

# OUTLOOK 2020



EVALUATION OF ECONOMIC TRENDS AND ECONOMIC POLICY IN SLOVENIA IN THE EUROPEAN CONTEXT  
CONFRONTATION OF GOOD BUSINESS PRACTICES WITH THE CHALLENGES OF SOCIAL DEVELOPMENT AND PROSPERITY



**DUŠAN MRAMOR, JOŽE SAMBT:** DOES THE SLOVENIAN SOCIAL MARKET MODEL HAVE A CHANCE OF SURVIVAL?

**ALEKANDER ZALAZNIK:** OUR AMBITION FOR A MORE COMPETITIVE SLOVENIA

**SAŠA MRAK:** RETHINKING PURPOSE AND GOOD MANAGEMENT PRACTICES

**JURIJ GIACOMELLI:** INSTITUTIONS, CREATIVITY AND SOCIAL CONSCIOUSNESS

**ALI ŽERDIN:** "SINCE YOU'VE GOT MORE, I'VE GOT LESS"

**VIOLETA BULC:** AN INVITATION TO THE EUROPEAN GREEN DEAL

## **COMPETITIVENESS, PRIVATE PROPERTY AND FREEDOM TO CONDUCT A BUSINESS**

**VERICA TRSTENJAK:** THE RULE OF LAW AND PRIVATE PROPERTY – WHAT DO THEY MEAN FOR THE ECONOMY?

**VOJKO ČOK:** ETHICS, PROPERTY AND FREEDOM TO CONDUCT A BUSINESS – THREE PREREQUISITES

**SERGEJ SIMONITI:** THE ECONOMIC ASPECTS OF THE ABSENCE OF THE RULE OF LAW

**IRENA PRIJOVIĆ:** SILENCE IS NOT ABOUT NEUTRALITY, BUT SUPPORT FOR THE CURRENT STATE OF AFFAIRS

**ANDRIJANA BERGANT:** INTEGRITY AND LEADERSHIP

**VELIMIR BOLE:** THE ECONOMY IN THE YEAR 2020 – RESILIENCE IN TIMES OF UNCERTAINTY



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# Impressum

**Outlook** is a project of the Managers' Association, which is the publisher of this annual professional publication.

## **Basic purposes of the project and publication:**

To educate managers and decision-makers; to raise awareness of everything concerning economic policy and the development challenges faced by Slovenia in the EU context; and to promote an active dialogue with experts, social partners and media concerning development issues in Slovenia and the EU in the broader international context.

Good economic results combined with favourable conditions for further development are considered part of the competitiveness of a country. In this sense, Outlook aims to contribute to raising awareness of the state's intelligent governance, one that, with as much transparency as possible, instils confidence in the participants in the positive spiral of social relationships, and which, with the strengthening of the common vision of citizens, can stand the test of time.

Outlook is published in collaboration with the Observatory ZM for competitiveness and increasing social wellbeing.

Once a year, it is published as a stand-alone publication, aimed at evaluating the economic trends and economic policies of Slovenia in the European context, and confronting good managerial practices with the challenges of social development and ensuring prosperity.

Outlook is published annually in Slovenian and English. Outlook is published quarterly in the pages of the daily newspaper Delo.

The editor-in-chief of Outlook is Jurij Giacomelli.

The **ZM Observatory** is an expert group operating within the Managers' Association. It consists of the Managers' Association leadership and selected experts in the field of economics and other sciences and professions. Observatory ZM acts as the Editorial Board of the publication.

The founding members of the Observatory were Professor Dušan Mramor (Chairman); Aleksander Zalaznik (President of the Managers' Association); Saša Mrak, MBA (Executive Director of the Managers' Association) as the Association's leadership; Jurij Giacomelli MSc (Editor-In-Chief of Outlook); Professor Vera Trstenjak; Dr Ali Žerdin; Veljko Bole MSc; Gabrijel Škof (President of the Management Board of the AS Group, the main partner of the publication, until the end of September 2019); and Sergej Simoniti (President of the Management Board of Coface – Prva kreditna Zavarovalnica).

## **All the members of the ZM Observatory are also the authors of Outlook 2020.**

In this issue, they are also joined by: Andrijana Bergant, Director of EISEP; Violeta Bulc, Slovenian Commissioner of the European Commission (2015-2019); Vojko Čok, President of the ZM Honorary Tribunal; Irena Prijović, Executive Director of the Slovenian Directors' Association; and Professor Jože Sambt, University of Ljubljana, Faculty of Economics.

