

Slovenia



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Slovenia is among the most successful of the countries that are moving from socialism to a market economy. It boasts stable GDP growth and ranks among the

countries with the lowest degree of risk. The already-completed privatization process, together with many other measures, is increasing Slovenia's competitiveness within the EU.

ECONOMIC OVERVIEW

GDP AND CPI

Key economic indicators	1999	2000	2001	2002	2003
GDP-real growth rate (%)	5.6	3.9	2.7	3.4	2.3
CPI (%)	6.1	8.9	8.4	7.5	5.6

Source: Statistical Office of the Republic of Slovenia

Slovenia is an economically successful and stable country, which has been registering average annual economic growth of 3.6% since 1999. The level of GDP measured by purchasing power (PPS) per capita stands at 74% of the EU average (2003).

UNEMPLOYMENT

	1999	2000	2001	2002	2003
Unemployment rate (%)	7.6	7.0	6.4	6.5	6.7

Source: Statistical Office of the Republic of Slovenia

EU membership means a more secure economic framework, within which Slovenia will be able to continue reducing unemployment (6.7% in 2003) and inflation (5.6% in 2003).



Area ('000 sq km): 20.25
(US 9,600 – EMU 2,500 – World 133,700)

Capital: Ljubljana

Population: 1,964,036
(US 288.4 – EMU 305.5 – World 6,200)

GDP (EUR million): 22.0
(US 10,400 – EMU 6,600 – World 32,300)

GNI per capita (USD): 10,200
(US 35,400 – EMU 20,320 – World 5,120)

Currency: Slovenian Tolar (SIT)

Language: Slovenian

Main religions: Roman Catholics 60%, other religions 30% (Muslims, Lutheran, atheist and other)

Government type: Parliamentary democracy

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ECONOMIC FORECASTS

GDP and CPI

	2004	2005	2006	2007
GDP-real growth rate (%)	4.4	4.6	4.9	5.0
CPI (%)	4.6	4.6	3.6	3.4

Sources: Statistical Office of the Republic of Slovenia, IMAD (Institute of Macroeconomic Analysis and Development)

Unemployment

	2004	2005	2006	2007
Unemployment rate (%)	5.9	5.5	5.1	4.5

Sources: Statistical Office of the Republic of Slovenia, IMAD

Assuming that international economic growth stabilizes, Slovenia's gross domestic product is expected to return to the previous average medium-term rate of 4.4%, after slowing down in 2001 and 2002.

Inflation continued to fluctuate at a relatively high level in 2003. Both the government and the Bank of Slovenia therefore undertook at the end of 2003 to slow the growth in prices to around 4% in 2004.

REGULATORY ENVIRONMENT

FOREIGN DIRECT INVESTMENT

In Slovenia, investment represents around 25% of GDP and was - as a component of domestic demand - an important impetus for economic activity. In the coming years, investment in the modernization of technological equipment in industry and services is expected to prevail. Slovenia is also expected to increase investment in housing, as a result of the expiry of the first National Housing Saving Scheme, and invest more in its motorway system and transport infrastructure.

Foreign direct investment inflows

Year	2000	2001	2002
FDI (EUR million)	149	562	1,950

Source: Bank of Slovenia - Direct investments 1994 - 2002

In 2002, FDI in Slovenia were estimated at EUR 3,918.1 billion.

Foreign direct investment in Slovenia by EU member states from 1998 to 2002

(in EUR million)

Country	1998	1999	2000	2001	2002
Austria	886.2	1,112.3	1,384.1	1,003.1	1,173.0
Germany	314.6	350.1	372.3	430.1	428.3
France	315.7	311.3	320.5	438.1	384.8
Italy	150.5	158.4	193.9	235.4	294.3
Netherlands	75.6	93.3	96.4	133.1	211.1
EU	1,924.5	2,207.9	2,596.7	2,433.1	3,065.8
Total FDI	2,369.5	2,675.0	3,109.8	2,952.4	3,918.1

Source: Bank of Slovenia - Direct investments 1994 - 2002.

Given the inflows and foreign takeovers that occurred in 2003, FDI is likely to continue growing. The Programme of the Government of the Republic of Slovenia for the Promotion of Foreign Direct Investments 2001-2004 and Measures to Reduce Administrative Barriers should also lead to a gradual increase in the FDI.

