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EUROSYSTEM

SUMMARY OF MACROECONOMIC DEVELOPMENTS

SEPTEMBER 2019

Summary of macroeconomic developments, September 2019

The economic situation in the euro area is deteriorating. Year-on-year GDP growth, which has been slowing since the third quarter of 2017, stood at just 1.1% in the second quarter of this year, largely because of problems in the German economy. The decline in industrial production deepened in comparison with the first quarter, while growth in construction activity and in retail turnover slowed. Growth is expected to remain low in the third quarter as various survey indicators showed no signs of a reversal in economic activity in the summer months. These developments are worse than had been expected by international institutions, whose baseline scenarios for this year envisaged a stabilisation of the situation in the second half of the year. The outlook for this year's growth in foreign demand for Slovenian products is also worse than at the beginning of the year, although it has remained relatively stable in recent months due to robust economic growth in the countries of central and south-eastern Europe. At the same time, the outlook for 2020 is deteriorating. The Fed responded to the uncertain economic situation and low inflation, reducing its key interest rate for the first time since 2008, while new stimulus measures by the ECB are becoming increasingly likely. The euro fell below the mark of USD 1.11 in August, its low of the last two years. The price of Brent crude was down fully 20% in year-on-year terms by the end of August, and this year energy prices have been the main factor in the fall in inflation in the euro area.

Economic growth also slowed in Slovenia, and only continued to outpace the euro area average in the year-on-year comparison. At the same time, the outlook for export sector deteriorated in the summer months. Quarterly GDP growth stood at just 0.2%, the lowest figure since the first quarter of 2018. There was a strongly negative impact from taxes, as growth in value-added remained unchanged at 0.5%. Year-on-year GDP growth slowed to 2.5%. In contrast to the situation in Germany, growth in merchandise exports and value-added in industry actually strengthened relative to the first quarter, although this was most likely only temporary. The situation worsened significantly in June, as output in the majority of manufacturing segments declined in year-on-year terms. Companies' assessments of growth in foreign demand also deteriorated. In line with the uncertain international situation, growth in investment in machinery and equipment is weakening. Quarterly growth in value-added in construction slowed sharply under the influence of bad weather, but year-on-year growth remained high, in line with investment activity. As in the euro area overall, the situation remained relatively favourable in private-sector services: domestic private consumption continues to strengthen, while growth in foreign demand for services has remained solid. Despite this, year-on-year growth in value-added in services is continuing to slow. The government sector also contributed to the increase in consumption, albeit to a significantly smaller extent than in the first quarter. Because there are still no signs in the international environment of an improvement in the situation in industry, and confidence in the domestic economy declined slightly, economic growth is expected to remain subdued this year.

The slowdown in economic growth is already being reflected in employment developments. According to monthly statistics, year-on-year growth in total employment, which exceeded 3% over the last two years, had slowed to a still-high 2.6% by June. The surveyed unemployment rate stood at just 4.2% in the second quarter. However, indicators of the current dynamics in employment reveal a sharper slowdown. Annualised monthly growth was merely around 1% in June, and was driven solely by the hiring of foreign nationals, the hiring of residents having come to a standstill. Nominal year-on-year growth in the average gross wage fell below 4% in May and June, primarily because of a slowdown in the private sector. Nominal wage growth nevertheless remained higher than last year. This allowed real growth in the wage bill to remain above 5% in the second quarter of this year, comparable to the same period last year, and encouraging from *the perspective of further growth in private consumption. In the second quarter, labour productivity stagnated in year-on-year terms, which is more favourable than for example in Germany, where it declined by almost 1%.*

The 12-month current account surplus remained above 5% of GDP in June, despite a decline in the merchandise trade surplus. The 12-month merchandise trade surplus fell from approximately EUR 1.6 billion last August to less than EUR 1 billion in June of this year, as rising domestic consumption saw nominal growth in imports outpace growth in exports. Year-on-year growth in merchandise exports, even to Germany, had remained high over the first five months of the year, particularly given the uncertain international situation. The figures for June were less favourable: growth in exports slowed to 4.3%, and was entirely attributable to increased exports of pharmaceutical industry. Growth in imports also slowed in June, having been particularly volatile this year because of occasional large imports of pharmaceutical products. The surplus of trade in services is continuing to widen, as growth in exports of a wide spectrum of services remains high. This suggests that the problems in the international environment are primarily related to manufacturing, at least for now. Other lesser factors in the maintenance of the current account surplus include primary income, which saw a sharp outflow of income from portfolio investments in June following the privatisation of a major bank, the continuing decline in interest payments on public debt, a narrower deficit in income from direct investment, and a strengthening surplus in labour income. The deficit in secondary income widened, primarily because of larger payments into the EU budget.

