BANKA SLOVENIJE

BANK OF SLOVENIA

EUROSYSTEM

SUMMARY OF MACROECONOMIC DEVELOPMENTS

OCTOBER 2016

Summary of macroeconomic developments, October 2016

Forecasts for this year's global economic growth remain relatively stable in the wake of slightly weaker activity in advanced economies and a gradual recovery in individual developing countries that are commodity exporters. Quarterly economic growth in the euro area slowed in the second quarter. The situation on the labour market is improving, although growth in the euro area is likely to remain merely moderate this year, which is also suggested by the confidence indicators. The latest weighted forecasts based on the Consensus forecasts also suggest that aggregate growth in Slovenia's main trading partners will be moderate but stable, which provides a solid outlook for growth in Slovenian exports and industrial production. The monetary policies of the ECB and the Fed have remained divergent in the third quarter, which is maintaining the euro's stability against the US dollar. After falling briefly in July, the oil price rose again and stabilised, as did prices of certain other commodities.

The economic situation in Slovenia is continuing to improve. Year-on-year economic growth reached 2.7% in the second quarter, its out-performance of the euro area overall having been driven by industry this year. At the same time domestic final consumption is also strengthening more quickly than last year, households having increased purchases of durables, which was partly attributable to the slightly faster recovery in real disposable income. The government is continuing to contribute to domestic final consumption, via a less restrictive fiscal policy. The gradual strengthening of domestic demand is also strengthening merchandise imports, although net trade still accounted for a third of GDP growth in the second quarter, export growth having remained high. At the same time there have been favourable changes in aggregate investment from the perspective of the economy's output potential, as investment in machinery and equipment in the second quarter was up in year-on-year terms for the fifth consecutive quarter.

On the labour market, the rise in employment and the fall in unemployment strengthened further in the second quarter. Growth in employment strengthened to 2% in the second quarter, while surveys of employment expectations suggest further growth over the remainder of the year. The fall in unemployment in the summer of this year was the sharpest in recent years. Unemployment stood at 97,895 in August, down 9.3% on last August. Despite the favourable developments on the labour market, structural unemployment is deepening, which is being reflected mainly in rising proportions of older unemployed people and those unemployed for more than three years. After trailing for several years, year-on-year growth in labour costs was comparable to the euro area average in the first half of the year.

The current account surplus continued to widen in year-on-year terms over the first seven months of this year, primarily as a result of the further year-on-year widening of the trade surplus. Nominal growth in merchandise trade was relatively low as a result of a fall in trade prices, although the national accounts figures indicate real year-on-year growth of 9% in the second quarter. Growth in industrial production and exports and faster growth in final consumption have brought a sharp increase in merchandise imports this year. The significant year-on-year narrowing in the deficit in capital income has contributed to the maintenance of the large overall surplus.

With the exception of the general government sector, all the domestic institutional sectors have recorded financial surpluses for the fourth consecutive year. The 12-month surplus vis-à-vis the rest of the world stood at 5.3% of GDP in the first quarter of 2016. Firms have been generating high profits for three years now, and a slight pick-up in the investment cycle has been evident in the last year. The corporate sector's financial surplus has primarily been directed towards debt reduction or invested in domestic banks in the form of sight deposits. Households are even more attracted to invest-

ments of this type: sight deposits have increased by EUR 2.9 billion over the last two years, while fixed-term deposits have declined by EUR 1.7 billion. The banks are continuing to reduce their total assets, on the investment side by reducing lending activity, and on the funding side primarily by repaying ordinary liabilities to the rest of the world.

The nominal general government deficit is forecast at 2.2% of GDP for this year, a small surplus in fact having been recorded in the second quarter. General government expenditure declined in the first half of the year as revenues increased moderately. The changeover to the disbursement of EU funds from the new 2014-2020 financial framework has brought slower growth in both aggregates. Growth in revenues from taxes and contributions remains solid, and reflects the ongoing strengthening of economic activity, and above all the favourable labour market indicators.

Inflation in Slovenia moved more reliably into positive territory for the first time in two years, reaching 0.2% in September. This was primarily attributable to the gradual slowdown in the year-on-year fall in energy prices, while year-on-year core inflation reached around 1% in May, before again falling slightly in the following months. There were rises in food prices and, more notably, in services prices. The latter rose by 2%, well above the comparable rate across the euro area. This acceleration has coincided with favourable developments on the labour market, with growth in employment and the wage bill, and with this year's increased growth in household consumption.