The broader discussion within the Observatory includes representatives of the Management Board, the Supervisory Board and the Honorary Tribunal of the Managers' Association.



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# Our ambition for a more competitive Slovenia

**Aleksander Zalaznik**

President of the Managers' Association of Slovenia



The Managers' Association can be completely satisfied. The profitability of the companies we highlighted years ago has improved dramatically.

Export volumes have been increasing for some time. On average, the value added per employee has increased. Employment is at a record high, as are wages. Innovation is gaining value, the development performance of small and medium-sized enterprises is improving, and competitiveness is increasing.

And yet, it is not enough. This is why we established the ZM Observatory within the Managers' Association, inviting some broad-minded individuals to shine a spotlight on the state, and the developmental challenges faced by Slovenia, in the Outlook quarterly edition, the annual publication, and at events, together with the board of the Managers' Association. These valuable insights stimulate and encourage us to think about how to proceed, what measures we need and

how to achieve them, and above all, whether we can unite in our decisions in a way that promotes prosperity for every citizen.

In my view, we still need a new, comprehensive, and development-oriented social agreement in order to achieve a general rise in prosperity. A recent example of this was a measure taken by the Bank of Slovenia. We have heard a great deal of controversy, including outrage, concerning the stricter criteria for determining an individual's creditworthiness, which has primarily been directed against the Bank of Slovenia. However, I have not found any comments saying that the Bank of Slovenia is not to "blame" for the reduced creditworthiness of Slovenians. The blame should be, above all, attached to the low Slovenian net salaries; these are the result of our added value, (too low) productivity, and one of the highest payroll taxes in the EU.

That's why there is still a lot of room for improvement. For the benefit of us all.

**For this reason, at the January meeting, we called for a social agreement to be made for higher salaries for all employees in Slovenia and thus for an increase in prosperity.** This must be carried out by management, as well as by the state. In doing so, we have made it clear that the condition for increasing wages is the steadily increasing productivity of companies, which results in higher added value per employee. It requires even better quality work from managers and employees, as well as continuous improvement in the competitiveness of the business environment. This in turn requires the participation of all the most responsible people in companies, institutions, and the country. Without a development-friendly and business-friendly environment, and at the same time a managerial commitment that productivity and innovation are the factors that deliver higher added value, it will be difficult to change the culture and mindset of "it's good enough". So far, we prefer to replace a culture of change and efficiency with more work.

The same applies to the economic environment, where the propensity towards over-regulation often prevails over the search for solutions to improve work processes

in organisations, thereby contributing to higher productivity and added value. Above all, it prevails over open-mindedness and confidence in institutions.

In recent years, we have dramatically increased exports, which was mainly achieved by a well-developed components industry. Some companies have gone a long way in this, becoming world leaders. I believe that there will come a time when the best companies and their innovative professionals will upgrade their knowledge and competence in components development and production by producing finished products with their own brands, with even greater added value.

In order to encourage continual change and development, my entire term as President of the Managers' Association has been imbued with ambition. I set the bar high and used it to encourage us all to achieve better results. I do not want us to settle for average in Slovenia. This is why we need LEADERS in all areas who will show the others the way out of the mediocre.

In this regard, we often come across what is, in my opinion, one of the greatest inhibitors of Slovenian development: egalitarianism, which is deeply embedded in us. Slovenia will progress faster when we are able to accept and allow success to be valued and rewarded. Therefore, we should create an environment conducive to achievement and support everyone who develops and achieves their ambitions. Among us are successful individuals, professionals, directors, and physicians who contribute to the development of companies, institutions and society itself. The speed of development of Slovenia and, in the end, the salaries of all employees, depend on them. They should be regarded by everyone as positive role models and motivators for development.

Although we have been able to "catch a good wave" over the last few years, in part due to global economic growth, that does not mean we cannot catch a better one; hence Outlook and its related events. We must take a hard look in the mirror more often and look to the future – and we should remind ourselves that ambition is important. We just need to focus it on our developmental and leadership sagacity, for the benefit of all citizens.

# Rethinking the business purpose and good management practices

For 30 years, the Managers' Association has shared, sought and offered good corporate development and management practices. Current membership is at an all-time high (1,200), representing over 900 companies and over a third of the Slovenian economy's revenue, intensively exchanging good practices, learning from the best, and striving to make the Slovenian business environment as stimulating, open, and connected to the world as possible.