In Slovenia, year-on-year inflation as measured by the HICP rose to 2.4% in August, significantly more than expected, while it remained at just 1% in the euro area. The rise was primarily attributable to unusually strong growth in prices of clothing and footwear, the year-on-year rate reaching fully 5% in August. Growth in prices of industrial products excluding energy thus markedly increased and strongly exceeded the euro area average. Nevertheless, Slovenia's above-average inflation is still primarily being maintained by high growth in services' prices, which in year-on-year terms accelerated also due to high wage growth in the public sector. The contribution of growth in food prices has also been relatively high since July, while the contribution of energy prices under the influence of global crude oil prices remains low. Inflation measured without food and energy prices accelerated amid domestic inflationary pressures stemming from rising labour costs and strengthened domestic demand. It reached 2.5% in August and widened the gap to the euro area average to 1.6%. The majority of the other countries in the European periphery with a stronger-than-average growth in domestic demand are also recording elevated inflation. Year-on-year price growth average of the first seven months of the year was above 3% in Latvia, while Portugal and Greece recorded the lowest inflation.

Over the first seven months of the year, the consolidated general government surplus was smaller in year-on-year terms. It narrowed by EUR 144 million to EUR 27 million. Revenues were up 5.6% in year-on-year terms; the slowdown in growth is primarily the result of the tax break on leave allowance, which meant that personal income tax revenues merely remained at last year's level. The most notable increase was in corporate income tax revenues, partly because of tax settlements for the previous year, and partly because of higher current tax prepayments. Year-on-year growth in expenditure outpaced growth in revenues. Investment expenditure and transfers continued to record high year-on-year growth, while there was notable growth in expenditure on wages due to a new wage agreement, and growth in social transfers strengthened because of new measures. Flows with the EU budget increased, but there was no significant change in the balance. According to the report on the execution of the state budget for 2019, the state budget is expected to record a surplus of EUR 194 million this year, as planned. However, the negative signals from the international environment demand caution in the drafting of the budget documents for 2020 and 2021, and in the adoption of other measures with financial effects, as government debt still remains relatively high, which limits potential countercyclical measures.

