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SLOVENIA – REVIEW OF PROGRESS ON POLICY MEASURES RELEVANT FOR THE CORRECTION OF MACROECONOMIC IMBALANCES

Table of contents

Executive summary

This report is the fourth specific monitoring report (the second of the second year) under the Macroeconomic Imbalances Procedure (MIP) for Slovenia. It reviews the latest macroeconomic and policy developments in Slovenia since the endorsement of the country-specific recommendations (CSRs) in July 2014, which target the correction of the imbalances identified in the In-depth report (IDR) in March 2014. The cut-off date for this report is the 10th of February 2015.

The Slovenian economy has continued to stabilise. Having exited recession in 2013, real GDP is expected to have grown by 2.6% in 2014. Unemployment decreased to 9.6% in November 2014 and is expected to decline further. The rising current account surplus is a consequence of the still subdued domestic demand and the good export performance which reflects the improvement in competitiveness. The NIIP has improved from its lowest level of -45.2% of GDP in 2012 to -37% in the thirst three quarters of 2014. Private sector debt is decreasing for the third consecutive year, driven almost entirely by a fall in corporate indebtedness. As a consequence private investment has been particularly affected in Slovenia but is anticipated to partially recover portended by high capacity utilisation level. Public debt has increased considerably in recent years and is forecast to peak at 83% of GDP in 2015.

Slovenia has made further progress in the implementation of initiatives relevant for the correction of macroeconomic imbalances. In spite of delays in some areas, a number of measures related to banking and corporate sector restructuring and the management of state assets have been approved by end-January 2015. Policy measures to stabilise the banking sector have been completed by the end of 2014. The operational restructuring of four major state-owned banks (NLB, NKBM, Abanka and Banka Celje) and the wind-down of two smaller domestic banks are progressing in line with the plans. The focus now needs to shift to the timely resolution of the high level of non-performing loans in the corporate sector given that the full benefits of restructuring takes time to materialise. The restructuring master plan was finalised in December 2014, but the centralised task force established in January 2015 still needs to prove its effectiveness. A new corporate governance code for state-owned enterprises was adopted in December 2014 and now needs to be implemented. The Slovenian Sovereign Holding, in charge of the management and divestment of state assets has implemented further organisational and structural measures to become fully operational but still lacks a strategy. The new supervisory board needs to be appointed by the Parliament in the coming months. The privatization programme is making progress, albeit with delays. The sales processes of the two largest assets, Telekom Slovenije and NKBM are expected to be completed by April 2015.

The Slovenian authorities have reaffirmed their commitment to reducing the deficit to below 3% of GDP in 2015 but additional measures are required to enhance long-term

sustainability of public finances. Progress has been made by Slovenia in reducing government consumption expenditure in recent years through freezes and cuts to the pay bill and intermediate consumption, although most of them are of a temporary nature. The 2013 pension reform is expected to enhance the mid-term sustainability of public finances. In order to protect this adjustment and enhance the sustainability of public finances in 2015 and beyond the focus should now shift from ad hoc measures to structural reforms and measures of a more permanent nature. The comprehensive review of healthcare expenditure, which is due to commence shortly, provides an opportunity to realign spending in the sector with priorities and generate efficiency savings. Furthermore, a robust fiscal framework can further underpin the credibility of budgetary planning going forward. The Fiscal Rules Act is delayed. The legislation passed first reading in January 2015 and is expected to be approved in the Parliament in March 2015. Every effort should be made to ensure the rules and the fiscal council are fully operational for the 2016 budgetary cycle. Further reforms to enhance the sustainability of public finances beyond 2020 need to be considered given the demographic pressures faced by Slovenia.

Reforms implemented in 2013-14 have yielded positive results, although there is room for further action. Labour market segmentation was reduced by the 2013 labour market reform. The government and social partners concluded a Social Agreement in January 2015 which includes an agreement to link the growth of wages to sectorial productivity. Labour market segmentation will be further reduced by the provisions on student work, amended in December 2014. The authorities need to step up the efforts to improve the business environment by further regulatory simplification, cutting the backlog in court cases, increasing the effectiveness of the public administration and credibility of institutions in order to increase the inflow of foreign direct investment.

Overall, the pace of structural reforms to adjust imbalances has been visibly accelerated over the last few months. However, the reform process is not yet complete and the implementation of the recently adopted measures will be challenging. The focus now needs to shift to implementation and the finalisation of key outstanding measures (privatisation of Telekom Slovenije and NKBM, asset management strategy, expenditure review, health and long term care reform) to support economic recovery. Looking further forward, continual progress needs to be made in addressing challenges relating to longer-term sustainability and the high level of state involvement in the economy.

1. Introduction

In November 2013, the European Commission presented, as part of the MIP, its third Alert Mechanism Report to underpin the selection of Member States requiring an in-depth investigation. The subsequent third In-Depth Review[1] for Slovenia examined the nature, origin and severity of macroeconomic imbalances and risks. The Commission concluded that "Slovenia continues to experience excessive macroeconomic imbalances, which require specific monitoring and continuing strong policy action". In April 2014, Slovenia submitted its Stability Programme and National Reform Programme (NRP), outlining fiscal targets and policy measures to restore economic growth and help unwind imbalances. On the basis of an assessment of these plans, the Commission proposed a set of eight CSRs[2], which were subsequently adopted[3] by the Council in July 2014. The CSRs addressed to Slovenia concern: sustainable public finance and national fiscal frameworks, the pension system, wage developments and other labour market issues, banking sector consolidation and restructuring, privatisation and governance of state-owned enterprises, corporate restructuring, including the functioning of the courts and the evaluation of the insolvency framework, better business environment and more efficient public administration. All CSRs were considered to be MIP relevant.

Moreover, the first CSR addressed to euro-area Member States[4] called for an assessment of progress in delivering on reform commitments by euro-area Member States with excessive imbalances.

The Commission therefore put in place a specific monitoring of policy measures that could contribute to the unwinding of imbalances. This report assesses the main policy measures taken by Slovenia since April 2014[5] and in particular the progress achieved since the last monitoring report published in December 2014.[6] For this purpose, a second specific monitoring mission to Slovenia was conducted on 21-23 January 2015.

[1] http://ec.europa.eu/economy_finance/publications/occasional_paper/2014/pdf/ocp187_en.pdf
[2] http://ec.europa.eu/europe2020/pdf/csr2014/csr2014_slovenia_en.pdf
[3] http://ec.europa.eu/europe2020/pdf/csr2014/csr2014_council_slovenia_en.pdf
[4] http://ec.europa.eu/europe2020/pdf/csr2014/csr2014_council_euroarea_en.pdf
[5] Details on the measures taken can be found in the overview table in annex 3.
[6] http://ec.europa.eu/economy_finance/economic_governance/documents/20141224_si_imbalances_epc_report_en.pdf

2. Recent macroeconomic developments

After having shrunk by 1.0% in 2013, real GDP is expected to have grown by 2.6% in 2014. Having exited recession in 2013, the Slovenia's economy grew in the first three quarters of 2014 faster than expected (2.6% y-o-y). Growth has been driven predominately by net exports and EU co-funded investment. Household consumption is expected to have grown in 2014 for the first time since 2010 and is expected to recover gradually over the period 2015-16. The Commission's 2015 Winter Forecast foresees a slowdown of economic growth in 2015 (+1.8%) and acceleration in 2016 (+2.3%). The deceleration is to be driven by a slowdown in gross fixed capital formation, mainly due to expected lower growth in public investment and decelerating net exports. Private investment in equipment and machinery is expected to pick up progressively and support growth going forward. In 2016, further increase in private consumption, together with the first increase in government consumption since 2010 (under a no-policy-change assumption) should drive the expected growth to 2.3% (Graph 1 in Annex 1).