Moreover, there have never been so many other economic associations, chambers, professional and research institutes, educational institutions, and media sources in Slovenia, all of which enrich our business environment through their missions. The Managers' Association constructively cooperates and joins forces with many of them.

From this position, our Association is leading the way towards enlightened action that will make our business environment more competitive, more productive and more successful, so that we achieve success ethically and know how to share it in a way that rewards and motivates all participants. The

Association represents the voices of those who are co-creating today's environment, and good examples attract followers.

**Who are these individuals and organisations that help us see further and dare more?** Among them we not only include individuals, our members, holders of outstanding economic achievements, and award winners, but also employees, customers, suppliers, and partners. A professional organisation can represent the managerial profession in an enlightened manner only when it respects all stakeholders. It is, indeed, all about them.

**Who are the award-winning managers and the companies in which the desire for development is ongoing?<sup>1</sup>**

**Bogomir Strašek**, director and majority owner of **KLS Ljubno**, has been associated with the company for 47 years. He has led the company, which specialises in the production of gear rings for the automotive industry, to global excellence, so that KLS now holds a 15% market share globally and a 50% market share in Europe. As many as 97% of the company's manufacturing processes are automated and robotic, while the number of employees is increasing. Productivity has increased tenfold since 2000, achieving extraordinary profitability, and the value added per employee was 115,000 euro at the time of winning the award.

<sup>1</sup> All of the examples described here have been selected from the line of winners of the Lifetime Achievement Award in Management, the Manager of the Year Award, or the Young Manager of the Year Award, presented by the Managers' Association of Slovenia.

**Domel is the story of Železniki,**

which is known by almost everyone.

**Jožica Rejec** has been associated with Domel for over 39 years; the leader of a successful company that is 100% owned by employees and former employees, she recently passed on her leadership to a successor after a long career. During the period of her leadership, the company developed into a successful and globally competitive enterprise, and she has gained considerable respect among her colleagues and partners through her authentic leadership style and a highly developed sense of the common good.

The dynamics of their growth result from the successful restructuring of the company. Half of their sales in the time before the restructuring consisted of suction units, which attained a 15% global market share and even a 60% market share in Europe. They transformed by continually investing 4.5% of their sales in research and development. The number of skilled jobs under Jožica Rejec's leadership increased by 100%, and the number of employees by 25%. In January 2018, when the company won the award, it employed 1,175 people. Due to the automation of routine jobs, productivity grew from 1% to 5% per annum during the leadership of Jožica Rejec, and value added per employee also increased annually.

One brand to which virtually every Slovenian is attached is **Medex**. The winner of the 2016 Lifetime Achievement Award, **Aleš Mižigoj**, has been inextricably linked to Medex for 55 years. At the time of his award he was, at the age of 88, also the oldest employed worker in Slovenia.

He ran Medex for 40 years. The company suffered a painful blow when the former common state collapsed, losing 70% of its market. The company was saved by a change of strategy, and further improvement was ensured through the systematic development of succession.



Saša Mrak

**Executive Director of the  
Managers' Association of Slovenia**

We also remember the story of **Cvetana Rijavec**, a chemical engineer and culture lover. At the age of 39 she took over the management of **Fructal Ajdovščina**. As President of the Management Board, she faced one of the most difficult tasks; ensuring the company's very existence. During the period in which Slovenia gained independence, Fructal lost most of its purchasing and selling markets and a large part of its production capacity. After a successful recovery, Fructal became the largest Slovenian fruit processor, with a presence in more than 18 world markets. In 1998 the Managers' Association recognised Fructal as a women-friendly company, and its "first lady" was nominated for the Slovenian Woman of the Year. Two years later, when the company generated 60 million euro in turnover and 2.3 million euro in profits, the municipality of Ajdovščina presented Fructal with the Fifth of May Award for its economic achievements.

Her last major career challenge was **Ljubljanske mlekarne**, which was deep in the red. By transforming the brands, rationalising the business and doubling its exports, she succeeded in turning an almost 13 million euro debt into a profit in just two years. The Manager Magazine thus honoured her with the Managerial Challenge in Crisis Management Award. In her eight years of successful presidency, Cvetana Rijavec succeeded in positioning Alpine milk as one of the most trusted Slovenian brands.