Selection of main macroeconomic indicators on a monthly basis

	12 m. 'till Jun.17	12 m. 'till Jun.18	12 m. 'till Jun.19	3 m. 'till Jun.18	3 m. 'till Jun.19	2019 Apr.	2019 May.	2019 Jun.	2019 Jul.
Economic Activity									* data for Aug.19
				balance of answers in percentage points					
Sentiment indicator	9.0	13.7	9.3	12.9	6.6	6.7	7.7	5.4	6.8 (6.0*)
- confidence indicator in manufacturing	7.4	10.5	4.0	8.7	0.0	0.0	3.0	-3.0	0.0 (0.0*)
				year-on-year growth rates in %					
Industry: - total	7.7	8.8	2.9	6.9	3.0	5.0	3.1	1.1	...
- manufacturing	8.5	9.5	3.2	7.4	3.2	5.8	3.2	0.7	...
Construction: - total	0.4	17.4	18.1	17.1	8.7	9.7	11.2	5.5	...
- buildings	23.4	20.3	13.0	16.5	6.2	6.7	5.7	6.1	...
Trade and service activities - total	6.0	7.1	6.5	7.8	4.0	5.3	2.8	4.0	...
Wholesale and retail trade and repair of motor vehicles anc	16.1	14.7	6.7	17.2	1.3	0.7	4.0	-1.0	...
Retail trade, except of motor vehicles and motorcycles	5.4	2.7	6.0	1.4	6.1	9.0	3.8	5.7	...
Other private sector services	5.2	7.2	5.9	8.8	2.6	2.4	2.2	3.3	...
Labour market				*year-on-year growth rates in %*					
Average gross wage	1.8	3.5	3.7	3.6	3.9	4.0	3.9	3.9	...
- private sector	1.9	3.9	3.9	4.2	3.5	4.0	3.3	3.2	...
- public sector	2.2	3.6	3.9	3.5	4.9	4.3	5.3	5.3	...
Real net wage[1]	0.9	1.8	1.3	0.9	1.5	1.5	1.8	1.3	...
Registered unemployment rate (in %)	10.3	8.7	7.9	8.1	7.5	7.6	7.4	7.3	...
Registered unemployed persons	-11.7	-14.3	-7.3	-12.6	-5.9	-5.8	-6.1	-5.7	-5.5
Persons in employment	2.7	3.5	3.0	3.0	2.7	2.8	2.7	2.6	...
- private sector	3.3	4.6	3.8	3.9	3.3	3.4	3.4	3.2	...
- public sector	1.2	0.7	1.0	0.7	1.0	1.0	1.0	1.0	...
Price Developments				*year-on-year growth rates in %*					
HICP	1.0	1.6	1.8	2.1	1.7	1.8	1.6	1.9	2.0 (2.4*)
- services	1.9	2.0	2.8	2.4	3.2	3.4	3.0	3.2	3.1 (3.3*)[4]
- industrial goods excluding energy	-0.7	-0.8	-0.3	-0.8	-0.1	-0.2	-0.4	0.3	0.8 (1.5*)[4]
- food	1.5	2.7	1.3	3.4	1.1	0.7	0.7	2.0	2.8 (2.7*)[4]
- energy	1.5	4.1	4.7	6.2	2.8	3.5	3.5	1.4	0.5 (1.1*)[4]
Core inflation indicator[2]	0.8	0.8	1.4	1.0	1.8	1.9	1.5	1.9	2.1 (2.5*)[4]
Balance of Payments - Current Account					*in % GDP*				
Current account balance	4.7	6.4	5.4	6.1	5.5	...	...	...	...
1. Goods	3.3	3.5	2.1	3.7	1.8	...	...	...	...
2. Services	5.1	5.3	6.1	5.6	6.2	...	...	...	...
3. Primary income	-2.8	-1.7	-1.6	-2.6	-1.6	...	...	...	...
4. Secondary income	-0.9	-0.7	-1.1	-0.6	-0.9	...	...	...	...
				nominal year-on-year growth rates in %					
Export of goods and services	8.7	12.3	9.1	10.8	9.9	14.4	10.8	4.8	...
Import of goods and services	9.8	12.3	10.5	11.3	12.2	27.6	6.0	4.0	...

Public Finances	2017	2018	12 m. 'till Jul.19		2018 Jan.-Jul.		2019 Jan.-Jul.	
Consolidated general government (GG) balance[3]	EUR milions		% GDP	y-o-y, %	EUR mio	y-o-y, %	EUR mio	y-o-y, %
Revenue	16,803	18,594	40.4	9.8	10,345	6.8	10,924	5.6
Tax revenue	15,162	16,225	35.3	6.3	9,251	6.6	9,762	5.5
From EU budget	391	796	1.9	107.1	296	17.6	402	35.7
Other	1,250	1,572	3.2	19.2	798	4.8	760	-4.8
Expenditure	17,102	18,068	39.6	7.1	10,175	4.6	10,897	7.1
Current expenditure	7,733	7,966	17.3	3.9	4,586	3.5	4,818	5.1
- wages and other personnel expenditure	3,938	4,168	9.2	7.8	2,413	5.2	2,619	8.5
- purchases of goods, services	2,627	2,634	5.7	0.5	1,437	5.9	1,523	5.9
- interest	985	868	1.7	-15.3	653	-7.7	574	-12.1
Current transfers	7,913	8,237	18.0	6.0	4,838	3.1	5,145	6.4
- transfers to individuals and households	6,665	6,926	15.2	5.9	4,082	3.2	4,347	6.5
Capital expenditure, transfers	1,078	1,432	3.2	26.7	500	32.7	590	18.0
GG surplus/deficit	-299	526	0.8		170		27	

Sources: SORS, Bank of Slovenia, Ministry of finance, Bank of Slovenia calculations.

Notes: Economic activity data are working day adjusted (with exception of sentiment and confidence indicators data, which are seasonally adjusted). Other data in the table are original. Monthly activity indicators for industry, construction and services are shown in real terms.

[1] HICP deflator. [2] Inflation excluding energy, food, alcohol, tobacco. [3] Consolidated central government budget, local government budgets and social security funds (pension and disability insurance fund and health insurance fund) in cash accounting principle. [4] Bank of Slovenia assessment.