The rising current account surplus is a consequence of the still subdued domestic demand and the good export performance which reflects the improvement in competitiveness. Slovenia continues to gain market shares on EU markets despite lower growth in some key trading partners. In 2013 and 2014, Slovenia recorded large trade surplus in goods which, coupled with traditional surplus in services, lifted the current account. The current account recorded a surplus of 4.8% of GDP in 2013 and it is expected to peak at 5.9% of GDP in 2014 (Graph 2 in Annex 1), before starting to slowly decline but is expected to remain on historically high levels. The NIIP has improved from its lowest level of -45.2% of GDP in 2012 to -37% in the thirst three quarters of 2014 (Graph 3 in Annex 1).

Active deleveraging has had a negative impact on domestic demand. Investment has been particularly affected in Slovenia. While saving rate of non-financial corporations remained largely unchanged, investment took the biggest hit in Slovenia compared to the euro area. Unless reversed, this trend will have negative consequences on productivity and economic growth in the medium and long term.

The private sector continues to deleverage which hinders private investment. Private sector debt is decreasing for the third consecutive year, driven almost entirely by a fall in corporate indebtedness (Graph 4 in Annex 1). Companies, striving to repay their debts, have been underinvesting compared to the historical average and peers in the region (Graph 5 in Annex 1). Households' indebtedness is already among the lowest in the EU, nevertheless the sector further deleveraged last year. Weakness in investment merits special attention not only with respect to domestic demand and short-term economic outlook but also because shortfalls in investment are detrimental for the future potential growth of the Slovenian economy. Despite the ongoing deleveraging, which is expected to continue but at a slower pace, domestic demand is now slowly recovering. Investment levels are anticipated to partially recover when private sector investment rebounds, portended by high capacity utilisation level and rising profitability expected over the next two years. However, it is expected to converge rather towards the EU average than the levels observed before the crisis (Graph 6 in Annex 1).

3. State-of-play of MIP-relevant reforms

3.1. Measures related to public finances and public debt sustainability

The authorities remain committed to reducing the deficit below 3% of GDP in 2015. Based on the Commission's 2015 Winter Forecast the deficit is expected to stand at 5.4% of GDP in 2014 (vs. 4.4% in the Draft Budgetary Plan (DBP)). This increase above what was expected in the DBP is due to the government approval[7] of a scheme to compensate depositors of LB Banka which was approved in December 2014. With respect to 2015, the authorities have published the supplementary budget, which indicates a deficit of 2.9% of GDP in 2015. This is broadly in line with the Commission Winter Forecast.

Public debt has increased considerably in recent years and is forecast to peak at 83% of GDP in 2015 and to start declining in 2016, but without further policy measures it is projected to increase somewhat in the medium term as cost of population ageing rises. In 2014, the authorities took advantage of the improved market sentiment and undertook considerable pre-financing. They have accumulated a cash buffer of more than EUR 3 billion which covers financing needs for 2015 and part of 2016 (although this will change when the supplementary budget is passed in February 2015). The focus of the Treasury Directorate in 2015 is to increase transparency of operations and improve liquidity in secondary markets. Any proceeds from the ongoing privatisation process represent a positive debt development and result in a lower debt level. Based on Commission's forecast debt is expected to increase to 83% in 2015. In the medium term the public debt is projected to increase to 87% of GDP in the absence of further measures as rising cost of population aging puts pressure on expenditure.

The Fiscal Rules Act (FRA) is considerably delayed. Slovenia is the one of the few countries where the adoption of the legislation transposing the directive on budgetary frameworks into the national legal order has been delayed and is still on-going**.** It is envisaged to be passed in March 2015 by the Parliament and that the Fiscal Council should be appointed by end-June 2015. Its rules of establishment are foreseen to be in place by end-September 2015[8]. This timeline considerably limits the scope for the Fiscal Council to engage in the 2016 budgetary process. The legislation needs to be complimented by revisions to the Public Finance Act, which will include detailed provisions defining the drafting, implementation and monitoring of the budget of all general government institutional units. The Government needs to prepare amendments to the Public Finance Act within six months of the enactment of the amendments to the FRA.

[7] In July 2014, the European Court of Human Rights in Strasbourg ruled that Slovenia has to repay deposit holders of Ljubljanska Banka within one year of the ruling. A scheme was approved by the government in December 2014.

[8] The draft act foresees that the appointment of the Fiscal Council members will commence within fifteen days of the act coming into force and the Council should establish its rules of procedure within 3 months after its members are appointed.

Progress has been made with respect to the launching of the comprehensive review in the health sector. It is understood, based on the discussions with the authorities, that the review will be undertaken in cooperation with the World Health Organisation (WHO) and the European Observatory for Health policies. A draft scope for the review has been prepared and a workshop was held with the relevant stakeholders at the end of January 2015 to finalise the proposal. The Terms of Reference and a timeline for the implementation of the review are currently being finalised. It is intended that the project will be wider than just expenditure and will include: (i) an analysis of the financing of the health system, (ii) an expenditure review, (iii) a review of benefit basket, and (iv) an assessment of health technology. The expenditure review element is expected to identify measures for 2016 (i.e. "quick wins") and also more long-term structural reforms that will require more time to implement.

Continued evaluation of the 2013 pension reform has shown positive results, but progress has yet to be made on adjusting key parameters of long-term fiscal sustainability. Through the implementation of the 2013 pension reform certain fiscal savings have been realised over 2013-14 and further containment of pension-related expenditures is expected for the period 2014-20. Despite this reform, the new preliminary projections (included into the 2015 Ageing Report: underlying assumption and projection methodologies) project the expenditures for pensions to increase from 11.3% of GDP in 2015 to 15.5% of GDP in 2060, a level among the highest in the EU. The adequacy of pensions is still deteriorating with implications on the risk of poverty in old-age, especially for women. Elements of a further pension system reform to ensure long-term stability of the pension system and adequacy of pensions (post 2020) are to be discussed in the context of a White Book, due to be published in mid-2015. The long-term budgetary pressures stemming from increasing demand for long-term care (LTC) have yet to be addressed. No progress has been made in the area of long-term care since the mission in October 2014.