### Ambitions in new generations

Since **Tomaž Berločnik** took over the management of **Petrol Group** in 2011, he, together with his team, has managed to transform it into the current largest company in Slovenia. They had a vision; Petrol Group is no longer just an oil trader, but a company of the future, setting new trends and business models in energy and trade while developing smart energy and mobility solutions. 2018 was the best fiscal year in Petrol's history. The company had 5.4 billion euro in net sales revenue, up 92% from 2010. The value added per employee is 63,800 euro. Petrol Group had 4,857 employees at the end of last year, while its employees (based on data for Slovenia) had an average of 26% higher gross earnings than the Slovenian average.

In 2017, **BSH Nazarje**, a company of the Bosch Group, under the leadership of **Boštjan Gorjup**, reached a record production rate of 8.1 million units, exporting over 97% of its output to other European countries. Within one of the largest industries, Gorjup and his team were able to increase total revenue per employee by 80% and achieve a value-added increase of 45% per employee with 62,806,000 euro. BSH Nazarje was the largest employer in the Upper Savinja Valley in the past, and in 2017 the number of employees increased by 10%.

It has only been a year since the entrepreneur and manager of the **Riko Group**, **Janez Škrabec**, received his award. Many of his company's successes are also the result of its trustworthiness and visibility, which Škrabec develops through

investments in local tradition and society. On the one hand, in 2016, 108 employees generated 117 million euro in net sales revenue and 7 million euro in net profit, with a value added per employee of 144,000 euro, among the highest in Slovenia. On the other hand, the company manages the development of the Škrabec Homestead in Hrovača, which, with its diverse cultural and artistic programme, was transformed into a local cultural incubator and nominated for the European Museum title in 2004. The company supports artistic creativity by maintaining a fine collection of contemporary Slovenian art that holds more than 300 works, and sponsoring a Slavistic Scholarship Fund within the framework of the Friar Stanislav Škrabec Foundation. The company also supports the activities of the most important cultural institutions in Slovenia, acts as a sponsor for athletes and sports clubs (with the support of the Ribnica handball club, as many as 250 children can advance in their handball skills) and supports numerous projects with humanitarian content.

### When the youngest become the leading global providers

Did you ever imagine that in Slovenia we would have a company that would become the leading global provider in the supply of hardware and software solutions for the control of nuclear accelerators and other large-scale physical experiments? A company that would have the ambition to become an indispensable supplier of proton therapy control systems for cancer treatment? We indeed have such a company, and its co-owner and procurator is this year's Young Manager, **Igor Verstovšek**. It is clear we can learn plenty from the younger generation. **Cosylab's** current main markets are the EU and the USA, with subsidiaries in the US, Switzerland, China, Sweden, and Japan. Value added per employee in 2017 was approximately 101,000 euro, which is almost 100% higher than the industry average, and Verstovšek is proud that they have managed to create a flat and relaxed organisational structure in the company and receive the Golden

Thread Award for the best employer in the category of medium and large size companies in 2015.

He personally strives to set an example for young people; that it is possible for them to remain playful and create an interesting career path with their passion for natural sciences, good ideas, and the right approach.

We are in dire need of all that in our environment.

### On agreements, arrangements, and leaps

With the first edition of Outlook a year ago, we opened a discussion on how, in a time of increasing global uncertainty and a slowdown in the European economy, we can take a firm position as a society early enough to enable us to cope with the challenges of the future and make a leap forward. We need a prosperous economy for greater prosperity, and therefore we need more companies like Cosylab, Domel, Medex, Petrol, Riko, and the others.

Some people call this development leap prosperity, others increased competitiveness, while employees see it as higher net wages. It can be seen as a long-lived company or just good fortune, such as in Bhutan, a country where they measure prosperity with a Gross National Happiness index every year. At the January meeting of the Association, we called it a social consensus. In subsequent months this was outlined through the eyes of experts, and a proposal for a new social agreement was made by the president of the ZM Observatory, Professor Dušan Mramor. However, we cannot reveal any successful accomplishments in this direction yet.

