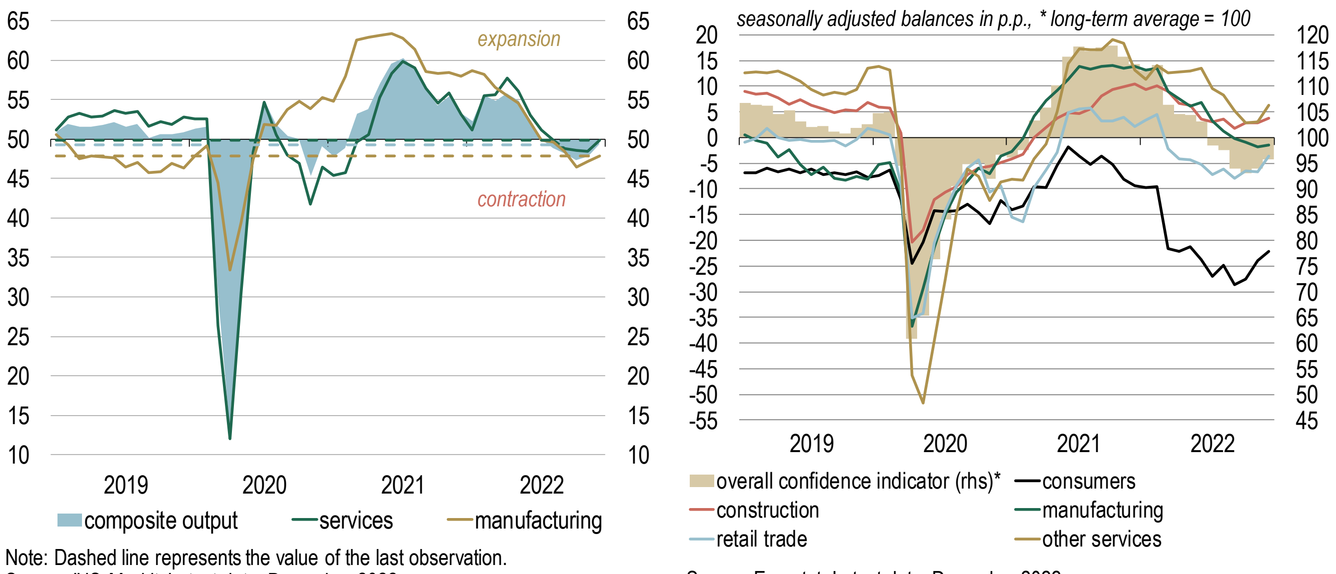
Economic activity in the euro area slowed again in the final quarter of last year, although the survey indicators suggest an improvement in sentiment among businesses.

The composite PMI averaged 48.1 points over the final quarter of last year, which points to the economy cooling by more than in the previous quarter, when it averaged 49.0 points.[1] The pace of the decline in activity is nevertheless slowing for the second consecutive month (see Figure 1.1). In addition, firms reported an improvement in the situation in manufacturing and services in December amid the normalisation of the conditions in supply chains and a slowdown in the fall in new orders. This has also been reflected in a second consecutive rise in the economic sentiment indicator, which nevertheless remains below its long-term average. All surveyed sectors reported an improvement in the confidence indicator, most notably retail trade, services and consumers (see Figure 1.1). The slightly higher level of optimism with regard to short-term economic developments is a reflection of sufficient energy supply for this winter, slightly more stable situation on the energy markets, and the figures showing a partial easing of inflation.

In its January report on global economic prospects, the World Bank raised its estimate of GDP growth in the euro area in 2022 to 3.3%, mainly on account of the favourable economic developments during the summer. It is forecasting zero growth for this year,

Figure 1.1: **Survey indicators of economic developments in the euro area**

Purchasing Managers' Index (PMI) | Confidence indicators



Note: Dashed line represents the value of the last observation.
Source: IHS Markit. Latest data: December 2022.

Source: Eurostat. Latest data: December 2022.

[1] Following the encouraging economic growth in the second quarter of last year, the adverse effects of the energy crisis, high inflation and tighter financing conditions began to be seen in the third quarter, which was reflected in a slowdown in quarterly GDP growth to a still-solid 0.3%. The main driver of the slowdown in quarterly growth was the negative contribution by net trade (-1.1 percentage points), amid a high 4.2% growth in imports as a result of an increase in Irish imports. The strong growth recorded by Irish multinationals was also a major factor in growth in gross fixed capital formation (3.6%), which contributed 0.8 percentage points to quarterly GDP growth. Quarterly growth in gross fixed capital formation would stand at merely 0.2% if Ireland was excluded. While quarterly growth in private consumption remained encouraging (0.8%), the year-on-year rate slowed significantly from 5.5% to 1.8%, which is also reflected in a decline in year-on-year GDP growth from 4.2% to 2.3%.

a downward revision of 1.9 percentage points compared with the June forecasts. Amid a more stable situation on the energy markets and easing inflation, the euro area economy is expected to gradually recover in 2024 to record growth of 1.6%

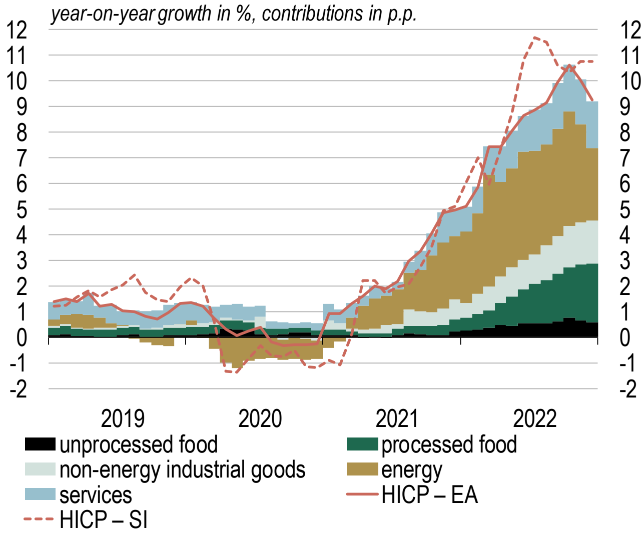
December's fall in inflation in the euro area was attributable to a decline in the contribution by energy prices, but the rate nevertheless remained above 9%.

Year-on-year headline inflation as measured by the HICP fell to 9.2% in the euro area, down from 10.1% in November (see Figure 1.2). The fall in inflation was attributable to a significant fall in energy prices, which were down 6.5% in monthly terms, slowing their year-on-year rate of growth to 25.7%. Various factors played a part: the fall in market prices of gas and electricity due to mild winter in Europe, further falls in fuel prices, and numerous government measures to reduce energy prices for households, including one-off government support for heating bills in Germany. The contribution to headline inflation by energy prices thus declined by 1 percentage point, while the contributions by the other main subcomponents increased slightly.

Food prices were up 13.8% in year-on-year terms at the end of the year, slightly more than in November, driven by current growth in prices of processed food. Prices of unprocessed food were unchanged in current terms, which slowed their year-on-year rate of growth, partly in reflection of the high base effect from the previous year and a shift in seasonal patterns. Meanwhile energy prices and prices of fertilisers remain high despite individual price falls, and together with the continuing rise in food prices are driving services prices upwards, the year-on-year rate of growth strengthening to 4.4% in December. Prices of non-energy industrial goods also strengthened: they were up 6.4% in year-on-year terms, amid high producer prices and persistent cost pressures in production chains. This raised core inflation excluding energy and food to 5.2% in December.

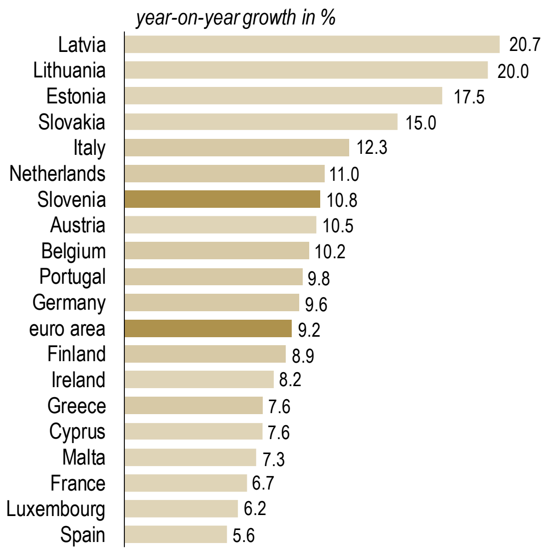
Figure 1.2: **Inflation in the euro area**

Contributions to headline inflation in the euro area



Source: ECB, Eurostat, Banka Slovenije calculations.
Latest data: December 2022.

Inflation among the euro area members – December 2022



Source: Eurostat.

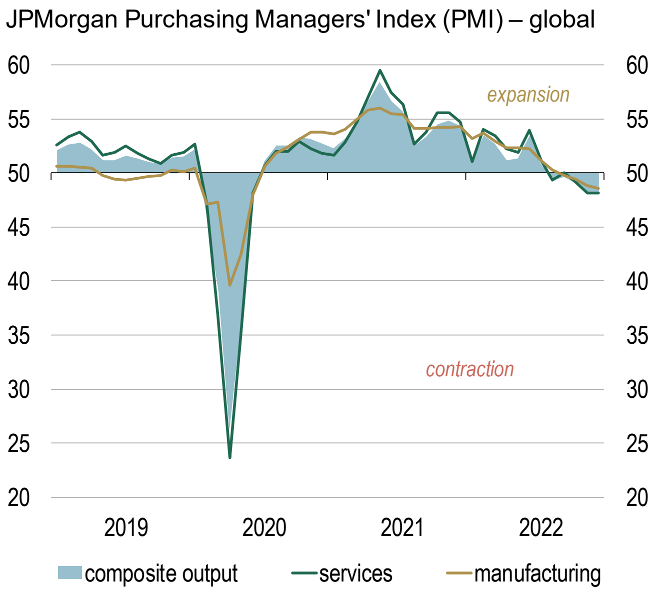
There remains great differences in inflation rates between euro area countries, particularly in energy prices, where alongside the variations in the national energy mix, governments are also making use of different forms of fiscal measures for different periods. Inflation in Slovenia outpaced the euro area average by 1.6 percentage points in December, although the contribution to headline inflation made by energy prices was 0.5 percentage points lower than in the euro area overall, while the contributions made by food, services and non-energy industrial goods were 2 percentage points higher in total.

The macroeconomic situation in the global economy deteriorated in the final quarter of last year, as demand cooled rapidly because of high prices.

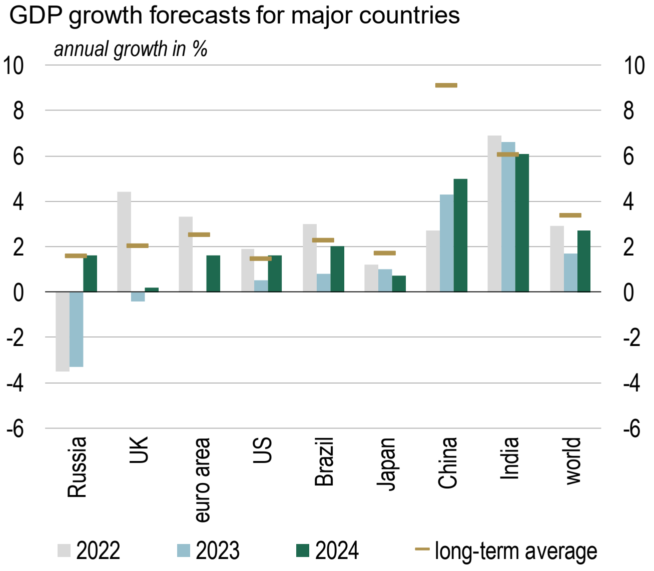
The composite PMI declined to average 48.4 points over the final quarter, down 6.1 points on a year earlier, and the lowest figure since 2009 (other than in the pandemic year of 2020).[2] In December it was up slightly on the previous month, but nevertheless remained below the 50-point mark for the fifth consecutive month (see Figure 1.3). The improvement was attributable to a smaller monthly decline in global manufacturing output as the situation in supply chains eased. Evidence of the sharp shortening of supply terms comes from the manufacturing PMI, which in December reached its lowest value since January 2020, i.e. just before the outbreak of the pandemic.

The situation in manufacturing remained difficult at the end of 2022, with firms continuing to report a sharp decline in new orders – indicative of further cooling in demand at the global level – but also the easing of price pressures. The services PMI remained in the zone of contraction (see Figure 1.3). The US saw the largest decline in activity in

Figure 1.3: **Global economic situation and GDP growth forecasts**



Source: Bloomberg. Latest data: December 2022.



Note: The World Bank forecasts are used (January 2023).
Source: IMF, World Bank.

[2] The economy was still in relatively good shape in the third quarter. The recovery in China and the US meant that global GDP strengthened in the third quarter of last year after stagnating in the previous quarter, although growth as estimated by the OECD remained moderate, as a result of high energy prices and a deterioration in consumer purchasing power. After declining in the second quarter of last year, GDP in China rose by 3.9% in the third quarter as containment measures were lifted, while India and the US both saw quarterly rises in GDP (of around 0.7%). Elsewhere the economic situation worsened: growth slowed to approximately 0.4% in the euro area and Brazil, while Japan and the UK saw GDP contract by 0.2%.