3.2. Measures related to the restructuring of the banking and corporate sector and the high level of state ownership in the economy

Several policy actions to stabilise the banking sector were completed by the end of 2014, although further action is still required given that the sector still displays strong asset deleveraging, low profitability and a relatively high proportion of non-performing loans.[9] The recapitalisation of Banka Celje with EUR 190 million together with a transfer of NPLs of EUR 412 million (gross value) in December have been the latest measures taken by the Slovenian authorities to stabilise the banking system. Overall in 2013 and 2014 six banks

[9] In December 2013, the state injected EUR 3.2 billion of capital in five domestic state-owned banks. For more details please consult the second monitoring report "Slovenia - Monitoring of policy progress under the Macroeconomic Imbalance Procedure", 20 February 2014, page 10-12 (http://ec.europa.eu/economy_finance/economic_governance/documents/20140224_si_imbalances_ epc_report_en.pdf).

have received capital amounting to EUR 3.6 billion and EUR 5.0 billion of assets have been transferred to the BAMC (Annex 2). No additional transfers to the BAMC are foreseen by the authorities and any further capital shortfall would be dealt with by the bank resolution fund which is expected to be established in the first quarter of 2015. Slovenian banks have significantly shrunk their balance sheets in 2013/2014, mainly due to negative credit growth and transfers to the BAMC. Funding risks have eased significantly and this has facilitated further deleveraging on the liabilities side, including the repayment of senior debt obligations (almost in full) and LTRO funds (about 90%).

The Bank Asset Management Company (BAMC)[10] has set out its strategy and business plan, which still needs to be published. Certain amendments to the legislation establishing the BAMC, including the prolongation of its life span and improving the efficiency of asset management are still to be adopted by the government. The BAMC has so far received assets with a total gross value of approximately EUR 5.0 billion (net value of EUR 1.7 billion) from four state-owned banks (Annex 2). In addition, it has acquired additional corporate exposures at market price from two smaller domestic banks in wind-down - Probanka and Factor Banka - with a view to consolidate loans to borrowers already in its portfolio. The legal transfers of the assets were completed by end of 2014, while the physical transfer of the loan files from Banka Celje is still on-going and expected to be finalised in the first quarter of 2015. About two thirds of the exposures are in default, where the objective of the BAMC will be to acquire the collateral (mostly real estate but also some equity and company assets) and sell it either individually or as part of a structured portfolio. The remaining approximately 100 cases in the portfolio of the BAMC are companies with potentially viable core activities, which could be maintained if they were to benefit from an appropriate financial and operational restructuring.

The operational restructuring of four major state-owned banks (NLB, NKBM, Abanka and Banka Celje) and the wind-down of the two smaller domestic banks are on track. Monitoring trustees have been appointed for each of the banks and are regularly reporting to the European Commission on the implementation of the plans and the progress achieved. The winding-down plans of Factor Banka could be realised ahead of schedule, with the full repayment of deposits and the return of the banking licences still in 2015 (the original plan foresaw the winding-down by end 2016).

The privatisation of NKBM is advancing, while the privatisation process for Abanka will only be launched once the merger with Banka Celje is completed. On 7 October 2014, the authorities received two binding offers for NKBM. Negotiations should be in the final stage and the government aims to sign the sales agreement in the first quarter of 2015 (CSR deadline end of 2014). In the case of Abanka, a new plan based on a merger scenario

[10] The BAMC was established in March 2013 as a government-owned company with the task of facilitating the restructuring of non-preforming loans of banks with systemic importance that were facing severe solvency and liquidity problems.

with Banka Celje was approved by the Commission in December 2014[11]. The timeline set by the authorities is to complete the merger by 1 January 2016 and the privatisation by 30 June 2019.[12] In light of these developments since the issuance of the CSRs, it is likely that the CSR deadline relating to the launch of the privatisation of Abanka in 2015 is going to be missed.

Bank of Slovenia has ensured an appropriate follow-up of the shortcomings identified by the national Asset Quality Review exercise of 2013. Following the conclusion of the Asset Quality Review and Stress Test exercise conducted in 2013, the Bank of Slovenia (BoS) requested the banks which benefitted from state aid to follow-up on the main findings and implement corrective measures by the end of 2014. The banks involved were required to improve risk management, corporate governance, data quality, credit underwriting practices, etc. For some banks Bank of Slovenia has conducted and will continue to perform on-site inspections during which it monitors all requirements addressed to the. The banks have improved practices in many areas, especially underwriting standards and NPL work-out. Since December 2014, NPL and forbearance definitions are in line with EBA definitions in all banks. New and tighter corporate governance rules have been introduced during 2014 in line with international standards. Further measures to address some shortcomings identified by the AQR in 2013 could be taken (IT, data and quantitative aspects), but overall, the risk management practices appear to have significantly improved during 2014. Since the second half of 2014 Bank of Slovenia has reorganised its supervisory activities, which will be performed within the Single Supervisory Mechanism (SSM) framework.

The restructuring of the highly leveraged corporate sector remains a key challenge for the banking sector and the Slovenian economy as a whole. The level of NPLs remains very elevated compared to pre-crisis level, despite the transfers made by banks to the BAMC. To some extent, this is the result of the selective and only partial transfer of NPLs to the BAMC, a still deteriorating quality of the domestic loan portfolio, the introduction of a stricter NPL definition (to align with EBA guidance) and the poor asset quality in the foreign direct lending portfolios (which were not transferred to the BAMC). NPL ratios are also affected by the contraction of new lending and the subsequent reduction of the loan stocks. The major state-owned banks have systematically higher NPL ratios than foreign-owned banks despite the fact that the former have benefitted from a transfer to the BAMC. Corporate restructuring has gathered momentum. All major banks have reorganised and reinforced the resources of their work-out and restructuring departments. The increased restructuring efforts will materialise in the NPL levels with a time lag due to the fact that restructured loans must be classified as NPL for at least one year after the restructuring is concluded..

[11] Further details available here: http://europa.eu/rapid/press-release_IP-14-2700_en.htm

[12] Abanka is not on the list of 15-companies earmarked for privatisation as adopted by the Parliament in June 2013. The commitment for privatising the merged entity of Abanka and Banka Celje was provided in the context of restructuring plan, approved by the Commission in December 2014.

The restructuring efforts are being coordinated but the task force yet needs to prove its effectiveness. . The Ministry of Finance supported by the Bank of Slovenia has taken ownership of the coordination role and has set up a comprehensive restructuring master plan in December 2014. A task force has been established in January 2015 to monitor and coordinate the overall restructuring process, to facilitate the negotiation process between all stakeholders involved and to provide the necessary guidance and advice. The coordinating body of the task force is composed of representatives of the Ministry of Finance, the Bank of Slovenia, the Ministry of Economics, the Ministry of Justice and the BAMC and meets twice a month. The taskforce promotes out-of-court solutions and has established a fast-track approach for SMEs, which will be the object of the second wave of the corporate restructuring process, after having focused first on the restructuring of the large corporates. The creation of special purpose vehicles holding structured portfolios of loans to attract foreign investors, as part of the strategy to reduce NPLs in banks' balance sheets is being considered and a pilot project is being prepared.