I recently had the opportunity to observe the 30th anniversary of the IMD World Competitiveness Centre, one of the most recognised business schools in the world. The first and largest debate sought an answer as to how countries were able to make the "leap": Colombia, Estonia, Latvia, the United Arab Emirates, and Singapore, among others. Was it magic

numbers and complex formulas? The answer is yes and no. They did it when they united in one of two situations. The first is one in which all stakeholders want greater prosperity and competitiveness, from the country's first person down. In the United Arab Emirates, boosting competitiveness has been on the Prime Minister's agenda for around ten years, and they have a special functioning organisation especially for this. The second occurs when the systems of countries are severely shaken and demolished to an extent that could only lead to a complete collapse, similar to the case of poverty-stricken Colombia. In 2002, almost 50% of the population was at or below the poverty threshold. That is when you have to do something if you care about your country. Their first goal was to reduce poverty, and the second to connect, digitise or technologically equip and support domestic start-ups. They made the leap. In the case of Lithuania, Dainius Kreivys, Minister of Economy in the years from 2008 to 2011, said: "The political agreement deficit is more devastating than the fiscal deficit". In 2008, Lithuania's GDP fell by almost 15%; today, it is one of the fastest growing countries in the EU. It is only three places behind Slovenia on the IMD World Competitiveness Scale.

Countries and their systems cannot be compared in all spheres, but we can learn good practices from one another, or at least learn about mistakes we do not want to make. And Slovenia? Some of the findings in Outlook 2020 are not encouraging. The President of the Observatory of the Managers' Association, Professor Dušan Mramor, points to the imminent danger of a black scenario of increasing the risk of poverty and social instability. According to him, the social market model of social arrangement in Slovenia is not yet sustainable, and this year we have made the situation even more dangerous by decisions that are primarily in the hands of politicians.

There are many arrangements. Which one will we be able to achieve in Slovenia for a long-lived society and greater prosperity and happiness? In other words, which of the two situations that led to consensus in the aforementioned countries will we choose?

# Institutions, creativity and social consciousness to foster development

## Jurij Giacomelli

### Editor-In-Chief, Outlook

Founder and managing director of Giacomelli media (Gm), an investment manager of the fund META Ingenium, a member of the Honorary Tribunal of the Managers' Association, and the President of the Italian-Slovenian Forum; he served as a CEO in several media and publishing companies, as well as in industrial and product design, and occupied senior positions in insurance and banking. He holds a Master's degree in Business Administration.

PHOTO: Andraž Kobe



What affects the competitiveness of a country? Why are certain countries able to significantly enhance their competitiveness, fending off stagnation or even poverty and social disintegration, in a relatively short period?

Beyond the short-term recommendations for improvements in the business environment suggested by the competitiveness rankings by distinguished think tanks, the answer lies in the following triangle: institutions, conditions for creativity, and the choice of the right direction. These seem to be bound by an invisible “institution”, a convention called a “development agreement” by Outlook. It may be used to cleverly move a country to a higher level of social consciousness and materialise the chosen path of development to preserve and strengthen social well-being. It is inevitably a generational challenge, which Slovenia has not yet accepted wholeheartedly.

Competition between companies, in both economic theory and business practice, is an unambiguous category, and a demonstration of a functioning market mechanism. The more competitive players in the market are more successful and create more value in exchange with buyers and other stakeholders. The market works as long as players compete. If they cannot be compared, or certain players are excluded from the market, the market mechanism does not work. But what about countries?

### The competitiveness of a country and the well-being of its people

The competitiveness of countries is their universal ability, in the investment destinations race, to convert natural, human and financial capital into social capital or well-being more or less efficiently. Well-being is their “market product”. It is the ability to create a business and broader social environment comprised of a string of institutions, policies and factors that determines a country’s productivity level, which in turn determines its level of well-being.

The competitiveness of countries is addressed by the World Competitiveness Centre of the Institute for Management Development in Lausanne, the World Economic Forum (WEF) in Davos, the World Bank, and other research and intellectual centres worldwide. Each of them follows an extensive set of largely overlapping criteria. They agree that more competitive countries produce goods more rapidly and efficiently, and also allocate them more successfully than others, opening up opportunities to preserve and increase the well-being of their residents. The fact that progress in competitiveness and well-being in one country does not mean a direct decline in competition and well-being in other countries is even more of a truism than it is in business competition. It is an endless “regatta” in the blue ocean in which we may all sail onwards.