Main macroeconomic indicators

	2013	2014	2015	15Q4	16Q1	16Q2	2013	2014	2015	15Q4	16Q1	16Q2
	Slovenia						*euro area*					
Economic developments	*y-o-y growth rates in %*											
GDP	-1.1	3.1	2.3	2.8	2.3	2.7	-0.3	1.1	2.0	2.3	1.6	2.2
- industry	-0.1	4.5	1.5	1.6	4.6	7.2	-0.9	2.0	3.8	4.2	0.9	2.7
- construction	-8.7	9.2	-1.3	1.6	-18.2	-12.8	-3.5	-0.8	0.4	1.6	1.0	1.8
- mainly public sector services	-1.1	0.1	1.0	1.2	1.1	1.4	0.1	0.5	1.1	1.1	1.1	1.4
- mainly private sector services	-0.7	4.7	2.5	3.3	2.5	3.2	-0.2	1.3	2.1	2.4	1.5	2.4
Domestic expenditure	-2.0	1.8	1.4	2.9	1.3	2.0	-0.6	1.1	1.9	2.5	2.1	2.3
- general government	-2.1	-1.2	2.4	3.4	3.4	2.1	0.2	0.6	1.4	1.9	2.0	1.7
- households and NPISH	-4.0	2.0	0.5	0.6	1.2	2.6	-0.6	0.8	1.8	1.7	2.0	2.0
- gross capital formation	4.3	4.3	2.8	10.0	-0.7	0.6	-1.7	2.6	2.7	5.3	2.7	3.9
- gross fixed capital formation	3.2	1.4	1.0	5.4	-7.8	-3.6	-2.4	1.5	3.1	4.1	2.2	4.0
- inventories and valuables, contr. to GDP growth in pp	0.2	0.6	0.4	0.7	1.4	0.8	0.2	0.2	-0.1	0.2	0.1	-0.1
Labour market												
Employment	-1.1	0.4	1.1	1.1	1.6	2.0	-0.7	0.6	1.1	1.3	1.4	1.4
- mainly private sector services	-1.2	0.5	1.2	1.1	1.6	2.0	-1.0	0.4	1.1	1.3	1.6	1.5
- mainly public sector services	-0.6	0.4	0.8	1.1	1.5	2.1	0.3	0.9	1.0	1.1	1.1	1.2
Labour costs per employee	0.5	1.3	1.4	2.0	2.6	1.0	1.6	1.3	1.2	1.2	1.3	1.1
- mainly private sector services	1.6	2.3	1.5	1.8	1.8	1.7	1.6	1.4	1.3	1.2	1.3	1.0
- mainly public sector services	-3.2	-2.0	1.2	1.2	2.3	1.8	1.5	1.1	1.1	1.2	1.3	1.3
Unit labour costs	0.1	-2.0	0.3	0.3	1.9	0.2	1.1	0.7	0.4	0.3	1.3	0.3
- industry	0.8	-0.8	1.1	2.0	0.2	-1.9	2.1	0.0	-1.7	-2.5	1.2	-1.0
	in %											
LFS unemployment rate	10.1	9.8	9.0	8.4	8.9	7.8	12.0	11.7	10.9	10.6	10.7	10.0
Foreign trade	*y-o-y growth rates in %*											
Current account balance as % of GDP	4.8	6.2	5.2	5.6	6.2	8.0	2.2	2.3	0.0	0.0	0.0	0.0
External trade balance as contr. to GDP growth in pp	0.8	1.4	1.1	0.1	1.2	0.9	0.4	0.0	0.2	-0.1	-0.4	0.0
Real export of goods and services	3.1	5.7	5.6	4.3	5.9	7.5	2.2	4.4	6.3	5.6	2.1	3.6
Real import of goods and services	2.1	4.2	4.6	4.7	4.9	7.2	1.5	4.8	6.3	6.3	3.4	4.0
Financing	*in % of GDP*											
Banking system's balance sheet	128.8	116.6	107.7	107.7	104.4	101.7	297.4	299.0	284.2	284.2	286.8	288.8
Loans to NFCs	45.1	31.5	26.5	26.5	25.1	24.1	42.0	40.2	38.9	38.9	38.7	38.6
Loans to households	22.6	21.4	21.2	21.2	21.0	21.1	51.8	50.6	50.1	50.1	49.8	49.6
Inflation	*in %*											
HICP	1.9	0.4	-0.8	-0.9	-0.9	-0.4	1.3	0.4	0.0	0.2	0.0	-0.1
HICP excl. energy, food, alcohol and tobacco	0.9	0.6	0.3	0.4	0.3	0.9	1.1	0.8	0.8	1.0	1.0	0.8
Public finance	*in % of GDP*											
Debt of the general government	71.0	80.9	83.1	83.1	83.5	82.3	91.0	91.9	90.3	90.3	91.3	...
One year net lending/net borrowing of the general government	-15.0	-5.0	-2.9	-2.9	-2.8	-1.9	-3.0	-2.6	-2.1	-2.1	-1.9	...
- interest payment	2.6	3.2	2.9	2.9	2.9	2.9	2.8	2.6	2.4	2.4	2.4	...
- primary balance	-12.5	-1.9	0.1	0.1	0.2	1.0	-0.2	0.1	0.3	0.3	0.4	...
- balance excl. bank recapitalisations	-4.9	-4.1	-2.9	-2.9	-2.8	-1.9						
- primary balance excl. bank recapitalisations	-2.3	-0.9	0.1	0.1	0.2	1.0						

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