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Assessment of the 2014 national reform programme and stability programme for SLOVENIA

Accompanying the document

Recommendation for a COUNCIL RECOMMENDATION

on Slovenia's 2014 national reform programme and delivering a Council opinion on Slovenia's 2014 stability programme

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EXECUTIVE SUMMARY

After a prolonged recession, recent data indicates that a fragile recovery has commenced in Slovenia. In 2013, real GDP was 10% below its 2008 peak but quarter-on-quarter growth in all quarters of 2013 was positive with a particularly strong pick up in the final quarter. The recovery appears to be broad based with improvements on both the external and domestic side. In light of the improving consumer and business confidence, real GDP is forecast to grow by 0.8% in 2014 and accelerate to 1.4% in 2015. The key drivers of the projected recovery are continued investment by the government mostly through EU-funded projects and the positive contribution from the external side

Slovenia has made some progress in addressing the 2013 country-specific recommendations. It has made substantial progress towards stabilising the banking sector and limited progress in fiscal consolidation, safeguarding long-term fiscal sustainability, restructuring of the corporate sector, privatisation and improving the business environment. New legislation to establish the Slovenian Sovereign Holding was adopted in late March 2014. The necessary legal basis to underpin restructuring of the corporate sector was approved at the end of 2013. The adoption of the Fiscal Rule Act, which would provide the legal basis for the general government budget balance/surplus rule, has been delayed and other important reforms identified in the 2013 country-specific recommendations have lagged.

The 2014 stability programme and national reform programme set out the policy priorities and the path for the correction of the excessive macroeconomic imbalances. The stability programme provides the macro-economic and fiscal forecasts for Slovenia until 2018 and reaffirms Slovenia's commitment to correcting the excessive deficit by 2015. The 2014 national reform programme sets out policy priorities and structural reforms for the next two years. The government presented a three-pillar strategy, covering the financial sector (further restructuring and consolidation of banks, restructuring and deleveraging of companies, insolvency procedures), management of state assets in the corporate sector including privatisation (the Slovenian Sovereign Holding) and further fiscal consolidation (including adoption of the Fiscal Rule Act, mid-term fiscal planning and long-term sustainability of public debt). The three-pillar strategy provides for additional structural measures that could underpin the economic recovery and improve the competitiveness of the Slovenian economy.

The main challenges for Slovenia are:

- **Fiscal policy and long-term fiscal sustainability:** There are risks to Slovenia reducing its deficit in line with the excessive deficit procedure (EDP) recommendation. Furthermore, the government debt-to-GDP ratio has increased substantially in recent years and is forecast to surpass 80% of GDP in 2014. High public debt may hamper growth prospects by dampening domestic demand and reducing productive public spending. In light of an ageing population, substantial pressure is mounting on the sustainability of public finances, especially from increasing expenditures on the pension and healthcare system.

- **Restructuring of the banking sector:** Significant effort has been made to stabilise the banking sector. However, the restructuring is far from complete and substantial challenges lie ahead. The level of non-performing loans is still high relative to pre-crisis levels. In turn, this erodes banks' profitability and discourages banks from providing new credit, affecting the corporate sector and especially SMEs. Further

recapitalisation and consolidation of the banking sector, particularly small state-owned banks, could be needed.

- **Corporate sector restructuring:** The insolvency framework has been amended in order to facilitate the swift resolution of non-performing loans. In practice the financial and operational restructuring of the corporate sector is just beginning. The successful restructuring of significant cases could substantially improve the business climate in the corporate sector, which is currently burdened with a high level of indebtedness. Reducing the sector's debt overhang could support its capacity to invest in innovative projects.

- **Better management of state-owned and state controlled enterprises:** The legal basis for the Slovenian Sovereign Holding was adopted in April 2014 and the strategy for classification of state assets is expected to be adopted by July 2014 as stipulated in the law. Greater clarity on the government's strategy for managing state-owned enterprises, coupled with improved corporate governance and a transparent privatisation process could assist in creating a more favourable business environment and help to attract foreign direct investment.

- **Better business environment:** Ongoing privatisation and corporate restructuring offer many new possibilities for private investors. However, the challenging business environment with lengthy bureaucratic procedures and vested interests hinders Slovenia from taking full advantage of this process. Furthermore, product market regulations are unfavourable and hinder effective competition, especially in services.

- **Labour market:** The 2013 labour market reform has yielded positive effects to date and has marginally reduced labour market segmentation. While the reform requires time to take full effect the evaluation published in April 2014 points to challenges that need to be addressed (i.e. employment of older workers).

- **Improvement of the efficiency of public administration:** Greater efficiency of public administration would improve the capacity to effectively implement and monitor strategies, laws and structural reforms. High levels of corruption weigh on the economy. Despite recent reforms and improvements, the civil justice system remains slow and suffers from a backlog of cases.

1. INTRODUCTION

In May 2013, the Commission proposed a set of country-specific recommendations (CSRs) for economic and structural reform policies for Slovenia. On the basis of these recommendations, the Council of the European Union adopted nine CSRs in July 2013. These country-specific recommendations cover the following topics: fiscal policy and long-term fiscal stability (including pension reform and long-term care); effective tailor-made active labour-market policy measures, skills mismatches, wages and labour market segmentation; restructuring of the banking and corporate sectors, including Slovenian Sovereign Holding; privatisation; selected aspects of the business environment; and the efficiency of the public administration. All of these issues impede the competitiveness of the Slovenian economy. This staff working document (SWD) assesses the state of implementation of these recommendations in Slovenia.

This SWD assesses policy measures in light of the findings of the Commission's Annual Growth Survey 2013[1] and the third annual Alert Mechanism Report[2], which were published in November 2013. The AGS sets out the Commission's proposals for building the necessary common understanding about the political priorities for action at national and EU level in 2014. It identifies five priorities to guide Member States to renewed growth in 2014: pursuing growth-friendly fiscal consolidation; restoring normal lending to the economy; promoting growth and competitiveness for today and tomorrow; tackling unemployment and the social consequences of the crisis; and modernising public administration. The AMR serves as an initial screening device to ascertain whether macroeconomic imbalances exist or risk emerging in Member States. The AMR found positive signs that macroeconomic imbalances in Europe are being corrected. To ensure that a complete and durable rebalancing is achieved, Slovenia and 15 other Member States were selected for a review of developments in the accumulation and unwinding of imbalances. These in-depth reviews were published on 5 March 2014, along with a Commission communication.[3]

Against the background of the 2013 Council Recommendations, the AGS, the AMR and the in-depth review, Slovenia presented the 2014 national reform programme (NRP)[4] on 15th of April 2014 and the stability programme[5] on 28th of April 2014. Both programmes have been prepared and approved prior to the dissolution of the Parliament in May 2014 and provide detailed information on progress made since July 2013 and on the government's planned measures. The 2014 national reform programme went through comprehensive public consultation. The information included in these programmes, combined with information provided on several bilateral meetings that have taken place in the course of 2014, are the basis for the assessment made in this staff working document.

[1] COM(2013) 800 final.
[2] COM(2013) 790 final.
[3] Aside from the 16 Member States identified in the AMR, Ireland was also covered by an in-depth review, following the Council's conclusion that it should be fully integrated into the normal surveillance framework after the successful completion of its financial assistance programme.
[4] http://ec.europa.eu/europe2020/pdf/csr2014/nrp2014_slovenia_sl.pdf
[5] http://www.mf.gov.si/fileadmin/mf.gov.si/pageuploads/mediji/2014/program_stabilnosti_2014.pdf

2. ECONOMIC SITUATION AND OUTLOOK

Economic situation

After a prolonged recession, recent data indicates the start of a fragile recovery. In 2013, Slovenia's real GDP contracted by 1.1% and was 10% below the peak levels experienced in 2008. However, in 2013 the economy grew quarter-on-quarter every quarter and growth was particularly strong in the fourth quarter. The recovery appears broad-based with improvements on both the external and domestic side. Exports remained resilient throughout 2013 and investment was slightly positive thanks to EU-funded projects. Unemployment increased from 4.4% in 2008 to 10.2%. The budget deficit increased significantly in 2013, to 14.7%, largely due to the support given to banks (4.4% without bank recapitalisation). The current account surplus increased to 5.3% of GDP in 2013.

Economic outlook

The recovery is expected to take hold in 2014. In light of the positive developments in 2013 and improving consumer and business confidence, the Commission 2014 spring forecast expects real GDP to grow by 0.8% in 2014, accelerating to 1.4% in 2015. The key drivers of the projected recovery are continued investment by the government mostly through EU-funded projects and net exports. While the ongoing deleveraging process is expected to continue weighing on domestic demand, private consumption is expected to turn positive in 2014 and increase further in 2015. The moderate recovery in domestic demand is expected to bring growth of real imports more in line with that of exports. However, the external balance of goods and services is set to improve further, also due to still favourable terms of trade. Employment is expected to stabilise in 2014 before growing modestly again in 2015. Labour force developments are projected to lag employment dynamics and the unemployment rate is expected to peak in 2014 at around 10%. Private sector wages are expected to continue increasing very moderately this year and slightly accelerate in 2015, while public-sector wages are frozen until end-2014 but are expected to increase by 1.5% in 2015, on a no-policy-change basis. As a result, overall unit labour costs are projected to grow moderately this year and next. Given the very low pressure on inflation from import prices and labour costs, inflation is forecast to decline further to historically low levels in 2014 and pick up slightly in 2015. The government deficit is forecast to stand at 4.3% of GDP in 2014, including 0.9% of GDP for the planned recapitalisation of Abanka and Banka Celje. Furthermore, the authorities have extended the deadline for the recapitalisation of Gorenjska Banka until 31 December 2014 and have committed to recapitalise the bank with state funds if private sources do not materialise. In 2015, the deficit is expected to fall to 3.1% of GDP, based on a no-policy-change assumption, helped by the improving economic outlook. No recapitalisation needs have been factored into the 2015 deficit forecast.

The macroeconomic scenario underlying the budgetary projections of the stability programme and the national reform programme was revised upwards in March 2014. According to the projections of the Institute of Macroeconomic Analysis and Development (IMAD), real GDP will grow by 0.5% in 2014, 0.7% in 2015 and 1.3% in 2016. Assessed against currently available information, including the Commission 2014 spring forecast and internal projections for growth beyond 2015, IMAD's macro scenario for 2014 and 2015 appears cautious.

3. CHALLENGES AND ASSESSMENT OF THE POLICY AGENDA

The 2014 national reform programme confirms that Slovenia has made some progress in implementing the 2013 country-specific recommendations, yet, the work is far from complete. Slovenia continues to experience excessive macroeconomic imbalances which require specific monitoring and continuing strong policy action (see Box 3). The national reform programme provides an insight into government plans on how to address the existing excessive imbalances and policy challenges and thus contains important new commitments, which could help to effectively tackle the challenges faced by Slovenia, if implemented in a rigorous and timely manner. A assessment of the implementation progress achieved in regard to the 2013 country-specific recommendations is available in Section 4. The remainder of this staff working document assesses the policy agenda in light of these challenges, with a particular emphasis on determining whether this agenda is sufficiently ambitious and credible in order to address the identified excessive imbalances.

The 2014 stability programme reaffirms Slovenia's commitment to correcting the excessive deficit by 2015 in line with the excessive deficit procedure and achieving a balanced budget position in structural terms by 2017. The programme provides the macro-economic and fiscal forecasts for Slovenia until 2018 and is the first update of the authorities' macroeconomic and fiscal projections since the 2014 Budget. Furthermore, it provides details of the path anticipated for the debt until 2018, which is projected to remain above the 60% of GDP reference value for the duration of the programme.

3.1. Fiscal policy and taxation

Budgetary development and debt dynamics

The objective of the budgetary strategy outlined in the 2014 stability programme is to correct the excessive deficit by 2015 and reach the medium-term objective (MTO) by 2017. While the programme confirms the previous medium-term objective of a balanced budget, which is in line with the Stability and Growth Pact requirements, it forecasts a deficit in structural terms for the duration of the programme. The programme plans to bring the deficit below 3% of GDP in 2015, in line with the target set in the excessive deficit procedure recommendation. Beyond 2015, the programme envisages a steady decline in the deficit before turning to a surplus of 0.3% of GDP in 2018.

The deficit increased significantly to 14.7% of GDP in 2013, from 4% in 2012, largely due to the one-off recapitalisation of the banking sector. The general government deficit excluding bank recapitalisations stood at 4.4% of GDP, as against the 4.2% target in the previous programme update and the 3.8% estimate in the Draft Budgetary Plan (also excluding recapitalisations), and 0.7 pp. of GDP above the excessive deficit procedure recommendation of 3.7%. The other key drivers of the deviation were non-financial one-offs unforeseen at the time, namely the impact of court rulings on public sector wages and the compensation of persons removed from the register of residents after independence, which added a net 0.7% of GDP to the deficit.

The structural adjustment, recalculated according to the commonly agreed methodology[6], falls short of the excessive deficit procedure requirement for 2013. The

[6] Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission services on the basis of the information provided in the programme, using the commonly agreed methodology.

shortfall amounts to 0.6 % of GDP in 2013. Based on a bottom-up assessment, which estimates the size of the additional fiscal effort on the basis of the discretionary revenue measures and the expenditure developments under the control of the government between the baseline scenario underpinning the June 2013 excessive deficit procedure recommendation and the Commission 2014 spring forecast, the overall fiscal effort for 2013 amounts to around 1% of GDP, broadly in line with the additional consolidation measures mentioned in the June 2013 excessive deficit procedure recommendation as consistent with reaching the structural target for 2013.

Box 1. Excessive deficit procedure for Slovenia

Slovenia is currently subject to the corrective arm of the Stability and Growth Pact. The Council opened the Excessive Deficit Procedure for Slovenia on 2 December 2009 and on 21 June 2013 recommended to correct the excessive deficit by 2015 at the latest. The recommendation specified a headline general government deficit target of 4.9% of GDP in 2013 (3.7% of GDP without 1.2% of GDP one-off expenditure to recapitalise the two largest banks as estimated at the time of the recommendation), 3.3% of GDP in 2014 and 2.5% of GDP in 2015, which is consistent with an annual improvement of the structural balance of 0.7 pp. of GDP in 2013, 0.5 pp. of GDP in both 2014 and 2015. Furthermore, the recommendation specified that Slovenia should rigorously implement the measures already adopted to increase indirect tax revenues and reduce the public-sector wage bill and social transfers, while standing ready to complement them with additional measures if their yield would prove less than foreseen. In addition, Slovenia should specify, adopt and implement new structural consolidation measures that are necessary to achieve the correction of the excessive deficit by 2015.

The year following the correction of the excessive deficit, Slovenia will be subject to the preventive arm of the Pact and should ensure sufficient progress towards its medium-term objective. As the debt ratio in 2015 is projected at 81.1% of GDP, exceeding the 60% of GDP reference value, during the three years following the correction of the excessive deficit Slovenia will be subject to the transitional arrangements as regards compliance with the debt criterion, during which it should ensure sufficient progress towards the debt benchmark.

Based on its 2014 winter forecast, the Commission considered that there were risks to Slovenia achieving a durable correction of the excessive deficit by 2015. In light of this, on 5 March 2014 an Autonomous Commission Recommendation was addressed to Slovenia indicating that Slovenia should make efforts to ensure full compliance with the Council recommendation of 21 June 2013 and take the necessary steps to ensure that the structural effort recommended by the Council is met.

In 2014, the headline deficit is projected to improve considerably to 4.1% of GDP. This is significantly below the headline deficit envisaged in the Draft Budgetary Plan of 6.7% of GDP but the difference is due to the timing of bank recapitalisations. Excluding bank recapitalisations, the stability programme envisages a deficit of 3.2% of GDP vs. 3.3% in the Draft Budgetary Plan. The most significant cause of the deviation from the Draft Budgetary Plan is the decision by the constitutional court to repeal the new real estate tax, which was expected to yield additional revenue of 0.5% of GDP in 2014. The government has introduced several revenue raising and expenditure reducing measures, which partially offset this, but the headline deficit remains above the 3.3% envisaged in the excessive deficit procedure recommendation. The programme also includes in 2014 one-off proceeds of 0.4% of GDP arising from the auction of the 4G telecom spectrum licenses, completed in April 2014.

In 2015, the authorities target a deficit of 2.4% of GDP, which is slightly below the excessive deficit procedure recommendation of 2.5% of GDP. No additional bank recapitalisation needs are included in the programme beyond 2014. The programme expects a significant further decline in the public-sector pay bill by 5% in 2015, which would be largely due to a continuation of both the freeze in wages that has yet to be agreed with the trade unions, and the reduction in public sector employment, which has proved difficult to enforce at the sub-central government level. The programme also includes cuts to other expenditure items that need to be specified in detail, while it projects tax revenues to decline in 2015 also due to the expected subdued nominal GDP growth, on the back of continued fiscal consolidation.

The consolidation is expected in the programme to continue also in 2016-18, focusing mainly on the expenditure side. The revenue-to-GDP ratio is projected to decrease by 1.3 pp. from 2013 to 2018, whereas total expenditure (without one-offs) is targeted to drop by around 6 pp. over the same period.

The revenue measures outlined in the programme are of a more permanent nature than the expenditure measures. The budgetary implications of most envisaged measures are quantified both for 2014 and 2015 (see Box 2). Furthermore, the programme envisages to step-up the fight against the grey economy and improve the collection of taxes, which is expected to yield 0.2 pp. of GDP in 2014. Several of the measures necessary to meet the deficit targets for 2015 and beyond are unspecified.

An Autonomous Commission Recommendation was issued to Slovenia in March 2014 asking for full compliance with the excessive deficit procedure recommendation. The programme does not include a dedicated section regarding the Autonomous Commission Recommendation and the actions that are being taken to address it, despite the Autonomous Commission Recommendation requesting one. The programme identifies some additional measures that assist in narrowing the gap between the planned fiscal effort and that recommended under the excessive deficit procedure. Based on this it is considered that the programme has partially responded to the Autonomous Commission Recommendation. To mitigate the risks identified in the Autonomous Commission Recommendation, additional measures beyond those specified in the programme may be needed.