EU member states are prevalent among the countries investing in Slovenia. Since 1997, their share of FDI has increased, to come in at 78% of the total value of FDI at the end of 2002. Austria, Germany, France and Italy alone represent three quarters of all FDI. An analysis of how FDI breaks down by sector indicates that 372 of FDIs in the processing sector comprised 43% of total FDI value.

According to the Companies Law, all legal entities are open to foreign investment and no performance requirements are imposed as a condition for establishing, maintaining, expanding or investing. Due to recent amendments to this law, companies can not only be fully owned but also fully managed by foreign nationals.

PROPERTY / REAL ESTATE REGULATION

The Act of Accession was voted in on April 16, 2003 to take effect on May 1, 2004. The most extensive part of the Act consists of eighteen annexes in which all the technical adjustments and agreed derogations and transitional periods are cited.

OTHER REGULATIONS

Protection of Competition Act

The first paragraph of Article 13 of the Law on the Protection of Competition prohibits unfair competition. The second paragraph of the same Article sets out that unfair competition is a company's action in the market which is in conflict with good business practice and which causes or may cause damage to other participants in the market. The third paragraph of the same Article lists, in terms of taxation, specific ("standard") instances of unfair competition.

Consumer Protection Act

Amendments to the Consumer Protection Act were adopted in parliament on April 23, 2004, making it mandatory to use Slovenian on product labels and in advertising. The amendments also set forth that Italian

and Hungarian can be used in advertising in areas where the respective minorities live.

Prices to be controlled by the government

A new price control law, which gives the government the authority to control prices and to its own judgment limit the price of any product or service in the country, came into force on Saturday, August 21, 1990. It replaced the 1991 law on prices, which listed the products whose prices were government controlled.

When determining price control measures, government bodies have to take account of the fact that companies should be free to decide prices in accordance with the rules of supply and demand as well as other factors. At the same time the law gives the government the authority to make use of the price control measures for a maximum of one year, albeit with the possibility of extension.

The law determines that the government can decide on price controls when one or more companies set prices too high, or when the price rise is disproportionate to international price movements, the general price index of the line of business or general prices in a given industry.

If the government decides that a company has set prices too high, it can correct it itself. The law also enables the government to set the highest, lowest or fixed price of a product or service.

Tax law

In an international comparison, the Slovenian tax system is characterized by a low rate of statutory corporate tax and an even lower effective income tax rate at the corporate level. Although the tax structure deviates somewhat from the EU average, the tax system of Slovenia is now broadly compatible with the tax systems of the EU Member States with the ratio of total taxes to GDP lower than the EU average. Taxation on investment income compares favorably with countries that operate a classical system of tax on investment income. As tax reform is an ongoing process, further changes are envisaged in 2005 - notably, changes in personal income tax and corporate income tax.

The corporate income tax amounts to 25%. The value

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added tax (VAT) amounts 20% (standard rate) and 8.5% (reduced rate).

Store opening hours

Stores are open on weekdays from 8am to 7pm and on Saturdays from 8am to 1pm. Numerous convenience stores also remain open for business on Sundays and public holidays. There are no special rules regulating store-opening hours in the Slovenia.

Environment

The Environmental Act, which incorporates a range of regulations, licenses and restrictions, lays out Slovenia's strategy for environmental protection. When products are deemed to place less strain on the environment, the environment minister can award them an environmental label.

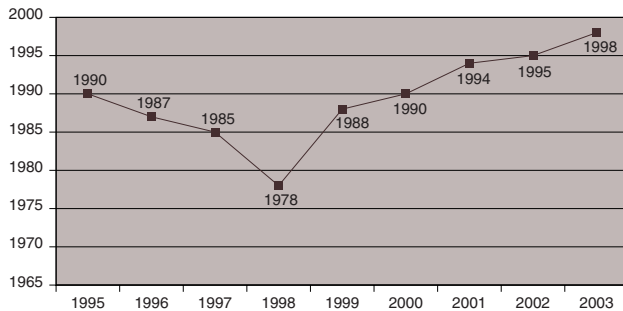
DEMOGRAPHICS AND CONSUMER BEHAVIOR

POPULATION

Population evolution

The total population of Slovenia increased by 0.4% between 1995 and 2003.