December of last year of any major economy according to the PMI figures, but the economic situation also deteriorated in Russia and Brazil. The PMI improved elsewhere, but remained below the key 50-point mark. The sole exception was India, which recorded the highest level of this indicator of the last decade.

Despite numerous measures to mitigate the impact of high energy and food prices, according to the World Bank's latest forecasts released in January global GDP growth will slow to 1.7% this year (see Figure 1.3), the lowest rate in almost three decades (with the exception of the global financial crisis and the pandemic). This is 1.3 percentage points less than forecast in June. The downward revision is attributable to tightening monetary policy and financing conditions, low confidence, and high energy prices. Global economic growth is forecast to rise to 2.7% next year as inflationary pressures ease, but will remain below its long-term average (see Figure 1.3).

2 Monetary Policy and Financial Markets

With inflation still running high, major central banks are continuing with their key interest rate hikes.

Headline inflation rates remain high in the euro area, the US and most other countries; although especially in the US there have been signs in recent months that inflation might have already peaked. In line with the figures showing persistently high inflation, major central banks have continued to raise their key interest rates, albeit with slightly less intensity. In the Eurosystem we raised all three key interest rates by 0.50 percentage points in December, following hikes of 0.75 percentage points in September and October (taking the total rise in 2022 to 2.50 percentage points). We also announced the beginning of the gradual wind-down of the securities portfolio under the APP programme from March 2023 onwards, with an average of EUR 15 billion being allowed to mature each month in the second quarter of this year.

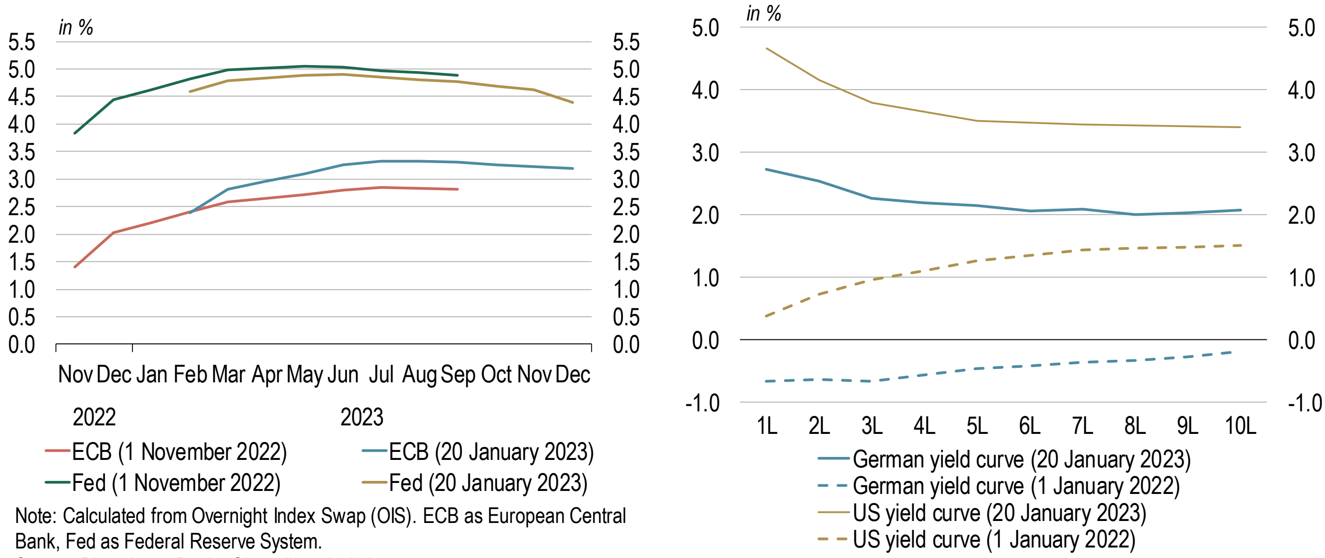
The Fed also continued with its interest rate hikes. It raised rates by 0.50 percentage points in December of last year, having raised them by 0.75 percentage points in each of the four previous meetings (taking the total rise to 4.25 percentage points in 2022). The size of the key interest rate hikes was also scaled back by the central banks of the UK, Canada, Australia and Norway.

Given the stubbornly high inflation in the euro area, the markets are currently expecting a higher terminal level for the interest rate on the ECB deposit facility than they did in November of last year. According to current overnight index swap rates, market participants have very high expectations that a terminal rate of 3.25% will be reached in the summer of 2023, compared with the expectations of a rise to 3.00% in November. Contrastingly, given the visible signs of a slowdown in inflation in the US, the market expectations with regard to the terminal level of the Fed's key interest rate have declined slightly (to a range of 4.75% to 5.00% by the spring of 2023; see Figure 2.1).

Figure 2.1: **Expectations of key interest rates at the ECB and the Fed, and German and US yield curves**

Implied key policy rate levels for ECB and Fed

US and German yield curve



Note: Calculated from Overnight Index Swap (OIS). ECB as European Central Bank, Fed as Federal Reserve System.
Source: Bloomberg, Banke Slovenije calculations.

Source: Bloomberg, Banka Slovenije calculations.

The mood of investors with regard to higher-risk assets has improved slightly in recent months, as the resilience of global economic growth and the mild winter in Europe have slightly reduced concerns about the impact of high interest rates on the economy.

Under the influence of investors' expectations that in light of the persistently high inflation, the Eurosystem is not yet close to finishing its interest rate hikes, yields on German government bonds rose again towards the end of last year (taking the total rise in 2022 to 3.40 percentage points at shorter maturities, and 2.75 percentage points at longer maturities). They then fell in the early part of this year, as expectations of further interest rate hikes in the Eurosystem were slightly reduced amid a further fall in energy prices and the gradual slowing of inflation in the US. The latter also marginally reduced the expectations of further interest rate hikes by the Fed, which was reflected in a fall of US Treasury yields (in 2022 they rose by 3.70 percentage points at shorter maturities, and 2.35 percentage points at longer maturities).

In the wake of the slight easing of concerns surrounding the impact of high interest rates on the economy, and the reopening of the Chinese economy, the mood among investors regarding higher-risk asset classes has improved slightly in recent months. The leading US equity index, S&P 500, has risen slightly since the beginning of the year, by 1.6% (having fallen by 19.7% in 2022, the largest annual fall since 2008). In light of the mild winter and a fall in benchmark European natural gas prices to a level last seen before the outbreak of the war in Ukraine, investors in Europe have been slightly more optimistic. This was reflected in a rise of the leading European equity index, STOXX Europe 600, by 6.4% since the beginning of the year (having fallen by 12.9% in 2022). The positive mood was also reflected in a sharp narrowing in the spreads of private-sector bonds over the benchmark government bonds.

The improved sentiment on the financial markets, amid investors' expectations that the Fed will finish its interest rate hikes in the second quarter of this year, had an adverse impact on the US dollar, which has lost 8.5% against a basket of major global currencies since the beginning of November. Conversely, the euro rose against most major global currencies, driven by the rising expectations of further rises in key ECB interest rates. The fall in the value of the US dollar contributed to the increase in the price of gold, which has gained 18.3% since the beginning of November.

3 Domestic Economy

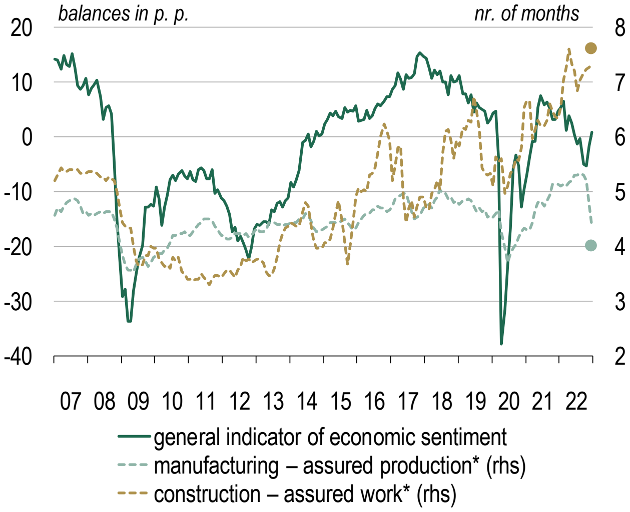
The economic sentiment improved at the end of last year, and according to the available indicators, the dynamics in demand in the final quarter were biased towards sectors tied to the domestic market.

The economic sentiment indicator turned positive in December for the first time since June. It was up 6.1 percentage points on its low of last year reached in October (see Figure 3.1). The rise in confidence was seen overall in November and December by all sectors and by consumers. Confidence in the economy nevertheless remains lower than a year ago.

Manufacturing firms were again pessimistic in December in their assessments of current demand, with their estimation of the number of months of assured production at its lowest since July 2020 (see Figure 3.1). At the same time, they significantly raised their assessments of output and exports in the first quarter of this year. By contrast, the situation in construction remains very robust: in December, firms again assessed their activity, order books, and months of assured work (see Figure 3.1) as very high. Further evidence of the maintenance of solid domestic demand comes from the survey indicators in retail and other private-sector services.

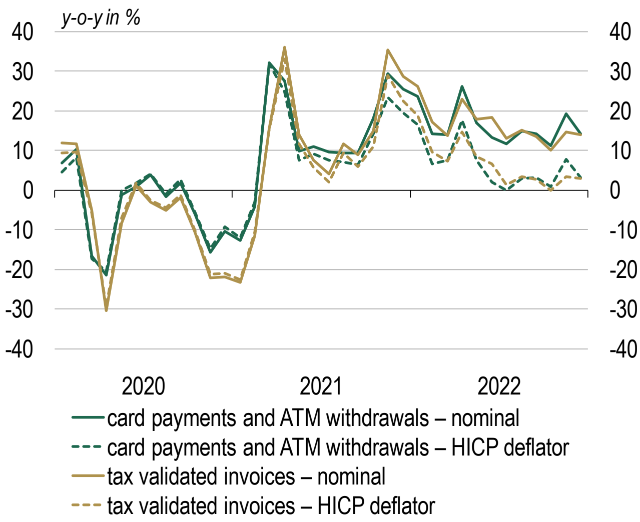
Figure 3.1: **Economic sentiment indicators and high-frequency indicators of consumption**

Selected indicators of economic sentiment



Note: * 3-month moving sums apart from the dots which represent the latest data.
Source: SORS, Banka Slovenije calculations. Latest data: December 2022.

High-frequency indicators of consumption



Source: SORS, FURS, Bankart, Banka Slovenije calculations.
Latest data: December 2022.

Having improved in the final quarter of last year, the mood of consumers underwent a downward reversal in January. Compared with December they were more pessimistic with regard to the current and expected financial situation in the household, the general economic situation in the country, and major purchases.

Sectors dependent on the domestic market were to the fore in the dynamics in demand. Manufacturing output was close to stagnation last year: in November, it was up 0.6% on December 2021 and 0.3% in year-on-year terms.[3] Contrastingly, activity rose sharply in construction: the amount of construction put in place in November was up fully 43.6% in year-on-year terms. Aggregate domestic demand did slow last year, but remained solid even at the end of the year. Real (as measured by the HICP deflator) year-on-year growth in total card payments and ATM withdrawals and in the value of invoices registered with tax authorities actually rose slightly at the end of last year, despite the inflation rate of more than 10% (see Figure 3.1).

Box 3.1: **Nowcasts for quarterly GDP growth**

The average estimate from the extensive set of nowcasting models suggests quarterly GDP growth of 0.1% in the final quarter of last year, with a slight discrepancy between the survey indicators and the indicators of economic activity.

The current nowcast for quarterly GDP growth for the final quarter of last year stands at 0.1% (see Figure 3.1.1).[4] The realisation of this nowcast would entail annual GDP growth of 4.7% in 2022, given the current estimates of last year's quarterly dynamics.

The nowcasts reflect the improvement in the survey indicators in the quarter in question, and the slightly mixed signals in the available indicators of economic activity. This is also reflected in the chart showing the distribution of nowcasts (see Figure 3.1.1).

The current dynamics in estimated economic activity are primarily attributable to the monthly improvements in economic sentiment indicators in November and December, most notably the rising indicators for services, retail, consumers and manufacturing.

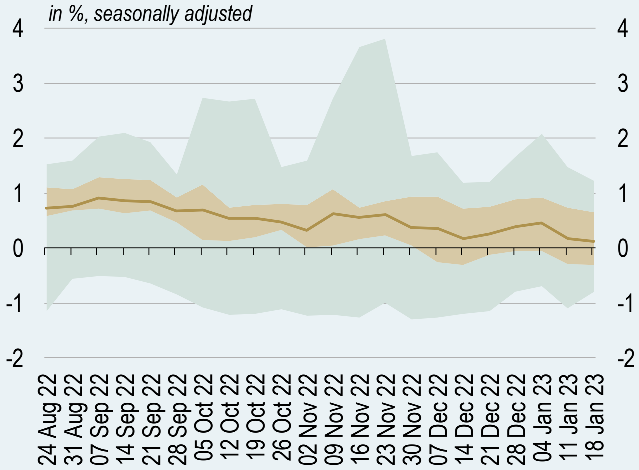
However, these trends have for now not been fully reflected in the available indicators of economic activity. After falling by 0.9% in October alone, industrial production rose by 0.6% in November. Mixed signals were also seen in the value of construction put in place and in services and trade production. The former rose by 9.7% in October before falling by 3.4% in November, while the latter fell by 1.8% in October.