Based on the assessment of the programme and the Commission 2014 spring forecast there are risks to Slovenia meeting its deficit targets for 2014 and in turn ensuring the correction of the excessive deficit in a credible and sustainable manner by 2015. In 2015, a risk to the envisaged deficit is the possible need of additional capital supports to the banks stemming from the 2013 asset quality review and stress test, as the deadline for the recapitalisation of Gorenjska Banka was extended until end-2014 and the government committed to use state funds if private sources do not materialise. There are also risks that measures producing a sufficient structural effort will not be adopted over the forecast horizon. In 2014 in (recalculated) structural terms, the programme projects an improvement of 0.8 pp. of GDP in 2014, i.e. above the 0.5 pp. recommended effort. The Commission 2014 spring forecast, however, expects no improvement in uncorrected structural terms and a -0.7 pp. of GDP deterioration in corrected structural terms. In 2015, the (recalculated) structural balance is planned to improve by 0.6 pp, again slightly better than the recommended 0.5 pp. of GDP. By contrast, the Commission forecast, based on a no-policy-change assumption, projects a headline deficit of 3.1% of GDP and a structural adjustment of just 0.2 pp. of GDP in uncorrected terms and 0.1pp. of GDP in corrected terms. Over the period 2013-2014, the cumulative fiscal effort in corrected structural terms falls short of the recommended effort by 1.4% of GDP. The bottom-up assessment of the forecast fiscal effort indicates that, in 2014,

the effort would be approximately 1% of GDP, some 0.5 pp. below the additional consolidation measures mentioned in the June 2013 excessive deficit procedure recommendation as consistent with reaching the structural target for 2014.

Box 2. Main measures

The public finances measures in 2014 largely continue policies initiated in 2012-13. The tax income shortfall created by the repealed real estate tax is planned to be partly offset by a combination of new and one-off measures (e.g. increased dividends). On the expenditure side, the intention is for several policies to extend into 2015: freezes in indexation arrangements (already agreed for pensions, planned also for public wages), decrease in public sector employment and continued reduction in intermediate consumption and subsidies. Detailed annual budgetary impacts of major macro-structural reforms (e.g. pension reform) over the programme horizon are not presented.

Main budgetary measures	
Revenue	**Expenditure**
2013	
• Reduction in the corporate income tax rate to 17% (-0.1% of GDP) • Higher road user charge (full-year impact 0.1% of GDP) • New tax on financial services and amended bank assets tax (0.1% of GDP) • Increase in VAT rates from 1 July (full year impact 0.7% of GDP) • New taxes on lottery tickets from 1 August (full year impact 0.05% of GDP)	• Cut in public sector holiday allowance (-0.15% of GDP) • Cancelled indexation of public sector wages (-0.15% of GDP) • Cancelled promotions for 2013 (-0.15% of GDP) • Higher meals allowance for students (permanent) (0.1% of GDP) • Additional measures to curb the public sector wage bill from 1 June (full year impact -0.2% of GDP) • Lower unemployment benefits from 1 July (full year impact -0.05% of GDP) • Lower capital expenditure (full year impact -0.3% of GDP) • Lower intermediate consumption (full year impact -0.1% of GDP)
2014	
• Biodiesel - the abolition of the excise duty refund labour law from April (0.05% of GDP in 2014 / full year impact 0.1% of GDP) • Increase of excise duty on fuels, alcohol and tobacco from April (0.1% of GDP in 2014 / full year impact 0.2% of GDP) • Continued measures to tackle grey economy (0.2% of GDP)	• Cancelled indexation of pensions (-0.1% of GDP) • Cancelled indexation of public sector wages (-0.15% of GDP) • Cancelled promotions for 2014 (-0.15% of GDP) • Lower transfers to indirect budgetary users (-0.1% of GDP) • Payment of promotions relating to 2011-2012 (+0.2% of GDP)
2015	
• PIT - Extension of 4th bracket – planned (0.04% of GDP)	• Cancelled indexation of pensions (-0.1% of GDP)

• Tax on insurance contracts - planned (0.10% of GDP)	• Cancelled indexation of public sector wages - planned (-0.15% of GDP) • Lower transfers to indirect budgetary users (-0.1% of GDP)
Note: The budgetary impact in the table is the impact reported in the programme, i.e. by the national authorities or in parallel budget documents. A positive sign implies that revenue / expenditure increases as a consequence of this measure. The degree of detail reflects the type of information made available in the stability programme and other budget documents.	

Looking beyond 2015, after correcting the excessive deficit, the consolidation effort declines gradually over the programme horizon. The (recalculated) structural balance is planned to continue improving at a slower pace in the outer years of the programme, by 0.5 pp. of GDP in 2016, 0.2 pp. in 2017 and 0.5 pp. in 2018. This is not fully in line with the requirement under the preventive arm of the Stability and Growth Pact of at least 0.6 pp. of GDP improvement when the output gap closes to above -1.5% of GDP, which is expected to happen as from 2016.

The general government gross debt is projected to remain above the 60% of GDP reference value for the duration of the programme. Debt increased sharply in recent years, to 71.7% of GDP in 2013, and continues to rise under the programme to 80.9% in 2014, due to the projected sharp increase in interest expenditure and the still negative primary balance. The debt ratio is projected to stabilise at 81.1% of GDP in 2015. This is broadly in line with the Commission 2014 spring forecast, which estimates debt at 80.4% and 81.3% of GDP in 2014 and 2015 respectively. For the period 2016-18 the debt is expected to fall steadily to 70.4% of GDP in 2018 due to the increasing primary surpluses and healthier output growth rates.

Fiscal framework

Slovenia did not progress adequately in improving its fiscal framework. In 2013, Slovenia received a country-specific recommendation concerning the adoption of a general government budget balance/surplus rule, the introduction of a binding, encompassing and transparent medium-term budgetary framework, and the strengthening of the independent bodies monitoring fiscal policy. The analysis in this staff working document leads to the conclusion that Slovenia has so far made limited progress in addressing this recommendation.

The authorities are currently preparing to overhaul the legislation underpinning Slovenia's fiscal framework, in compliance with the Treaty on Stability, Coordination and Governance in the European Monetary Union and secondary European legislation on fiscal governance (in particular Council Directive 2011/85/EU on requirements for budgetary frameworks). The Slovenian Constitution was amended in May 2013 to provide the basis for the general government budget balance/surplus rule. Nevertheless, the authorities have missed the November 2013 deadline for implementation of the necessary legislation, namely the binding Fiscal Rule Act.[7] A draft bill has been prepared and made available to the Commission in mid-March 2014. The programme foresees the Fiscal Rule Act to be adopted

[7] The legislation must provide definitions of revenue and expenditure, general government, structural balance, as well as the format and mandate of the Fiscal Council. It must also provide details of the escape clause, a definition of significant deviations from the mid-term objective (MTO) or the adjustment path towards it, and the activation of the underlying correction mechanism. Furthermore, the necessary legislation has to be passed by a two-thirds majority in the parliament.

by parliament with two thirds majority but fails to define a timeline for its adoption. Given the current political situation in Slovenia, there are risks to the adoption of the legislation.

A fiscal council was established in 2009, but its effectiveness has been limited by its unclear mandate and it is currently not operational. The Fiscal Rule Act provides an opportunity to strengthen the role of the fiscal council and enhance its visibility and resources so that it can provide a genuine multi-annual perspective on fiscal policy. It is envisaged that the responsibility for producing the macroeconomic forecast on which the government's budgetary plans are based will remain with the Slovenian Institute of Macroeconomic Analysis and Development, which is a government entity charged with monitoring and analysing current and structural economic developments.

Linked to the Fiscal Rule Act, the government also foresees the adoption of the Public Finance Act, which would contain very specific provisions for preparation, implementation and monitoring of the budget of all the governmental budgetary users. This act would regulate preparation and implementation of budgets with special attention to be given to control mechanism and sanctions, in order to reduce fiscal imbalances and consequently ensure medium-term sustainability. The national reform programme fails to define a timeline for its adoption, thus it cannot be excluded that adoption of this act may be postponed.

Long-term sustainability

Slovenia appears to face fiscal sustainability risks in the medium term. The medium-term sustainability gap[8] , showing the adjustment effort up to 2020 required to bring debt ratios to 60% of GDP in 2030, is at 1.9% of GDP, primarily related to the high level of government debt (forecast at 81.3% of GDP in 2015) and the projected ageing costs (contributing 0.9 pp. of GDP per year until 2030).

In the long term, Slovenia appears to face high fiscal sustainability risks, primarily related to the projected ageing costs, in particular in the field of pensions. Aging costs are projected to contribute 6 pp. of GDP over the very long run. The long-term sustainability gap[9] shows that the adjustment effort needed to put the debt-to-GDP ratio on a non-increasing path is of 6.6 pps of GDP. Risks would be higher in the event of the structural primary balance reverting to lower values observed in the past, such as the average for the period 2004-2013. It is therefore appropriate for Slovenia to reduce government debt and to further contain age-

[8] See Table 5 in the Annex. The medium-term sustainability gap (S1) indicator shows the upfront adjustment effort required, in terms of a steady improvement in the structural primary balance to be introduced until 2020, and then sustained for a decade, to bring debt ratios back to 60% of GDP in 2030, including financing for any additional expenditure until the target date, arising from an ageing population. The following thresholds were used to assess the scale of the sustainability challenge: (i) if the S1 value is less than zero, the country is assigned low risk; (ii) if a structural adjustment in the primary balance of up to 0.5 p.p. of GDP per year until 2020 after the last year covered by the autumn 2013 forecast (year 2015) is required(indicating an cumulated adjustment of 2.5 pp.), it is assigned medium risk; and, (iii) if it is greater than 2.5 (meaning a structural adjustment of more than 0.5 p.p. of GDP per year is necessary), it is assigned high risk.

[9] See Table 5 in the Annex. The long-term sustainability gap (S2) indicator shows the immediate and permanent adjustment required to satisfy an inter-temporal budgetary constraint, including the costs of ageing. The S2 indicator has two components: i) the initial budgetary position (IBP) which gives the gap to the debt stabilising primary balance; and ii) the additional adjustment required due to the costs of ageing. The main assumption used in the derivation of S2 is that in an infinite horizon, the growth in the debt ratio is bounded by the interest rate differential (i.e. the difference between the nominal interest and the real growth rates); thereby not necessarily implying that the debt ratio will fall below the EU Treaty 60% debt threshold. The following thresholds for the S2 indicator were used: (i) if the value of S2 is lower than 2, the country is assigned low risk; (ii) if it is between 2 and 6, it is assigned medium risk; and, (iii) if it is greater than 6, it is assigned high risk.

related expenditure[10] growth to contribute to the sustainability of public finances in the medium and long term.

Risks to the long-term sustainability of the pension, health and long-term care systems, as identified in the 2013 country-specific recommendations, persist. In 2013, Slovenia received a country-specific recommendation on strengthening the long-term sustainability of the pension system and improving the efficiency and cost-effectiveness of the long term care. The analysis in this staff working document leads to the conclusion that Slovenia has made limited progress on addressing this recommendation. The pension reform, adopted in December 2012 and taking effect from January 2013, has shown positive first effects despite the initial transition period. While certain fiscal savings have been realised in 2013, further stabilisation of pension-related expenditures is expected for the period 2014-20, before it would become unsustainable (as projections after 2020 show). Old-age pensions benefit levels remained largely unchanged, but the Act on Executing the State Budget temporarily froze the indexation of pensions in 2014-15. The number of new old-age pensioners in 2013 decreased almost by 40% compared to 2012.[11] Such a low level in 2013 could be explained by anticipation effects of the new regime. People, eligible for retirement, retired under the old legislation that provided benefits for years of education and military service. Despite certain positive developments, the 2012 pension reform does not link pensionable age to gains in life expectancy and does not explore measures to stimulate private contributions to the second pillar. These options could be explored in the framework of the White Paper that would launch public consultation on a comprehensive post 2020 pension reform, as suggested by the national reform programme.

To avoid inefficient linear budgetary cuts, a targeted reorganisation of the healthcare system to explore internal synergies and realise savings would be beneficial. In the last two years, efforts have concentrated on budget consolidation measures including cutting prices of healthcare services and increasing the share of private funding and contribution rates for certain groups. In parallel, the number of patients on waiting lists (which measures access to healthcare services) increased substantially from around 40 000 for 52 services (end of 2011) to 62 000 for 46 services (end of 2012). The authorities have requested the World Bank's technical assistance to review expenditures in health care system in order to improve cost-effectiveness, quality and service delivery. As suggested by the national reform programme, the authorities are committed to the reorganisation of health care sector that would bring substantial savings through the joint public procurement and regional organisation of back-office services but the timeline for action is unclear. A pilot project of joint public procurement was conducted and substantial savings have been realised, proving that it would be beneficial to extend this approach to the whole system. However, increasing the scope of the procurement bids could increase the risk of overpricing[12] or delivering unsatisfactory quality of products. To address previous allegations of corruption, the introduction of common tenders should be transparent, with sufficient reviews and quality control mechanisms.

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[10] Ageing costs comprise long-term projections of public age-related expenditure on pension, health care, long-term care, education and unemployment benefits. See the 2012 Ageing Report for details.

[11] According to the national reform programme 2014-15 and the Evaluation of the pension reform (April 2014) the number of new retirees in 2013 reached 15.512, almost 40% lower than in 2012 (25.262).

[12] The national TV Slovenia 1 reported on 5 April 2014 about a public procurement for a blood thinner in the hospital in Slovenj Gradec (http://www.rtvslo.si/zdravje/video-varcevanje-v-zdravstvu-v-praksi-direktor-bolnisnice-kar-k-proizvajalcu/333911). Two domestic wholesalers (Salus & Kemofarmacija) offered practically identical offers charging EUR 200.643 and EUR 199.973, while the French producer Sandofi-Aventis directly submitted a 10 times cheaper offer at EUR 19.546.

Long-term sustainability pressures stem from increasing demand for long-term care. The government adopted a blueprint for long-term care reform at the end of 2013, and the related legislation is expected to be adopted by November 2014, as suggested by the national reform programme. However, the adoption of the legislation risks to be postponed given its linkages to the healthcare reform. More particularly, the financing of the long-term care is linked to the redistribution of the existing funding received through several sources, including the current healthcare insurance system. The reform is a step in the right direction to contain age-related increase in long-term care, while ensuring access to quality services. It envisages creating a single entry point, a uniform expert procedure for assessing long-term care needs, individual care plans, training measures for informal carers as well as a stronger focus on prevention and rehabilitation.

Tax system

At 37.7% (in 2013), Slovenia's total tax-to-GDP ratio was slightly below the EU average (38.8% in 2011). Taxation on labour has declined, as shown by a drop of the implicit tax rate on labour from 37.3% in 2006 to 35.2% in 2011. While the implicit rate on consumption is above the EU average, taxation of capital, especially corporate income, is one of the lowest in the EU. Revenues from environmental taxation have increased in percentage of GDP since 2006; in particular, revenues from energy taxation were the highest in the EU in 2012. To support fiscal consolidation, the government increased VAT rates in July 2013, which yielded an estimated additional 0.35% of GDP in 2013 and expected cumulative increase of 0.7% of GDP in 2014. Excise duties on fossil fuels, biofuels, alcohol and tobacco products were also raised in 2014, while the previously planned reduction in corporate income tax rates was stopped last year.

Property taxes are low in Slovenia, with revenues amounting to 0.5% of GDP in 2012. A real-estate tax, to take effect as of January 2014 and replace the existing levies, was a key element of the government's 2014 budgetary plan. The proposed tax was expected to contribute an additional EUR 200 million annually however, in March 2014 the Slovenian Constitutional Court repealed the act underpinning the tax citing that the law does not specify the methods of real estate evaluation. In light of this, the compensation for the use of land will remain in force in 2014. In the stability programme the government states it will explore options to propose a new property tax, taking on board the comments from the Constitutional Court, however no clear timeline for the introduction of a new property tax is provided and no revenues from it are factored in the budgetary plans.

The government adopted a programme to mitigate the impact of the 'grey economy', including measures to prevent undeclared employment. The size of the non-observed economy in Slovenia is estimated at more than 10 % of GDP.[13] To support fiscal consolidation efforts, the 2013 recommendation asked for improved tax compliance. The analysis in this staff working document leads to the conclusion that Slovenia has made some progress in addressing this recommendation but challenges persist. Undeclared employment will be addressed through the introduction of special online voucher register. The law was adopted by the parliament in April 2014 and should be implemented in timely manner. The level of tax frauds was contained through stricter rules for using cash-register software. Early indications suggest that the programme, introduced in July 2013, has yielded positive results; the authorities anticipate additional revenues amounting to 0.2% of GDP in 2014. A more

[13] http://www.stat.si/eng/novica_prikazi.aspx?id=4526

detailed assessment of the effectiveness of measures to date is required in order to determine whether further steps, such as comprehensive online systems, would be beneficial. Proposals for tighter restrictions on cash operations are currently also being prepared and the further modernisation of tax administration could be beneficial.

3.2. Financial sector

In 2013, Slovenia received a country-specific recommendation on carrying out a system-wide bank asset quality review, the implementation of a comprehensive banking sector strategy, and the divestment of banks' state shareholdings. Slovenia has made substantial progress on addressing this recommendation. The government took decisive action but the work is far from complete and focused action is required to fully restructure banking sector.

Doubts regarding the health of the Slovenian banking sector highlighted the need for an asset quality review and stress test.[14] In order to regain market confidence and provide the necessary clarity regarding the outlook a system-wide bank asset quality review, as requested in the 2013 country-specific recommendation was conducted. The exercise[15] was carried out by independent experts and identified weaknesses in the banking sector and in particular in the area of corporate governance and risk management systems (i.e. limited workout capacity and weaknesses in risk assessment, data quality, the credit approval process and statistical disclosure). It is important that these weaknesses are addressed in a comprehensive way to minimise the risk of a repeated build-up of losses. The authorities announced a strategy for the banking sector in December 2013, yet the progress to date has been limited.