A new corporate governance code for State-owned Enterprises (SOEs) was adopted in December 2014 and needs to be implemented. The new framework is reportedly in line with international practice: it (i) provides that SOEs and private companies operate on an equal footing; (ii) enhances the separation of the functions of the state from its capacity as an owner; (iii) applies across the spectrum of SOEs (with limited exceptions) the "comply or explain" principle; (iv) reinstates the roles of the company corpora, in particular the supervisory board, and the company's position towards the different stakeholders and (v) realises the principles of transparency and touches upon a number of long-open issues such as the remuneration and bonuses of the company boards. Contrary to its predecessor, the new code does not exclude the parallel application of other corporate governance frameworks (e.g. that of listed companies), thus eliminating the cases of privileged or otherwise differentiated treatment of SOEs in comparison with privately held companies. Finally, corporate governance of SOEs is explicitly connected to the goals of the forthcoming management strategy on state assets (see below), which ensures a consistent treatment of SOEs.

The Slovenian Sovereign Holding (SSH), in charge of the management and divestment of state assets is operational but still lacks a strategy. Following its institution and in order to perform its mandate, SSH still needs to have a strategy reflecting the country's strategic and development objectives and specifying the classification of state assets in strategic, important and portfolio investments. Although initially scheduled for discussion at the Parliament in July 2014, a draft strategy only entered intergovernmental consultations in January 2015 and is expected to be approved by the Parliament in March 2015. Progress has been made as regards the rest of the acts and corporate transformations foreseen in the law on SSH,[13] whereas a new supervisory board needs to be appointed by the Parliament within the

13 The Asset Management Policy was adopted in December 2014, which establishes the principles, criteria and procedures applicable to SSH when discharging its duties. Also, in December 2014 a management contract was concluded by SSH and

next months. Based on this strategy and within one month after its adoption, SSH is due to set up the first annual asset management plan to include the new divestment schedule for state assets, valid for the next 1-2 years, subject to Government's approval.

The privatization programme is advancing, albeit with delays. Since October 2014, the sale process of the biggest asset, Telekom Slovenije, has been re-launched and is currently projected to be signed in April 2015. The authorities have provided updated outlines of the progress made and of the indicative timelines for the different procedures, which are run by the Slovenian Sovereign Holding (SSH) in cooperation with or by other state funds (see table in Annex 3).

3.3. Measures related to competitiveness, business environment and institutional capacity

The preparation of the medium-term strategy to attract foreign direct investment (FDI) has been postponed to February 2015. The forthcoming strategy is expected to be divided into annual implementation plans. The Strategic Council for FDI is foreseen to be the central coordinator of all stakeholders in the process. The strategy is expected to propose various market activities in order to promote Slovenia as an investment destination (special B2B meetings, workshops and investment conferences) and the establishment of a one-stop-shop for foreign investors.[14] The objective is to increase the stock of FDI to the EU average (from 31% in 2012 to 40% of GDP) within 3 years and increase export growth to 7% per year in the same period of time. So far only one quarter of the measures of the Single Document[15] has been implemented and limited progress has been noted since the previous report. Especially burdensome remain the licensing and permits, which is to be addressed in the context of the forthcoming strategy for simplification of spatial planning (due by the end 2015).

A comprehensive strategy for the development of public administration at central government level over 2015-2020 is currently in public consultation. The Strategy aims to build an effective and efficient public administration as well as user-friendly services for citizens and businesses. The legal basis for public procurement is to be revised in summer 2015 in order to transpose the new procurement directives. The e-procurement system will

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the Republic of Slovenia, determining the payment of management fees to the first. On 1 January 2015 a compliance officer was appointed by SSH, mandated to prepare the organisation's integrity plan. The criteria for measuring the performance of SOEs, shall be adopted within 1 month approximately after the endorsement of the strategy. As regards the corporate transformations and the transfer of various assets to SSH, the progress made so far has been in line with the schedule stipulated in the law. More specifically: In July 2014, SSH acquired 13.7% of the shares in the fund Posebna družba za podjetniško svetovanje, d d. ("PDP") from the consultancy & management firm Družba za svetovanje in upravljanje d.o.o. ("DSU"). In October 2014, SSH acquired all the assets (including shares in different companies) owned by DSU. In January 2015, SSH became the sole owner of PDP after it acquired a 66.04% stake in the company from KAD for 5.7 m Euro. SSH is now expected to merge with PDP by absorbing it within the next months.

[14] http://ec.europa.eu/economy_finance/economic_governance/documents/20141224_si_imbalances_epc_report_en.pdf

[15] http://www.stopbirokraciji.si/en/smart-regulation/concrete-realised-measures/

only be fully operational by the end of 2015. Reforms of the procurement system will generate efficiency savings, enhance transparency and re-establish trust into the system.

The new government reiterated its commitment to fight corruption and adopted a new two-year programme in January 2015.[16] The programme includes 11 perennial measures targeted at restoring the quality and credibility of public administration in Slovenia, including the public procurement and the ethics code for politicians and government officials. However, the crucial point in the fight against corruption is restoring the credibility of the Commission for Prevention of Corruption.

Lengthy court proceedings and a high number of unresolved cases remain a challenge. Positive trends in the rate of resolving litigious civil and commercial cases and the length of proceedings have been maintained (in 2014, disposition time decreased to 294 days) and backlog has been further reduced by -18%. In the area of enforcement, further improvements are expected as a result of recent amendments to enforcement legislation and the case management reforms (project led by the Supreme Court). However, the improvements regarding litigious civil and commercial cases can be partly attributed to a notable decrease in the number of new cases. While the commercial courts have been reacting to a large surge in incoming insolvency cases, the backlog nonetheless increased.

The latest legislative amendments to the insolvency framework represent progress compared to the previous regime. In January 2015, the authorities presented the advanced version of the on-going evaluation exercise of the insolvency legislation adopted in 2013. The key finding of the evaluation is that the new framework allows more restructuring opportunities to companies in financial difficulties. In addition, the existence of such legal tools has reportedly offered an indirect incentive to the parties to negotiate and reach out-of-court settlements. Access to personal bankruptcy proceedings was significantly facilitated by lowering the costs of such proceedings. A large number of liquidations without any distribution to creditors may indicate that debtors are not properly incentivised to file early enough. The authorities do currently not see a need for further amendments to the 2013 insolvency framework.