[3] There remain pronounced differences in the year-on-year performance of different subsectors of manufacturing. For example, output in the manufacture of other transport equipment was up 36.0% in year-on-year terms, while it was down 15.4% in the manufacture of paper and paper products. Ten of the subsectors saw growth, and 11 saw contractions. After a decline of 3.9% in October, aggregate industrial production was down 3.6% in year-on-year terms in November, because of the extended refit of the Krško nuclear power plant and the disconnection of Šoštanj power station to save coal amid the technical difficulties at coalmine in Velenje.

[4] The nowcast is entirely model-based, and does not incorporate any expert assessment of current macroeconomic developments. The set of 67 forecasting models consists of various dynamic factor models, and also PC, (U)MIDAS, (B)VAR, ARDL and bridge models. The changes in quarterly GDP growth forecasts over the forecast quarter are mostly related to releases of high-frequency data, while fluctuations are to a lesser extent also caused by re-estimation of the model parameters.

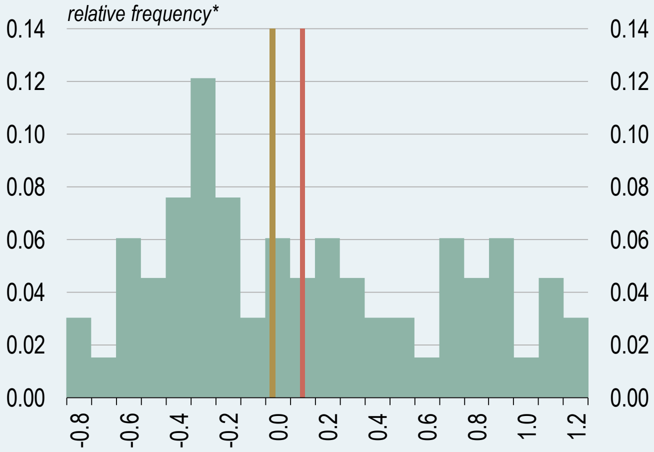
Figure 3.1.1: **Technical nowcast for GDP growth**

Model estimates of quarterly GDP growth – Q4 2022



Note: Graph shows model estimates of quarterly GDP growth. The darker interval represents values between the 25th and the 75th percentiles of all estimates. Average model estimate of quarterly GDP growth is represented by the line. Date of estimate: 18 January 2023.
Source: Banke Slovenije calculations.

Histogram of quarterly GDP growth estimates – Q4 2022



Note: Distribution of model estimates of quarterly GDP growth in Q4 2022. The vertical gold line shows the median and red the average of all estimates. Date of estimate: 18 January 2023. * Relative frequency represents the share of models that estimate a certain growth in the entire set of models.
Source: Banka Slovenije calculations.

4 Labour Market

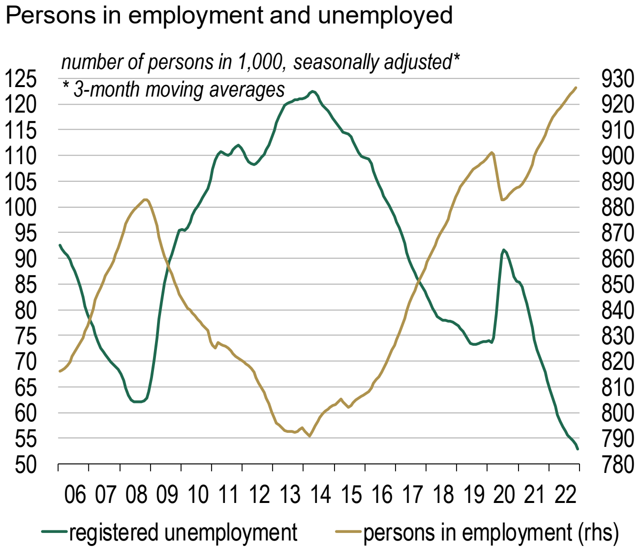
The labour market remains robust, and wage growth remains moderate for now, even amid a major labour shortage.

The number of persons in employment[5] reached a new record high of 911,003 in November of last year. The year-on-year increase of 2.1% was unchanged from October, and was down just over 1 percentage point on the beginning of the year (see Figure 4.1). The year-on-year growth remains broadly based across sectors, and highest in construction. Registered unemployment did rise in December, which was attributable to the seasonal effects of temporary employment contracts coming to an end at the end of the year, but its average of 56,665 over the year was the lowest figure to date, and was down 23.8% on 2021. The registered unemployment rate also remains low: it stood at 5.4% in October, down 1.4 percentage points in year-on-year terms, but up 0.1 percentage points on its record low in September.

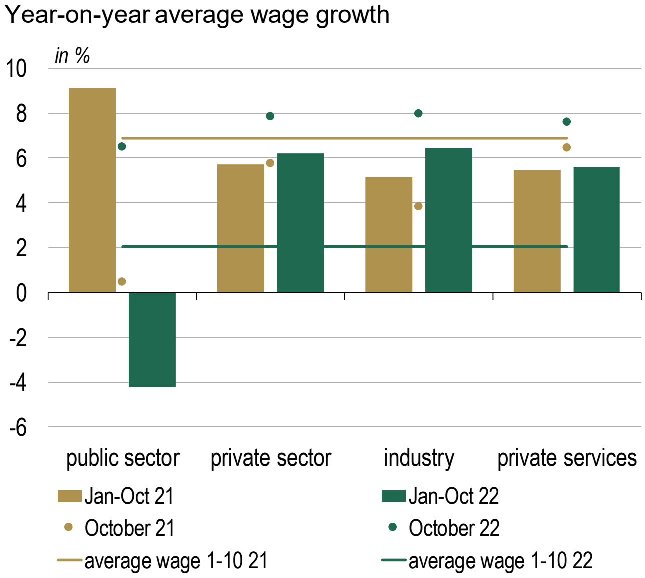
There remain large imbalances on the labour market. The survey figures of the SORS and the Employment Service point to further growth in employment in the first half of the year, where the occupations most in demand will include those where firms are already having difficulty in hiring. The *Employment Preview* survey conducted by the Employment Service last autumn reveals that more than half of employers are facing shortages of qualified workers, with the most pronounced difficulties being seen at large enterprises. More than two-thirds of firms cited a shortage of workers on the domestic labour market as a reason for difficulty in hiring, for which reason they have extended

[5] Excluding self-employed farmers.

Figure 4.1: **Labour market**



Source: SORS, Banka Slovenije deseasonalisation and calculations.
Latest data: registered unemployment – December 2022, persons in employment – November 2022.



Note: Industry consists of BCDE activities and private services of G-N;R-S.
Source: SORS, Banka Slovenije calculations.

their hiring processes, sought workers abroad, and introduced overtime. Other countries in the euro area are also facing a tight labour market (see Box 4.1).

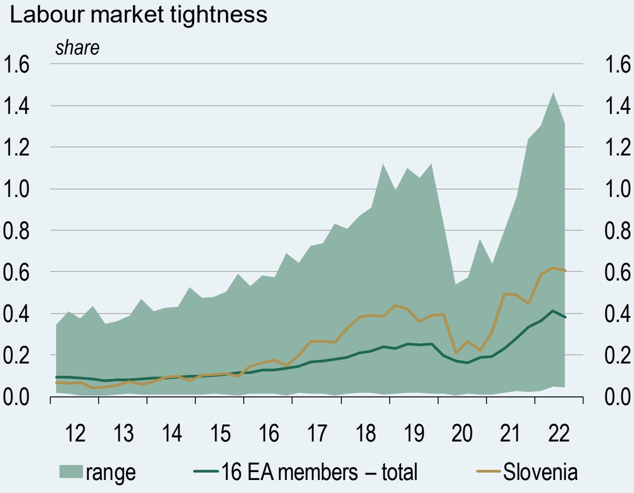
Year-on-year growth in the average gross wage is continuing to strengthen, but remains moderate for now, and is being outpaced by inflation and by productivity growth (see Box 4.2). It stood at 7.3% in October of last year. It began to strengthen in the middle of the year as the effects of the abolition of the majority of pandemic bonuses in the public sector in July 2021 dropped out of the year-on-year calculations, and as wages rose in the private sector. Wage growth in the latter stood at 7.9% in October, while the rate in the public sector was just 1.4 percentage points slower, the first time in a long period that the rates had roughly equalised. The most notable strengthening within the private sector was in industry, where according to the latest figures growth in the average wage is outpacing the comparable growth in private-sector services by approximately 0.5 percentage points (see Figure 4.1). Year-on-year growth in the wage bill also strengthened slightly in October (to 8.8%). The minimum wage was raised by 12.0% in January to EUR 1,203 gross.

The labour market remains very tight, despite the slowdown in economic activity.

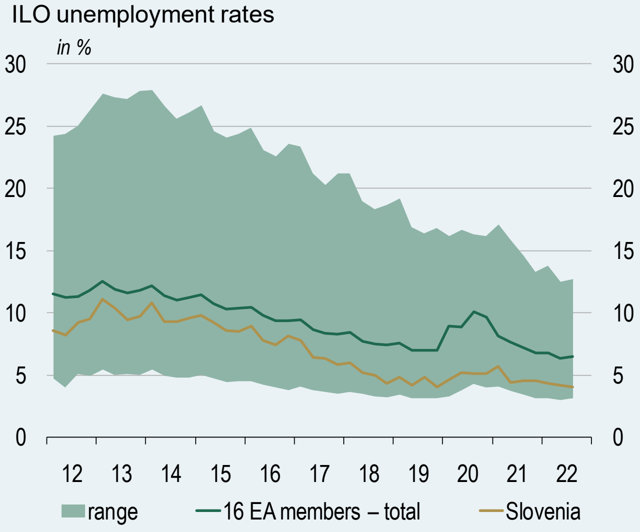
The tightness of the labour market is evidenced in the relatively large ratio of vacancies to jobseekers, as a result of which the matching efficiency on the labour market is declining and the share of firms having difficulties in hiring workers is rising. The indicator of labour market tightness in this box is calculated as the ratio of vacancies to unemployment.[6] The indicator reflects demand for labour relative to the available supply on the labour market, whereby the latter takes no account of structural unemployment or the potential additional labour force.[7] Given the limited availability of data on vacancies, the calculation of the indicator takes no account of three-euro area countries: Estonia, Italy and Malta.

As can bee seen in Figure 4.1.1, labour market tightness in the countries concerned remains high, despite declining slightly in the third quarter of last year. The indicator hit its record high in the second quarter of last year, with an overall value of 0.4 for the countries in question, although there was great variation between them. The indicator exceeded 1.0 in three countries (Germany, the Netherlands and Austria), which means that employers there notified more job vacancies than there were unemployed people available. Tightness then declined in the third quarter, driven by a rise in unemployment and a decline in the number of vacancies alike. Tightness remains highest in Germany and the Netherlands, where the indicator still exceeds 1.0, and these two countries also have the lowest unemployment rates. The unemployment rate in the observed countries stood at 6.5% in the third quarter of last year, just 0.2 percentage points above its record low of the previous quarter (see Figure 4.1.1). As in the majority of the observed countries, tightness also declined slightly in the third quarter in Slovenia, but remains at a historically high level.

Figure 4.1.1: **Labour market tightness in euro area countries**



Note: Due to the limited availability of data on the number of vacancies, 3 EA Member States are excluded from the comparison: Estonia, Italy and Malta. Labour market tightness indicator is calculated as the share of job vacancies in unemployment.
Source: Eurostat, Banka Slovenije calculations. Latest data: Q3 2022.



Note: The calculation includes the 16 EA Member States, excluding Estonia, Italy and Malta. Age class: 15-74 years.
Source: Eurostat, Banka Slovenije calculations. Latest data: Q3 2022.

[6] The time series for unemployment refers to the 15 to 74 age group, while the data for vacancies refers to Sectors B to S. The data for France solely takes account of firms with more than ten employees. The results are comparable to those of the ECB.

[7] Detailed analysis of the potential additional labour force in the Slovenian labour market is given in Box 2.1.3 of the December 2022 issue of the Review of macroeconomic developments with projections.

Wage growth lagging behind productivity growth and inflation is cyclically expected, as the gap between wage growth on one side and deflation and falling productivity on the other widened during the pandemic.[8]

Over the long term wage growth[9] moves within the rough bounds set by labour productivity, particularly in the private sector, and keeps up with inflation so that consumers do not lose purchasing power. This is what the data since 1997 shows for Slovenia and for the euro area (see Figure 4.2.1). The growth trend in both is similar, although the dynamics are greater in domestic variables owing to the catch-up effect, similarly to other newer members of the euro area.

In certain periods (particularly pronounced during the most recent global crises), wage growth has significantly outpaced inflation and productivity growth because of its rigidity. Deviations of this type are usually followed by a correction as wage growth lags at least one variable or both, and this is indeed being seen now (see Figure 4.2.1). This normalisation is particularly pronounced because of the complex responses to the pandemic and the war in Ukraine, which triggered multiple shocks on the supply and demand sides. Inflation too is therefore higher than it has been in decades, as are the geopolitical tensions, which is altering the expectations of the markets and allowing for the possibility of deviating from previous trends.