Based on the outcome of this exercise, banks were promptly recapitalised in line with state-aid rules. The stress test identified capital deficits of up to EUR 4 778 million under the adverse scenario.[16] The European Commission approved recapitalisation measures for the two largest state-owned banks (NLB, NKBM) on 18 December 2013. In parallel, it temporarily approved rescue aid for Abanka and adopted a decision allowing for the liquidation of Probanka and Factor Banka. Once these decisions were adopted, recapitalisation to the five institutions, totalling EUR 3 214 million, was completed.[17]

The transfers of non-performing loans to the Bank Asset Management Company have been completed but the loan workout strategy needs to be refined. Loans from the two largest banks (NLB and NKBM) with a gross value of EUR 3 301 million were transferred to the Bank Asset Management Company in December 2013 for a total consideration of EUR 1 012 million, representing an average discount of 69 %. For Abanka, Slovenia's third largest bank, loans with a gross value of approximately EUR 1 150 million are due to be transferred once the submitted restructuring plan is approved by the European Commission. The Bank Asset Management Company's strategy for the workout of these loans remains unclear. In the national reform programme, the government has committed to adopt a business plan and

[14] SWD(2013) 374 final.

[15] The exercise covered 70 % of the banking system and the participating institutions provided granular data for two million loans and 14 000 collateral assets. The AQR incorporated the results of 4 235 individual loan file reviews and the assessment of 15 358 real estate valuations carried out by independent third parties. The implementation was coordinated and supervised by a Steering Committee, comprised of representatives of the Bank of Slovenia, the Ministry of Finance, international consultants, and observers from the European Commission, the ECB and the EBA.

[16] See: *Slovenia — Review of progress on policy measures relevant for the correction of macroeconomic imbalances, European Commission* (20 February 2014).

[17] Further details available here: http://europa.eu/rapid/press-release_IP-13-1276_en.htm

strategy for the Bank Asset Management Company by September 2014. A comprehensive business plan would provide greater clarity on the strategy for the workout of each portfolio of asset, details on the redemption targets, budget, asset management plans and expected returns. The Board has not yet fully put in place the necessary infrastructure and corporate governance arrangements to ensure transparency and help maximise the recovery value for the state. It is important that any subsequent transfers of loans from other banks are designed in a way that would provide the Bank Asset Management Company with a majority of the outstanding loans in the major restructuring cases and as a consequence allow it to take the lead in the restructuring.

Privatisation of state-owned banks and considerable restructuring and consolidation of the sector will continue in 2014. As a result of four consecutive years of balance sheet contraction and asset transfer, the total assets of the banking sector in Slovenia shrunk by one-fifth between 2009 and 2013. In September 2013, a decision was taken to wind down two smaller domestic banks (Probanka and Factor Banka), in line with Bank of Slovenia's strategy to consolidate the sector. Both banks will most likely exit the market in 2014. Despite significant consolidation, a further reduction in the size of banks' balance sheets is likely.[18] Banka Celje, a small privately owned domestic bank, requested state aid at the end of April 2014 and is preparing a restructuring plan. Gorenjska Banka, which currently complies with the Bank of Slovenia's capital requirements but has to increase its capital in line with the stress test result. The government committed to use state funds if private sources do not materialise. Mergers, in particular between smaller domestic banks, could exploit cost synergies and result in creating the third largest domestic bank. In December 2013 the government announced its intention to fully dispose of the ownership of NKBM and Abanka, and to reduce its participating share in NLB to 25 % plus one share in the medium term[19]. In the national reform programme, the government confirmed the commitment to privatise the banks, referring to the timeframe agreed with the European Commission in the state aid restructuring plans for NLB and NKBM. Prompt implementation of these measures would send a strong signal to the market and could facilitate further restructuring in the sector.

The banks' capacity to work out non-performing loans could be reinforced. The transfer of non-performing loans to the Bank Asset Management Company has improved banks' balance sheets, but the levels remain high relative to pre-crisis levels and still need to be restructured in a sustainable manner. The successful restructuring of non-performing loans would be key to restore sustainability and profitability in both the banking and the over-indebted corporate sector. Although the national reform programme has recognised the importance of this issue, more concrete measures (as part of the wider action plan on restructuring) could accelerate the process. Enhancing banks' internal workout capacity is one of the key prerequisites for successful restructuring and could include strengthening the internal asset management units and management incentives. Workout units focused on maximising recovery value and tackling the loan books in a comprehensive and strategic way could reduce the potential for further state injections in the future.

The approved restructuring plans need to be fully implemented. The restructuring plans for the NLB and NKBM, and the corresponding commitments, provide for (i) enhanced corporate governance designed to prevent unnecessary state influence on banks; (ii) an

[18] See Box 3.2 in the 2014 IDR (COM(2014) 150 final).

[19] Further details are available in the press release "Bank of Slovenia and Slovenian government announce results of stress tests" of 12 December 2013 available here: https://www.bsi.si/iskalniki/sporocila-za-javnost-en.asp?VsebinaId=16219&MapaId=202#16219.

improved risk-management framework; (iii) divesture of non-core businesses; (iv) reduction of exposure to non-performing loans; (v) adequate capital levels over the restructuring period, and (vi) increase efficiency and introduction of adequate pricing aimed at restoring banks' profitability. Prompt implementation of the plans will help to restore the sector's profitability and long-term sustainability. It will also enhance banks' attractiveness as investments.

Box 3: Conclusions from the March 2014 in-depth review on Slovenia

The third in-depth review (IDR) for Slovenia was published on 5 March 2014. On the basis of this review, the Commission concluded, for the second consecutive year, that Slovenia continues to experience excessive macroeconomic imbalances which require specific monitoring and continuing strong policy action. These imbalances have been unwinding over the last year, thanks to macroeconomic adjustment and decisive policy action by Slovenia. Yet the magnitude of the necessary correction means that substantial risks are still present. More specifically, the risks stemming from an economic structure characterised by weak corporate governance, high level of state involvement in the economy, losses in cost competitiveness, the corporate debt overhang, the increase in government debt warrant very close attention. While considerable progress has been made in repairing the banks' balance sheets, determined action with respect to the full implementation of a comprehensive banking sector strategy, including restructuring, privatisation and enhanced supervision is still required.

The main observations and findings from the IDR analysis are:

- Slovenia has taken decisive policy action in 2013 which has stabilised the banking sector but further restructuring and consolidation is required for the sector to return to long-term sustainability and profitability.
- The sharp increase in government debt in recent years, albeit from a relatively low level, creates new challenges and risks, which underscores the need for sustainable policy actions.
- A substantial loss of export market shares over the past five years shows that Slovenia is not competing effectively in world markets.
- The postponement of the financial restructuring of viable companies delays the re-establishment of investment capacity and the recovery of the economy.
- The complex nexus of state ownership limits adjustment and distorts resource allocation, especially as regards new investment.

The IDR discusses policy challenges that could be explored in order to address the identified imbalances and risks:

- Further restructuring and consolidation in the financial sector beyond the progress made in 2013 is required to return to long-term profitability and sustainability.
- Prudent and credible fiscal policy, including pension and long- term care reform, is necessary to maintain market confidence and ensure debt sustainability in the medium-term.
- Containment of labour costs is essential for restoring, including through a reform of the minimum wage, labour taxation and public- sector wages.
- Enhancing governance in the corporate sector and providing the tools to effectively address the debt overhang will help to unlock productivity.
- Encouraging private ownership and a comprehensive strategy for the management of strategic/core assets could improve the adjustment capacity of the real economy.

3.3. Corporate restructuring and State ownership

Corporate restructuring

Reforms to the legal framework to facilitate the swift rehabilitation of viable companies and the acceleration of restructuring were adopted in 2013. A simplified compulsory settlement procedure and a preventive restructuring procedure (in the pre-insolvency stage) are among the new tools included in the Insolvency Act in May and December 2013. The law has shortcomings, for example, it is not possible to impose a principal haircut on a secured creditor as part of a restructuring plan. The effectiveness of these tools and of other insolvency procedures should be closely monitored and evaluated based on appropriate indicators at aggregate level, such as recovery rates in all types of insolvency procedures, the types of measures agreed in the restructuring plan and their applicability and effectiveness, the proportion of the principal haircut agreed, where relevant, and the amount of debt involved in the restructuring (per business sector and size of company). The commercial courts have seen a rise in insolvency cases and their capacity to resolve cases has not yet stabilised. In bankruptcy cases against legal entities, the clearance rate fell from 83 % in 2012 to 67 % in 2013, leading to a 32 % increase in the number of pending cases. Case-management reforms in commercial courts have not yet brought stable improvements to insolvency proceedings. Nevertheless, despite a rising number of incoming cases, the proportion of insolvency proceedings involving legal entities resolved within nine months of filing improved slightly, from 57 % in 2009 to 63 % in 2013.[20]

Despite the recent amendments to the legal framework, the financial and operational restructuring of the corporate sector is yet to begin on a larger scale. The initial plan was to attribute a key role in pushing forward corporate restructuring to the Bank Asset Management Company. Following the transfers of assets executed in December 2013 the Bank Asset Management Company faces difficulties in taking the lead in many major restructuring cases due to the fragmented nature of the loans transferred and their minority position vis-à-vis other creditors. A centralised and comprehensive approach towards the various credit exposures in the banking system could accelerate the workout process and facilitate restructuring negotiations, particularly in the case of complex inter-connected groups with a high number of bilateral contracts and conflicting interests. A task force with experienced representatives of all stakeholders (including the government, the Bank of Slovenia and possibly external experts) could provide the necessary expertise, guidance and advice, and facilitating the negotiation process between all stakeholders involved. It could further drive the negotiation process for a number of large cases by establishing a list of the most urgent restructuring cases and setting priorities in an action plan for the overall restructuring process. Furthermore, it could ensure hands on training to relevant stakeholders regarding the application of the revised insolvency framework, promote the use of the available legal mechanisms and international best practices and explore foreign and domestic private investment as sources of financing.

In the national reform programme the government has committed to establish a working group coordinating the overall restructuring process. The working group will be responsible for overlooking some of the largest cases, for monitoring, accelerating and coordinating the overall restructuring process. It will further prepare an action plan for improving corporate governance in restructured companies. To guide the process, the government has adopted non-binding restructuring principles, as proposed by the Banking

[20] All data from the Supreme Court of Slovenia.

Association, though their effectiveness has not yet been tested. In the meantime, swift and efficient closure of some ongoing urgent cases would help establish best practice for corporate restructuring in Slovenia. Moreover, building strong management incentives and technical capacity within banks' internal asset management units, as well as ensuring that companies have sufficiently experienced management in place to implement turn-around plans, is also an integral part of corporate restructuring.

State ownership

The level of state ownership and influence prevalent in Slovenia poses a serious impediment to improving the real economy's adjustment capacity. State-owned and state-controlled enterprises account for one-sixth of total value added in Slovenia and form a complex network of domestic banks, insurance groups and non-financial corporations. Cross-shareholding and the level of state influence in Slovenia create significant risks to public finances, both directly and indirectly through guarantees[21] given that the state-owned and state-controlled enterprises continue to generate losses and remain highly indebted. Sub-optimal corporate governance, inefficient governmental subsidies, political interference and vested interests have been identified as the main reasons for the subdued performance as well as low attractiveness of business environment for foreign direct investment and the instability of the banking sector. Recent studies[22] have indicated that political connections are more prevalent in state-owned and state-controlled enterprises or firms owned by municipalities, rather than in private companies. Politically affiliated supervisory board members represent negative influence on productivity of the company, whereas on the contrary, participation of non-affiliated parties on supervisory board increases productivity and efficiency. This is especially evidenced in non-tradable sector. In light of these challenges, Slovenia received a recommendation in 2013 for better management of state-owned enterprises. The government has made limited progress in addressing this recommendation.

The authorities identified a list of 15 companies for accelerated privatisation in May 2013. While progress to date has been mixed, the national reform programme sets out the government's commitment to implement the privatisations over 2014-2015. The sales of two companies from the list have been completed to date.[23] The privatisation of Elan is in final stage, with sales agreement expected to be closed before summer 2014. The privatisation of Telekom Slovenije (the largest asset on the list is expected to be completed by July 2014 in line with the government's commitment. The privatisation of NKBM (the second largest bank in Slovenia and the only bank on the list), is proceeding slowly. The process for Airport Ljubljana and Adria Tehnika is moving forward, with a call for interest published for the airport and non-bonding bids received for Tehnika. The authorities have provided a timeline for each of the remaining sales processes, but limited progress has been made to date.[24]

The new legislation underpinning the Slovenian Sovereign Holding was adopted in late March 2014. In 2013, Slovenia received the country-specific recommendation to make the Slovenian Sovereign Holding fully operational by September 2013 in order to consolidate both the ownership and the management of the government stakes in companies under one umbrella, and prepare a comprehensive strategy and a precise classification of assets. Should the recently adopted legislation be implemented as planned, it could address the immediate

[21] Slovenia: State-Owned and State-Controlled Enterprises, S. Georgieva and D. M. Riquelme (June 2013)

[22] Domadenik et al., Political connections and productivity of firms: micro evidence of legal corruption.

[23] The sales agreement for Helios was signed in October 2013 and sales agreement for Fotona was signed in at the end of January 2014.

[24] Table 2 in *Slovenia — Review of progress on policy measures relevant for the correction of macroeconomic imbalances*, European Commission (20 February 2014).

risks stemming from the complex nexus of state ownership. In order for the Slovenian Sovereign Holding to become operational, it must be underpinned by an efficient strategy for classification of State assets that could be divided into strategic, important and portfolio assets. The strategy is currently being prepared and is planned to be proposed by the government in July 2014 (deadline set by the law and proposed by the national reform programme). However, given the political situation, there is a tangible risk that the strategy may be delayed. An experienced and capable management and supervisory board are still to be appointed in a transparent way for the SSH and for the companies under its management. This will be key for ensuring the success of the SSH as an effective and independent manager of state-owned assets.

The government did not opt for full consolidation of ownership and management of State assets under the Slovenian Sovereign Holding umbrella. Only a part of the State assets will be consolidated under the Slovenian Sovereign Holding. The SSH will be a result of transforming the *Slovenska odškodninska družba, d.d.* (SOD), a compensation fund, with the competences stipulated by the new law and incorporating several other holdings. However, *Kapitalska družba, d.d.* (KAD), a pension insurance scheme, and its assets as well as assets in the energy transmission and distribution sector will not be transferred to the Slovenian Sovereign Holding. The Slovenian Sovereign Holding will have the capacity to independently manage its assets, as well as those belonging to the state. The mandate includes running the privatisation process, whereas under certain conditions it will coordinate and drive the sales procedures in case of KAD's assets. According to the authorities, the different ownership structures (State, Slovenian Sovereign Holding and KAD) do not weaken the Slovenian Sovereign Holding's powers, as it is meant to act autonomously on the mandate given by the law. The Slovenian Sovereign Holding also acts as the fiduciary of corporate governance by promoting best practices and codes to be applied in the management of State assets. Various mechanisms to ensure integrity, reduce conflicts of interest, prevent corruption, and reinforce transparency have been laid down in the law. The election of the supervisory and management board will confirm whether the provisions are applied in practice. Similar issues are to be addressed in the forthcoming Corporate Governance Code for State assets to be prepared by September 2014 as proposed by the national reform programme. If designed and implemented properly, this code should contribute to more efficient and independent management of state assets.

Despite its shortcomings, thee new legal basis underpinning the Slovenian Sovereign Holding is a welcomed step in the right direction. Weaknesses arising from the adopted legislation include: unclear definitions and inconsistencies, multiple implementing acts, complicated relationship between the State, the Slovenian Sovereign Holding, the KAD and proposed Demographic Fund and lack of clarity regarding the relationship of the initial 15 companies identified for privatisation and possible incorporation of the other holdings. The capacities of the management and supervisory boards of the Slovenian Sovereign Holding and its underlying companies (the same applying also to KAD), will play a key role in applying sound management policies and attaining the goals outlined in the law. The supervisory board of the Slovenian Sovereign Holding will be appointed by the parliament on a proposal from the government but all steps should be taken to ensure a politically non-affiliated body. For the Slovenian Sovereign Holding supervisory and management board to succeed, its work must be closely based on its mission, and the separation of the State’s functions must be respected.

3.4. Structural measures promoting sustainable growth and competitiveness

Focused measures to spur the competitiveness and productivity of the real economy can help Slovenia to unlock its growth potential. Slovenia's industrial structure is dominated by low to medium technology and labour-intensive products. There is a lack of focus on high-value-added segments, which would sustain the country's export market share in the coming years. Exports are driving Slovenia's fragile recovery, but the economy tends to be characterised by a low inward foreign direct investment stock (34.1% of GDP vs. 47.1% of GDP on average in the EU in 2012)). Increasing foreign direct investment would bring in fresh capital, new technology, higher productivity and better corporate governance. Privatisation and corporate restructuring offer many new possibilities for private investors, yet the business culture has to adapt to embrace new realities and take full advantage of it. The biggest obstacle to businesses is the complex network of state-owned and state-controlled enterprises, including banks (see Section 3.3). Furthermore, domestic business tends to be hampered by poorly designed policy measures, whose goal is to improve the business environment. The underlying environment has to facilitate the business, providing for a solid legislative framework, efficient bureaucracy and independent functioning of the Competition Protection Agency. The 2013 OECD study on product market regulation[25] shows that Slovenia has a highly-regulated business environment with high government involvement, in particular in the network sectors. Burdensome business and competition environment, lengthy and costly licencing procedures,[26] state involvement and complex cross ownership of Slovenian companies deter both domestic and foreign investment, needed to produce the necessary value added and ensure sustainable economic growth. Against this background, Slovenia received a country-specific recommendation in 2013 to improve business environment. While reforms undertaken need time to take full effect the government has made limited progress in addressing this recommendation.

Modulation of a single strategy for business support

Slovenia would substantially benefit from an improved business environment and modulation of a single comprehensive strategy for business support. Currently, Slovenia would need a set of clear and consistent objectives to improve business conditions and restore, in some cases, competitiveness. Various strategies have been prepared, but they are not integrated and are inconsistent despite the fact that they are administrated by the same ministry. Lack of prioritisation, implementation and hands-on ex-post controls for monitoring weighs on their credibility. The 2013 Industrial Policy Strategy, which aims to increase the country's productivity from the current 60 % to 80 % by 2020 in order to close the productivity gap, has not been implemented; the fate of the 2011 Research and Innovation Strategy is similar. The Smart Specialisation Strategy linked to absorption of the European Investment and Structural Funds for the period 2014-20 will provide an opportunity to focus on key measures, such as the creation of tradable innovative products but its preparation lags behind. Given the current environment of reduced public investments and scarce foreign direct investment, these strategies provide the opportunity to focus resources on maximising returns of the European Investment and Structural Funds. The OECD report[27] for Slovenia,

[25] See: http://www.oecd.org/eco/reform/indicatorsofproductmarketregulationhomepage.htm

[26] Construction permits, property registration and paying taxes are the three problematic backlogs identified by the Doing Business Report 2014. According to this report, it takes 182 days to obtain a construction permit in Slovenia (against the OECD average of 147.1 days), registering a property takes 109.5 days (against the OECD average of 24.1 days) and the tax declaration takes 260 hours to complete (against the OECD average of 175 hours).