Population 1995-2003



Source: Statistical Office of the Republic of Slovenia

Population by age group

0-14 years	15.0%
15-65 years	70.2%
65 and over	14.8%

Source: Statistical Office of the Republic of Slovenia (December 2002)

Urbanization of the population

Approximately 50% is urban and 50% is rural.

INCOME / BUYING POWER

Average net earnings per person stands at approximately SIT150,000 per month. Over the last two years, growth has remained positive in real terms, with net earnings rising 3.2% in 2001 and 2.0% in 2002.

Real wage flexibility is indeed higher under fixed exchange rate regimes as opposed to flexible ones. To the extent that the exchange rate regime choice is exogenous (i.e. given by political factors), it follows that real wage flexibility has a tendency to increase along with the adoption of the fixed exchange rate regime. However, this increase in real wage flexibility is only marginal and, therefore, it is not sufficient to compensate for the loss of an exchange rate adjustment tool in the face of exchange rate pegs. Real wage flexibility itself is not sufficient to be an effective adjustment tool: the elasticity of real wage to

unemployment is only at the level of several percentage points.

Average monthly earnings per person (in SIT)

Year	Gross	Net
1998	158,069	99,919
1999	173,245	109,279
2000	191,669	120,689
2001	214,561	134,856
2002	235,436	147,946

Source: Statistical Office of the Republic of Slovenia

Slovenians spend around 19% of their income on food and beverages. The second biggest expense is transport.

Lifestyles

Around 5% of Slovenia's population is affluent. The emergence of this well-to-do middle class is a positive sign for the entry of up-market products.

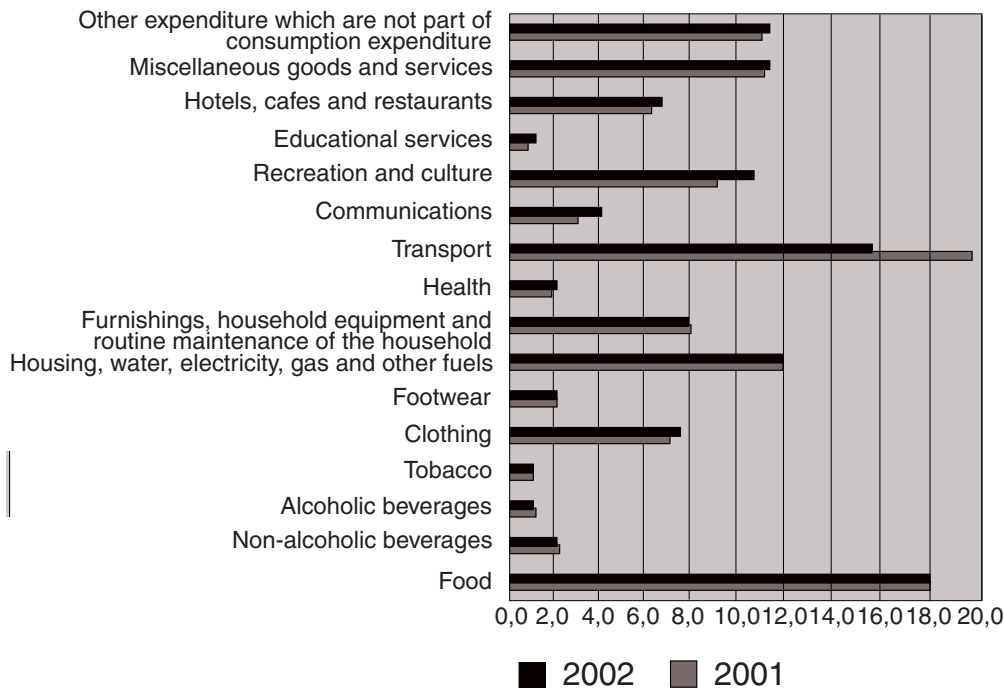
Price sensitivity

Despite its development, the Slovenian market is still extremely price sensitive; other customer satisfaction measures assume much less importance.