In Slovenia nominal wages over the year to the third quarter were up 3.2% in year-on-year terms, compared with productivity growth of 11.4% and inflation of 7.8%.[10] By contrast, annual wage growth had outpaced productivity growth and inflation over the previous three years, by an average of almost 3 percentage points and 4 percentage points respectively, and by twice as much during the peaks of 2020 and 2021[11] (see Figure 4.2.1). The euro area also saw divergence between wage growth and inflation and productivity growth during and after the pandemic, but it was significantly smaller. Wage growth over the year to the third quarter stood at 4.1%, 1.5 percentage points and 3.0 percentage points respectively less than productivity growth and inflation, having exceeded them by just over 2 percentage points annualised at the individual peaks during the pandemic (see Figure 4.2.1).

The tightness of the domestic and euro area labour markets (for more, see Box 4.1), and the high inflation and anticipated rises in national minimum wages across the euro area are currently creating upward pressure on wages. The ECB's expectation is that wage growth will be very high over the next few quarters, before slowing under the influence of significantly lower economic growth and the uncertainty surrounding the economic outlook.[12] In the current situation of high inflation and forecasts of a cooling economy, demands for significant wage rises are increasing the risk of a wage-inflation spiral. The IMF (2022) estimates it to be limited for now, as the underlying inflation shocks are not coming from the labour market and the decline in real wages is reducing

[8] This box compares variables in nominal terms.

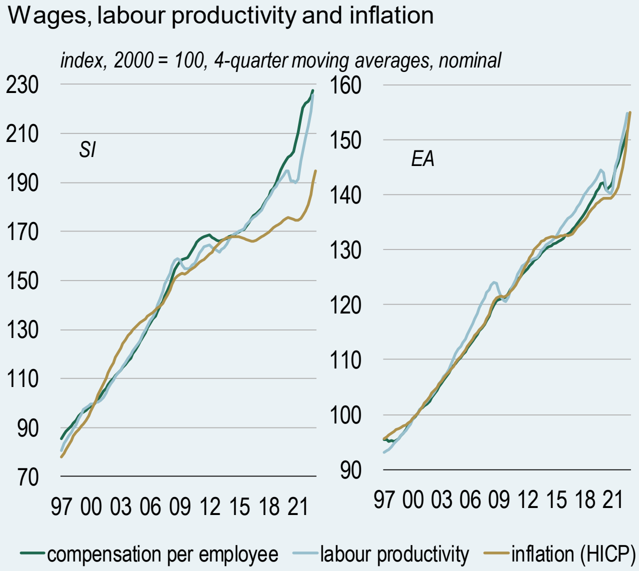
[9] The wage variable in this box is represented by compensation of employees per employee (according to national accounts statistics).

[10] These are year-on-year comparisons of the average level of the variables over the last year (i.e. Q4 2021 to Q3 2022) relative to the preceding year (i.e. Q4 2020 to Q3 2021).

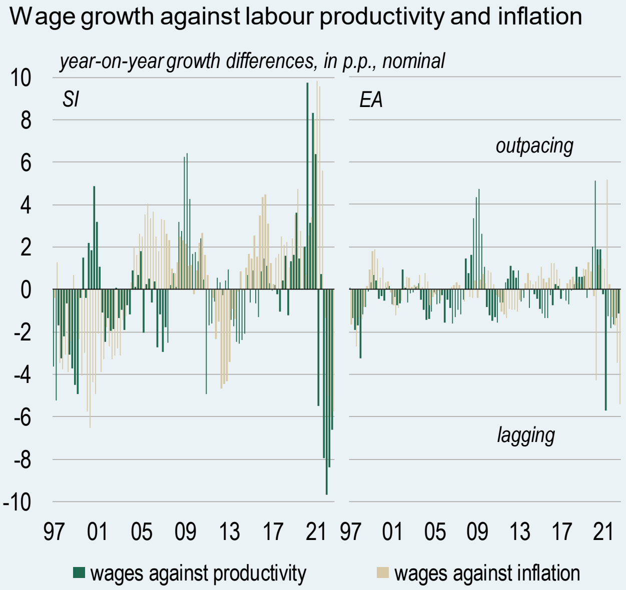
[11] The results of the analysis were also affected by the volatility in economic activity (and consequently in productivity) and the effects of job preservation measures during the pandemic and the payment of pandemic bonuses in exposed occupations, which make it harder to interpret the majority of labour market variables and to make international comparisons.

[12] ECB – Economic Bulletin.

Figure 4.2.1: **Wages, productivity and prices in Slovenia and the euro area**



Source: Eurostat, Banka Slovenije calculations.
Latest data: Q3 2022, except inflation: Q4 2022.



Source: Eurostat, Banka Slovenije calculations. Latest data: Q3 2022.

price pressures, while central banks (including the ECB) are tightening monetary policy and thus reducing inflation expectations.[13] Avoiding a loop of prices and wages feeding off each other nevertheless necessitates support from moderate fiscal policy, including in setting wages in the public sector.

[13] IMF – World Economic Outlook.

5 Current Account

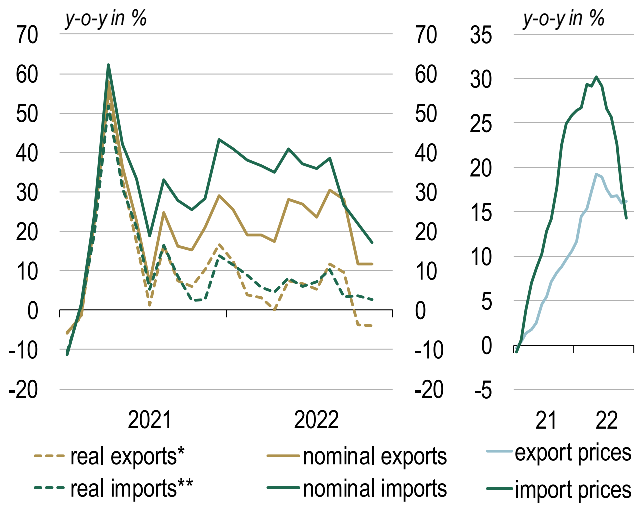
Export developments slowed towards the end of last year, primarily on account of weaker demand on EU markets, but imports also slowed, in part because of slower growth in import prices.

Nominal year-on-year growth in merchandise trade slowed towards the end of last year (see Figure 5.1). On the export side, it was down 11.7 percentage points and 15.6 percentage points respectively on the third quarter in October and November. Exports were actually down on a year earlier in real terms, if domestic producer prices on the foreign market are taken into account (see Figure 5.1). The nominal contribution by energy exports declined sharply, but lower growth was also evident in the majority of other product categories, most notably in various machinery and metal products. In geographical terms the slowdown in export growth was driven by EU Member States, most notably Italy and Croatia, while exports to Russia are continuing to strengthen. Amid a marked slowdown in year-on-year growth in import prices in November of last year (to 14.3%), nominal year-on-year growth in merchandise imports halved relative to the third quarter to 17.2%. One of the main drivers was a decline in the contribution by imports of oil and electricity, although the slowdown in growth was again evident in most categories of goods.

Nominal year-on-year growth in services trade also slowed significantly, having averaged 34% between April 2021 and the third quarter of last year. Growth in services exports slowed to 12.8% in November, as exports of miscellaneous business services recorded a year-on-year decline for the second consecutive month, and growth in exports of transport services slowed in line with the situation in international trade. The

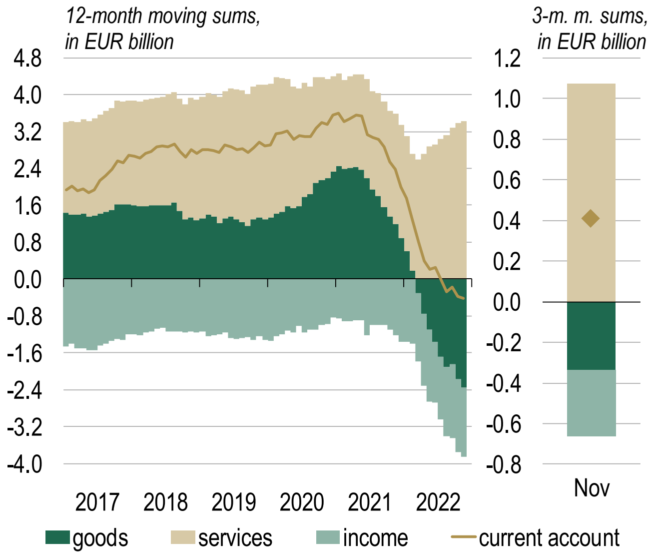
Figure 5.1: **Merchandise trade and current account balance**

Merchandise trade and industrial producer prices



Note: * Deflated using the index of producer prices for industrial products on the foreign market. ** Deflated using the import price index.
Source: SORS, Banka Slovenije. Latest data: November 2022.

Current account components



Source: Banka Slovenije. Latest data: November 2022.

contribution by exports of travel services also declined.[14] Nominal growth in services imports slowed to 8.7% in November, largely because of a year-on-year decline in imports of transport services.

The 12-month current account deficit amounted to EUR 430 million in November, the position having deteriorated by EUR 2.8 billion in year-on-year terms (see Figure 5.1). The 12-month comparison is still dominated by the widening of the merchandise trade deficit driven by higher import prices and strong domestic demand. This deficit had already reached EUR 2.4 billion by November, even more than in the period of the overheating economy before the global economic and financial crisis. The deficit in income also widened, by EUR 280 million to EUR 1.5 billion. Conversely, the services trade surplus is rising rapidly: the November figure of EUR 3.4 billion was the highest to date. This is no longer based solely on a surplus in travel and transport services, but increasingly reflects an aggregate surplus in other services. The notable 12-month deficit is primarily attributable to balance of payments developments in the period to August of last year; a small surplus was recorded over the autumn months (see Figure 5.1).

Box 5.1: **Slovenia's current account balance with Croatia**

Croatia is Slovenia's third most important export market and current account surplus with Croatia is significant due to strong merchandise exports.

According to balance of payments figures, exports of merchandise and services to Croatia over the 12 months to November of last year were up 42.5% in year-on-year terms, fully 18.5 percentage points more than aggregate growth in exports. Croatia's share of total exports stood at 9.6% (see Figure 5.1.1), ranking it once again slightly above Austria. According to SORS figures, the largest components of Slovenia's merchandise exports are oil and refined petroleum products, road vehicles, electricity, medical and pharmaceutical products, non-ferrous metals, and electrical machinery and appliances.[15] The main services exports according to balance of payments figures are travel services, which account for 43.9% of total services exports, followed by business services, transport services and construction services.

Imports are also rising fast: according to balance of payments figures, imports over the 12 months to November were up 39.0% in year-on-year terms, 6.4 percentage points more than aggregate growth in imports. Excluding the transmission of electricity across Croatia to Slovenia and then to Italy, there is considerable diversity in the make-up of merchandise imports according to SORS figures. Only non-ferrous metals, road vehicles, mineral products, and cereals and cereal products recorded shares of more than 3%. Since the normalisation of conditions in international tourism, imports of travel services have been rising markedly: the annual amount of EUR 647 million has already passed its pre-pandemic peak, and they accounted for 58.0% of total services imports.

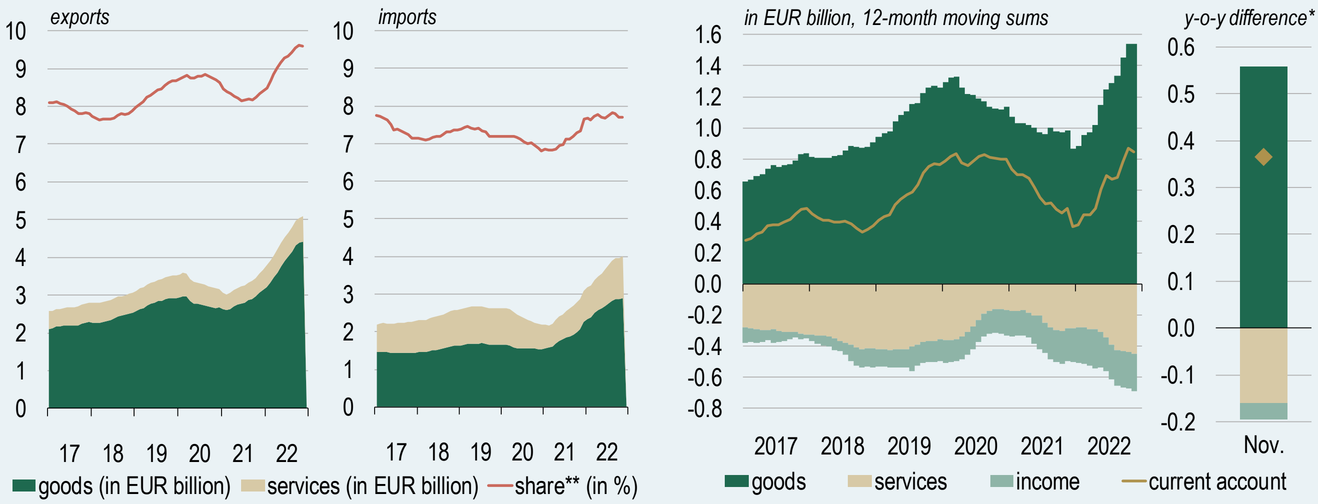
[14] Year-on-year growth in exports of travel services increased to 54.8% in November, the highest figure since June. They accounted for 8.4 percentage points of the 12.8% growth in aggregate services exports, 4.0 percentage points less than in the third quarter of last year. This was attributable to the smaller share of exports of travel services in November 2021 compared with the summer months, when the seasonal high is usually seen.