[27] See: http://www.oecd.org/innovation/oecdreviewsofinnovationpolicyslovenia.htm

analysing innovation policy, states that the main weakness of the system is uneven innovation performance, proliferation of policy tools and diverging views of stakeholders. Slovenia would thus benefit substantially from improved framework conditions. While the national reform programme does not put focus on this issue,, the Partnership Agreement, within the thematic objective number one, proposes measures to strengthen research, technological development and innovation.

Slovenia displays average performance in innovation and R&D.[28] Since 2000, the level of R&D investment in Slovenia has increased substantially and Slovenia now ranks 6th among EU Member States in term of R&D intensity. But its lower ranking in term of innovation performance calls into question the quality of the investment.[29] Improving governance and setting clear research and innovation priorities in a context of smart specialisation with a stronger focus on knowledge transfer remain the main challenges for the Slovenian research and innovation system. The split in the governance of research and innovation has resulted in fragmentation and lack of cooperation with the stakeholders of the knowledge triangle as well as significant delays in implementation, putting the effective and efficient use of available resources at risk. An assessment of the efficiency of spending would be a beneficial input for any further measures in this respect. Measures to foster knowledge transfer and commercialisation of research results, such as the introduction of funding linked to research performance, removal of obstacles to establishing university spin-offs and cross-border venture capital investments would contribute to creating a favourable business environment for innovative companies in key sectors. While state subsidies are not the most efficient way to support businesses, development of new, upgraded financial instruments, and closer cooperation of relevant stakeholders to establish a coherent strategy that promotes research, innovation and industrial policy, with a clear objective of the maximisation of the economic value added and job creation may also be beneficial. Low employment in fast-growing innovative firms could be related to the low levels of venture capital in Slovenia, and particularly to seed finance, aggravated by the low levels of foreign direct investment. According to the Partnership Agreement, Slovenia will make efforts to increase the share of innovation-active firms and the number of researchers and developers in the economy.

Financing future growth potential

Business activities are affected by fiscal consolidation and the credit crunch,[30] indicating the need for alternative sources of finance. The positive effects resulting from the stabilisation of the banking sector will take time to materialise. Meanwhile, given SMEs' dependency on bank lending and scarce alternative sources of finance, access to credit is likely to remain constrained, further aggravating the situation for viable SMEs and hampering their growth and competitiveness. The Slovenian Enterprise Fund, co-financed by the Structural Funds, provides funding for SMEs through public guarantees and has backed a handful of local venture-capital funds. Based on experience from 2007-13, the Slovenian

[28] A new indicator proposed by the Commission. Slovenia ranks 14th, showing diversified performance in its components: while performing exceptionally well in exports of medium- and high-tech manufacturing goods, it performs poorly in knowledge-intensive services. Employment in fast-growing innovative firms is relatively low. http://ec.europa.eu/economy_finance/publications/qr_euro_area/2013/pdf/qrea4_section_2_en.pdf

[29] The research and innovation system in Slovenia has obvious weaknesses in knowledge commercialization (3.1 patents per billion GDP compare to the EU average of 3.9) and research quality (only 7% of cited scientific publications compare to the 11% at EU level).

[30] The amount of bank loans to domestic non-banking sectors fell by EUR 1.9 billion in the first eleven months of 2013, nearly three times as much as in the same period of 2012. Source: IMAD, Economic Mirror, December 2013.

Enterprise Fund developed instruments that were considered a success, showing better results than traditional subsidies. Despite low absorption (i.e. in the case of the SID bank programme)[31] and overlapping of certain financing, programmes offered by the Slovenian Enterprise Fund and SID banks worked well and helped SMEs by providing guarantees and subsidised loans. However, these instruments were not enough to compensate for the reduction in banking finance. In line with the structural funds' regulatory framework, a gap assessment of the potential for financial instruments on the Slovenian market is being carried out. New financial instruments are currently being prepared, which focus on start-ups and fast-growing micro-enterprises and companies in the first phases of growth, neglected by the existing instruments. Moreover, given limited equity market with developing alternative financial sources for viable smaller firms, there may be scope to further incentivise venture-capital investments from foreign sources, given that currently only locally-established funds benefit from tax breaks. However, in the national reform programme the authorities explore options for establishment of a single channel for financial instruments that would underpin the funds received from the European Investment and Structural Funds.

Service market regulation and competition issues

Enhancing competition in the service sector could unlock further growth potential. For several services (e.g. chimney sweeping, cemetery and funeral services, nature and environmental conservation), Slovenia introduced a system of concessions, which limits the number of service providers through quantitative and territorial restrictions and tariff setting. These concessions, predominantly managed at local level, mostly hamper domestic businesses from entering into service sectors, but they also hinder cross-border provision of services. The limited choice in terms of quality and the higher costs of these services which are inputs for business have a negative impact on the potential growth of the Slovenian economy. Neighbouring countries do not impose such a high number of authorisation rules. Authorisation rules must be in line with internal market principles, and in particular with the rules established by the Service Directive.

Deregulation of regulated professions would contribute to increasing the number of domestic and foreign services providers and thus contribute to increased competitiveness. In 2012, a process of deregulating regulated professions started, and so far the number of regulated professions decreased from 323 to 262. Some progress has been achieved, but at a slower pace than initially planned. The adoption of the Slovenian Small Business Act in July 2013 reduced the number of regulated craft activities from 64 to 24. In addition, acquired knowledge and experience is now also accepted to justify the required qualification level for a number of craft activities. Revisions made to the legislation on professions in construction and tourism should be finalised in the first half of 2014. The second package of amendments to sectorial legislation is under way and should be adopted by the end of October 2014. The national reform programme announces the government's commitment to reduce the number of regulated profession by 100, respecting the needs of business and cross border mobility in provision of services. The ongoing mutual evaluation of regulated professions at European level could be an opportunity for the authorities to accelerate the reform process.

The product and service markets need efficient oversight, but the Competition Protection Agency still faces threats to its independence. The agency has been subject to severe cuts in its 2014 budget allocation (its funding has been cut by around 10%, much

[31] See finance programme of EUR 333 million from SID Bank. Only EUR 16 million were absorbed.

higher than the average cost reductions across public service), which affects its operations, in particular the possibility to carry out inspections, and makes its participation in European and international cooperation nearly impossible. Moreover, its expenditure has been subject to very detailed budgetary scrutiny by the Ministry of Economic Development and Technology, which is not required by law. This excessive oversight of its expenses together with sustained administrative investigations into the Competition Protection Agency's actions, including final decisions upheld by the court, weigh on its independence and daily operations and, through press leaks, may adversely affect its reputation. Unlike other agencies, the Competition Protection Agency also lacks the power to impose fines directly on undertakings in its administrative decision establishing an infringement of the EU competition rules. Instead, following the adoption of the administrative decision, it has to conduct separate minor offence proceedings identifying the responsible natural persons in order to fine the undertakings involved. The procedure is further complicated by the fact that the administrative decision and the minor offence decision imposing fines are appealed before different review courts. This duplication of procedures impairs the efficiency of the Competition Protection Agency and could even lead to limited imposition of fines and under-deterrence.

The lack of appeal reduces access to the review procedures and limits competition on public procurement market. Despite formal guarantees of the National Review Commission's independence, there is no possibility to appeal against the decisions of the National Review Commission, which adversely affects access to public procurement review procedures.

Box 4: Potential impact of structural reforms on growth – a benchmarking exercise

Structural reforms are crucial for boosting growth. It is therefore important to know the potential benefits of these reforms. Benefits of structural reforms can be assessed with the help of economic models. The Commission uses its QUEST model to determine how structural reforms in a given Member State would affect growth if the Member State narrowed its gap vis-à-vis the average of the three best EU performers on key indicators such as the degree of competition in the economy or labour market participation. Improvements on these indicators could raise Slovenia's GDP by 5.3% in a ten-year period. Some reforms could have an effect even within a relatively short time horizon. The model simulations corroborate the analysis of Section 3.4 and 3.5, according to which (i) final goods sector mark-ups (e.g. through increased competition on product and service markets and thus improved functioning of the Competition Protection Agency) and (ii) carrying out labour market reforms focused on raising participation of the elderly could produce particularly large gains.

Table 1: Structural indicators, targets and potential GDP effects[32]					
Reform areas		SI	Average 3 best EU performers	GDP % relative to baseline	
				5 years	10 years
Market competition	Final goods sector markups (price-cost margin)	0.20	0.13	1.7	2.1
Market regulation	Entry costs	0.00	0.13	0.0	0.0
Tax reform	Implicit consumption tax rate	23.0	28.6	0.2	0.2
Skill enhancing reforms*	Share of high-skilled	6.2	10.7	0.0	0.1
	Share of low-skilled	15.0	7.5	0.0	0.1
Labour market reforms	Female non-participation rate (25-54ys):			0.2	0.2
	- low-skilled	30.5	26.4		
	- medium-skilled	11.4	10.5		
	- high-skilled	4.3	4.3		
	Low-skilled male non-participation rate (25-54ys)	19.8	7.7	0.0	0.1
	Elderly non-participation rate (55-64ys):			0.9	2.1
	- low-skilled	30.7	13.4		
	- medium-skilled	16.2	4.8		
	- high-skilled	6.8	3.3		
	ALMP (% of GDP over unemployment share)	6.3	37.4	0.3	0.3
	Benefit replacement rate**	61.0	52.6	0.2	0.3
Total				3.6	5.3

Source: Commission services. Note: Simulations assume that all Member States undertake reforms which close their structural gaps by half. The table shows the contribution of each reform to total GDP after five and ten years. If the country is above the benchmark for a given indicator, we do not simulate the impact of reform measures in that area; however, the Member State in question can still benefit from measures taken by other Member States.[33] *The long-run effect of increasing the share of high-skilled labour in the population could be 2.2% of GDP and of decreasing the share of low-skilled labour could be 2.0%. **EU average is set as the benchmark.

Energy and infrastructure

Inefficiencies in the governance of infrastructure has hindered economic performance. The limitations of Slovenia's transport infrastructure weighs on its growth potential as a transit country. Slovenia remains heavily reliant on road transport modes, while railways still play a marginal role for both freight and passengers. Market barriers in the railway sector prevent the market from functioning properly. Railway infrastructure and transport operators are not fully separated, and both remain state-owned. Furthermore, a lack of administrative capacity is endangering the implementation of co-financed projects and the preparation of a comprehensive transport strategy. This strategy will be instrumental for investments under the European Investment and Structural Funds and the Connecting Europe Facility in 2014-20 and will aim to address all bottlenecks in all transport sectors, especially the underdevelopment of railway infrastructure. A large part of the Slovenian TEN-T railway network does not meet TEN-T standards, which creates bottlenecks for business (the one-tier Divača-Koper railway line is the main logistical bottleneck for freight transport from Port of Koper, a core TEN-T port). Most large railway and environmental infrastructure projects co-financed by the Cohesion Fund in 2007-13 are delayed due to lengthy project preparation, procedures for permits and public procurement. If they are not completed by the end of 2015,

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[32] Final goods sector mark-ups is the difference between the selling price of a good/service and its cost. Entry cost refers to the cost of starting a business in the intermediate sector. The implicit consumption tax rate is a proxy for shifting taxation away from labour to indirect taxes. The benefit replacement rate is the % of a worker's pre-unemployment income that is paid out by the unemployment scheme. For a detailed explanation of indicators see Annex.

[33] For a detailed explanation of the transmission mechanisms of the reform scenarios see: European Commission (2013), "The growth impact of structural reforms", Chapter 2 in QREA No. 4. December 2013. Brussels; http://ec.europa.eu/economy_finance/publications/qr_euro_area/2013/pdf/qrea4_section_2_en.pdf

Slovenia will risk losing available funds and will fail to comply with Accession Treaty commitments on EU environmental legislation.

Unpredictable winter weather and floods[34] **has damaged a large part of energy and railway infrastructure.** The natural disasters have exposed the serious underinvestment in maintenance and causing significant economic losses to businesses and the general population. Yet this is an opportunity for investment in modern infrastructure.

There is untapped potential to increase absorption and the efficiency of the electricity grid through the deployment of smart grids, which could also enhance the functioning of the electricity market. In 2012-13, competition on the electricity market increased, and the incumbent providers lost some of its market share in favour of competitive providers GEN-I and Petrol, who together secured 12.5 % of the market. Slovenian industry has managed to keep its ratio of energy costs to value added well below the EU average, maintaining the relative importance of high-energy-intensive sectors such as chemicals, plastics, metals and paper in its manufacturing structure.[35] Energy imports are quite well diversified. The proportion of renewable energy in Slovenia slowly increased from 19.4 % in 2011 to 20.2 % in 2012. However, the Europe 2020 target (25 %) can only be achieved if further measures are put in place. The renewable energy used for electricity (31.4 % in 2012) comes primarily from hydropower. Renewable heating is based almost exclusively on solid biomass. In February 2014, a new comprehensive Energy Act was adopted. However, it is too early to assess its impact on the energy market. Slovenia has not yet transposed the third package. Two infringement procedures are open before the European Court of Justice, which can issue a judgment at any time.

Slovenia has made progress in bringing energy efficiency gains to businesses and individuals as a result of policy initiatives. However, the level of energy intensity remains high due to the very high energy intensity of its transport sector, which is partially explained by the geographical position and transit through Slovenia. Furthermore, Slovenia continues to stand out because of its high levels of CO_2 emissions, again especially in the transport sector and in households, both of which have one of the highest carbon intensities in the EU. Energy import origins are quite diversified, but energy's contribution to the trade deficit is approximately double the EU average. The outlook for energy efficiency looks promising, but achievements will depend on the policy commitment and funding provided. Slovenia has developed a strong package targeting the industrial sector, including excise duties on gas and electricity above the EU minimum rates, and a CO_2 tax. In addition, Slovenia used cohesion policy funding to tackle the refurbishment of buildings (public and private), although work had to be slowed down due to budget constraints. Policy plans for the future are well developed and comprehensive, and are a good basis for the complete and prompt transposition and effective implementation of the Energy Efficiency Directive (due to be transposed by June 2014). Slovenia saw moderate increases in the proportion of renewable energy it used[36], but it can only reach the Europe 2020 target if further measures are put in place.

More could be done to raise further energy efficiency gains. Slovenia's percentage of SMEs that take resource-efficiency actions (saving energy, minimising waste, saving

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[34] Between 2002 and 2013, the total direct costs of the seven recorded floods amounted to EUR 1 500 million - *Study on economic and social benefits of environmental protection and resource efficiency related to the European Semester*, February 2014, Risk & Policy Analysts Limited.

[35] European Commission, *European Economy, Energy Economic Developments in Europe*, 1/2014.

36 Slovenia increased its proportion of renewable energy to 20.2 % in 2012, up from 19.4 % in 2011; the proportion of renewables used in transport increased to 2.9 % in 2012, up from 2.1 % in 2011.

materials and water) is below the EU average.[37] There is scope for further support to businesses in order to economise resources and save jobs. Significant savings could be made through support programmes that help SMEs to implement resource-efficiency measures, targeted and comprehensive support to SMEs could bring average savings of EUR 8 000 for energy firms and over EUR 19 000 for environmental technologies.[38]

3.5. Labour market[39], education and social policies

The employment and social indicators for Slovenia worsened in the course of 2013. Unemployment increased, affecting young people and the long-term unemployed. In 2013, unemployment reached 10.3% and youth unemployment reached 21.6%, %, while the long-term unemployment rate peaked to 5.2%. The increase in the proportion of young people, who are not in education, employment, or training (NEET), from 6.5 % in 2008 to 9.3 % in 2012, is also worrying. Given high unemployment rates in 2012-13 and VAT increase, Slovenia experienced the fourth highest fall in gross household disposable income in the EU, while inequalities remained at a low level compared to the EU average.[40] Also low labour productivity affects the competitiveness of the Slovenian economy. Labour market segmentation, distortive use of student work, ineffectiveness of labour market policy and wage setting, as identified in the 2013 country-specific recommendations, remain significant challenges for Slovenia. The government has made limited progress in implementing the 2013's recommendations addressing labour market issues. In the social policy field, there has been limited progress as regards the long-term sustainability and adequacy of the pension system and access to long-term and health care services.

Labour market issues

Slovenia has adopted a labour market reform in 2013. The reform aimed to reduce segmentation and introduce greater flexibility to the labour market by reducing protection of permanent contracts, simplifying dismissal procedures and reducing dismissal costs. Furthermore, it tightened the regulation of fixed-term contracts and restricted the use of temporary agency work. The evaluation of the reform was presented in April 2014. The first results point towards decreased segmentation of the labour market, an increasing use of permanent contracts and in-company flexibility measures that resulted in renegotiation of seven different collective agreements in order to explore options for containment of labour costs. Despite reduced social contributions and the introduction of occasional work for retired persons, the employment rate of older workers (above 55) did not increase, while the use of other contractual forms increase somewhat. The effects of the reform will display in full over a longer period of time.

Currently, Slovenian labour productivity is below the EU average.[41] This is the result of many factors, including poor reallocation of labour across firms and sectors, high employment

[37] Flash Eurobarometer 381: SMEs, resource efficiency and green markets, report, fieldwork: September 2013, Publication: December 2013.
[38] Study on economic and social benefits of environmental protection and resource efficiency related to the European Semester, February 2014, Risk & Policy Analysts Limited.
[39] For further details, see the 2014 Joint Employment Report, COM(2013)801, which includes a scoreboard of key employment and social indicators.
[40] These data are part of the scoreboard of key employment and social indicators (2014 JER). The scoreboard aims at the identification of key employment and social challenges, taking due note of the Employment Performance Monitor and of the Social Protection Performance Monitor.
[41] Member States Competitiveness Report 2013.

in state-owned enterprises, which tend to have low productivity but disproportionally high growth of salaries, low inflow of foreign direct investment, poor technology transfer and skills mismatch. Nominal compensation per employee between 2008 and 2011 has been increasing, though it has been accompanied by a decrease in output.[42] Salaries slowly started to adjust in 2012. In 2013 salaries adjusted in all sectors except for the state-owned utilities sector (electricity and gas), where net salaries rose by 13 % in 2008-13.[43] Civil servants' wages have been temporarily cut by an average of 1.25% (on top of the 3 % cut from June 2012) and some workers' allowances have been cut in the framework of consolidating public finances. Incentives to employ both young and older workers through reductions in social contributions have been introduced.