Slovenia’s competitiveness is rated in both the IMD and the WEF rankings. Setting aside the small size of the market, which is an objective restriction, Slovenia’s weakness lies in the operation of its institutions. Low administrative efficiency, the functioning of the rule of law, a weak financial system, an insufficiently flexible labour market, the taxation of labour, and the fragile healthcare system may all be deemed the result of the operation of institutions that are too weak to allow us to rank higher. Not even above-average



PHOTO: Andraž Kobe

Social partners at the roundtable at the Managers Association Congress in Portorož, on 26th September, 2019 (from the right): Zdravko Počivalšek, Minister for Economic Development and Technology, Ksenja Klampfer, Minister for Labour, Family and Social Affairs, Boštjan Gorjup, President of the Chamber of Commerce and Industry of Slovenia, Lidija Jerkič, President of the Association of Free Trade Unions of Slovenia, and the host, ZM President, Alexander Zalaznik.

results in primary and secondary education can change this conclusion. Another systemic deficiency is the poor connection of our decision-makers to their counterparts around the world, which is stressed in the IMD report.

No competitiveness ranking or report based on it shows the path of development a country

**Table 1: IMD World Competitiveness Ranking 2019, in the annual report of the World Competitiveness Centre**

	Country	2018	Difference
1	Singapore	3	2
2	Hong Kong	2	-
3	USA	1	-2
4	Switzerland	5	1
5	UAE	7	2
6	Netherlands	4	-2
7	Ireland	12	5
8	Denmark	6	-2
9	Sweden	9	-
10	Qatar	14	4
11	Norway	8	-3
12	Luxembourg	11	-1
13	Canada	10	-3
14	China	13	-1
15	Finland	16	1
16	Thailand	17	1
17	Germany	15	-2
18	Australia	19	1
19	Austria	18	-1
20	Iceland	24	4
.....			
37	Slovenia	37	-

#### Note

The IMD ranking is based on 338 criteria and focuses primarily on reliable statistical data of international, national and regional organisations; a survey in the business community constitutes 34% of the data. In the WEF ranking, Slovenia is placed 35th of 140 countries. The WEF research includes 120 criteria, and data from a survey is prevalent (70%). The focus on various types of data is determined by the number of countries included in each research study; the WEF ranking comprises 140 economies, while the IMD ranking only includes 60 countries. The difference results from the availability of "hard" data, as it is almost impossible to gather such information for numerous economies. The criteria constantly undergo professional assessment, and those who compile these rankings continually verify and supplement them if necessary. It also seems that the greater weight on surveys in the WEF ranking prioritises larger countries and western countries in general. In recent years, the criteria which show the innovation ability of societies and the level of their sustainable development have become more important in both rankings.

**Report on Slovenia according to the IMD:** <https://www.imd.org/wcc/world-competitiveness-centrehttp://reports.weforum.org/global-competitiveness-report-2018/country-economy-profiles/#economy=SVNr-rankings/countries-profiles/>.

**Slovenia's ranking according to the WEF:** <http://reports.weforum.org/global-competitiveness-report-2018/country-economy-profiles/#economy=SVN>.

should move along to boost its competitiveness and social well-being. On the basis of the most reasonable comparisons with countries ranked higher than Slovenia, we may find that an increase in competitiveness is the result of long-term social processes leading to concurrent improvements in several areas. It is a generational challenge which needs to comprise international positioning, the adjustment of institutions, and constant checks and adjustments on the chosen path of development.

It should be pointed out that the competitiveness of a certain business environment (a society or country) is related to **the productivity of all factors**, not only labour. In our civilised era, in which we face absolute global scarcity of resources, resource productivity has been gaining significant momentum. It is a complex and two-way interaction, even at first glance. Nevertheless, higher productivity is largely the result of greater competitiveness. The latter depends, first and foremost, on the chosen path of development, strategy, and the collective ability to achieve it.

Perhaps it may seem that the highest positions in the competitiveness rankings are always reserved for the same winners: Singapore, Hong Kong, the USA and Switzerland, among others. But of the European countries, **Ireland** has made the most progress in the IMD ranking, climbing to seventh place, trailing **the Netherlands** and followed by **Sweden** and **Denmark**. During its economic expansion, it has thrived in investment initiatives, the efficiency of public procurement and the management of the country's talents, image and brand; all this despite the fact that it is among the "peripheral" EU and eurozone member states, with typically greater variability in economic activity, and no benefits from the introduction of the euro, as prescribed by the Centre for European Policy in Freiburg, and by Germany in particular.