[15] The exports of oil and refined petroleum products primarily consist of re-exports by Petrol, which in the autumn of 2021 expanded its presence in the Croatian market, while the electricity exports come from Krško nuclear power plant, which is under shared ownership with Croatia.

Figure 5.1.1: **Slovenia's current account balance with Croatia**

Slovenia's merchandise and services trade* with Croatia

Slovenia's current account balance with Croatia



Note: * 12-month moving sums. ** Share of Croatia in Slovenia's total exports (imports) of goods and services.
Source: Banka Slovenije. Latest data: November 2022.

Note: * Change in EUR billion in the last 12 months compared to the same period a year ago.
Source: Banka Slovenije. Latest data: November 2022.

Croatia is Slovenia's fourth most important trading partner on the import side, accounting for 7.7% of total imports (see Figure 5.1.1), but it is ranked first in terms of services imports with a 14.5% share, thanks to tourism.

Slovenia's 12-month current account balance with Croatia is in permanent surplus, and its figure of EUR 849 million in November of last year was one of the largest to date. The increase over the last year is attributable to a widening merchandise trade surplus (see Figure 5.1.1), driven largely by re-exports of oil and refined petroleum products.[16] Services trade is in deficit as expected: imports of travel services from Croatia are much larger than exports, and Slovenian visitors were ranked second in terms of overnight stays last year. The 12-month deficit in travel services amounted to EUR 354 million in November, while the total services deficit amounted to EUR 448 million. There is also a deficit in income. The increasing hiring of Croatian workers means that labour income is the dominant factor,[17] but capital income is also mostly in deficit, as Croatian FDI in Slovenian firms is larger than Slovenia's corresponding outward FDI.[18]

[16] According to SORS figures, the 12-month surplus of trade in oil and refined petroleum products with Croatia stood at EUR 774 million in November, up EUR 584 million in year-on-year terms. The euro price of a barrel of Brent crude was up EUR 36.4 or 63.2% over the same period. Trade in gas also recorded a notable surplus of EUR 124 million, in the wake of large price rises. At the same time, the deficit in electricity trade strengthened by EUR 381 million to EUR 462 million as electricity prices rose sharply. The aggregate surplus in other categories of products amounted to EUR 971 million, up EUR 199 million.

[17] The number of daily migrants from Croatia to Slovenia in 2021 was double that a decade earlier, and the number of Croatian nationals of working age (15 to 64) living in Slovenia was up 20.3%.

[18] Excluding real estate, Croatia's outward FDI in Slovenia in 2021 was EUR 470 million larger than Slovenia's FDI in Croatia.

6 Inflation

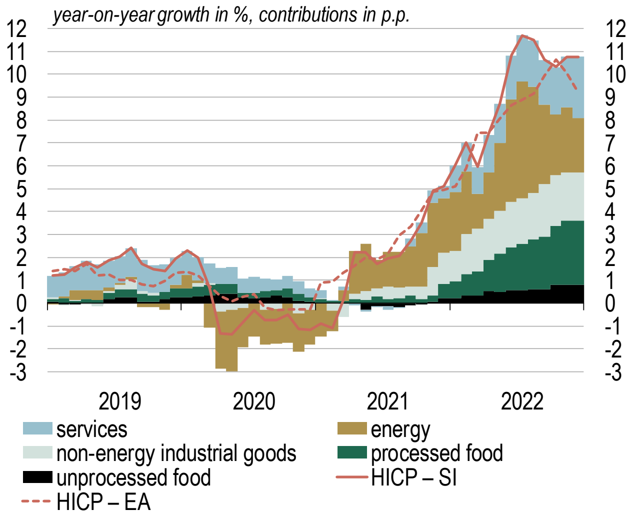
With rising prices now broadly based, headline inflation remains high despite the fall in energy prices, services prices having risen notably in December.

The price of the consumer basket was up 10.8% in year-on-year terms in December. The inflation rate was unchanged from November, an increase in service price inflation having compensated for the fall in energy prices (see Figure 6.1). Services prices were up 1.0% in current terms, their year-on-year rate of growth surging to 8.2% (see Figure 6.1). There were increases in the contributions by all categories of services, most notably health services,[19] catering services, and sporting services, which is indicative of the widespread nature of the pass-through of higher input costs into services prices, and the impact of wage growth, which remains limited for now. Domestic consumption also remains solid.

Growth in prices of non-energy industrial goods remains high at 6.7%.[20] Growth in import prices has slowed significantly in recent months, but remains well above 10%, while the slowdown in producer prices on the domestic market is considerably less pronounced as the year-on-year rate of growth remains above 20%. Core inflation as measured by services prices and prices of non-energy industrial goods thus rose to 7.5%, with almost half of the products and services included in the indicator recording higher price growth than this.

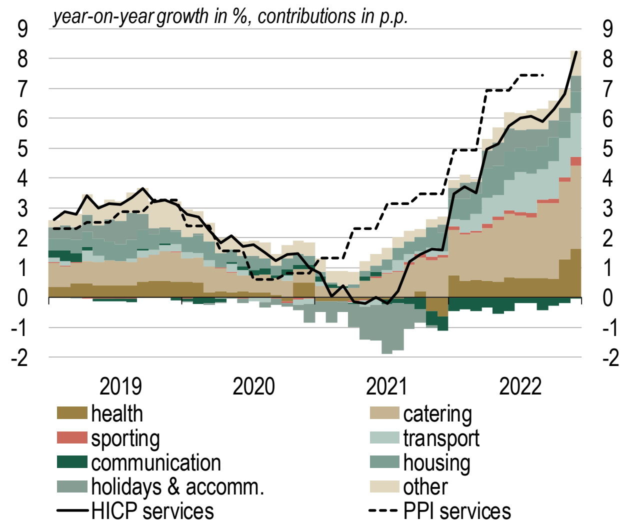
Figure 6.1: **Domestic price developments and contributions to service price inflation**

Contributions to headline inflation



Source: ECB, Eurostat, Banka Slovenije calculations.
Latest data: December 2022.

Contributions to services inflation



Source: SORS, Eurostat, Banka Slovenije calculations.
Latest data: December 2022.

[19] Following ECOICOP, we construct health services group from outpatient medical, dental, paramedical and hospital services, and private health insurance. The aggregate index reveals that health services were up 16.0% in year-on-year terms, with hospital services and general practice services up more than 20%. Services related to private health insurance, which include supplementary health insurance, were unchanged in current terms, but up 12.9% in year-on-year terms. This is attributable to an one-off discount at Vzajemna in December 2021 as their policyholders paid approximately a third of their usual premiums. The low base effect in this time series is thus raising service price inflation by 0.2 percentage points in December 2022, but it will drop out already in January 2023.

[20] Prices of non-energy industrial goods have displayed a pronounced positive trend over the last two years, amid the usual seasonal patterns. They were up 11.4% on December 2020.

The broadly based nature of price growth is a consequence of the persistence of the high inflation driven most notably last year by rising energy prices. Their contribution to headline inflation declined by 0.5 percentage points in December as prices of refined petroleum products fell during the month, however, energy prices will rise again in January as electricity rises in price.[21] Measured year-on-year energy price inflation, which slowed to 17.8% in December, will be eased slightly by the effect of last January's rise in network charges dropping out of the calculation.

Food price inflation also remains elevated. Prices of food and non-alcoholic beverages were up 18.7% in year-on-year terms in December. A fall in market prices of commodities (e.g. oil, gas, fertilisers) might slow future inflation, particularly in prices of unprocessed food, although there remain risks regarding food production related to geopolitical situation and weather conditions.

Box 6.1: **Structure of consumption and inflation according to household income bracket**

The inflation felt by households depends on the share of their expenditure that they earmark for particular goods. Higher inflation was felt last year by households for whom energy and food make up a comparatively higher share of spending.

Inflation as measured by the HICP averaged 9.3% last year. This rate reflects the rise in the average price of the consumer basket in Slovenia, but its structure can vary considerably from one household to another, as it reflects the share of spending that goes to individual categories of consumption.

Inflation was broadly based last year, but the largest contributions to headline inflation came from energy and food prices, which are basic categories in the basket of consumer essentials. All households are thus exposed to rising prices, but those who spend more of their income on the most basic consumer essentials are exposed even more.

The structure of consumption shows that households with the lowest income spend close to half of their income on food and essential housing costs, while the highest income households spend just a quarter (see Figure 6.1.1).[22] Conversely, they spend more on less-essential consumer goods and on transport, which includes car purchases. Transport accounts for a quarter of the spending of the highest-income households, compared with approximately a tenth for the most vulnerable.[23]

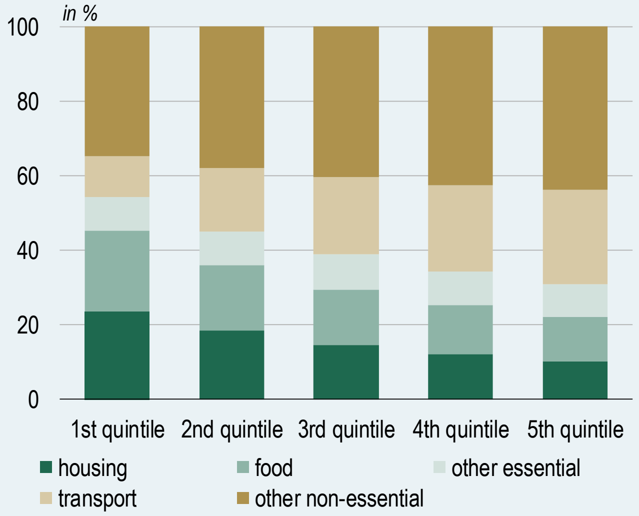
Given the elevated energy price inflation and food price inflation last year, inflation for the households with the lowest income in the second half of the year was an average

[21] From January of this year, the electricity supplier with the largest market share is raising its prices to the retail price cap set by the Decree setting electricity prices (Official Gazette of the Republic of Slovenia, No. 95/22 of 14 July 2022).

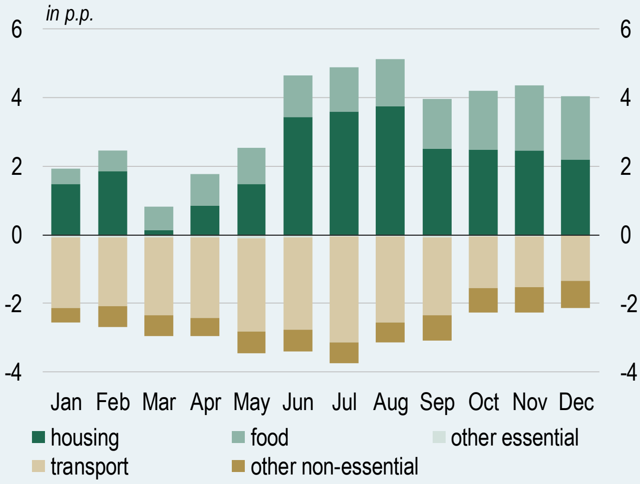
[22] The left figure illustrates the results of the Household Budget Survey conducted by the SORS in 2018. Certain categories were combined for the sake of simplicity. The housing category includes housing rents, housing maintenance and repair, water supply and various housing-related services, and electricity, gas and other fuels excluding motor fuels. Spending in connection with the purchase or renovation of flats or houses is not included. The category of other essentials includes healthcare, education and communications, while the category of other includes alcoholic beverages and tobacco, clothing and footwear, furnishings and household appliances, recreation, hotels and restaurants, and miscellaneous goods and services. The category of transport includes car purchases and air tickets.

[23] See also October 2021 issue of Economic and Financial Developments (page 76 to 83) for a more comprehensive analysis on this topic.

Figure 6.1.1: **Structure of consumption and differences in inflation with regard to household income bracket**



Note: See note 21 in the text.
Source: Household Budget Survey (HBS) – SORS, Banka Slovenije calculations.



Note: See note 23 in the text.
Source: Household Budget Survey (HBS) – SORS, Eurostat, Banka Slovenije calculations.

of 1.6 percentage points higher than the inflation faced by the highest-income households. Given the described structure of spending, the gap was mainly driven by housing costs (including electricity and heating) and food, but was also narrowed by less essential consumer goods and transport (see Figure 6.1.1).[24]

The results indicate that the most vulnerable households in income terms were comparatively more exposed to last year's rising prices. This shall be taken into account when designing and targeting measures aimed at mitigating the impact of high inflation, in particular energy and food prices.

[24] In the right figure the shares of spending on individual categories of consumption according to household income bracket are calculated from the most recent Household Budget Survey from 2018. These shares changed in 2020 and 2021 in particular because of the pandemic, which was elaborated in the selected theme entitled *Consumer price inflation across income groups, and income inequality* in the October 2021 issue of Economic and Financial Developments. Our assessment is that the structure of consumption in 2022 would have further converged to the patterns seen before the pandemic, which is reflected by the use of the shares from the most recent survey. Caution is therefore necessary in the interpretation of the results, as the actual inflation felt by income groups might be slightly different on account of changes in patterns of consumption, perhaps by a few tenths of a percentage point. The results thus allow only for a qualitative explanation of differences in inflation between the highest and lowest household income brackets with any great certainty. The figure illustrates the contributions by individual categories of consumption to the gap in inflation between the highest and lowest household income brackets.