CONSUMER BEHAVIOR

Average household spending patterns

Composition of average household consumption (2001- 2002)



Source: Statistical Office of the Republic of Slovenia

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RETAIL & CONSUMER SECTOR PERFORMANCE

MAJOR CONSUMER GOODS PLAYERS

Major food companies

Ranking	Company name	Category of products	2003 Sales (EUR million, excl. VAT)
1	Pivovarna Laško	Beverages	609
2	Kolinska	Food	478
3	Fructal	Beverages	391
4	Radenska	Beverages	304
5	Eta	Food	217

Major non-food consumer goods companies

Goods manufactured by Gorenje (household appliances), Iskratel (telecommunications equipment and systems), Iskraemerc (electricity meters), Rotomatika (special electrical motors and components), as well as many other companies, are marketed under their own trademarks all over the world. Some enterprises in this sector, such as Kolektor (commutators) are particularly renowned for their high quality and low prices.

Of long-standing importance, Slovenian textiles, clothing and leather processing industries are in need of rapid technological development to be able to closely follow world fashion trends. Most of the basic raw materials are imported and 55% of products are exported. At the same time, some companies sell in excess of 90% of their production abroad.

Slovenian products can now be found all over the world under their own trademarks (Mura's Gallus and LeOna fashion collections, together with the trekking and mountaineering footwear produced by Planika and Alpina).

The three largest companies in the electronics and electrical appliance sector are:

- Danfoss Compressors
- ETA Cerkno
- Danfoss Trata

These firms are major exporters of air-conditioning, refrigeration and heating equipment, and represent a potential force for growth in the future.

Slovenia's advanced manufacturing technologies have been in the fast lane for the past few decades. Being both innovative and export-orientated, Slovenia's leading companies have been enjoying earnings growth and have strengthened their workforces at a rate of 4 to 5% per year. Many new alliances with foreign partners and investors have been forged, particularly since 2000, in what is a tangible reflection of internationalization.

MAJOR RETAIL PLAYERS

Retail sales

Number of outlets	1998	1999	2000	2001	2002
Food, beverages and tobacco	4,928	4,538	4,512	4,587	4,604
Non-food products	5,937	5,981	6,959	6,391	5,410

Source: Statistical Office of the Republic of Slovenia

Services account for the biggest slice of Slovenia's economy, representing around 60%, followed by industry with 37% (including construction). Agriculture represents around 3% of GDP but, as in other European countries, it is important politically and in terms of systemic solutions.

Top 3 food retailers

Group name	Store brands	Retail formats	Number of stores (2002)	2002 Sales (EUR million, ex. VAT)
Mercator	Mercator	Hypermarket	18	2,000
		Supermarkets	72	
		Discount stores	3	
		Cash & carry	11	
Engrotuš	Tuš	Hypermarket	3	580
		Supermarkets	27	
		Cash & carry	3	
Spar	Spar	Hypermarket	7	300
		Supermarkets	16	
		Cash & carry	7	

Source: Companies' annual report

Retail channels

The various distribution channels used are evolving, but the main trend is towards larger retail formats and better satisfaction of consumer needs. This trend is producing two important effects: the importance of larger retail formats is growing and power is shifting towards retailers and consumers and away from manufacturers.

Number of shopping centers in 2001	
Hypermarket	11
Large specialized stores	13
Shopping malls	36
Shopping complex	1

Source: Statistical Office of the Republic of Slovenia

Larger retail formats in almost all retail sectors have grouped together producing a concentration of power and capital strength, often foreign. This has led to public and political discontent. One of the main

implications is that fewer new constructions will go ahead, so the number of new greenfield investment options will be reduced. Another aspect is a reduction in the number of jobs in smaller retail formats and the bankruptcy of companies that used to be relatively big players but failed to restructure. Nevertheless, scope will still remain for smaller retail formats, since Slovenia is a small country with only a few cities big enough to support large retail formats such as hypermarkets. Smaller towns and villages are lucrative for smaller, individual shops, but the big players will leave them alone.

Growing prosperity and changes in lifestyle are expected to continue driving development. In short, the retail sector in Slovenia is characterized by fast change within a small, but lucrative market.

E-commerce

As an indication, after the various developments of the last few years, the number of Internet users per 1,000 inhabitants is again close to the EU-15 average. Slovenia is ahead of most EU-25 countries. In terms of Internet hosts per 100 inhabitants, Slovenia stood at about 42% of the average for the EU-15 in 2001.

