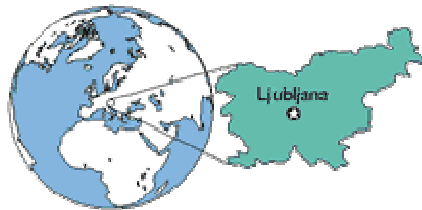


COUNTRY REVIEW

Slovenia



16 June 2010

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EULER HERMES COUNTRY RISK GRADE: AA

Country Risk Grades are on a scale of AA, A, BB, B, C, D
where AA is the lowest and D the highest risk.

Strengths

- Low systemic political risk
- Good regional and international relations; EU membership
- Euro zone membership provides for low transfer and convertibility risk
- Strong business environment overall
- Solid banking sector

Weaknesses

- High export dependence
- Modest FDI inflows
- Slow court proceedings

ECONOMIC STRUCTURE

Country Profile	
Capital city:	Ljubljana
Population:	2.013 mn (2008)
GDP:	USD 54610 mn (2008)
Currency:	Euro (EUR)
Form of state:	Parliamentary democracy
Head of government:	Prime Minister Borut PAHOR (since November 2008)
Next elections:	Presidential and parliamentary: 2012

Major Industries (% of GDP at market prices, 2008)	Global Assumptions	2009	2010	
Services	63.7%	Real GDP grth (% yr/yr) *	-3.9	0.9
Industry	34.0%	Inflation (% av) *	-0.1	1.3
Manufacturing	22.1%	Dated Brent (USD/b)	61	80
Construction	8.9%	* Major economies		
Agriculture, forestry & fishing	2.3%			

Main Exports (% of total, 2008)		Main Imports (% of total, 2008)	
Machinery & transport equipment	40.0%	Machinery & transport equipment	33.5%
Manufactures, classified	24.0%	Manufactures, classified	20.5%
Chemicals	14.5%	Chemicals	12.0%
Miscellaneous articles	12.0%	Manufactures, miscellaneous	9.5%
Lead Export Markets (% of total exports, 2009)		Lead Import Markets (% of total imports, 2009)	
Fellow EU-27 members	69.8%	Fellow EU-27 members	78.6%
Germany	19.7%	Germany	18.3%
Italy	11.6%	Italy	17.6%
Countries of former Yugoslavia	13.0%	Countries of former Yugoslavia	6.9%
Croatia	6.2%	Croatia	3.7%

Basic indicators

Selected economic indicators	2006	2007	2008	2009	2010f
Nominal GDP (USD mn)	38,736	47,354	54,611	48,464	44,844
Population (mn)	2.01	2.01	2.01	2.02	2.02
GDP per capita (USD)	19,272	23,559	27,129	24,040	22,222
Real GDP growth (% yr/yr)	5.8	6.8	3.5	-7.8	0.5
Inflation (HICP%, eop)	3.0	5.7	1.8	2.1	2.5
Fiscal balance (ESA 95, % of GDP)	-1.3	0.0	-1.7	-5.5	-6.1
Public debt / GDP (%)	26.7	23.4	22.6	35.9	41.6
Current account balance (% of GDP)	-2.6	-4.7	-6.1	-1.0	-1.8
Gross external debt / GDP (%)	81.8	108.0	99.8	120.0	117.1
Net external debt / GDP (%)	11.5	19.7	25.1	31.4	32.1
Debt-service ratio (%)	17.7	14.4	16.4	36.9	23.7
Foreign exchange reserves (EUR mn)	5,590	*	*	*	*
Import cover (months)	3.2	*	*	*	*
Exchange rate assumption, EUR:USD (av)	0.80	0.73	0.68	0.72	0.80
f: CRU central forecast					
* Slovenia adopted the EUR in 2007 and has since access to pooled foreign exchange reserves of the ECB.					

Sources: National sources, IMF, European Commission, ECB, Eurostat, Euler Hermes Economic Studies

Political Stability

Slovenia gained independence in 1991 after a one-week war with the Yugoslavian People's Army. A constitution was adopted soon thereafter, which established the country as a parliamentary democratic republic with an independent judicial system. Since then, a high degree of domestic political stability, historical ties to Western Europe, and a strong economy have assisted in Slovenia's transition to a modern state, culminating in EU and NATO membership in spring 2004. Moreover, an accession agreement with the OECD was signed on 1 June 2010. Regional instability in the Balkans has declined considerably, and Slovenia's relations with Croatia have improved significantly in recent years. On 6 June 2010, Slovenes endorsed in a binding referendum the government's decision to settle by international arbitration a long-standing Croatian-Slovenian land and maritime boundary dispute.

On the domestic front, the parliamentary election in September 2008 resulted in the defeat of the then ruling centre-right coalition which was succeeded by a four-party coalition government that includes three centre-left parties and the Pensioners' Party which also belonged to the previous administration. Meanwhile the incumbent government has lost popularity, mainly because it has tried to break the Slovenian "tradition" of slow progress on structural reforms. Planned reforms of employment legislation, the state pension system and healthcare in order to boost competitiveness have sparked strikes and protests by trade unions. Reportedly there are also disagreements within the government over the reform proposals as well as over personalities. Hence there is a risk that the government collapses over occasionally arising tensions. However, this does not threaten political stability as the direction of economic and foreign policies would unlikely be altered significantly under any potential new government. Overall, systemic political risk is very low.