The government and social partners concluded a new Social Agreement in January 2015, but the ultimate effect on external price competitiveness remains uncertain. The Social Agreement will be valid for the period 2015-2016 and covers a wide range of topics: sustainability of public finances, sustainable economic development, efficiency of the public sector, implementation of cohesion policy, health, labour market, investments, education and training system and pensions.[17] It has been agreed that the general growth of wages would

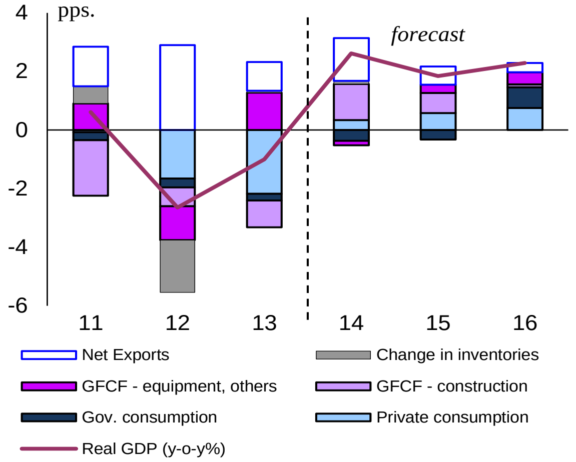
[16] http://www.vlada.si/medijsko_sredisce/sporocila_za_javnost/sporocilo_za_javnost/article/17_redna_seja_vlade_rs_50638/
[17] http://www.mddsz.gov.si/fileadmin/mddsz.gov.si/pageuploads/dokumenti__pdf/mddsz/parafa_Socialni_sporazum_200115.pdf

take into account sectorial productivity developments, albeit without any formal link, so that the ultimate effect on external price competitiveness remains uncertain. The government undertook the analysis of the burden of social contributions on employers that arise from different types of contractual work arrangements. Preliminary results show that there are significant differences in the non-wage cost for the employer, resulting from different type of work contracts. The government has announced to prepare proposals for concrete measures in 2015.

The regulation of student work has been amended. The legislative changes of student work were adopted in December 2014 and incorporated into the Act on balancing public finances. [18] The Act introduces minimum hourly wage (gross EUR 4.50) and social contributions for pension and disabilities insurance on student work contracts (15.5% will be contributed by students and 8.8% by employers) and is expected to have positive fiscal implications starting from 2015. The effects of the Act will be evaluated in September 2015 and further amendments to the act could be considered. The revision of the Act would bring along the digital work booklet necessary for the official recognition of student work experience. It is expected that labour market segmentation will be further reduced by the new act, but the overall flexibility of the labour market has yet to be enhanced further.

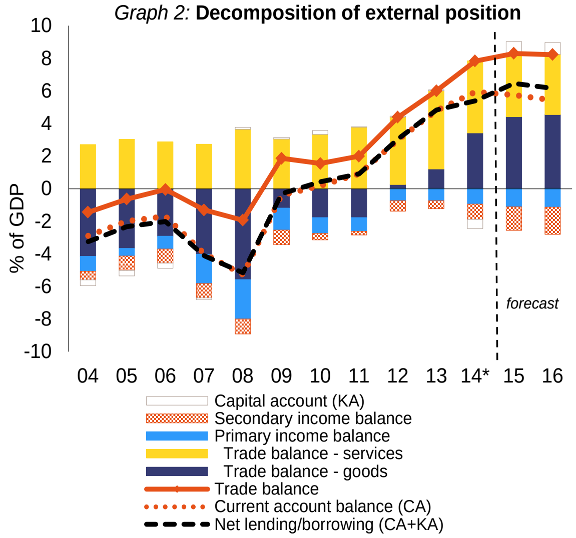
[18] http://www.mddsz.gov.si/si/delovna_podrocja/delovna_razmerja_in_pravice_iz_dela/delovna_razmerja/zacasno_in_obcasno_delo_dijakov_in_studentov_po_1_2_2015/

Annex 1: Graphs



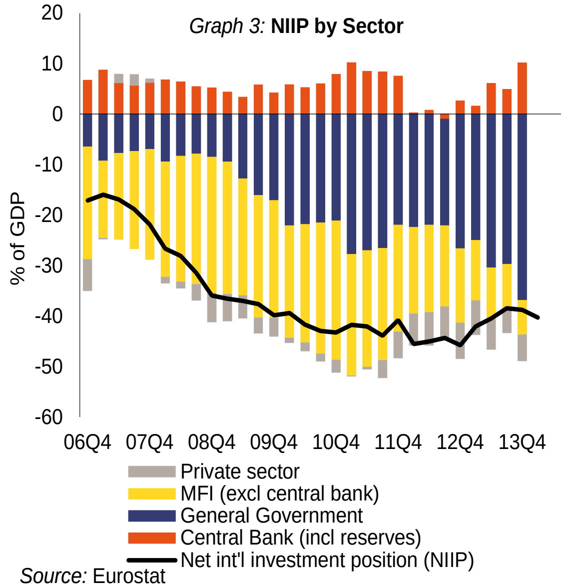
Graph 1: **Slovenia - Real GDP growth and contributions**

Source: DG ECFIN, Winter Forecast



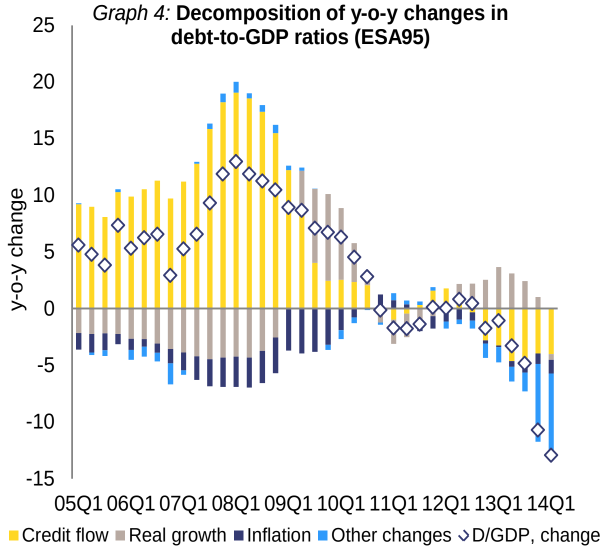
Graph 2: **Decomposition of external position**

Source: Eurostat, Winter Forecast 2015
* estimate based on quarterly data



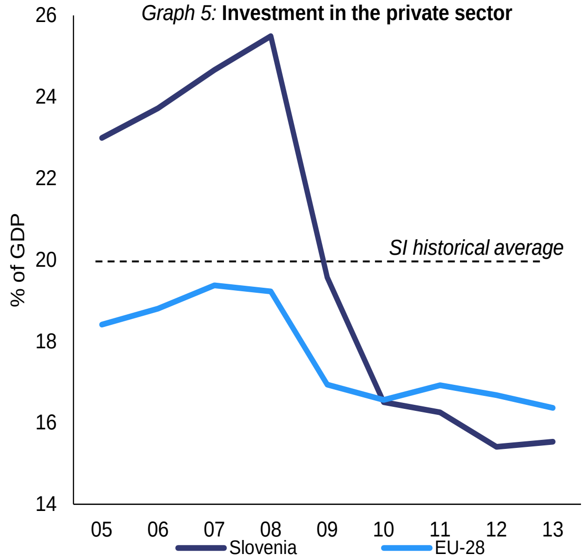
Graph 3: **NIIP by Sector**

Source: Eurostat



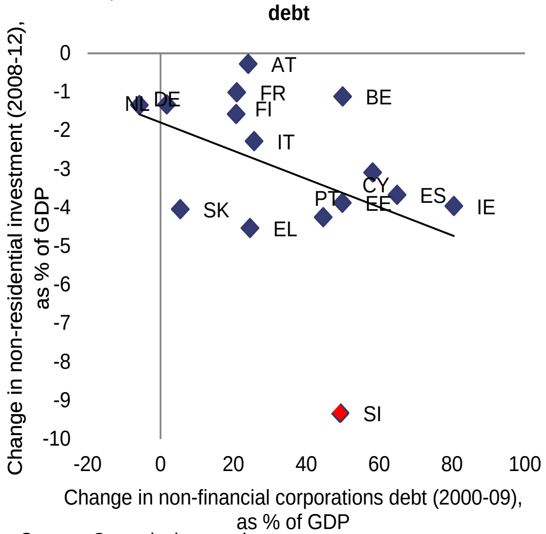
Graph 4: **Decomposition of y-o-y changes in debt-to-GDP ratios (ESA95)**