Box 6.2: **Developments in wholesale and retail prices of gas and electricity**

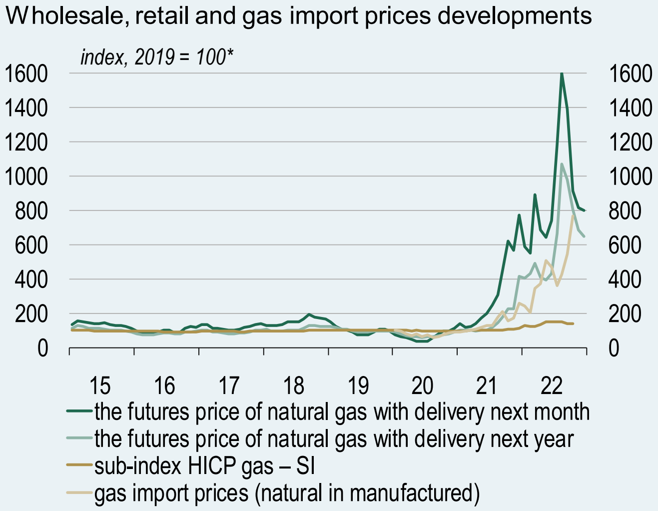
After the expiry of the government measures to mitigate rising energy prices, which are currently reducing inflation, the increase in retail energy prices over the next two years could significantly contribute to inflation, in particular as a result of the delayed pass-through of wholesale prices.

The major factors in the volatility in gas and electricity prices in recent years have been the fluctuations in demand caused by the pandemic, and the (un)availability gas supplies driven by the war in Ukraine. The steep rise in wholesale energy prices began in the second half of 2021 following the lifting of containment measures and the rebound in economic activity. In a situation of increased demand for energy, the war in Ukraine and the subsequent EU sanctions brought a profound reduction in the supply of cheap gas from Russia, which caused an additional spike to wholesale gas and electricity prices.

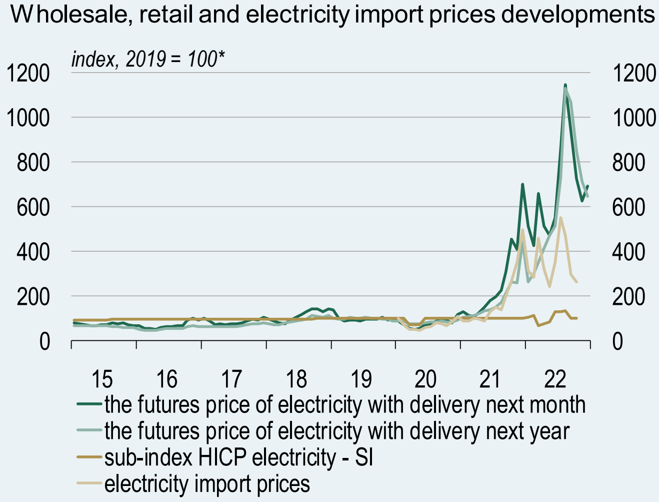
Wholesale gas and electricity prices are largely formed on the basis of supply-side and demand-side factors as the cost of the last unit needed to meet current short-term demand. Wholesale electricity prices are usually determined by the cost of producing electricity from gas, as gas is the most expensive of all the resources used to produce electricity. Demand for gas and electricity is highly price inelastic over the short term, as a result of which small changes in quantity cause large fluctuations in price, which are often temporary in nature.

Despite a fall in European gas prices in October and early November caused by the very mild weather conditions, futures prices remain well above the long-term average, in reflection of the significant risks to supply. While futures prices of gas and electricity for delivery next month are currently approximately six times higher than at the beginning of 2021, import prices, which reflect the actual price paid in international trade, are eight times higher in the case of gas, and three times higher in the case of electricity

Figure 6.2.1: **Evolution of wholesale, retail and import prices of gas and electricity**



Note: Futures prices of natural gas on the Dutch TTF exchange.
* For the gas import price index applies 2020 M1 = 100. Data for import gas prices for 2022 are provisional.
Source: Bloomberg, ECB, SORS, Banke Slovenije calculations.
Latest data: October 2022, except for futures prices: December 2022.



Note: Futures prices of electricity on the German EEX exchange.
* For the electricity import price index applies 2020 M1 = 100. Data for electricity import prices for 2022 are provisional.
Source: Bloomberg, ECB, SORS, Banke Slovenije calculations.
Latest data: October 2022, except for futures prices: December 2022.

(see Figure 6.2.1). Consequently measures have been taken at EU level to directly intervene in the wholesale gas markets to limit the adverse impact of high prices.[25]

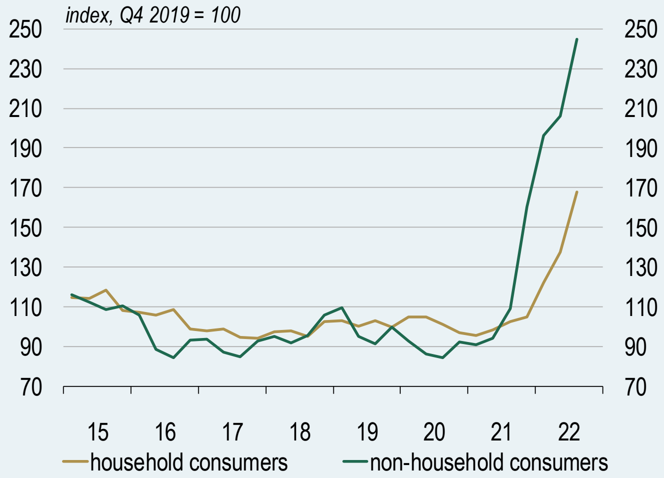
Given the persistent uncertainty surrounding natural gas supplies, and the related search for alternatives, retail energy prices have also begun to rise, although the pass-through of wholesale prices remains largely limited because of government measures.[26] The measures to mitigate rises in electricity and natural gas prices are designed to keep prices at sustainable levels for household consumers in particular.

While the retail electricity price for the average household consumer in Slovenia was 18% higher year-on-year in the third quarter of last year, the growth in retail price for the average non-household consumer was 106%. The rises in the retail prices of natural gas for the average representative of each group were somewhat larger, at 116% for non-household consumers and 64% for household consumers (see Figure 6.2.2).

After the expiry of measures in connection with high gas and electricity prices, the persistence of wholesale prices above their long-term average could lead to stronger growth in retail prices, which would extend the period of high inflation.

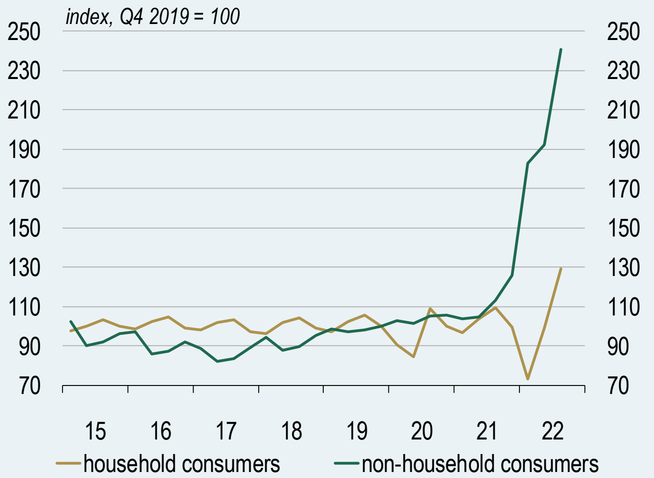
Figure 6.2.2: **Evolution of retail prices of natural gas and electricity for average household and non-household consumer in Slovenia**

Natural gas prices developments for the average household and non-household consumer in Slovenia



Note: Price for household consumers includes all taxes. Price for non-household consumers does not include VAT.
Source: SORS, Banka Slovenije calculations.

Electricity prices developments for the average household and non-household consumer in Slovenia



Note: Price for household consumers includes all taxes. Price for non-household consumers does not include VAT.
Source: SORS, Banka Slovenije calculations.

[25] European energy ministers reached an agreement in December to cap gas prices at 180 EUR/MWh. To trigger the mechanism, the benchmark gas price needs to exceed EUR 180 for three days, and the price difference compared to global LNG prices must exceed EUR 35 over the same period. The agreement will enter into force on February 15.

[26] By taking measures to mitigate rising electricity and natural gas prices, the government has limited electricity and gas prices for various groups of consumers. The currently valid measures also encompass a reduction of 50% in the contribution to support electricity generation from renewables and high-efficiency cogeneration (RSE+CHP contribution) for household and small business consumers, and cuts in excise duties and VAT.

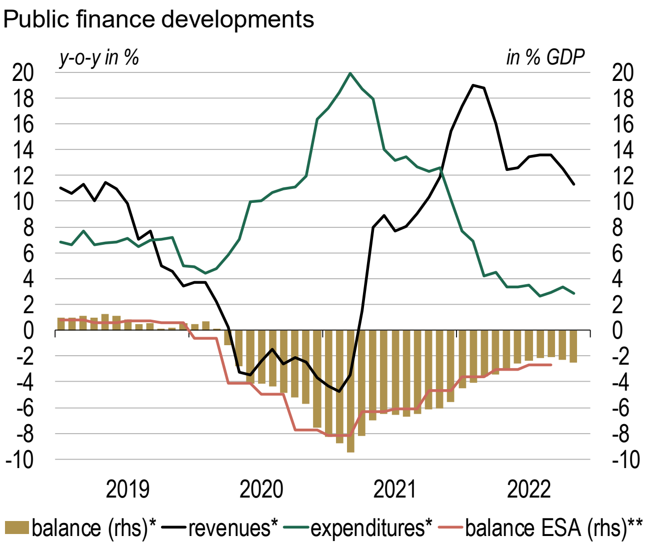
7 Fiscal position

The general government deficit narrowed significantly last year, particularly in the first half of the year. Growth in revenues slowed profoundly towards the end of the year and growth in expenditure picked up, which was reflected in a worsening position in October and November.

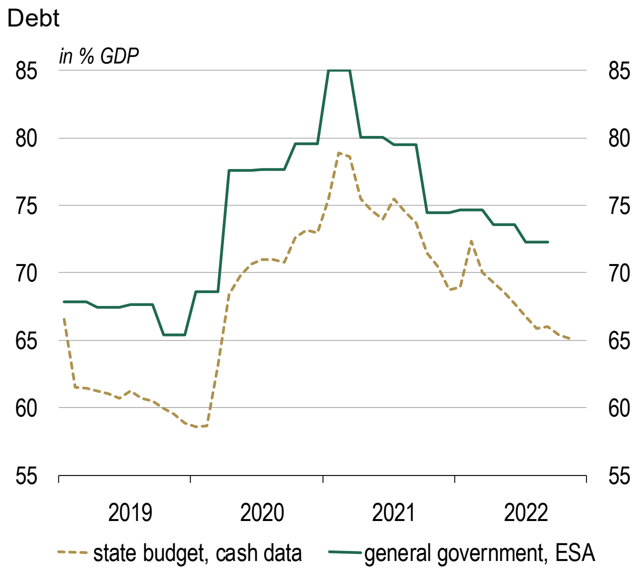
The consolidated general government deficit amounted to EUR 750 million by November last year according to cashflow methodology, significantly less than in the same period of the previous year (EUR 2.2 billion). The year-on-year improvement mainly occurred in the first half of the year, on account of a decline in pandemic-related expenditure amid high growth in revenues. The second half of the year, particularly from September onwards, saw growth in expenditure pick up, which amid the low growth in revenues in October and November led to a year-on-year deterioration in the position (see Figure 7.1). The largest increase on the expenditure side was in investment, while transfers to individuals and households also increased, in part because of measures in connection with the energy crisis. Wages in the public sector rose by 4.5% in October, in line with the agreement reached. The state budget recorded a deficit of EUR 1.4 billion last year according to preliminary figures, significantly less than planned by the revised budget (EUR 2.0 billion). The position worsened again in year-on-year terms in December, as a result of the continuing rise in investment while growth in revenues slowed.

A similar picture is presented by the quarterly figures in accrual terms. The 12-month general government deficit amounted to 2.7% of GDP in September of last year, having continued to narrow since June. The largest increase on the revenue side was in indirect taxes. Lower taxation rates mean that personal income tax and excise duties are

Figure 7.1: **Fiscal position**



Note: * 12-months sum, cash data. ** 4-quarters sum.
Source: SORS, Ministry of finance, Banka Slovenije calculations.
Latest data: November 2022, except balance ESR – Q3 2022.



Sources: SORS, Ministry of finance, Banka Slovenije calculations.
Latest data: State budget – November 2022, general government – Q3 2022.

growing more slowly. The largest increases on the expenditure side were in social benefits and in intermediate consumption. Government investment was up approximately a tenth. The general government deficit is forecast to be wider this year, on account of measures in connection with the energy crisis, which are expected to be significantly larger than last year, while economic growth is also expected to be sluggish. The general government debt had declined to 72.3% of GDP by the end of September, and was forecast to be even lower by the end of the year. The debt-to-GDP ratio is also forecast to continue declining this year.