Limited progress has been made in ensuring that wage developments support competitiveness and job creation. The minimum wage is only indexed to inflation, while the Act on Minimum Wage allows for indexation to other economic conditions, which are not defined by the Act. Also, the structure of the minimum wage includes a wide range of allowances. However, the minimum wage increased in January 2014, resulting in a further rise in labour costs, adding pressure on the cost competitiveness of the economy. While the social partners find themselves deadlocked due to their diverging interests, the NRP envisages that the Social Agreement should have been negotiated in April 2014. As stated in the NRP, the government has plans to globally address the issue of labour costs and, in this context, to discuss the revision of the minimum wage. The review of the minimum wage may have implications for households' disposable income and for expenditure on social benefits. In January 2014, more than 46.700 (or 8%) of employees received minimum salary, most commonly in manufacturing (almost a quarter of employees in this sector).[44]

Slovenia made limited progress in developing measures to increase the employment rate of vulnerable groups. In 2013, Slovenia implemented a new active labour market policy, whose effectiveness will be closely monitored and evaluated in the context of European Social Fund implementation, which is the main source of funding. The share of GDP invested in active labour market policies is low but increased in 2013 compared to 2012, thus the number of participants also increased. The share of older workers remains low (15.9% in 2013), although their labour market participation is projected to somewhat increase as a consequence of the increasing retirement age. A public works programme totalling EUR 43 million and targeting the long-term unemployed was adopted in 2014. It promotes new activities in social enterprises for vulnerable groups, but does not address the specific needs of low-skilled or older workers. Measures to adapt work environments to longer working lives would be important, but the active and healthy ageing strategy is not expected before 2016. The national reform programme announces an analysis of active labour market policies and the introduction of additional tailor made measures in the period 2014-2015.

Student work and youth unemployment

The high incidence of temporary work among students is a result of the current legislative arrangement. The current legislation provides disincentive for students to finish their studies in time, causes late integration into labour market and burdens the budget through generous student benefits. According to the national reform programme, the new Student Work Act should be adopted by the summer 2014. The proposed Act allows students

[42] IDR 2014, Chapter 3.3.
[43] Data of Statistical Office or Republic of Slovenia.
[44] Economic Mirror, March 2014

to continue earning extra money, but the introduction of social contributions will increase the overall cost of student work by 43%. Thus it will limit its appeal, reducing unfair competition from student work and thus labour market segmentation. Establishment of central register of students will increase transparency and control in order to prevent misuse of student status.

Contrary to the high uptake of student work, it is increasingly difficult for young graduates to find regular employment. The increase in youth unemployment was one of the highest in the EU-28 in 2012 (4.9 pp). The growing unemployment rate among young and young graduates has been addressed through Youth Guarantee Implementation Plan, which was adopted in January 2014. The plan, which covers the young up to the age of 29, includes measures to fight youth unemployment through the provision of traineeships and apprenticeships, to facilitate education-to-work transitions, and integration of entrepreneurship into all levels of education with a view of empowering the young. However, there remain numerous challenges to delivering Youth Guarantees[45] in Slovenia. Namely, there is a lack of a sustainable long term strategy that goes beyond the currently planned two-year time-frame and there is insufficient outreach and support provided for the NEET.[46] Public employment services will need to have the capacity to ensure that young people register for the programme.

Education

Although the education system in Slovenia performs rather well, skills mismatches persist. The quality of lower secondary education is uneven.[47] A rapid succession of governments has slowed down reforms in the area of education and training, failing to address skills mismatches. According to the national reform programme, amending the Law on Primary Schools has allowed to better focus on special interests and learning a second language whilst improving quality of education. Slovenia's employment service is preparing ways to assess future labour market needs based on a pilot project. A comprehensive system of life-long career guidance will be put in place at all levels of education and linked to the system delivered by the public employment service.

Vocational education and training (VET) is not attractive enough to engage young talent. Students prefer to enrol in general education, but Slovenian industry offers mainly medium- and low-skilled jobs. This has led an increasing number of educated young people to emigrate.[48] The main challenge for VET, in particular at upper-secondary level, is to stop the decline in enrolment and to intensify cooperation with employers (both in defining curricula and providing apprenticeships). This task requires a targeted action plan from the government, since the economy consists mainly of SMEs, which are unable to set up such a system on their own. Amendments to the Post-Secondary Vocational Education Act, adopted in November

[45] Pursuant to the Council Recommendation of 22 April 2013 on establishing a Youth Guarantee (2013/C 120/01): "ensure that all young people under the age of 25 years receive a good-quality offer of employment, continued education, an apprenticeship or a traineeship within a period of four months of becoming unemployed or leaving formal education".

[46] Eurostat data, NEET rate aged 15-24, 2013.

[47] Slovenia shows mixed results in the 2012 OECD Programme for International Student Assessment (PISA): while mathematics and science scores remain above the EU average (but with no improvement), reading skills lag behind the EU average and show a deteriorating trend.

[48] SORS data: in 2011, 2006 people with a high school degree and 919 people with a higher education degree left Slovenia in search of a better job. In 2012, this figure increased to 3598 for high school graduates and 1588 for higher education graduates. 2013 data are not yet available, but the trend continued with similar intensity.

2013, strengthened the link between education and economic operators.[49] The government plans to reintroduce a dual system for vocational training in 2016-17, although the national reform programme does not contain any specific measures on this issue. However, the national reform programme provides the commitment of the government to increase funding of scholarships for pupils and students, who preparing to enter deficit professions.

Skills mismatches and long study times remain significant issues for the higher-education sector. Tertiary graduates are less likely to be employed by organisations that employed them in the past[50] and universities have been given more autonomy in determining study content. Institutions need to teach additional skills, such as entrepreneurial skills, and students need to consider professions that are more attuned to labour-market needs. Further amendments to the Higher Education Act are currently under discussion, and would address university quality and financing. Defining student status more restrictively and putting in place an electronic student register should help to shorten study times.

Social policies

The social situation in Slovenia continues to deteriorate. Initially**,** the crisis only had a moderate impact on household income, as the social protection system performed well despite relatively low social protection expenditure (as a proportion of GDP). However, as the crisis dragged on, the power of automatic stabilisers weakened and household disposable income dropped, undermining private consumption. This was also a partial effect of the 2012 social policy reform, which increased targeting of social benefits (such as social assistance, supplementary allowance and child benefits). In 2013, the take-up of social assistance increased again, with almost 75 % receiving social assistance for more than a year. One of the most vulnerable segment of the population are the older people, especially women. The increasing debt-to-income ratio combined with falling saving rates indicates pressure on household income and indebtedness. However, the indebtedness of Slovene households is still very low when comparing to other EU member states.[51] These trends have translated into an increasing risk of poverty and social exclusion and changes in taxation are expected to further reduce households' disposable income. However, given the public finance consolidation needs, the national reform programme does not foresee any measures to address these issues outside of the Cohesion Funds.

Limited progress has been made in safeguarding the adequacy of pensions. The 2012 pension reform introduced new rules for calculating the pension assessment base in order to halt the gradual decrease of pensions.[52] According to the assessment of the 2012 pension reform, the difference between average pension and average salary remained fairly constant between 2012 and 2013, while the replacement rate stabilised in 2013. However, pension indexation has been frozen for 2014 and 2015 and the take-up of income-support benefits considerably decreased with the adoption of the 2012 social reform, which increased the risk of poverty for older people. Amendments to the reform were therefore introduced in

[49] They increased the number of hours of compulsory practical work included in courses and made it easier for young experts from enterprises to teach in post-secondary vocational institutions.
[50] Historically, tertiary graduates were mainly employed by the public sector and large corporations, who stopped hiring because of the economic crisis. Finding employment in SMEs requires different or additional skills, like entrepreneurship, which so far have been given less attention in education.
[51] Eurostat data for gross debt-to-income ratio of households show that the indicator for Slovenia reached 47.08% in 2012, well below the Eurozone average of 98.43%.
http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&plugin=1&language=en&pcode=tec00104
[52] The ratio of average pensions to average salary in 2012 stood at 62.1%, down from 73.2% as in 2001.

December 2013 to ease the income and property conditions for entitlement to social benefits, and to extend eligibility to income support for the elderly. There is no concrete information on the financial impact of these changes on the budget.

3.6. Modernisation of public administration

The 2014 Annual Growth Survey outlines priorities in the area of public administration, such as delivering better services, improving the business environment and providing for efficiency gains through better coordination of and cooperation with stakeholders. Slovenia must address these challenges if it is to improve the credibility of and trust in its public administration and create a simpler business environment. According to the 2013 Autumn Barometer[53], trust into national authorities in Slovenia is very low. For instance, trust into the national parliament (6%) is the lowest among all surveyed member states and candidate countries and trust into national government (10%) is the second lowest.

More efficient judiciary

Some progress has been achieved in increasing the efficiency of the judiciary system. While a case management reform on commercial and civil justice has improved the functioning of the court system, the length of trials remains long. Recent positive trends concerning litigious civil and commercial cases have been maintained. The disposition time was reduced from 431 days in 2010 to 348 days in 2013 and unresolved pending cases were reduced by 17 %. The courts were largely able to resolve more cases than they received in 2012 and 2013.[54] Despite this progress, the backlog of enforcement cases remains high in comparative terms[55] and the target set in the 2013 national reform programme has not been achieved. The current statistical methodology used to keep track of enforcement cases at local courts does not accurately reflect the status of the enforcement process. The electronic system for the enforcement of authentic documents continued to resolve cases quickly. According to the 2014 national reform programme, amendments will be introduced to the enforcement legislation to improve decision-making and efficiency.

Challenges of public administration

Slovenia is taking up the initiative in using e-government. As of 2015, doing business with the government will only entail e-invoicing. Paper invoices will no longer be accepted. A fully-operational one-stop-shop enables online registration of a company for free. Yet, on the other hand, the Point of Single Contact, set up in the framework of the Service Directive, is far from completed, lacking the possibility of completing procedures online. Furthermore, the transition to e-procurement has not been fully achieved. An electronic portal was launched in 2012 but electronic tenders cannot be submitted. Slovenia is one of the few remaining EU Member States, in which it is not possible to submit electronic tenders.

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[53] http://ec.europa.eu/public_opinion/archives/eb/eb80/eb80_anx_en.pdf

[54] Data from the Supreme Court of Slovenia and the 2014 EU Justice Scoreboard — Communication from the Commission to the European Parliament, the Council, the European Central Bank, the European Economic and Social Committee and the Committee of the Regions, COM(2014) 155 final, available at: http://ec.europa.eu/justice/effective-justice/scoreboard/index_en.htm

[55] In 2012, there were 8.3 pending enforcement cases per 100 inhabitants in Slovenia. This is above the EU median of 0.3 cases per 100 inhabitants. See Council of Europe (CEPEJ), *Study on the functioning of judicial systems in the EU Member States: Facts and figures from the CEPEJ 2012-2014 evaluation exercise*, prepared for the European Commission (DG Justice).

The newly-adopted strategy is set to cut red tape by 25% and thus improve the legislative and business environment and to boost competitiveness. It is comprised of a set of measures, contributed by various stakeholders, to be implemented in the medium term. These measures firstly need to be clearly prioritises and secondly, the implementation of these measures must be monitored to assess the efficiency of the policy action. The government failed to undertake a full-scale SME test (SME test is still in the pilot phase) about the potential influence of proposed measures on small businesses, causing a potential risk that the new legislation would not be SME-friendly. Municipal fragmentation and administrative inefficiencies pose severe burden on businesses, namely, long lasting and costly spatial planning procedures and delays in issuing building permits, which are a significant barrier to entering Slovenian business environment – for local and in particular foreign investors as well as for absorption of EU funds. In the national reform programme, the government is dedicated to fight the red tape and reduce burden on businesses, including resolution of long procedures for building permits. However, the issue of municipal fragmentation is only going to be addressed through the optimisation of public expenditures and modification of municipality funding that would in turn bring to a merger of smaller municipalities, rather than through a comprehensive analysis and planning on how to best merge the municipalities. If Slovenia used its resources efficiently, it could reduce business costs and facilitate trade.

The challenge for the future is to ensure high-quality public services. Quick successions of governments, coupled with numerous changes of ministers, have had a negative impact on the policy implementation record of several ministries, in particular in health care sector. A targeted reorganisation of the healthcare system designed to exploit internal synergies and realise necessary savings has been pending on the reform agenda of the government. In spite of the political rhetoric, there appears to be little political will to tackle accumulated problems. Slovenia is in the early stages of preparing a comprehensive public-sector reform (to be adopted by January 2015), which aims to ensure better quality and accessibility of services, addressing human resource management and strategic planning of legal, organisational and procedural aspects. Various strategies have been prepared, but implementation is weak.

There is a need to ensure adequate administrative capacity in the office involved in managing the cohesion funds in order to be able to reap full benefits of the programmes. In 2014, activities related to the two programming periods will cumulate. In order to deal with the challenging tasks of finalising the 2007-2013 period and starting of the 2014-2020 period at the same time, the managing authority will need to reinforce in terms of sufficient staffing and administrative capacity. This will require specific expertise, most notably in the field of public procurement, state-aid and project management, to ensure that projects are closely monitored and rationalised. A stronger leadership of the managing authority vis-à-vis other ministries and municipalities is also necessary in order to ensure needed systemic changes and to allow for timely reprogramming decisions, leading to a full absorption. Without improving the management of cohesion policy in Slovenia and without addressing the key bottlenecks (lengthy public procurement and permit procedures), the whole exercise may be at risk. The burden on the State of cohesion fund implementation could be substantially reduced by making more use of technical assistance within the operational program. So far, Slovenia has one of the lowest allocations of funds for technical assistance of all member states.

Credibility of public administration

Slovenia has to restore the quality and credibility of public administration and improve the management of structural funds and enhance transparency. Slovenia is facing interruption of the interim payments for the operational programmes for the second

consecutive year due to allegations of corruption and systemic control problems. The Commission interrupted payment claims in March 2014 (total amount of EUR 185 million) on the basis of the Commission audit, which identified deficiencies in the audited operations in Slovenia. This deficiency relates to the first-level management verifications of the managing authority. The Commission has also found that expenditure in a certified statement of expenditure is linked to serious irregularities in application of public procurement rules.

The EU Anti-Corruption Report 2014 shows a decline in the political drive against corruption.[56] Allegations of corruption, political interference and doubts about the integrity of high-level officials either within the public administration at state and local level or in state-owned companies came to the forefront of public attention in 2013-2014. The 2013 Eurobarometer on corruption shows that 76 % of respondents in Slovenia (the second-highest number in the EU) believe that corruption increased, and 88 % of respondents consider that using connections is the easiest way to obtain public services. In this context, the Commission for Prevention of Corruption, which has achieved some results in detecting corruption, needs to preserve its independence and influence. However, the recent appointment procedure of the leadership of the Commission for Prevention of Corruption has contested its image and has been univocally seen as inappropriate. Insufficient progress has been done to safeguard the operational independence of anti-corruption bodies and prosecution services specialised in combating financial crime, to put in place strong anti-corruption systems in state-owned and state-controlled companies, or public procurement and privatisation procedures. Gaps remain between the legal and strategic framework and effective enforcement due to weak control mechanisms at both the state and fragmented local level. For public procurement, in spite of limited progress in achieving transparency, particular vulnerabilities are broadly noted in the energy, construction, urban planning and healthcare sectors, where anti-corruption safeguards are not working, also because they are not protected from strong political interference. Corruption allegations have been reported also in allocation of subsidies. According to the 2013 Eurobarometer, 94 % of Slovenian businesses (the highest number in the EU) believe that business competition in their country is hampered by favouritism.

4. CONCLUSIONS

Structural weaknesses of the Slovenian economy weigh on its performance. Fiscal consolidation has not been sufficiently addressed. The sharp increase in government debt in recent years, albeit from a relatively low level, could be a major source of long-term vulnerability. The postponement of financial restructuring of viable companies delays the re-establishment of investment capacity and the recovery of the Slovenian economy as a whole. The complex nexus of state ownership limits adjustment and distorts resource allocation, especially as regards new investment.

The analysis in this document leads to the conclusion that Slovenia has made some progress in addressing the 2013 country-specific recommendations. Substantial progress has been made in repairing the banks' balance sheets, but further restructuring and consolidation is required for the sector to return to long-term sustainability. Policy action has included asset quality reviews, stress tests and recapitalisation of the state owned banks and asset transfer. The markets have welcomed the government's prompt recapitalisation and announced strategy for restructuring, as evidenced by the recent decrease of yields. However, limited progress has been made in fiscal consolidation, safeguarding long-term fiscal

[56] COM(2014) 38 final.

sustainability, restructuring of the corporate sector, privatisation and improving the business environment.

The priorities presented in the 2014 national reform programme echo the main challenges identified in the 2014 in-depth review on Slovenia and this staff working document. These measures signal welcome reform intentions, which could help to effectively tackle the challenges faced by Slovenia, if implemented in a rigorous and timely manner.

The stability programme reaffirms Slovenia's commitment to correcting the excessive deficit by 2015 in line with the excessive deficit procedure and achieving a balanced budget position in structural terms by 2017. Furthermore, it provides details of the path anticipated for the debt until 2018, which is projected to remain above the 60% of GDP reference value for the duration of the programme. Greater details on the further fiscal consolidation measures required to sustainably achieve the stated objectives of the programme would further enhance the robustness of the document.