Source: Eurostat



Graph 5: **Investment in the private sector**

Source: AMECO



Graph 6: **Non-residential investment and NFC debt**

Source: Commission services

Annex 2: Overview of recapitalisation measures and asset transfers to the BAMC executed in 2013 and 2014

	Capital increase (EUR million)		Transfer of assets to BAMC (transfer /gross value, EUR million)	
	2013	2014	2013	2014
Total	**3 188**	**433**	**1 012/ 3 301**	**690/ 1 671**
NLB	1 551		622/ 2 278	
NKBM	870		390/ 1 023	
Abanka	348	243		538/ 1 087
Banka Celje		190		113/ 412
Probanka	170			28/ 118
Factor Banka	259			11/ 54

Annex 3: Progress on privatizations

State of play of on-going processes regarding the companies earmarked for privatization following a Parliamentary decision in 2013. Progress as of 30th January 2015.			**Preparation**	**1st phase**	**2nd phase**				**Comments******
Entity / Sector or business	**Market value of company (EUR million)****	**% identified for disposal** **State-owned % / total percentage incl. consenting shareholders*****	**Selection of financial advisor**	**Request for non-binding offer**	**Due diligence by investors**	**Request for binding offer**	**Signing of SPA**	**Closing**	
ADRIA AIRWAYS / Airline	9.1	91.58%	Feb 15*	Jun 15*	Jul - Aug 15*	Sep 15*	Oct 15*	-	In the **preparatory phase**. On 8 January 2015, the sellers signed an Agreement on the Joint Sale of Shares. Proposals for advisory services are to be submitted by 23 January 2015.
ADRIA AIRWAYS TEHNIKA / Maintenance, repair and overhaul	5	52%/100%	Nov 13	Feb 14	May14 / Oct 14/ Jan-Feb 15	Mar 15*	-	-	In the **2nd phase**. Ongoing due diligence.
AERODROM LJUBLJANA (listed) / Airport operator	234	65%/73%	Dec 13	May 14	May 14	Jul 14	Sep 14	Oct 14	**Successfully completed.** 75.5% shares sold to Fraport AG Frankfurt Airport Services Worldwide in consideration of EUR 15.9 million (for the 6.82% stake held by SSH) and EUR 118.8 million (for the 50.67% stake held by the Republic of Slovenia).
CINKARNA CELJE (listed) / Chemical processing	144.1	31%/73%	Apr 14	Nov 14	Jan-Feb 15	Mar 15*	Jun 15*	-	In the **2nd phase**. A vendor's due diligence has been prepared on the legal, financial and environmental issues.
ELAN / Manufacturer of sport products	37	75%/100%	Jun 13	Sep 13	Oct-Dec 13/ Nov – Dec 14	Dec 14	-	-	In the **2nd phase**. The offers received in December 2014 were not unconditional; the sellers are therefore engaged in negotiations with the investors, who are at the same time engaged in (separate) negotiations with different creditors of the company (BAMC and Gorenjska Banka and Korže d.o.o.). State aid issues involved.
FOTONA / Manufacturer of laser systems	15.2	70%	-	-	-	-	Jan 14	Mar 14	**Successfully completed**. The seller (PDP) has already received EUR 12.7 million, and may receive another EUR 0.4 million in two years after closing, if additional conditions are fulfilled.
GOSPO DARSKO - RAZSTAVIŠČE / Organisation of fairs and exhibitions	22	31%	-	-	-	May 14	-	-	**Temporarily suspended** due to the submission of unacceptable offers.

HELIOS (listed) / Chemical industry, manufacturer of coatings	144,7	18%/73%	May 12	-	-	-	Oct 13	Apr 14	**Successfully completed**. 77.93% shares sold to Remho Beteiligungs GmbH in consideration of EUR 106 million (SSH received EUR 13.8 million for its 9.54% stake).
NOVA KBM / Banking sector	560	100%	Jan 14	Jul 14	Aug 14 – Jan 15	Jan 15	Mar 15*	-	In the **2nd phase.** Binding offers received in mid-January 2015.
PALOMA / Manufacturer of hygienic paper products	6.5	71%	Aug 14	Mar 15*	Apr-May 15*	Jun 15*	Jul 15*	-	In the **preparatory phase.** New investor will enter the company through capital increase, while the current shareholders will exit following a take-over bid after the capital increase.
TELEKOM SLOVENIJE (listed) / Telecommunications	947.6	72%/73%	Oct 13	Jul 14	Jun 14-Jan 15	Mar 15*	Apr 15*	-	In the **2nd phase.** The investors are performing additional due diligence on the pending litigation cases of the company. A major claim of 300 million Eur approximately has been recently settled.
TERME OLIMIA / Tourism; hotel with thermal facilities	26.6	28,8%/75%	-	-	-	-	-	-	Companies merged in September 2014 into one company, Terme Olimia. Considered as a new asset. As a result thereof, process is expected to be treated under the Strategy of the SSHA-1 (in the new wave of privatizations), and will **no longer to be followed under this list**.
ŽITO (listed) / Food industry	46.6	27%/51%	Mar 14	Oct 14	Dec 14 – Jan 15	Jan 15	Apr 15*	-	In the **2nd phase**. Binding offers received at the end of January.
AERO / Production of self-adhesive materials and provision of technical support	2.2	1%	-	-	-	-	-	Oct 14	**Debt to equity swap and change of ownership** (it qualifies as a **successful completion** since it will be no longer followed under this list). A decrease of share capital and a debt-to-equity conversion took place in October 14. State–owned % decreased from 32.60% to 1.44%. The company is now owned by its former creditors / banks, which will be in charge of any further divestment initiatives.
UNIOR (listed) / Tool producer & tourism	22.7	45%	-	-	-	-	-	-	In the **preparatory phase.** The company is heavily indebted and will first go through restructuring. The plan is to split the non-core business (tourism programme) and do an asset sale thereof rather than privatizing the whole company.

Source: Slovenian Sovereign Holding (SSH), reporting progress as on January 30th 2015.

* Estimated dates.

** For listed companies market value on LJSE on December 31st 2014, for all the others audited book value of equity as at the end of 2013, except for Terme Olimia: book value on June 30th 2014, Adria Airways: book value on September 30th 2014; Helios and Aerodrom: Purchase price

*** State-owned refers to stakes held directly by either of the following: the Republic of Slovenia, the Slovenian Sovereign Holding ("SSH"; ex-*Slovenska odškodninska družba, d.d*. fund, "SOD"), *Kapitalska družba, d.d.* fund ("KAD"), *Posebna družba za podjetniško svetovanje, d d.* fund ("PDP"), *Družba za svetovanje in upravljanje d.o.o.* consultancy and management firm ("DSU"), and *Modra zavarovalnica d.d.* insurance company ("MZ"). Through shareholders' agreements there have been established consortia of sellers holding larger stakes.