8 Selected Themes

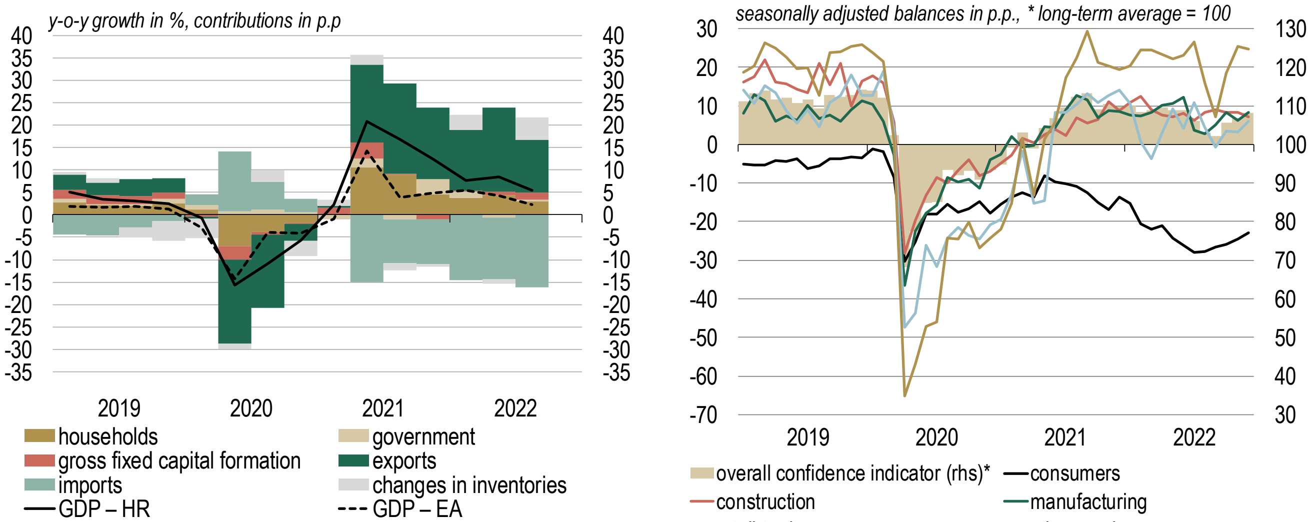
8.1 Macroeconomic picture of Croatia

Croatia's macroeconomic position was relatively favourable last year, despite high inflation, but the forecasts for this year's economic growth are low.

The Croatian economy has grown strongly over the last two years. Economic activity increased by 13.1% in 2021, surpassing its pre-pandemic level by 3.4%. Year-on-year GDP growth in the first half of last year remained high at 8.0% (seasonally adjusted; see Figure 8.1), significantly higher than in the euro area (4.9%). It was supported mainly by strong final household consumption and by strong services exports in the wake of the normalisation of the situation in international tourism. It stood at 5.5% in the third quarter over a rising base. With the year-on-year increase in exports slowing slightly and growth in imports picking up, net trade made a strong negative contribution to growth, while year-on-year growth in private consumption was down slightly but still high.

Figure 8.1: **Indicators of economic developments in Croatia**

Structure of GDP growth* – expenditure side | Confidence indicators



Note: * Seasonally and working days adjusted data.
Source: Eurostat, Banka Slovenije calculations.

Source: Eurostat. Latest data: December 2022.

The economic situation in Croatia is thought to have improved in the final quarter of last year, at least according to the economic sentiment indicators (see Figure 8.1). However, increased uncertainty, high inflation and declining real household disposable income have led to much lower economic growth forecasts. The European Commission is forecasting GDP to increase by just 1.0% this year and 1.7% in 2024, following last year's growth of 6.0%. Growth will thus be comparable to that in the euro area overall.

The labour market remains robust, and firms are optimistic in their future employment expectations.

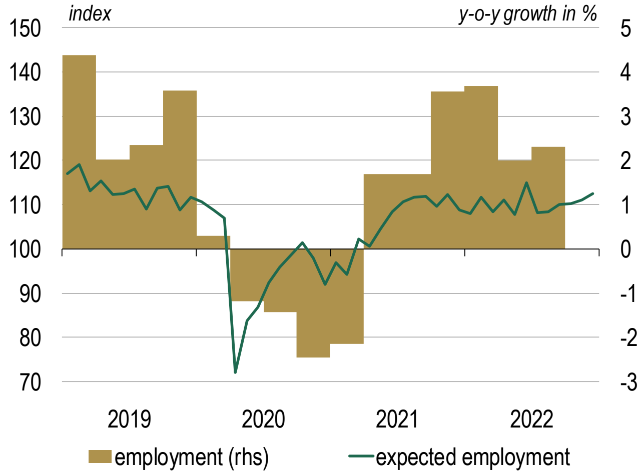
Employment in Croatia in the third quarter of last year was already fast approaching its peak from the first quarter of 2009, and its year-on-year growth remained high at 2.3% (see Figure 8.2). The outlook for the first quarter of this year is also favourable: employment expectations remained well above their long-term average (see Figure 8.2). The surveyed unemployment rate is low, and comparable to the euro area average, but at 6.7% in the third quarter of last year it was slightly higher than before the pandemic. The registered unemployment rate stood at 6.5% in November, down 0.3 percentage points in year-on-year terms. According to the European Commission's latest projections from November of last year, the situation on the labour market is expected to remain robust this year, despite weak employment growth (0.2%) and labour shortages. The surveyed unemployment rate is forecast at 6.3%.

Inflation remains high, despite government measures to curb rises in energy and food prices.

Having begun to strengthen in the second half of 2021, inflation in Croatia picked up further pace last year (see Figure 8.2). The high inflation was primarily attributable to

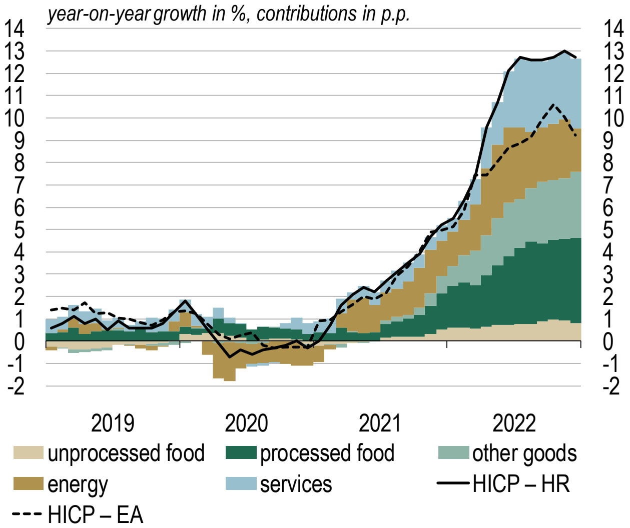
Figure 8.2: **Labour market situation and inflation in Croatia**

Employment and expected employment



Note: For the expected employment indicator value 100 represents the long-term average.
Source: Eurostat, Banka Slovenije calculations. Latest data: expected employment – December 2022.

Contributions to headline inflation



Source: ECB, Eurostat, Banka Slovenije calculations.
Latest data: December 2022.

external influences, namely rising prices of energy, commodities and food, and strong demand for recreation services and services related to tourism following the lifting of containment measures. Inflation as measured by the HICP stood at 12.7% in December of last year, 3.5 percentage points more than the euro area average. The narrowest core inflation indicator also remained high (10.5%). As a result of the cap on certain prices of energy and basic foods, tax changes, and the effects of last year's high base, inflation will slow slightly this year, but will remain above the euro area average at 6.5%. It is forecast to slow to 2.3% in 2024, similar to the European Commission's forecasts for the euro area overall.

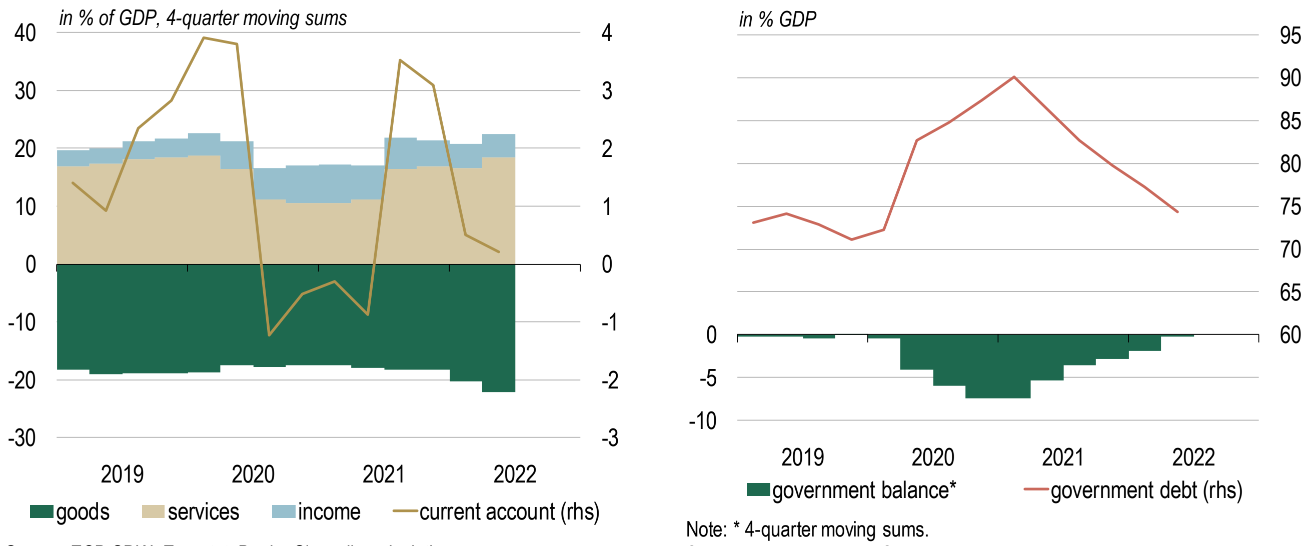
The current account balance is deteriorating under the influence of high import prices.

Previously in deficit, Croatia's current account balance moved into surplus in 2021, in the amount of 3.1% of GDP, but had narrowed to 0.2% of GDP over the 12 months to the second quarter of last year (see Figure 8.3). The main factor was the widening merchandise trade deficit driven by a sharp increase in imports in value terms caused by high prices on global markets. This was slightly mitigated by the growing surplus in services trade, mostly as a result of an increase in tourism-related exports, which measured over 12 months amounted to a record EUR 10.8 billion in the second quarter of last year, equivalent to approximately a fifth of Croatia's GDP. Croatia's current account balance is expected to move from surplus to deficit this year, with the deficit widening to 0.8% of GDP next year according to the European Commission's forecasts.

Figure 8.3: **Current account balance and public finance developments in Croatia**

Current account balance

General government balance and debt



Source: ECB SDW, Eurostat, Banka Slovenije calculations.

Note: * 4-quarter moving sums.
Source: Eurostat, Banka Slovenije calculations.

The general government deficit remains below the limit of 3%, and government debt is fluctuating close to 70% of GDP.

According to the European Commission's November projections, the general government deficit narrowed to 1.6% of GDP last year. For the second consecutive year the improvement was driven by economic growth and the withdrawal of measures to mitigate the impact of the pandemic. The debt-to-GDP ratio, which was estimated at 70.0% last year, down approximately 1 percentage point on its pre-pandemic level, is forecast to decline to 67.2% this year, before rising to 68.0% in 2024 (see Figure 8.3). This year's deficit is forecast at 2.4% of GDP, its widening relative to last year mainly reflecting the measures to support households and businesses in the energy crisis, and the decline in nominal economic growth. It is then forecast to widen to 2.7% of GDP next year. Croatia's fiscal position will thus remain better than the euro area average.