OVERVIEW TABLE

2013 commitments	Summary assessment[57]
Country-specific recommendations (CSRs)	
CSR 1: For 2013 and beyond, implement and reinforce the budgetary strategy, supported by sufficiently specified structural measures, to ensure the correction of the excessive deficit by 2015 in a sustainable manner and the improvement of the structural balance specified in the Council recommendation under the EDP. After the correction of the excessive deficit, pursue a structural adjustment effort that will enable Slovenia to reach the MTO which should be set in line with the Stability and Growth Pact by 2017. Durable correction of the fiscal imbalances requires the implementation of ambitious structural reforms, which would increase the adjustment capacity of the economy and boost potential growth and employment. Safeguard growth-friendly spending, adopt measures to improve tax compliance and implement measures on the expenditure side underpinned by systematic reviews of public expenditure at all government levels. To improve the credibility of consolidation, complete the adoption of a general government budget balance/surplus rule in structural terms, make the medium-term budgetary framework binding, encompassing and transparent, and strengthen the role of independent bodies monitoring fiscal policy by end 2013. Take measures to gradually reduce the contingent liabilities of the state.	Slovenia has made **limited progress** in addressing CSR 1: • Slovenia has made limited progress in safeguarding fiscal sustainability. After the excessive deficit procedure has been extended to 2015, the government implemented several structural reforms both on the revenue side (increase in VAT rates as of July 2013 and other duties), and on the expenditure side (nominal public sector wages were temporarily cut by 1.25% in 2013, on top of the 3% cut from June 2012, and some allowances were also cut). The Commission stated that the draft budget for 2014-15 is in line with the Stability and Growth Pact rules, albeit with no margin. The consolidation of public finances is progressing slowly, predominantly through revenue-increasing reforms without a thorough review of the expenditure side. • Slovenia has made limited progress in safeguarding a durable correction of the fiscal imbalances. In May 2013, a constitutional amendment providing the basis for the general government budget balance rules was adopted. It was stipulated that the Fiscal Rules Act, which would detail the applicable concepts and mechanisms, would be adopted within six months (by November 2013), but it has been delayed.
CSR 2: Strengthen the long-term sustainability of the pension system beyond 2020 by further adjusting all relevant parameters, including through linking the statutory retirement age to gains in life expectancy, while preserving the adequacy of pensions. Contain age-related expenditure on long-term care and improve access to services by refocusing care provision from institutional to home care, sharpening targeting of benefits, and reinforcing prevention to reduce disability/ dependency.	Slovenia has made **limited progress** in addressing CSR 2**:** • Slovenia has made limited progress in safeguarding the sustainability and adequacy of its pension system. The pension reform began in January 2013, and aimed to ensure the medium-term sustainability of pension system. Evaluation of the reform was presented in April 2014, showing first positive results. A White Book (due by the end of 2014) will launch a public consultation on the long-term sustainability of the pension system post-2020.

[57] The following categories are used to assess progress in implementing the 2013 country-specific recommendations: No progress: The Member State has neither announced nor adopted any measures to address the CSR. This category also applies if a Member State has commissioned a study group to evaluate possible measures. Limited progress: The Member State has announced some measures to address the CSR, but these measures appear insufficient and/or their adoption/implementation is at risk. Some progress: The Member State has announced or adopted measures to address the CSR. These measures are promising, but not all of them have been implemented yet and implementation is not certain in all cases. Substantial progress: The Member State has adopted measures, most of which have been implemented. These measures go a long way in addressing the CSR. Fully addressed: The Member State has adopted and implemented measures that address the CSR appropriately.

	Apart from the evaluation, no further action has been taken. • Slovenia has made limited progress in reforming the system of long-term care: legislation is expected to be adopted before the end of 2014. However, there is a risk that the act will be delayed due to its link to the reform of the health insurance scheme (its funding) and the review of public spending in the healthcare sector, which is being negotiated with the World Bank. Discussions are ongoing since 2002 and there are limited expectations that the act will be finalised in 2014. • A sharp increase in government debt (Spring forecast: 80.4% in 2014) creates new challenges and risks that require durable policy action to ensure debt sustainability.
CSR 3: Ensure that wage developments, including the minimum wage, support competitiveness and job creation. Monitor closely the effects of the recent labour market reform and if necessary identify the areas where further action is needed to foster job creation and tackle segmentation, including through the regulation for student work. Take further measures to increase the employment of young tertiary graduates, older persons and the low-skilled by focusing resources on tailor-made active labour market policy (ALMP) measures while improving their effectiveness. Address the skills mismatch by improving the attractiveness of the relevant vocational education and training programmes and by further developing cooperation with the relevant stakeholders in assessing labour market needs.	Slovenia has made **limited progress** in addressing CSR 3**:** • Slovenia has made limited progress in ensuring that wage developments support competitiveness and job creation. No amendments to the act on the minimum wage have been made; the minimum wage now stands at EUR 789.15 and is indexed to inflation. Social partners are in a deadlock, and the government remained inactive. A new social agreement, which envisages a comprehensive approach to labour costs, is being negotiated. Gross wages fell slightly in 2013, mostly as a result of wage restraint in the public sector, while wages in non-tradable sector continued to grow. • Slovenia has made some progress in labour market reform. A reform was adopted in May 2013 and an evaluation is was prepared in April 2014, which showed the first positive developments. The Student Work Act is to be adopted by summer 2014. It introduces social contributions, making student work more expensive. It is not clear what kind of an impact this would act have on the position of young graduates on the labour market. The draft amended Higher Education Act aims to tighten student-status eligibility. However, the timeline for adoption of this act is unclear. • Slovenia has made limited progress in implementing tailor-made active labour market policy measures; it would focus mostly on the young unemployed (up to the age of 30) by using the Youth Guarantees (action plan adopted in January 2014). Some tailor-made active labour-market policy measures have been introduced, however their effectiveness still needs to be ascertained. • Slovenia has made limited progress on vocational education and training and on developing ways of cooperating with stakeholders in assessing labour-market needs.
CSR 4: Take the necessary steps, with input from European partners, to contract an independent external adviser in June 2013 to conduct a system-wide	Slovenia has made **substantial progress** in addressing CSR 4**:** • Slovenia has fully addressed the recommendation regarding the independent bank asset quality review

bank asset quality review. Complete this exercise in 2013, with faster progress in the cases of the two banks already subject to the state aid procedure, to accelerate their balance sheet repair. Stand ready to provide additional capital should the asset transfer or asset quality review reveal additional shortfalls. All measures, including objective assessments of capital needs, transfer of assets to Bank Asset Management Company (BAMC), asset protection scheme, operational implementation of the restructuring measures should be implemented in full compliance with state aid rules in case state aid is involved. In parallel, develop by March 2014 and implement a comprehensive sector strategy to ensure arms-length management of reformed banks and to substantially improve governance, risk management and profitability in the sector, including through consolidation where appropriate. Swiftly proceed with preparations for the announced privatisation of NKBM and establish, by September 2013, an ambitious timetable for the divestment of direct and indirect state shareholdings of banks.	and stress test, which were carried out in the second semester of 2013 and covered 70 % of the banking sector. The results were published on 12 December 2013. Transfers of non-performing loans took place after the Commission approved restructuring plans and state aid for the NLB and NKBM banks (18 December 2013). The given concessions were to fully privatise the NKBM and 75 % of the NLB. State-aid approval for the third largest bank, Abanka, is pending for the Commission's approval of the restructuring plan sent in mid-February 2014. • Slovenia has fully addressed the recommendation on the recapitalisation of banks. Based on the results of the exercise, the government provided a total of EUR 3.2 billion in December 2013. • Slovenia has made no progress regarding the situation of the Bank Asset Management Company (BAMC). The BAMC has been made operational but it lacks an asset management strategy and a business plan. • Slovenia has made limited progress in privatising the NKBM (to be completed by the end of 2014).
CSR 5: Review the bank regulatory framework by end 2013, and based on this review, strengthen supervisory capacity, transparency and statistical disclosure.	Slovenia has made **limited progress** in addressing CSR 5**:** • Slovenia has fully addressed the recommendation on reviewing the bank regulatory framework by the end of 2013. However, it appears that reflection on the asset quality review and stress test results has been limited. The Bank of Slovenia stated that it would provide a report specifying the further steps to be taken. • Slovenia has made no progress on strengthening supervisory capacity, transparency and statistical disclosure. Despite CRD IV coming into force on 1 January 2014, the authorities have not adopted the necessary legislation (adoption is planned before summer 2014).
CSR 6: Accelerate the reform of regulated services, including a significant reduction of entry barriers. Improve the business environment, including through ensuring the independence of and providing sufficient and autonomous financing to the Competition Protection Agency.	Slovenia has made **limited progress** in addressing CSR 6**:** • Slovenia has made some progress in addressing the regulated professions; their number has been reduced from 323 to 262. The authorities have also made it easier to obtain business licences. • Slovenia has made no progress on improving its business environment (especially in streamlining and shortening the time required to obtain necessary spatial planning and building permits, which are currently one of the most significant obstacles for foreign direct investment). • Slovenia has made no progress in ensuring sufficient and autonomous financing of the Competition Protection Agency, whose budget was cut by approximately 10 % in 2014, and it is subject to administrative investigations and a high degree of budgetary ex-ante oversight by the Ministry of Economy.
CSR 7:	Slovenia has made **some progress** in addressing CSR 7**:**

Build on previous efforts to further reduce the length of judicial proceedings at first instance in litigious civil and commercial cases and the number of pending cases, in particular enforcement cases.	• Slovenia has made some progress in reducing the length of judicial proceedings: disposition times and case backlogs in overall litigious civil and commercial cases improved, as a consequence of the case management reforms (e.g. Triaza project) and other initiatives. However, the length of trials remains long and the same indicators have not shown a positive trend for enforcement cases.
CSR 8: As part of the planned strategy of the government, to be completed by September 2013, classify core and non-core state assets according to economic criteria, with a view to divesting non-core assets. Make the Slovenian Sovereign Holding (SSH) fully operational in a timely manner, and transfer both ownership and management of all stakes to the SSH, potentially excluding those that are on the list for immediate full privatisation. Ensure professional management of the SSH from the outset, potentially including international expertise, and a clearly defined arms' length relationship with the companies involved. For core stakes, develop sector-specific strategies to improve profitability and corporate governance. Introduce an obligatory and publicly available register of management and supervisory board appointments in state-owned enterprises with requirements for disclosure of interests. Ensure that the regulatory framework facilitates divestment of non-core state assets and administrative hurdles are minimised.	Slovenia has made **limited progress** in addressing CSR 8**:** • Slovenia has made limited progress regarding the Slovenian Sovereign Holding (SSH). A new law was adopted in the parliament in late March 2014. The law empowers the government to submit a strategy for the SSH within three months of the law coming into force (that is July 2014).
CSR 9: Identify and start to work on removing all existing legal and administrative impediments to sustainable restructuring of over-indebted/undercapitalised but viable companies through market-based solutions. In this context, take measures to ensure sufficient private burden sharing, to increase private investment, including foreign direct investment, and to achieve efficiency gains in troubled companies as part of the restructuring process. Adopt the necessary legal framework for out-of-court restructuring by September 2013, ensuring that it is coherent with the existing provisions on insolvency and provides incentives for both creditors and shareholders to reach out-of-court restructuring agreements. Improve the enforcement of corporate insolvency procedures and in-court settlements, including swiftly resolving pending court cases related to bankruptcy procedures, in order to maximise recovery value and to facilitate the prompt and efficient resolution of non-performing loans.	Slovenia has made **some progress** in addressing CSR 9**:** • Slovenia has made no progress in ensuring a restructuring of the economy and increasing private investment, especially FDI. • Slovenia has made some progress by adopting several amendments to the Insolvency Act introducing, amongst others, a preventive restructuring proceeding (in the pre-insolvency stage) and a simplified compulsory settlement proceeding. The impact of the reform is yet to be assessed as it remains largely untested. The level of non-performing loans in the corporate sector has substantially increased. Slovenia has made limited progress in addressing the case backlogs and the length of proceedings governed by the Insolvency Act.

Europe 2020 (national targets and progress)	
Policy field target	**Progress achieved**
Employment rate (%): 75 %	As the employment rate stagnated in 2012 (68.3 %) compared to 2011 (68.4 %), Slovenia moved away from its target.
R&D target: 3 %	In the 2007-12 period, R&D intensity increased at an annual rate of 12.7 % and reached 2.8 % in 2012 (2.6 % in the private sector and 0.64 % in the public sector). Slovenia is on track to reach its target by 2020.
Greenhouse gas (GEG) emissions target: +4 % compared to 2005	Slovenia is on track to meet its target on GHG emissions in sectors not covered by the EU Emissions Trading System (ETS). GHG emissions are projected to increase by 4 % (compared to 2005) by 2020.[58] Non-ETS emissions have been reduced by 1 % between 2005 and 2012. Slovenia continues to stand out for its high level of CO2 emissions, especially in transport and households, both of which have one of the highest carbon intensities in the EU.
Renewable energy target: 25 % Proportion of renewable energy in the transport: 10 %	The proportion of renewable energy reached 20.2 % in 2012, up from 19.4 % in 2011. The share of renewables in transport increased and reached 2.9 % in 2012, up from 2.1 % in 2011.
Energy Efficiency target: 10 809 GWh saving By 2020: level of 7.31 Mtoe primary consumption and 5.1 Mtoe final energy consumption	Slovenia has set an indicative national energy efficiency target of 7.31 Mtoe primary consumption and 5.1 Mtoe final energy consumption by 2020. Slovenia notified the Commission about its plans to implement Article 7 of the Energy Efficiency Directive.
Early school leaving target: 5 %	The target has been achieved. Early school leaving fell from 5.6 % in 2006 to 3.9 % in 2013.
Tertiary education target: 40 %	Tertiary education rates continuously improved and reached the target in 2013 (40.1 %)
Target for reducing the population at risk of poverty or social exclusion: 40 000 (compared to 360 000 in 2008)	The number of people at risk of poverty or social exclusion, which is still far below the EU average, increased markedly between 2010 and 2012, from 366 000 in 2010 to 392 000 in 2012. This shows that Slovenia is moving away from the target.

[58] Latest European Environmental Agency greenhouse gas emission projections.

ANNEX

Standard Tables

Table I. Macro-economic indicators

	1996-2000	2001-2005	2006-2010	2011	2012	2013	2014	2015
Core indicators								
GDP growth rate	4.3	3.6	1.9	0.7	-2.5	-1.1	0.8	1.4
Output gap [1]	0.5	0.6	1.7	-0.8	-2.7	-3.1	-2.4	-1.5
HICP (annual % change)	8.2	5.6	3.0	2.1	2.8	1.9	0.7	1.2
Domestic demand (annual % change) [2]	4.6	3.1	1.4	-0.3	-6.4	-2.5	0.5	1.0
Unemployment rate (% of labour force) [3]	7.0	6.4	5.7	8.2	8.9	10.1	10.1	9.8
Gross fixed capital formation (% of GDP)	24.8	24.6	25.1	18.6	17.8	17.9	18.2	18.2
Gross national saving (% of GDP)	24.0	24.9	24.3	20.4	20.6	22.4	23.3	23.5
General Government (% of GDP)								
Net lending (+) or net borrowing (-)	**-2.5**	**-2.6**	**-3.1**	**-6.4**	**-4.0**	**-14.7**	**-4.3**	**-3.1**
Gross debt	**23.6**	**27.1**	**29.1**	**47.1**	**54.4**	**71.7**	**80.4**	**81.3**
Net financial assets	**n.a**	**11.5**	**7.2**	**-2.1**	**-8.1**	**n.a**	**n.a**	**n.a**
Total revenue	42.8	43.5	42.7	43.5	44.4	44.7	45.2	44.4
Total expenditure	45.3	46.1	45.8	49.9	48.4	59.4	49.5	47.4
of which: Interest	2.3	1.9	1.4	1.9	2.2	2.6	3.0	2.9
Corporations (% of GDP)								
Net lending (+) or net borrowing (-)	**-2.1**	**-3.7**	**-4.2**	**1.9**	**2.5**	**13.5**	**4.7**	**3.8**
Net financial assets; non-financial corporations	**n.a**	**-94.4**	**-118.3**	**-118.3**	**-121.0**	**n.a**	**n.a**	**n.a**
Net financial assets; financial corporations	**n.a**	**6.9**	**3.8**	**6.5**	**9.5**	**n.a**	**n.a**	**n.a**
Gross capital formation	16.1	16.9	17.0	12.5	10.3	10.4	10.2	10.6
Gross operating surplus	15.2	17.1	18.7	17.9	17.4	17.5	17.3	17.6
Households and NPISH (% of GDP)								
Net lending (+) or net borrowing (-)	**3.0**	**5.0**	**4.5**	**4.4**	**4.2**	**6.6**	**6.5**	**6.2**
Net financial assets	**n.a**	**69.2**	**73.9**	**69.9**	**72.8**	**n.a**	**n.a**	**n.a**
Gross wages and salaries	46.4	45.4	45.4	46.4	46.7	44.4	44.0	43.6
Net property income	1.3	1.5	1.0	0.9	0.9	0.6	1.0	1.3
Current transfers received	20.2	20.9	19.7	22.1	22.4	22.7	22.0	21.4
Gross saving	9.1	10.2	9.4	7.9	7.7	9.1	9.0	8.7
Rest of the world (% of GDP)								
Net lending (+) or net borrowing (-)	**-1.7**	**-1.3**	**-2.8**	**0.0**	**2.9**	**5.2**	**6.9**	**7.0**
Net financial assets	**n.a**	**7.1**	**33.9**	**45.0**	**47.9**	**n.a**	**n.a**	**n.a**
Net exports of goods and services	-2.2	-0.3	-0.2	1.5	4.8	6.7	7.6	7.9
Net primary income from the rest of the world	0.3	-0.6	-1.8	-1.1	-1.1	-0.6	-1.0	-1.1
Net capital transactions	0.0	-0.4	-0.1	-0.3	-0.3	-0.1	0.9	0.8
Tradable sector	47.5	47.2	45.4	45.2	45.7	46.5	n.a	n.a
Non tradable sector	39.0	40.3	42.2	42.0	41.3	40.0	n.a	n.a
of which: Building and construction sector	5.7	5.5	6.7	5.2	5.2	4.9	n.a	n.a
Real effective exchange rate (index, 2000=100)	99.5	99.2	104.7	107.6	105.2	104.0	104.1	103.4
Terms of trade goods and services (index, 2000=100)	100.8	101.6	100.0	97.1	96.2	97.0	97.9	97.9
Market performance of exports (index, 2000=100)	87.3	94.3	108.0	109.8	111.3	113.9	113.9	113.9

Notes:

[1] The output gap constitutes the gap between the actual and potential gross domestic product at 2005 market prices.

