We welcome the opportunity to discuss the CAS Progress Report for Slovenia. This country is a “Washington Consensus” success story. Prices were liberalized, barriers to trade reduced, fiscal policy was tight, and a whole set of first-generation reforms was launched. Gradually, following these orthodox policies, per-capita income has increased by more than 50% to reach roughly $10,000 in only seven years. Slovenia is the first transition country to initiate graduation from the World Bank and is moving fast to access the European Union. The key to Slovenia success story has been its careful macroeconomic management and its highly educated workforce.

While the most important macroeconomic variables are showing significant convergence with EU standards, there are some indicators that raise questions that may need to be addressed. We see the foreign sector as potentially weak.

Despite the fact that the real exchange rate is a non-issue in Slovenia we would like to be reassured that there is no problem of currency appreciation. We reflect on this because we think that competitiveness is a very important matter for this country. When we measure the real exchange rate as the ratio of tradable to non-tradable goods, approximated by the ratio of domestic whole sale price index (WPI) to domestic consumer price index (CPI), there is a steady downward appreciating trend. To highlight this matter, we are presenting below a chart showing the real exchange rate and the deficit in goods and services.
Furthermore, Slovenia experienced during 1999 a rather high current account deficit, 2.9%, its first one since 1996. It seems this current account deficit was due to an expansion in the domestic credit. Chart No 2 below presents the net change in foreign assets and the change in domestic credit.

Chart 2

Change in Net Foreign Reserves and Change in Domestic Credit

Source IFS. Domestic credit includes total credit to private and public sector

Chart 2 is a textbook example of the monetary approach to the balance of payments. We would very much appreciate staff comments regarding the source of domestic credit changes, as we deem this of significant importance to explain recent pressures on the balance of payments.

In relation to the fiscal and labor market policies, we are indeed concerned by a very high ratio of government expenditures to GDP and the fact that Slovenia may be setting up the stage for a European style structural unemployment. A flexible labor market will be crucial for a small and open economy like Slovenia to be able to absorb the volatility of capital flows. Open access to those flows would be of great benefit, but the costs would be substantially reduced by a very flexible economy.
Slovenia has been rather slow in some areas of structural reforms. We believe a faster track would be desirable as there is no other way to play in a world class league. We support the government program, adopted last January, to encourage FDI. Eliminating obstacles to foreign investors will stimulate a wide range of productive sectors and export penetration in the EU.

The unfinished agenda

a) Privatization
   Complete privatization of the State-owned banks, insurance companies, utilities and residual stakes in privatized enterprises;

b) Corporate governance
   Strengthen the enterprise sector through measures such as protecting minority shareholders’ rights, improving the quality and disclosure of information and supervision, and increasing the enforcement capacity of the capital market regulatory agency;

c) Pension system
   Ensure the expansion of a voluntary fully-funded pension system;

d) Labor market
   Remove labor market rigidities –such as the semi-centralized wage setting mechanism and the over-protective legislation– that discouraged employment creation and impeded the efficient allocation of labor.

We encourage the Bank to be prepared to support the Government of Slovenia through policy advice and analytic activities in these fields, or in those Slovenian authorities may require. We also encourage IFC and MIGA to provide technical assistance and advice to the Slovenian private sector.