**** The acronyms used in the table stand for the entities mentioned above. In addition, "BAMC" stands for the Bank Asset Management Company, "KD" stands for *KD Skladi druzba za upravljanje, d.o.o.*

Annex 4: Overview of MIP-relevant reforms

	2014 CSRs	Action taken		
		Announced measures	**Adopted measures**	**Implemented measures**
1	*Reinforce the budgetary strategy with sufficiently specified structural measures for the year 2014 and beyond, to ensure correction of the excessive deficit in a sustainable manner by 2015 through the achievement of the structural adjustment effort specified in the Council recommendation under the Excessive Deficit Procedure. A durable correction of the fiscal imbalances requires a credible implementation of ambitious structural reforms to increase the adjustment capacity and boost growth and employment. After the correction of the excessive deficit, pursue a structural adjustment of at least 0,5 % of GDP each year, and more in good economic conditions or to ensure that the debt rule is met in order to put the high general government debt ratio on a sustained downward path. To improve the credibility of fiscal policy, 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 establish the necessary legal basis for a functioning fiscal council defining its remit within the budgetary process and introducing clear procedural arrangements for monitoring budgetary outcomes as soon as possible. Launch a comprehensive review of expenditure covering state and local government levels, direct and indirect budget users and municipality-owned providers of utilities and services in the area of healthcare by the end of 2014 with a view to realising budgetary savings in 2015 and beyond.*	• The supplementary budget for 2014 is expected to be passed by Parliament in December 2014 • The supplementary budget for 2015 is expected to be passed by Parliament in February 2015 • The Government has announced in October 2014 that the Fiscal Rules Act is expected to be adopted in Q1 2015. The Act defines the structural balance, fiscal rule as well as correction mechanism and exceptional circumstances for deviation from the rule. It also provides for the establishment of a fiscal council; setting out its composition of members, functions and role. • The concepts forming the Fiscal Rules Act will be further defined in the Public Finance Act. Amendments to the Public Finance Act are currently under preparation, with the intention of adoption in mid-2015. • The expenditure review and the National Healthcare Resolution are both in preparation with the objective to launch the expenditure review in February 2015. The Ministry of Health in cooperation with the World Health Organisation and the European observatory for health systems and policies are currently preparing consolidated TOR for the expenditure review (subject to revision awaiting confirmation). The expenditure review will be a basis for a comprehensive healthcare reform, to enter into force from January 2016.	• **October 2014:** The authorities publish a Draft Budgetary Plan, which targets a deficit below 3% of GDP in 2015, the deadline for correcting the excessive deficit. • **December 2014**: Approval of scheme to compensate depositors of LB Banka. • **December 2014**: The Supplementary budget for 2014 is adopted by the Parliament. • **December 2014**: The Fiscal Rules Act is adopted by the government. • **January 2015:** The supplementary budget for 2015 is published. The revised estimate of the deficit is 2.89% of GDP. • **January 2015**: The first reading of Fiscal Rules Act is passed by Parliament (30 January 2015) with 79 votes in favour (out of 90), 5 votes opposed. • **January 2015**: A draft scope for the review has been prepared and a workshop was held with the relevant stakeholders to finalise the proposal.	• **December 2014:** Necessary legislative basis for measures underpinning the DBP (reduction in the overall pay bill, excise duties) have been adopted.
2	*Based on the public consultation, agree measures to ensure the sustainability of the pension system and adequacy of pensions beyond 2020, encompassing adjustments of key parameters, such as linking the statutory retirement age to gains in life expectancy and encouraging private contributions to the second pillar of the pension system. Contain age-related expenditure on long-term care by targeting benefits to those most in need and refocusing care provision from institutional to home care.*	• A white paper on the long term sustainability of pensions is announced to be published in mid-2015. • The Law on Establishment and Functioning of the demographic reserve fund is to be adopted by 30 June 2015. • The blueprint for long term care, adopted in September 2013, remains a valid point of departure for preparation of reform. The adoption of the law is postponed to the end of 2015 in order to match it with the reform of health insurance schemes.		• **January 2013**: The results of the evaluation of the impact of the 2013 pension reform are published. Through the implementation of the reform fiscal savings have been realised over 2013-14 and further containment of the pension-related expenditures is expected for the period 2014-20.

		• Nothing significant to report on the long-term care.		
3	*Following consultation with social partners and in accordance with national practices, develop a comprehensive Social Agreement by the end of 2014 ensuring that wage developments, including the minimum wage, support competitiveness, domestic demand and job creation. Redefine the composition of the minimum wage and review its indexation system. Take measures for further decreasing segmentation, in particular addressing the efficiency of incentives for hiring young and older workers and the use of civil law contracts. Adopt the Act on Student Work. Prioritise outreach to non-registered young people ensuring adequate public employment services capacities. To increase employment of low-skilled and older workers, adapt the working environment to longer working life and focus resources on tailor-made active labour market policy measures, while improving their effectiveness. Address skills mismatches by improving the attractiveness of vocational education and training and by further developing cooperation with the relevant stakeholders in assessing labour market needs.*	• Government has announced further measures to reduce labour market segmentation after the analysis of the non-wage costs of the different forms of work contracts in mid-2015. • The new Apprenticeships Act is announced to be adopted in Q1 2015. This act will primarily aim to redefine the role of apprentices as an employee with employment rights and obligations and not as a student. The Act is expected to determine the financing of the dual system and the contentious role of the social partners. • The employment services are currently working on a bi-annual forecast of deficit occupations in parallel to the establishment of the National Career Point, which aims to develop the methodology for career orientation. • Work has started on the new Higher Education Act. One of the provisions is expected to delineate the student status from the student benefits in order to repel incentives to prolong studies in order to prolong student benefits. The new electronic Information system of records and analysis for higher education has become an official source of information on student status used by public institutions to grant scholarships, transport and food subsidies, dormitories, health insurance, student work and others. By the end of 2015, the system will become a valuable analytical tool for evidence-based policy making	• **2014:** Alongside the Scholarships Act a policy paper is published identifying 24 deficient occupations, which are to be supported through scholarship. • **December 2014**: The legislative changes of student work were incorporated into the Act on balancing public finances. • **January 2015**: The government and social partners conclude a new Social Agreement which will be valid for the period 2015-2016 and covers a wide range of topics.	• **January 2015:** Scholarships for deficient professions will be awarded starting from the year 2015 based on the 2014 Scholarship Act. • **January 2015**: The implementation of Youth Guarantee Programme is on track. 22,000 young are included in the measures; 90% of them received an offer from the public employment services.
4	*Complete the privatisation of NKBM in 2014 as planned, prepare Abanka for privatisation in 2015, continue the prompt implementation of restructuring plans of the banks in receipt of State aid and the necessary consolidation of the banking sector. Based on the lessons from the asset quality review and stress test finalise the comprehensive action plan for banks in August 2014, including specific measures to improve governance, supervision, risk management, credit approval process and data quality and availability. Reinforce banks' capacity to work out non-performing loans by strengthening the internal asset management and restructuring units. Clarify the mandate of the Bank Asset Management Company by publishing a*	• Finalization of BAMC strategy and business plan by end of 2014. Approval of necessary amendments to the BAMC legislation in Q1 2015. • Sale of NKBM to be completed in Q1 2015. Abanka/Banka Celje restructuring will be based on merger of both entities. Launch of Abanka/Banka Celje privatisation process will start in January 2016 once the merger is completed. The privatization of the combined entity is expected to be completed by 30 June 2019. • Recapitalisation of Banka Celje and transfer of assets to the BAMC in December 2014. • Bank of Slovenia ensures follow up of	• **December 2014:** Banka Celje recapitalisation and transfer to the BAMC are approved by the Commission. • **December 2014:** BAMC strategy and business plan are agreed by the government. • **January 2014:** Comprehensive action plan for banks has been finalized and submitted to the Prime Minister office.	• **January 2015**: Binding offers for NKBM have been submitted. Negotiations are in the final stage and the government aims to sign the sales agreement in the first quarter of 2015 • **February 2015:** The operational restructuring of four major state-owned banks (NLB, NKBM, Abanka and Banka Celje) and the wind-down of the two smaller domestic banks are on track. • **February 2015**: Bank of Slovenia has ensured follow-up of the shortcomings identified by the 2013 AQR and will resume on-site inspections in Q1-2015 to verify whether the recommendations have been implemented by banks. Major banks