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RETAIL & CONSUMER CHALLENGES, OPPORTUNITIES AND EMERGING TRENDS

CHALLENGES

Changes after entering the European Union

Among the benefits of EU membership, Slovenia expects increased security and stability, a stronger position in the international community and the chance to take part in decision-making in relation to various European policies and the formulation of Europe's future image. It also hopes to become a part of the institutional structure of one of the key global players.

Moreover, EU membership will also bring many economic benefits to Slovenia: a larger internal market with additional consumers; increased opportunities for exports of investment goods; increased investment opportunities (reduced risks, the opportunity to bring down costs with the aim of increasing competitiveness); pressures for the necessary economic reforms of the Union; better access to equipment, know-how, new technologies; reduced business risks, more favorable access to capital; new employment and education opportunities; the possible penetration of new markets.

EU membership will also mean that Slovenia becomes better known, its culture will be enriched and its national confidence increased. On entering the EU, Slovenia hopes to break through the existing barriers of an inward-looking mindset with a more open-society outlook. The establishment of common European rules is expected to result in increased transparency, stability and predictability of the economy, which is particularly important for the operations of economic subjects.

In addition to the economic, political and security aspects, EU membership will also provide a new multicultural framework for Slovenia. Here it will be able to lean on its historic experience of living in multinational communities, the experience of a short and successful transition and on its knowledge of various cultures, chiefly those of southeastern European countries which are the successors of the former Yugoslavia.

OPPORTUNITIES

Shopping centers in Slovenia

A very salient feature is a tendency to have branches or representatives of large store chains. In addition to stores, shopping centers include numerous catering outlets (restaurants, small cafes, and bistros). Large shopping centers also offer various services, including business centers, postal and banking services. The majority of Slovenian towns benefit from shopping centers; the supply has become comparable to that which is found in the more developed countries. Furthermore, shopping centers have become the new hubs of the community - exceeding mere shopping needs, to cater for numerous leisure time pursuits. The negative impact of shopping centers on trade in downtown areas cannot yet be objectively evaluated, as the real effects are not yet visible.

Slovenia as a location for regional headquarters

- Strong trade and business links with countries in southeastern Europe (Croatia, Bosnia & Herzegovina, Serbia, Macedonia)
- High level managerial skills
- Widespread knowledge of foreign languages
- Strategic position on crossroads of the fifth and the tenth pan-European corridors
- Good international transport and communication links
- Favorable international country rating

Greenfield investment

- Quality of workforce with high level of technical skills
- Favorable value added to labor cost ratio
- Pivotal geographic position
- Developed trade and transportation links with main regional markets
- Long industrial tradition and especially experience in manufacturing middle technology level products
- National treatment principle
- High quality of life

Logistics base

Lying at the heart of Europe, Slovenia is well served in terms of international flights, rail links, and motorway networks. The Adriatic town of Koper is best known for its cargo port that wedges deep into Europe's mainland. Infrastructure in general, and information and communication technology (ICT) in particular, is well developed. Nevertheless, there are continued investments in modernization. Thanks to Slovenia's pivotal position, it has all the attributes of a trade hub and a unique logistics base. Fully serviced industrial sites are widely available at competitive terms and industrial parks are growing close to trunk roads and rail links.

EMERGING TRENDS

Privatization

The plans for privatization in Slovenia were stalled for some time. The original plan was to have made significant privatization progress in the banking and energy sectors before accession to the EU. After the initial rash of privatizations in 2002 (largely in the pharmaceutical and financial sectors), little progress was made until earlier this year, when we have seen increasing merger and acquisition activity.

The long awaited privatization process in the energy, telecoms and insurance sectors is currently coming to fruition and we expect the activity to increase throughout 2004 and 2005. The retail sector is still something of a closed market with the dominant player, the domestic giant, Mercator.

Conditions for foreign direct investment (FDI) have to be improved by speeding up the work of the courts in resolving corporate disputes and by bolstering privatization and adopting a suitable tax policy.

Slovenia also needs a suitable FDI policy to earmark those sectors that would be open to FDI.

As FDI increases the need for international structuring expertise increases. In relation to tax planning this is a relatively new service offering on the Slovenian market. Due to the accession to the EU, Slovenia will adopt a variety of new tax laws. A new corporate tax law will come into effect at the beginning of 2005 and a new VAT law has already been adopted as a result of EU Accession.