[2] The indicator on domestic demand includes stocks.

[3] Unemployed persons are all persons who were not employed, had actively sought work and were ready to begin working immediately or within two weeks. The labour force is the total number of people employed and unemployed. The unemployment rate covers the age group 15-74.

Source:
Commission 2014 spring forecast (COM); Stability programme (SP).

Table II. Comparison of macroeconomic developments and forecasts

	2013		2014		2015		2016	2017	2018
	COM	SP	COM	SP	COM	SP	SP	SP	SP
Real GDP (% change)	-1.1	-1.1	0.8	0.5	1.4	0.7	1.3	1.7	1.7
Private consumption (% change)	-2.7	-2.7	0.2	-0.4	1.1	0.7	1.8	1.8	1.8
Gross fixed capital formation (% change)	0.2	0.2	2.7	-0.5	1.4	1.0	0.0	2.5	2.5
Exports of goods and services (% change)	2.9	2.9	3.9	4.2	5.4	4.8	5.2	5.3	5.3
Imports of goods and services (% change)	1.3	1.3	3.9	3.5	5.3	5.2	5.3	5.3	5.4
Contributions to real GDP growth:									
- Final domestic demand	-1.9	-2.4	0.6	-0.4	0.9	0.6	0.9	1.3	1.3
- Change in inventories	-0.5	-0.5	-0.2	0.2	0.0	0.2	0.1	0.0	0.0
- Net exports	1.3	1.3	0.3	0.8	0.5	0.1	0.4	0.4	0.4
Output gap[1]	-3.1	-2.9	-2.4	-2.2	-1.5	-1.7	-0.8	0.4	1.5
Employment (% change)	-2.0	-2.0	0.0	-0.4	0.3	0.0	0.5	0.7	0.8
Unemployment rate (%)	10.1	10.1	10.1	10.2	9.8	10.0	9.7	9.1	8.6
Labour productivity (% change)	0.9	0.9	0.8	0.9	1.1	0.7	0.8	1.0	0.9
HICP inflation (%)	1.9	1.8	0.7	0.3	1.2	1.1	1.5	1.6	1.7
GDP deflator (% change)	1.0	1.0	0.9	0.5	1.3	1.0	1.4	1.4	1.5
Comp. of employees (per head, % change)	0.1	-0.3	1.0	0.6	1.6	1.1	2.0	2.2	4.3
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	5.2	5.4	6.9	n.a.	7.0	n.a.	n.a.	n.a.	n.a.

Note:

[1] In percent of potential GDP, with potential GDP growth recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

Source:

Commission 2014 spring forecast (COM); Stability programme (SP).

Table III. Composition of the budgetary adjustment

(% of GDP)	2013	2014		2015		2016	2017	2018	Change: 2013-2018
	COM	COM	SP	COM1	SP	SP	SP	SP	SP
Revenue	**44,7**	**45,2**	**46,4**	**44,4**	**45,5**	**44,6**	**43,8**	**43,4**	**-1,3**
of which:									
- Taxes on production and imports	15,1	15,5	15,9	15,4	15,5	15,5	15,3	15,2	0,1
- Current taxes on income, wealth, etc.	7,3	7,4	7,5	7,4	7,5	7,4	7,4	7,4	0,1
- Social contributions	15,2	15,1	15,3	15,0	15,2	15,2	15,1	15,0	-0,2
- Other (residual)	7,0	7,2	7,7	6,5	7,3	6,5	6,0	5,8	-1,2
Expenditure	**59,4**	**49,5**	**50,5**	**47,4**	**47,9**	**46,1**	**44,5**	**43,1**	**-16,3**
of which:									
- Primary expenditure	56,8	46,5	47,1	44,5	44,6	42,8	41,4	40,1	-16,7
of which:									
Compensation of employees	12,3	12,0	12,0	11,8	11,6	11,2	10,7	10,3	-2,0
Intermediate consumption	6,7	6,6	6,5	6,5	6,5	6,0	5,7	5,6	-1,0
Social payments	19,9	19,7	19,8	19,4	19,6	19,3	18,8	18,4	-1,5
Subsidies	1,0	0,9	0,9	0,9	0,6	0,6	0,6	0,5	-0,5
Gross fixed capital formation	3,7	4,2	4,6	3,9	4,3	3,9	3,6	3,2	-0,5
Other (residual)	13,3	3,1	3,2	2,1	2,0	2,0	2,1	2,0	-11,3
- Interest expenditure	2,6	3,0	3,4	2,9	3,3	3,3	3,1	3,0	0,4
General government balance (GGB)	**-14,7**	**-4,3**	**-4,1**	**-3,1**	**-2,4**	**-1,5**	**-0,7**	**0,3**	**15,0**
Primary balance	**-12,1**	**-1,3**	**-0,7**	**-0,1**	**0,9**	**1,8**	**2,4**	**3,3**	**15,4**
One-off and other temporary measures	-10,7	-0,7	-0,9	0,0	0,0	0,0	0,0	0,0	10,7
GGB excl. one-offs	**-4,0**	**-3,6**	**-3,2**	**-3,1**	**-2,4**	**-1,5**	**-0,7**	**0,3**	**4,3**
Output gap2	-3,1	-2,4	-2,2	-1,5	-1,7	-0,8	0,4	1,5	4,6
Cyclically-adjusted balance2	-13,3	-3,2	-3,1	-2,4	-1,6	-1,1	-0,9	-0,4	12,9
Structural balance (SB)3	**-2,5**	**-2,5**	**-2,2**	**-2,4**	**-1,6**	**-1,1**	**-0,9**	**-0,4**	**2,2**
Change in SB	*0,2*	*0,0*	*0,8*	*0,2*	*0,6*	*0,5*	*0,3*	*0,5*	-
Two year average change in SB	*1,2*	*0,1*	*0,3*	*0,1*	*0,7*	*0,5*	*0,4*	*0,4*	-
Structural primary balance3	-0,3	0,5	1,2	0,6	1,7	2,2	2,2	2,6	2,9
Change in structural primary balance		*0,8*	*1,5*	*0,1*	*0,5*	*0,5*	*0,1*	*0,4*	-
Expenditure benchmark									
Applicable reference rate4	0,54	-0,72	-0,72	-0,72	-0,72	-0,72	-0,72	n.a.	-
Deviation5 (% GDP)	7,3	-10,5	-13,1	-0,8	-1,6	0,2	0,5	n.a.	-
Two-year average deviation (% GDP)	1,3	-1,6	-3,1	-5,6	-7,3	-0,7	0,3	n.a.	-

Notes:

[1]On a no-policy-change basis.

[2]Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

[3]Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.

[4] Reference medium-term rate of potential GDP growth. The (standard) reference rate applies from year t+1, if the country has reached its MTO in year t. A lower rate applies as long as the country is adjusting towards its MTO, including in year t.The reference rates applicable to 2014 onwards have been updated in 2013.

[5] Deviation of the growth rate of public expenditure net of discretionary revenue measures and revenue increases mandated by law from the applicable reference rate. The expenditure aggregate used for the expenditure benchmark is obtained following the commonly agreed methodology. A positive sign implies that expenditure growth exceeds the applicable reference rate.

Source:

Stability programme (SP); Commission services' 2013 spring forecasts (COM); Commission services' calculations.

Table IV. Debt dynamics

(% of GDP)	Average 2008-2012	2013	2014		2015		2016	2017	2018
			COM	SP	COM	SP	SP	SP	SP
Gross debt ratio[1]	**39.5**	**71.7**	**80.4**	**80.9**	**81.3**	**81.1**	**76.0**	**72.5**	**70.4**
Change in the ratio	6.3	17.4	8.7	9.2	0.9	0.2	-5.1	-3.5	-2.1
Contributions: [2]									
1. Primary balance	**3.3**	**12.1**	**1.3**	**0.7**	**0.1**	**-0.9**	**-1.8**	**-2.4**	**-3.3**
2. "Snow-ball" effect	**1.6**	**2.7**	**1.8**	**2.7**	**0.8**	**2.0**	**1.2**	**0.8**	**0.8**
Of which:									
Interest expenditure	1.6	2.6	3.0	3.4	2.9	3.3	3.3	3.1	3.0
Growth effect	0.3	0.6	-0.5	-0.4	-1.1	-0.6	-1.0	-1.3	-1.2
Inflation effect	-0.4	-0.5	-0.7	-0.4	-1.0	-0.8	-1.1	-1.1	-1.0
3. Stock-flow adjustment	**1.4**	**2.6**	**5.6**	**5.8**	**0.0**	**-0.8**	**-4.5**	**-1.8**	**0.4**
Of which:									
Cash/accruals diff.	-0.6	0.3							
Acc. financial assets	2.0	2.3							
Privatisation	0.0	0.0							
Val. effect & residual	0.0	0.0							

	2013	2014		2015		2016	2017	2018
		COM	SP	COM	SP	SP	SP	SP
Gap to the debt benchmark[3,4]	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Structural adjustment[5]	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
To be compared to:								
Required adjustment[6]	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

Notes:

[1]End of period.

[2]The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

[3]Not relevant for Member Sates that were subject to an EDP procedure in November 2011 and for a period of three years following the correction of the excessive deficit.

[4]Shows the difference between the debt-to-GDP ratio and the debt benchmark. If positive, projected gross debt-to-GDP ratio does not comply with the debt reduction benchmark.

[5]Applicable only during the transition period of three years from the correction of the excessive deficit for EDP that were ongoing in November 2011.

[6]Defines the remaining annual structural adjustment over the transition period which ensures that - if followed – Member State will comply with the debt reduction benchmark at the end of the transition period, assuming that COM (SP) budgetary projections for the previous years are achieved.

Source:

Stability programme (SP); Commission 2014 spring forecast (COM); Commission calculations.

Table V. Sustainability indicators

	Slovenia			European Union		
	2013 scenario	**No-policy-change scenario**	**Stability programme scenario**	**2013 scenario**	**No-policy-change scenario**	**Stability programme scenario**
S2*	7.6	6.6	4.7	2.4	2.4	0.7
of which:						
Initial budgetary position (IBP)	1.3	0.6	-1.0	0.5	0.4	-1.3
Long-term cost of ageing (CoA)	6.3	6.0	5.7	1.9	2.0	2.0
of which:						
pensions	4.0	4.1	4.0	0.7	0.8	0.9
healthcare	0.8	0.8	0.7	0.9	0.9	0.8
long-term care	1.1	1.1	1.0	0.6	0.6	0.6
others	0.3	0.1	0.0	-0.4	-0.4	-0.3
S1**	3.2	1.9	-1.5	1.5	1.7	-0.2
of which:						
Initial budgetary position (IBP)	1.3	-0.5	-2.4	-0.2	-0.4	-2.0
Debt requirement (DR)	0.7	1.5	0.4	1.5	1.8	1.5
Long-term cost of ageing (CoA)	1.2	0.9	0.6	0.2	0.3	0.3
S0 (risk for fiscal stress)***	0.31	:			:	
Debt as % of GDP (2013)		71.7			88.9	
Age-related expenditure as % of GDP (2013)		24.1			25.8	

Source *: Commission; 2014 stability programme.*

Note : The 2013 scenario depicts the sustainability gap under the assumption that the budgetary position evolves until 2013 in line with the Commission's 2014 spring forecast. The 'no-policy-change' scenario depicts the sustainability gap under the assumption that the budgetary position evolves until 2015 in line with the Commission's 2014 spring forecast. The 'stability programme' scenario depicts the sustainability gap under the assumption that the budgetary plans in the programme are fully implemented. Age-related expenditure as given in the 2012 Ageing Report.

* The long-term sustainability gap (S2) indicator shows the immediate and permanent adjustment required to satisfy an inter-temporal budgetary constraint, including the costs of ageing. The S2 indicator has two components: (i) the initial budgetary position (IBP), which gives the gap vis-à-vis the debt-stabilising primary balance and (ii) the additional adjustment required due to the costs of ageing. The main assumption used in the derivation of S2 is that, in an infinite horizon, the growth in the debt ratio is bound by the interest rate differential (i.e. the difference between the nominal interest and the real growth rates); thereby not necessarily implying that the debt ratio will fall below the EU Treaty 60 % debt threshold. The following thresholds were used for the S2 indicator: (i) if the value of S2 is lower than 2, the country is classed as low risk; (ii) if it is between 2 and 6, it is classed as medium risk; and (iii) if it is greater than 6, it is classed as high risk.

** The medium-term sustainability gap (S1) indicator shows the upfront adjustment effort required, in terms of a steady improvement in the structural primary balance in the period to 2020 and then sustained for a decade, to bring debt ratios back to 60% of GDP in 2030, including financing for any additional expenditure by the target date, arising from population ageing. The following thresholds were used to assess the scale of the sustainability challenge: (i) if the S1 value is less than zero, the country is classed as low risk; (ii) if a structural adjustment in the primary balance of up to 0.5 pp of GDP per year until 2020 after the last year covered by the 2014 spring forecast (2015) is required (indicating a cumulated adjustment of 2.5 pp), it is classed as medium risk; and (iii) if the S1 value is greater than 2.5 (i.e. a structural adjustment of more than 0.5 pp of GDP per year is necessary), it is classed as high risk.

*** The S0 indicator reflects up-to-date evidence on the role played by fiscal and financial competitiveness variables in creating potential fiscal risks. The methodology for the S0 indicator differs fundamentally from that for the S1 and S2 indicators. Unlike S1 and S2, S0 is not a quantification of the required fiscal adjustment effort, but a composite indicator which estimates the extent to which there might be a risk of fiscal stress in the short term. The critical threshold for the S0 indicator is 0.43.

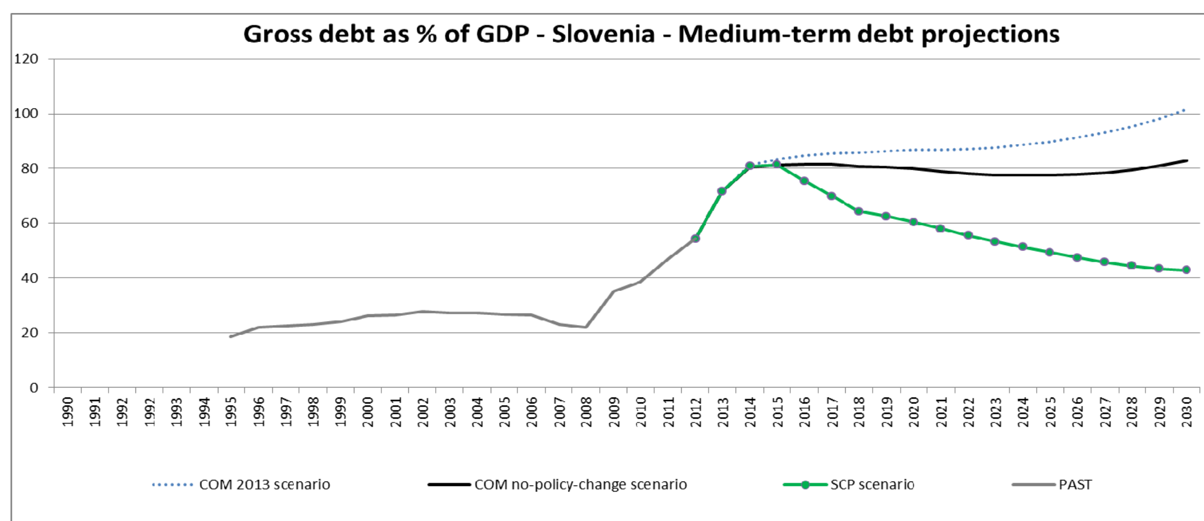

Table VI. Taxation indicators

	2002	2006	2008	2010	2011	2012
Total tax revenues (incl. actual compulsory social contributions, % of GDP)	37.8	38.3	37.3	37.7	37.2	37.6
Breakdown by economic function (% of GDP)[1]						
Consumption	13.7	13.2	13.4	14.0	13.9	14.2
of which:						
- VAT	8.5	8.5	8.5	8.2	8.3	8.2
- excise duties on tobacco and alcohol	0.9	1.1	1.1	1.4	1.4	1.5
- energy	2.6	2.3	2.3	3.0	2.8	3.1
- other (residual)	1.6	1.3	1.5	1.4	1.3	1.4
Labour employed	19.8	19.4	18.5	18.8	18.5	18.7
Labour non-employed	0.7	0.7	0.6	0.9	1.0	1.0
Capital and business income	2.8	4.3	4.0	3.2	3.0	2.7
Stocks of capital/wealth	0.9	0.9	0.9	0.9	0.9	1.0
p.m. Environmental taxes[2]	3.3	3.0	3.0	3.6	3.4	3.8
VAT efficiency[3]						
Actual VAT revenues as % of theoretical revenues at standard rate	64.4	67.6	68.3	59.2	59.2	58.9

Note:

1. Tax revenues are broken down by economic function, i.e. according to whether taxes are raised on consumption, labour or capital. See European Commission (2014), Taxation trends in the European Union, for a more detailed explanation.

2. This category comprises taxes on energy, transport and pollution, and resources included in taxes on consumption and capital.

3. The VAT efficiency is measured via the VAT revenue ratio. It is defined as the ratio between the actual VAT revenue collected and the revenue that would be raised if VAT was applied at the standard rate to all final (domestic) consumption expenditures, which is an imperfect measure of the theoretical pure VAT base. A low ratio can indicate a reduction of the tax base due to large exemptions or the application of reduced rates to a wide range of goods and services ('policy gap') or a failure to collect all tax due to e.g. fraud ('collection gap'). It should be noted that the relative size of cross-border shopping compared to domestic consumption also influences the value of the ratio, notably for smaller economies. See European Commission (2012), Tax Reforms in EU Member States and OECD (2012), Consumption tax trends for a more detailed discussion.

