

Slovenia: serious financial problems present a challenge to the future government

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On 11 November the interest rate of the Slovenian ten years' bonds exceeded 7% which is treated by investors as an alarm bell pointing to the risk of serious problems with servicing the country's debt. On that day the Slovenian parliament, with the votes from the right-wing opposition, rejected the package of austerity laws drafted by the left-wing cabinet of Borut Pahor. The government, serving as a caretaker since it lost a confidence vote in September this year, made another attempt to curb public spending by such measures as extending the freezing of pensions and budget-funded salaries for another year (which will provide savings of EUR 300 million).

The Slovenian economy, badly hit by the financial crisis of 2009, has been struggling with increasingly slower economic growth (1.4% of GDP in 2010, 1% of GDP is forecast for 2011 and 2012) and a soaring public debt which since 2008 has doubled in terms of its ratio to GDP and now stands at 45.5% (the European Commission's prediction for the end of 2011). After the collapse of the Borut Pahor government, caused by a dispute within the coalition over the pension scheme reform, Slovenia is awaiting a snap election on 4 December. The most likely winner of the elections seems to be the Slovenian Democratic Party (SDS) led by the former Prime Minister Janez Jansa. SDS is calling for such measures as tax reduction for companies, cutting of red tape and privatisation as a way of boosting the economy.

Commentary

- The increase in the government bond yields does not entail the risk of bankruptcy. It does, however, send an important warning to Slovenian politicians. According to the declarations of the Slovenian government, the state has sufficient funds for establishing next year's budget and for servicing the debt by 2014. However, two weeks before the parliamentary elections Slovenian politicians are not able to effectively reassure financial markets.
- The increase in the interest rate of the bonds and the lower rating of Slovenia by main rating agencies which preceded it are caused above all by the lack of structural reforms which were hindered by disputes in Borut Pahor's government. Slovenia's export-dependent economy is further compounded by Italy's financial problems (Italy is the second most important recipient of Slovenian exports, after Germany).

- The fact that SDS, the party leading opinion polls, rejected the austerity package calls into question the party's preparedness for introducing socially costly structural reforms (including the pension scheme reform, liberalisation of the labour market) which are demanded by the international financial institutions. The first important challenge for the new government will be to present a reliable plan for a reduction in the public debt, which would enable Slovenia to improve the reputation of its debt securities on the world's markets.