9 Statistical Appendix

Table 9.1: **Key macroeconomic indicators at the monthly level for Slovenia**

	2020	*2021*	*12 m. 'till Oct.22*	*3 m. 'till Oct.21*	*3 m. 'till Oct.22*	*2022 Aug.*	*2022 Sep.*	*2022 Oct.*	*2022 Nov.*	*2022 Dec.*
Economic Activity										
					balance of answers in percentage points					
Sentiment indicator	-11.8	2.4	1.3	4.9	-3.6	-0.4	-5.0	-5.3	-1.7	0.8
- confidence indicator in manufacturing	-8.7	8.2	2.0	7.7	-6.0	-1.0	-8.0	-9.0	-5.0	-3.0
					year-on-year growth rates in %					
Industry: - total	-5.2	10.2	4.5	4.9	0.4	4.6	1.3	-3.9	-3.6	...
- manufacturing	-5.0	11.8	6.4	6.4	3.9	7.9	3.8	0.7	0.3	...
Construction: - total	-0.7	-0.5	21.3	-2.1	38.2	31.8	26.1	57.0	44.0	...
- buildings	-7.8	-23.0	51.0	-25.8	106.0	84.0	86.1	149.3	111.1	...
Trade and service activities - total	-9.7	12.2	12.6	13.1	5.6	7.1	6.1	3.9	...	...
Wholesale and retail trade and repair of motor vehicles and motorcycles	-14.5	8.3	1.5	-3.0	3.4	1.6	4.2	4.2	...	...
Retail trade, except of motor vehicles and motorcycles	-5.9	16.2	13.3	15.8	4.6	8.8	7.8	-2.2	...	...
Other private sector services	-11.6	12.3	14.2	15.6	5.7	6.9	5.1	5.1	...	...
Labour market					*year-on-year growth rates in %*					
Average gross wage	6.0	6.0	2.1	4.2	6.3	5.7	6.1	7.3	...	...
- private sector	4.5	5.9	6.4	6.0	7.3	7.3	6.8	7.9	...	...
- public sector	7.9	6.4	-4.4	1.6	4.8	3.0	5.0	6.5	...	...
Real net wage[1]	7.1	3.0	-5.0	0.8	-3.1	-4.2	-3.3	-2.0	...	...
Registered unemployment rate (in %)	8.7	7.6	...	6.9	...	5.5	5.3	...	...	...
Registered unemployed persons	14.6	-12.6	-24.3	-20.9	-21.3	-22.2	-21.3	-20.5	-19.6	-19.4
Persons in employment	-0.6	1.3	2.5	2.3	2.1	2.2	2.1	2.0	...	...
- private sector	-0.9	1.3	3.2	2.7	2.7	2.8	2.7	2.6	...	...
- public sector	0.1	1.1	0.8	1.2	0.5	0.5	0.4	0.5	...	...
Price Developments					*year-on-year growth rates in %*					
HICP	-0.3	2.0	8.4	2.8	10.8	11.5	10.6	10.3	10.8	10.8
- services	1.8	0.6	4.5	1.0	6.1	6.1	5.9	6.3	6.8	8.2
- industrial goods excluding energy	-0.5	1.3	5.8	1.6	7.0	6.6	7.4	7.0	6.8	6.7
- food	2.8	0.7	8.4	0.5	13.3	12.2	12.7	15.0	16.0	15.8
- energy	-10.8	11.3	25.6	16.7	27.9	36.6	27.2	20.1	20.9	17.8
Core inflation indicator[2]	0.8	0.9	5.1	1.2	6.5	6.3	6.6	6.6	6.8	7.5
Balance of Payments - Current Account					*in % GDP*					
Current account balance	7.6	3.8	-0.7	4.5	1.6	-1.9	7.2	-0.3	1.3	...
1. Goods	5.0	1.7	-3.7	0.3	-3.0	-5.2	1.5	-5.2	-3.0	...
2. Services	4.4	4.7	5.8	5.8	7.4	6.6	8.9	6.9	5.7	...
3. Primary income	-0.8	-1.7	-1.8	-0.8	-2.2	-2.3	-2.8	-1.4	-0.5	...
4. Secondary income	-1.0	-0.9	-0.9	-0.8	-0.6	-0.9	-0.3	-0.6	-0.9	...
					nominal year-on-year growth rates in %					
Export of goods and services	-10.0	19.5	25.2	21.6	23.7	29.9	29.2	13.1	11.9	...
Import of goods and services	-11.7	25.4	34.0	30.3	27.1	36.5	26.0	20.3	16.0	...

Public Finances	*2020*	*2021*	*12 m. 'till Nov.22*		*2021 Jan.-Nov.*		*2022 Jan.-Nov.*	
Consolidated general government (GG) balance[3]	*EUR milions*		*% GDP*	*y-o-y, %*	*EUR mio*	*y-o-y, %*	*EUR mio*	*y-o-y, %*
Revenue	18,529	21,383	40.0	11.3	19,289	14.2	21,200	9.9
Tax revenue	16,460	18,786	35.2	11.2	17,025	13.2	18,749	10.1
From EU budget	730	950	1.7	12.6	774	24.2	816	5.4
Other	1,338	1,646	3.1	11.5	1,490	22.1	1,636	9.7
Expenditure	22,071	24,300	42.5	2.8	21,491	10.3	21,950	2.1
Current expenditure	9,128	10,394	18.0	2.7	9,123	13.2	9,191	0.7
- wages and other personnel expenditure	4,965	5,751	9.3	-5.2	5,300	17.1	4,989	-5.9
- purchases of goods, services	3,021	3,351	6.2	10.0	2,820	9.9	3,070	8.9
- interest	778	732	1.1	-9.7	719	-6.0	648	-9.8
Current transfers	10,868	11,319	19.2	-2.0	10,344	5.3	10,176	-1.6
- transfers to individuals and households	8,251	9,168	15.9	0.9	8,449	11.9	8,513	0.8
Capital expenditure, transfers	1,549	1,959	4.2	27.3	1,466	31.6	1,928	31.5
GG surplus/deficit	-3,542	-2,917	-2.5		-2,202		-750	

Note: The figures for economic developments are calendar-adjusted (with the exception of economic sentiment indicators, which are seasonally adjusted). The other figures in the table are unadjusted. The monthly activity indicators in industry, construction and services are given in real terms.
[1] HICP deflator. [2] Inflation excluding energy, food, alcohol and tobacco. [3] Consolidated position of the state budget, local government budgets, pension and disability insurance subsector and compulsory health insurance subsector, according to the principle of paid realisation.
Source: SORS, Banka Slovenije, Ministry of Finance, Banka Slovenije calculations.

Table 9.2: **Key macroeconomic indicators at the quarterly level for Slovenia and the euro area**

	2019	2020	2021	21Q4	22Q1	22Q2	22Q3	2019	2020	2021	21Q4	22Q1	22Q2	22Q3
	Slovenia							*euro area*						
Economic developments	*q-o-q growth rates in %*													
GDP				5.2	-0.1	0.2	-1.4				0.5	0.6	0.8	0.3
- industry				1.2	0.3	1.1	0.3				0.5	0.5	0.6	0.7
- construction				1.4	2.6	1.4	3.3				0.3	2.4	-0.7	-1.7
- mainly public sector services (OPQ)				0.6	0.2	-0.2	-0.1				-0.8	0.9	-0.6	1.4
- mainly private sector services (without OPQ)				3.7	1.1	1.4	-0.7				0.5	0.9	0.9	0.5
Domestic expenditure				3.2	3.0	1.6	-4.8				1.4	-0.4	1.0	1.5
- general government				1.3	0.7	-2.8	0.1				0.4	0.0	-0.1	0.1
*- households and NPISH**				0.5	1.3	0.4	0.4				-0.1	0.0	1.0	0.9
- gross capital formation				-0.9	12.2	3.9	-6.8				6.1	-1.7	1.9	4.1
- gross fixed capital formation				1.8	3.3	-0.8	2.6				3.4	-0.7	0.9	3.6
	y-o-y growth rates in %													
GDP	3.5	-4.3	8.2	10.5	9.7	8.3	3.4	1.6	-6.1	5.3	4.6	5.6	4.3	2.3
- industry	6.9	-3.4	9.2	5.7	4.9	4.1	2.2	0.5	-6.4	7.0	1.7	2.3	2.1	2.4
- construction	8.0	-1.9	10.0	7.2	7.8	7.7	10.4	0.8	-5.7	5.3	0.7	5.6	1.1	-0.4
- mainly public sector services (OPQ)	1.7	2.4	3.8	4.8	3.7	1.3	-0.1	1.1	-2.8	3.5	1.9	2.0	0.8	0.8
- mainly private sector services (without OPQ)	2.3	-5.5	8.3	10.4	10.4	10.0	4.9	1.6	-6.7	5.6	5.1	6.3	5.1	2.8
Domestic expenditure	3.5	-4.7	9.9	13.5	16.9	10.7	2.7	2.4	-5.8	4.2	5.1	6.1	4.4	3.3
- general government	1.8	4.1	5.8	8.3	4.5	0.7	-0.9	1.7	1.0	4.3	2.6	3.0	0.8	0.4
- households and NPISH	5.3	-6.9	9.5	21.2	19.3	12.3	2.5	1.4	-7.7	3.8	6.2	8.6	5.8	1.8
- gross capital formation	0.6	-7.1	15.1	1.1	23.8	15.9	6.7	5.7	-7.4	5.0	5.0	3.6	4.9	9.9
- gross fixed capital formation	5.1	-7.9	13.7	13.2	9.4	7.3	7.1	6.9	-6.2	3.6	1.6	4.3	2.7	7.2
- inventories and valuables, contr. to GDP growth in p.p.	-0.8	0.1	0.4	-2.3	3.2	2.2	0.0	-0.2	-0.3	0.3	0.7	-0.1	0.5	0.6
Labour market	*q-o-q growth rates in %*													
Employment				0.7	0.7	0.5	0.3				0.5	0.5	0.3	0.3
- mainly private sector (without OPQ)				0.7	0.7	0.6	0.2				0.6	0.6	0.4	0.3
- mainly public services (OPQ)				0.5	0.4	0.3	0.4				0.4	0.4	0.3	0.3
	y-o-y growth rates in %													
Employment	2.5	-0.7	1.3	2.5	3.2	3.1	2.0	1.3	-1.5	1.4	2.4	3.0	2.6	1.8
- mainly private sector (without OPQ)	2.6	-1.3	1.0	2.5	3.4	3.4	2.1	1.3	-2.3	1.2	2.6	3.5	3.0	1.9
- mainly public services (OPQ)	1.8	2.2	2.7	2.6	2.4	1.8	1.6	1.3	1.0	2.1	1.6	1.7	1.5	1.4
Labour costs per employee	5.0	3.4	7.9	3.2	1.3	3.0	5.5	2.2	-0.2	3.8	3.3	4.5	4.6	3.9
- mainly private sector (without OPQ)	4.5	1.5	8.0	7.3	6.1	6.7	7.0	2.1	-1.3	4.6	4.2	5.2	5.3	4.1
- mainly public services (OPQ)	6.6	9.4	7.7	-8.5	-11.7	-7.8	1.0	2.4	2.3	1.9	1.3	2.7	2.7	3.5
Unit labour costs, nominal**	4.0	7.3	1.1	-4.3	-4.7	-2.0	4.1	2.0	4.7	-0.1	1.1	1.9	3.0	3.4
Unit labour costs, real***	1.7	6.0	-1.5	-7.2	-8.7	-7.5	-5.9	0.2	2.9	-2.1	-1.7	-1.5	-1.3	-1.1
	in %													
LFS unemployment rate	4.5	5.0	4.7	4.5	4.3	4.2	4.0	7.6	7.9	7.7	7.1	7.0	6.6	6.6
Foreign trade	*q-o-q growth rates in %*													
Real export of goods and services				6.4	-1.1	2.6	3.6				2.6	1.4	1.7	1.7
Real import of goods and services				5.5	2.6	1.4	1.8				4.7	-0.7	2.2	4.3
	y-o-y growth rates in %													
Real export of goods and services	4.5	-8.6	14.5	13.8	8.1	8.6	11.0	2.8	-8.9	10.5	8.0	8.3	7.5	7.6
Real import of goods and services	4.7	-9.6	17.6	18.1	16.5	11.6	10.8	4.8	-8.5	8.3	9.3	9.6	8.1	10.4
Current account balance as % of GDP****	5.9	7.6	3.8	3.8	1.5	0.4	-0.3	2.3	1.6	2.3	2.3	1.6	0.6	-0.1
External trade balance as contr. to GDP growth in p.p.	0.2	0.0	-0.8	-1.9	-5.7	-1.7	0.8	-0.7	-0.5	1.3	-0.3	-0.2	0.0	-0.9
Financing	*in % of GDP*													
Banking system's balance sheet	87.8	98.0	94.5	94.5	92.6	88.5	...	260.1	294.8	285.9	285.9	293.5	294.3	...
Loans to NFCs	19.9	20.2	19.3	19.3	19.3	19.3	19.4	35.9	40.0	37.9	37.9	37.6	37.6	37.9
Loans to households	21.9	22.8	21.6	21.6	21.3	21.1	20.9	49.0	53.0	51.4	51.4	50.8	50.4	50.2
Inflation	*in %*													
HICP	1.7	-0.3	2.0	4.5	6.3	9.0	11.3	1.2	0.3	2.6	4.6	6.1	8.0	9.3
HICP excl. energy, food, alcohol and tobacco	1.9	0.8	0.9	2.4	4.4	5.6	6.4	1.0	0.7	1.5	2.4	2.7	3.7	4.4
Public finance	*in % of GDP*													
Debt of the general government	65.4	79.6	74.5	74.5	74.7	73.5	72.3	83.9	97.0	95.4	95.4	95.2	94.2	...
One year net lending/net borrowing of the general government****	0.6	-7.7	-4.7	-4.7	-3.6	-3.1	-2.7	-0.6	-7.0	-5.1	-5.1	-4.0	-2.9	...
*- interest payment**** *	1.7	1.6	1.2	1.2	1.2	1.1	1.1	1.6	1.5	1.5	1.5	1.5	1.5	...
*- primary balance**** *	2.3	-6.1	-3.4	-3.4	-2.4	-2.0	-1.6	1.0	-5.5	-3.7	-3.7	-2.5	-1.4	...

Note: Original figures are used to calculate the year-on-year rates, and seasonally adjusted figures are used to calculate the current rates of growth.
* The figures for Slovenia are calculated as the difference between the seasonally adjusted figures for aggregate final consumption and government final consumption.
** Nominal unit labour costs are the ratio of nominal compensation per employee to real labour productivity.
*** Real unit labour costs are the ratio of nominal compensation per employee to nominal labour productivity.
**** 4-quarter moving sums.
Source: SORS, Eurostat, Banka Slovenije, ECB, Ministry of Finance, Banka Slovenije calculations.

10 Figures and Tables

Figures

Tables