Source: Commission

Table VII. Financial market indicators

	2009	2010	2011	2012	2013
Total assets of the banking sector (% of GDP)	150.8	149.4	145.0	143.8	131.4
Share of assets of the five largest banks (% of total assets)	59.7	59.3	59.3	58.4	-
Foreign ownership of banking system (% of total assets)	29.1	28.2	28.3	29.3	-
Financial soundness indicators:					
- non-performing loans (% of total loans)[1)]	5.8	8.2	11.8	15.2	18.0
- capital adequacy ratio (%) [1)]	11.7	11.3	11.9	11.4	11.1
- return on equity (%) [1)]	2.0	-3.2	-11.8	-19.6	-15.6
Bank loans to the private sector (year-on-year % change)	2.3	1.6	-2.3	-4.1	-11.0
Lending for house purchase (year-on-year % change)	16.0	18.4	6.2	1.8	1.3
Loan to deposit ratio	159.3	156.5	149.0	143.8	119.0
CB liquidity as % of liabilities	4.5	1.3	3.9	9.6	10.3
Banks' exposure to countries receiving official financial assistance (% of GDP)	-	-	-	-	-
Private debt (% of GDP)	115.9	118.0	115.7	114.1	-
Gross external debt (% of GDP)					
- Public	18.6	22.9	24.0	31.3	43.8
- Private	38.9	39.7	41.6	43.0	43.6
Long term interest rates spread versus Bund (basis points)*	115.3	108.9	236.3	431.3	424.2
Credit default swap spreads for sovereign securities (5-year)*	97.1	71.2	159.1	330.1	273.2

Notes:

[1)] Latest data 2013Q3.

* Measured in basis points.

Source:

Bank for International Settlements and Eurostat (exposure to macro-financially vulnerable countries), IMF (financial soundness indicators), Commission (long-term interest rates), World Bank (gross external debt) and ECB (all other indicators).

Table VIII. Labour market and social indicators

Labour market indicators	2008	2009	2010	2011	2012	2013
Employment rate (% of population aged 20-64)	73.0	71.9	70.3	68.4	68.3	67.2
Employment growth (% change from previous year)	2.6	-1.8	-2.2	-1.6	-0.8	-2.0
Employment rate of women (% of female population aged 20-64)	68.5	67.9	66.5	64.8	64.6	63.0
Employment rate of men (% of male population aged 20-64)	77.4	75.6	74.0	71.8	71.8	71.2
Employment rate of older workers (% of population aged 55-64)	32.8	35.6	35.0	31.2	32.9	33.5
Part-time employment (% of total employment, 15 years and more)	9.0	10.6	11.4	10.4	9.8	10.1
Part-time employment of women (% of women employment, 15 years and more)	11.4	13.2	14.7	13.3	13.1	13.5
Part-time employment of men (% of men employment, 15 years and more)	7.1	8.4	8.6	7.9	7.0	7.3
Fixed term employment (% of employees with a fixed term contract, 15 years and more)	17.4	16.4	17.3	18.2	17.1	16.5
Transitions from temporary to permanent employment	38.7	40.7	31.8	37.9	36.6	:
Unemployment rate[1] (% of labour force, age group 15-74)	4.4	5.9	7.3	8.2	8.9	10.1
Long-term unemployment rate[2] (% of labour force)	1.9	1.8	3.2	3.6	4.3	5.2
Youth unemployment rate (% of youth labour force aged 15-24)	10.4	13.6	14.7	15.7	20.6	21.6
Youth NEET rate (% of population aged 15-24)	6.5	7.5	7.1	7.1	9.3	9.2
Early leavers from education and training (% of pop. 18-24 with at most lower sec. educ. and not in further education or training)	5.1	5.3	5.0	4.2	4.4	3.9
Tertiary educational attainment (% of population 30-34 having successfully completed tertiary education)	30.9	31.6	34.8	37.9	39.2	40.1
Formal childcare (from 1 to 29 hours; % over the population less than 3 years)	4.0	4.0	4.0	3.0	2.0	:
Formal childcare (30 hours or over; % over the population less than 3 year)	27.0	27.0	33.0	34.0	36.0	:
Labour productivity per person employed (annual % change)	0.8	-6.2	3.5	2.4	-1.7	0.9
Hours worked per person employed (annual % change)	0.9	-6.0	0.7	-1.5	-1.3	0.7
Labour productivity per hour worked (annual % change; constant prices)	-0.1	-0.2	2.8	3.9	-0.4	0.2
Compensation per employee (annual % change; constant prices)	2.9	-1.4	5.0	0.5	-1.2	-0.9
Nominal unit labour cost growth (annual % change)	6.4	8.6	0.4	-0.7	0.8	:
Real unit labour cost growth (annual % change)	2.1	5.1	1.5	-1.9	0.5	-1.8

Notes:

[1] Unemployed persons are all persons who were not employed, had actively sought work and were ready to begin working immediately or within two weeks. The labour force is the total number of people employed and unemployed.

[2] Long-term unemployed are unemployed persons for at least 12 months.

Sources:
Commission (EU Labour Force Survey and European National Accounts)

Expenditure on social protection benefits (% of GDP)	2007	2008	2009	2010	2011
Sickness/Health care	6.7	7.0	7.8	7.9	7.8
Invalidity	1.7	1.6	1.8	1.8	1.7
Old age and survivors	9.7	9.6	10.9	11.4	11.6
Family/Children	1.7	1.8	2.1	2.2	2.2
Unemployment	0.4	0.4	0.6	0.7	0.8
Housing and Social exclusion n.e.c.	0.0	0.0	0.0	0.0	0.0
Total	20.7	20.9	23.7	24.4	24.6
of which: means tested benefits	1.8	1.8	2.0	2.0	2.0
Social inclusion indicators	**2008**	**2009**	**2010**	**2011**	**2012**
At-risk-of-poverty or social exclusion[1] (% of total population)	18.5	17.1	18.3	19.3	19.6
At-risk-of-poverty or social exclusion of children (% of people aged 0-17)	15.3	15.1	15.2	17.3	16.4
At-risk-of-poverty or social exclusion of elderly (% of people aged 65+)	24.4	23.3	22.8	24.2	22.8
At-Risk-of-Poverty rate[2] (% of total population)	12.3	11.3	12.7	13.6	13.5
Severe Material Deprivation[3] (% of total population)	6.7	6.1	5.9	6.1	6.6
Share of people living in low work intensity households[4] (% of people aged 0-59)	6.7	5.6	7.0	7.6	7.5
In-work at-risk-of poverty rate (% of persons employed)	5.1	4.8	5.3	6.0	6.5
Impact of social transfers (excluding pensions) on reducing poverty	46.5	48.6	47.5	43.8	46.4
Poverty thresholds, expressed in national currency at constant prices[5]	6 299	6 501	6 376	6 385	6 319
Gross disponsable income (households)	22 677	22 839	23 043	23 567	22 923
Relative median poverty risk gap (60% of median equivalised income, age: total)	19.3	20.2	20.2	19.9	19.1

Notes:

[1] People at-risk-of poverty or social exclusion (AROPE): individuals who are at-risk-of poverty (AROP) and/or suffering from severe material deprivation (SMD) and/or living in household with zero or very low work intensity (LWI).

[2] At-risk-of poverty rate (AROP): share of people with an equivalised disposable income below 60% of the national equivalised median income.

[3] Share of people who experience at least 4 out of 9 deprivations: people cannot afford to i) pay their rent or utility bills, ii) keep their home adequately warm, iii) face unexpected expenses, iv) eat meat, fish, or a protein equivalent every second day, v) enjoy a week of holiday away from home once a year, vi) have a car, vii) have a washing machine, viii) have a colour tv, or ix) have a telephone.

[4] People living in households with very low work intensity: share of people aged 0-59 living in households where the adults (excluding dependent children) work less than 20% of their total work-time potential during the previous 12 months.

[5] For EE, CY, MT, SI, SK, thresholds in nominal values in Euros; HICP - index 100 in 2006 (2007 survey refers to 2006 incomes)

Sources:
For expenditure for social protection benefits ESSPROS; for social inclusion EU-SILC.

Table IX. Product market performance and policy indicators

Performance indicators	2004-2008	2009	2010	2011	2012	2013
Labour productivity[1] total economy (annual growth in %)	3.2	-5.8	3.6	2.1	-1.4	1.0
Labour productivity[1] in manufacturing (annual growth in %)	5.7	-8.3	14.7	3.6	-1.3	1.6
Labour productivity[1] in electricity, gas, water (annual growth in %)	2.7	-6.1	1.1	-3.4	-4.6	n.a.
Labour productivity[1] in the construction sector (annual growth in %)	1.2	-12.8	-9.2	1.1	1.1	0.5
Patent intensity in manufacturing[2] (patents of the EPO divided by gross value added of the sector)	113.1	116.7	123.7	129.6	n.a.	n.a.
Policy indicators	**2004-2008**	**2009**	**2010**	**2011**	**2012**	**2013**
Enforcing contracts[3] (days)	1368.0	1290	1290	1290	1290	1270
Time to start a business[3] (days)	51.8	6	6	6	6	6
R&D expenditure (% of GDP)	1.5	1.9	2.1	2.5	2.8	n.a.
Tertiary educational attainment (% of 30-34 years old population)	27.9	31.6	34.8	37.9	39.2	40.1
Total public expenditure on education (% of GDP)	5.5	5.7	5.7	5.7	n.a.	n.a.
	2008	**2009**	**2010**	**2011**	**2012**	**2013**
Product market regulation[4], Overall (Index; 0=not regulated; 6=most regulated)	2.0	n.a.	n.a.	n.a.	n.a.	1.8
Product market regulation[4], Retail (Index; 0=not regulated; 6=most regulated)	0.9	n.a.	n.a.	n.a.	n.a.	0.6
Product market regulation[4], Network Industries[5] (Index; 0=not regulated; 6=most regulated)	3.4	n.a.	n.a.	n.a.	n.a.	2.9

Notes:

[1] Labour productivity is defined as gross value added (in constant prices) divided by the number of persons employed.

[2] Patent data refer to applications to the European Patent Office (EPO). They are counted according to the year in which they were filed at the EPO. They are broken down according to the inventor's place of residence, using fractional counting if multiple inventors or IPC classes are provided to avoid double counting.

[3] The methodologies, including the assumptions, for this indicator are presented in detail on the website http://www.doingbusiness.org/methodology.

[4] The methodologies of the product market regulation indicators are presented in detail on the website http://www.oecd.org/document/1/0,3746,en_2649_34323_2367297_1_1_1_1,00.html.

[5] Aggregate ETCR.

Source :

Commission, World Bank - *Doing Business* (for enforcing contracts and time to start a business) and OECD (for the product market regulation indicators).

Table X. Green Growth

		2003-2007	2008	2009	2010	2011	2012
Green Growth performance							
Macroeconomic							
Energy intensity	kgoe / €	0.28	0.26	0.25	0.26	0.26	0.25
Carbon intensity	kg / €	0.78	0.71	0.70	0.69	0.69	n.a.
Resource intensity (reciprocal of resource productivity)	kg / €	1.56	1.39	1.25	1.17	1.04	n.a.
Waste intensity	kg / €	n.a.	0.17	n.a.	0.18	n.a.	n.a.
Energy balance of trade	% GDP	-4.2%	-6.3%	-4.2%	-5.4%	-6.7%	-7%
Energy weight in HICP	%	13	13	12	14	14	15
Difference between change energy price and inflation	%	3.3	8	-5.1	11.5	7.8	2.9
Environmental taxes over labour taxes	ratio	15.7%	15.7%	18.3%	18.5%	17.8%	n.a.
Environmental taxes over total taxes	ratio	8.3%	8.1%	9.5%	9.6%	9.3%	n.a.
Sectoral							
Industry energy intensity	kgoe / €	0.23	0.19	0.18	0.18	n.a.	n.a.
Share of energy-intensive industries in the economy	% GDP	13.8	13.3	12.1	n.a.	n.a.	n.a.
Electricity prices for medium-sized industrial users**	€ / kWh	n.a.	0.09	0.10	0.09	0.09	0.09
Gas prices for medium-sized industrial users***	€ / kWh	n.a.	0.04	0.04	0.04	0.04	0.05
Public R&D for energy	% GDP	n.a.	0.01%	0.01%	0.01%	0.02%	0.02%
Public R&D for the environment	% GDP	n.a.	0.02%	0.02%	0.02%	0.02%	0.02%
Recycling rate of municipal waste	ratio	18.3%	20.1%	20.9%	23.0%	35.1%	40.7%
Share of GHG emissions covered by ETS*	%	n.a.	41.4%	41.6%	41.9%	41.1%	40.2%
Transport energy intensity	kgoe / €	0.79	0.86	0.82	n.a.	n.a.	n.a.
Transport carbon intensity	kg / €	2.36	2.57	2.48	n.a.	n.a.	n.a.
Security of energy supply							
Energy import dependency	%	52.6%	55.1%	48.4%	49.4%	48.1%	51.6%
Diversification of oil import sources	HHI	n.a.	0.23	0.25	0.21	0.20	n.a.
Diversification of energy mix	HHI	0.24	0.26	0.25	0.24	0.24	0.24
Share renewable energy in energy mix	%	10.6%	11.0%	14.3%	14.3%	13.5%	14.8%

Country-specific notes:
The year 2012 is not included in the table due to lack of data.
General explanation of the table items:
Source: Eurostat unless indicated otherwise; ECFIN elaborations indicated below
All macro intensity indicators are expressed as a ratio of a physical quantity to GDP (in 2000 prices)
Energy intensity: gross inland energy consumption (in kgoe) divided by GDP (in EUR)
Carbon intensity: Greenhouse gas emissions (in kg CO2 equivalents) divided by GDP (in EUR)
Resource intensity: Domestic Material Consumption (in kg) divided by GDP (in EUR)
Waste intensity: waste (in kg) divided by GDP (in EUR)
Energy balance of trade: the balance of energy exports and imports, expressed as % of GDP
Energy weight in HICP: the share of the "energy" items in the consumption basket used in the construction of the HICP
Difference between energy price change and inflation: energy component of HICP, and total HICP inflation (annual %-change)
Environmental taxes over labour or total taxes: from DG TAXUD's database "Taxation trends in the European Union"
Industry energy intensity: final energy consumption of industry (in kgoe) divided by gross value added of industry (in 2005 EUR)
Share of energy-intensive industries in the economy: share of gross value added of the energy-intensive industries in GDP
Electricity and gas prices medium industrial users: consumption band 500 - 2000MWh and 10000 - 100000 GJ; figures excl. VAT.
Recycling rate of municipal waste: ratio of municipal waste recycled over total municipal waste
Public R&D for energy or for the environment: government spending on R&D (GBAORD) for these categories as % of GDP
Share of GHG emissions covered by ETS: based on greenhouse gas emissions as reported by Member States to EEA (excl LULUCF)
Transport energy intensity: final energy consumption of transport activity (kgoe) divided by transp industry gross value added (2005 EUR)
Transport carbon intensity: greenhouse gas emissions in transport activity divided by gross value added of the transport sector
Energy import dependency: net energy imports divided by gross inland energy consumption incl. energy consumption international bunkers
Diversification of oil import sources: Herfindahl index (HHI), calculated as the sum of the squared market shares of countries of origin
Diversification of the energy mix: Herfindahl Index over natural gas, total petrol products, nuclear heat, renewable energies and solid fuels
Share renewable energy in energy mix: %-share in gross inland energy consumption, expressed in tonne oil equivalents
* Commission and EEA.
** For 2007 average of S1 & S2 for DE, HR, LU, NL, FI, SE & UK. Other countries only have S2.
*** For 2007 average of S1 & S2 for HR, IT, NL, FI, SE & UK. Other countries only have S2.

List of indicators used in Box 4 on the potential impact on growth of structural reforms.

Final goods sector mark-ups: Price-cost margin, i.e. the difference between the selling price of a good or service and its cost. Final goods mark-ups are proxied by the mark-ups in selected services sectors (transport and storage, post and telecommunications, electricity, gas and water supply, hotels and restaurants and financial intermediation but excluding real estate and renting of machinery and equipment and other business activities[59]).
Source: Commission services estimation using the methodology of Roeger, W. (1995). "Can imperfect Competition explain the Difference between primal and dual Productivity?" *Journal of Political Economy* Vol. 103(2) pp. 316-30, based on EUKLEMS 1996-2007 data.

Entry costs: Cost of starting a business in the intermediate sector as a share of income per capita. The intermediate sector is proxied by the manufacturing sector in the model.
Source: World Bank, Doing Business Database. www.doingbusiness.org. 2012 data.

Implicit consumption tax rate: Defined as total taxes on consumption over the value of private consumption. In the simulations it is used as a proxy for shifting taxation away from labour to indirect taxes. The implicit consumption tax-rates are increased (halving the gap vis-à-vis the best performers) while labour tax-rates are reduced so that the combined impact is ex-ante budgetary neutral.
Source: European Commission, Taxation trends in the European Union, 2013 edition, Luxembourg, 2013. 2011 data.

Shares of high-skilled and low-skilled: The share of high skilled workers is increased, the share of low-skilled workers is reduced (halving the gap vis-à-vis the best performers). Low-skilled correspond to ISCED 0-2 categories; high-skilled correspond to scientists (in mathematics and computing, engineering, manufacturing and construction). The remainder is medium-skilled.
Source: EUROSTAT. 2012 data or latest available.

Female non-participation rate: Share of women of working age not in paid work and not looking for paid work in total female working-age population
Source: EUROSTAT. 2012 data or latest available.

Low-skilled male non-participation rates: Share of low-skilled men of working age not in paid work and not looking for paid work in total male working-age population
Source: EUROSTAT. 2012 data or latest available.

Elderly non-participation rates (55-64 years): Share of the population aged 55-64 years not in paid work and not looking for paid work in total population aged 55-64 years.
Source: EUROSTAT. 2012 data or latest available.

ALMP: Active Labour Market Policy expenditures as a share of GDP over the share of unemployed in the population.
Source: EUROSTAT. 2011 data or latest available.

[59] The real estate sector is excluded because of statistical difficulties of estimating a mark-up in this sector. The sector renting of machinery and equipment and other business activities is conceptually part of intermediate goods sector.

Benefit replacement rate: Share of a worker's pre-unemployment income that is paid out by the unemployment insurance scheme. Average of net replacement rates over 60 months of unemployment.
Source: OECD, Benefits and Wages Statistics.
www.oecd.org/els/benefitsandwagesstatistics.htm. 2012 data.