Economic Stability

Slovenia is classified as a high income economy by the World Bank. The EU has estimated per capita GDP at EUR18,400 in 2008, which was more than in Portugal (EUR15,700) and close to the figure of Greece (EUR21,300). Other measures of living standards are also comparable to those in these two countries. Services account for about 64% of GDP, industry for 34% and agriculture for just 2%. The economy's export-intensity (ratio of exports of goods and services to GDP) had increased to almost 70% in 2007-2008, but fell back to 59% in 2009. Fellow EU members absorbed 70% of merchandise exports in 2009, while the share of countries of former Yugoslavia fell to 13% from 17% in 2008. The high dependence on exports and on the EU business cycle implies a high susceptibility to external shocks.

After annual average growth of 4.8% in 2004-2008, real GDP contracted by a hefty 7.8% in 2009 owing to the impact of the global economic crisis. The economy remained in recession in Q1 2010, shrinking 0.5% qtr/qtr and 1.2% yr/yr. We expect a mild recovery to set in in the remainder of the year and currently forecast about 0.5% growth in calendar 2010 and 2% in 2011. However, potential weaknesses in major euro zone economies pose considerable downside risks to this outlook.

Since Slovenia's accession to the euro zone in 2007, monetary policy is conducted by the European Central Bank (ECB). Inflation (EU harmonised measure) peaked at 6.9% yr/yr in July 2008 owing to rises in food and energy prices but eased sharply during 2009 on account of lower global oil prices and shrinking domestic demand. Average inflation in the first five months of 2010 was 2.1% and we expect a slightly higher rate for the year as a whole. The real effective exchange rate based on consumer prices is not overvalued, however, based on unit labour costs in Q4 2009 it was 6.8% higher than the average of the previous five years (this compares to 6.1% for the euro zone and 1% for Germany). Membership of the euro zone provides for low transfer and convertibility risk (as long as the euro zone remains intact) and has substantially decreased external vulnerabilities related to exchange rate volatility.

Budgetary policy has been reasonably sound in the past, reflected in annual fiscal deficits of less than 3% of GDP (ESA 95 standard) in 2002-2008. Public debt had fallen to 22.6% of GDP in 2008. As a result of recession-related lower revenues and several crisis-related supplementary budgets, however, the fiscal deficit rose sharply to 5.5% of GDP in 2009 and is forecast to reach about 6% in 2010. Public debt rose to 35.9% of GDP in 2009 which, however, was still well below the euro zone average of 79%.

Slovenia's external position is still reasonably good. The current account deficit narrowed to just 1% of GDP in 2009 and is forecast to remain low at about 2% in 2010-2011. Gross external debt is relatively high in relation to GDP (approximately 120% at end-2009) and export earnings (203%). However, around 75% of gross external liabilities are balanced by gross external assets such that net external

debt stood at 31% of GDP at end-2009. While this ratio is more favourable, it should be noted that it is sharply trending upwards; in 2004 Slovenia was still a net external creditor.

Structural Business Environment

The Structural Business Environment is strong. The solid macroeconomic environment has allowed Slovenia to implement structural and institutional reforms more gradually than other transition countries. In particular, the privatisation process has been somewhat slower than elsewhere, but there was no urgent need to privatise. Foreign direct investment has been modest because of political opposition to privatisation of state-owned sectors as well as the small size of the Slovene market, which has made it less attractive for foreign investors. Nonetheless, the economy is market-oriented and the government today allows foreign investment in most industries. Foreign investors are free to repatriate profit and capital after tax. The Slovene legal framework, including insolvency legislation, is sound and protects property rights well. What still could be a problem, however, is the reported inadequate staffing of the court system. With the exception of the labour market, the level of regulation in Slovenia is low and the administrative ability is assessed as good. Corruption is not a major problem. According to Transparency International, the level of corruption in Slovenia is the lowest among all Eastern European countries, on a par with Estonia. The *2009 Corruption Perception Index* assigns the country rank 27= out of 180 countries with a rating of 6.6 on a scale from 10 (highly clean) to 0 (highly corrupt).

Slovenian banks have withstood the impact of the global financial crisis relatively well so far, thanks to limited exposure to structured financial products and other toxic assets, the modest level of household debt (about 30% of GDP) and adequate financial stability measures adopted by the authorities. Private sector credit growth has decelerated from 33% in H2 2007 (43% above the median of 160 emerging markets) to 17% at end-2008 (19% below the median) and just 3% at end-2009. This has reduced credit risks but also corporate funding possibilities. The level of nonperforming loans is relatively low but increasing according to an IMF note from June 2010, owing to the banks' exposure to highly leveraged companies, in particular in the construction sector. Another source of risk is earlier lending to risky countries in South Eastern Europe.

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Charts