	comprehensive management strategy and business plan by September 2014, detailing its role in restructuring of its assets, redemption targets, budgets, asset management plans and expected returns, while ensuring adequate resources.	shortcoming identified in the 2013 AQR exercise. • Comprehensive action plan for banks to be adopted in Q1 2015 as part of Asset Management Strategy.		have reorganized and reinforced their work-out and restructuring units.
5	*Continue to implement the privatisations announced in 2013 with the time-frames set. Adopt a strategy for the Slovenian Sovereign Holding (SSH) with a clear classification of assets in line with the timeline and definitions established in the 2014 Slovenian Sovereign Holding Act. By November 2014, commit to a short-term (one- to two- year horizon) divestment schedule for a number of well-targeted assets with a clear time scale. Make it fully operational as a vehicle for the management of assets remaining in State ownership and divestment of the assets earmarked according to the management acts, within the time frame stipulated by the law. By September 2014, adopt and implement a corporate governance code for state-owned enterprises to ensure professional, transparent and independent management.*	• A draft asset management strategy has been prepared by the Ministry of Finance in December 2014, entered intergovernmental consultations in January 2015 and is expected to be approved by the Parliament in March 2015. The criteria for measuring the performance of SOEs shall be adopted within 1 month approximately after the endorsement of the strategy. .	• **December 2014**: SSH adopts Asset Management Policy • **December 2014:** A new corporate governance code for State-owned Enterprises is adopted. • **December 2014:** A management contract between the SSH and the Government is signed, determining the payment of management fees to the first.	• **October 2014**: The third company from the list of 15, Aerodrom Ljubljana, is divested. The sale of Telekom Slovenije, the biggest asset on the list, is re-launched and is currently projected to be signed in April 2015. • **October 2014:** SSH acquired all the assets (including shares in different companies) owned by DSU. • **December 2014**: An open public process is launched for compiling a list of candidate members for the new supervisory board of SSH. • **January 2015**: A compliance officer is appointed by SSH and is mandated by law with the preparation of an integrity plan in the next months. • **January 2015**: SSH became the sole owner of PDP.
6	*Finalise a corporate restructuring master plan by the end of 2014 within clear priorities and effective implementation process. Set up a central corporate restructuring task force monitoring and coordinating the overall restructuring process, providing the necessary expertise, guidance and advice, and facilitating the negotiation process between all stakeholders involved. Establish a list of the most urgent restructuring cases, while maximising the recovery value for creditors. Promote the use of the available legal mechanisms and international best practices to all stakeholders in the restructuring process. Evaluate recent changes in the insolvency legislation by September 2014, being ready to introduce any additional necessary measure. Further reduce the length of judicial proceedings at first instance in litigious civil and commercial cases including cases under the insolvency legislation, and the number of pending cases, in particular enforcement and insolvency cases.*		• **December 2014**: The restructuring master plan has been finalised. • **January 2015**: A centralised corporate restructuring task force is established to monitor and coordinate the overall restructuring process, to facilitate the negotiation process between all stakeholders involved and to provide the necessary guidance and advice. The coordinating body of the task force is composed of representatives of the Ministry of Finance, the Bank of Slovenia, the Ministry of Economics, the Ministry of Justice and the BAMC.	• **January 2015**: The authorities presented the advanced version of the on-going evaluation exercise of the laws adopted in 2013 which amended and complemented the insolvency law. The authorities do currently not see a need for further amendments to the insolvency framework. The key finding of the evaluation is that the new framework allows more restructuring opportunities to companies in financial difficulties. • **January 2015**: The authorities presented the 2014 statistics on the functioning of the Court system. Although progress has been made, the length of trials and backlogs remain still significant.
7	*Reduce obstacles to doing business in Slovenia in key areas*	• Strategy for FDI (promotion, marketing, counselling, financial initiatives, and	•	• **January 2015**: 25% of measures in Single document to reduce administrative burden

	for economic development rendering the country more attractive to foreign direct investment particularly through accelerated liberalisation of regulated professions, reduction of administrative burden including leaner authorisation schemes. Ensure sufficient budgetary autonomy for the Competition Protection Agency (CPA) and increase its institutional independence. Streamline priorities and ensure consistency between the 2011 Research and Innovation and the 2013 Industrial Policy Strategies with the upcoming strategies on Smart Specialisation and Transport, ensure their prompt implementation and assessment of effectiveness.	competitiveness analysis) is expected to be adopted in Q1 2015. • Smart Specialization Strategy is expected to be adopted in Q1 2015.		are implemented. • **January 2015**: The number of regulated professions has decreased from 323 to 242. • **January 2015**. The CPA can be considered to be institutionally independent and autonomous.
		• Nothing significant to report on streamlining of priorities and ensuring consistency among the existing strategies and leaner authorisation schemes.		
8	*Take effective measures to fight corruption, enhancing transparency and accountability, and introducing external performance evaluation and quality control procedures.*	• A comprehensive public-sector reform is in public consultation and is expected to be adopted by end of February 2015.	• **January 2015**: The new government reiterated its commitment to fight corruption and adopted a new two-year programme of 11 perennial measures in January 2015.	• **February 2015:** Certain measures of the initial March 2015 programme have been implemented in due time (Act on the State Holding, the amendment of the Banking Act, changes to the law on access to public information enhanced communication between the prosecution and the police).
		• Nothing significant to report on performance evaluation and quality control procedures.		