Ireland is undoubtedly an example of competitiveness, which is the result of policies based on long-term development commitments, its position in, and outside of, the EU, and on the ability to adjust to crisis situations rapidly and decisively. This means that progress depends on the ambitions of a broad coalition

of social groups. It is a question of the creation of a social system focused on future generations. Ireland was able to position itself between good and bad external and internal circumstances, to its development-related advantage.

In this year's IMD ranking, Slovenia ranks 37<sup>th</sup>, the same as last year.

### Context: opportunities and restrictions of the economic policy in the EU

The year 2020 marks the beginning of the term of office of the new European Commission. It is clear from its structure and priorities that most attention and existing resources will be aimed at the European Green Deal and the further promotion of innovation abilities, digitalisation and more efficient infrastructural connections in the European Union, where the safeguarding of the single internal market and competition has become an increasingly important geopolitical leverage. Modernised solidarity mechanisms that should foster greater macroeconomic stability, i.e. the European Stability Mechanism (ESM) and the European Banking Union (EBU), both "products" of the economic crisis faced by the second Barroso Commission and the Juncker Commission and the result of the Juncker Commission's work, constitute a new grip, within which lies the power to override the apparently too tight and, from the aspect of convergence in the development of EU Member States, unsuitable Maastricht criteria. This was analysed by Professor Dušan Mramor, President of the Observatory of the Managers' Association, in his feature in the second quarterly issue of Outlook. In this area, which is closely connected to its relationships, the European Commission will particularly need to seek solutions with the three global superpowers – the USA, China and Russia – for a more harmonised fiscal policy in the Union, which will merely mitigate the current considerations of the European Central Bank. The ECB needs to keep insisting on quantitative easing to compensate for the lack of a traditional fiscal instrument in at the level of the 19 countries in the eurozone, and indirectly, at the level of whole European alliance.

Resource-depleted Europe, home to the highest criteria of respect of humanity and human rights, is up against the gruelling test of achieving a global balance. The EU is a preselected leader in the global process of decoupling the economic growth and the overall improvement of human well-being from resource use, and in the transition to a more sustainable society overall. In this challenge the EU needs more than one ally.

The EU must thoroughly consider **how to upgrade the criteria for conducting economic policy** for them to grant greater autonomy to individual member states and improve convergence. For the time being, the divide in well-being between the core and the other EU member states is increasing, reducing opportunities for its greater unity, which is supported by the results of the IMD and WEF rankings.

**The challenge of sustainable development** has undoubtedly become an inherent civilisation issue of our time. It dictates a shift to a new mental paradigm to redistribute the burdens between the most crucial sources of risks and crisis areas, and lead the way to the revaluation of global trade. For this reason, resource-depleted Europe, home to the highest criteria respect for humanity and human rights, is up against the gruelling test of achieving a global balance. The EU is a preselected leader in the global process of decoupling economic growth and the increase well-being from resource use, and in the transition to a sustainable society overall. To this end, the EU needs more than one ally, and internal unity in particular.

Is the temptation towards a more active EU defence strategy an indispensable element or a sidestep? Is a powerful "European army" an essential precondition for the EU to be more unified and extend its influence worldwide? Slovenian Commissioner (2014-2019) Violeta Bulc provides her outlook on the future of the EU in this issue, as the end of her term of office approaches.



## Respect for institutions and conditions for creativity

In this issue of Outlook, a lack of common ambition is frequently attributed to Slovenia. We can read the findings of Professor Mramor and his colleague from the School of Economics and Business of the University of Ljubljana, Professor **Jože Sambt**, supported by the forecast of economic trends made by **Veljko Bole**. Slovenia may be experiencing economic stability, a relatively high employment rate, and better resilience than before the crisis for it to preserve growth in economic activity and productivity in the years to come, when the EU is expecting an economic slowdown; however, the country is not ready to face the tightening conditions to preserve its well-being imposed by demographic trends and the global transition to technological sustainability, constricted by internal deficiencies: immutability, resistance to change, refusing competences, lack of self-criticism, and an unplanned approach to problem-solving, which frequently results from avoiding responsibility.

Let me give you some examples. The last prime minister to openly speak of reforms was Borut Pahor (2008-2011), and the last major reform in Slovenia was a pension reform which entered into force in 2011 and “legitimised” the Democratic Party of Pensioners of Slovenia (DeSUS). Since then, we have had quite a few intervention acts and minor amendments to the pension system – which was largely inherited from “former times”. On the other hand, healthcare is being constantly reformed by unplanned administrative measures, while we reject wider systemic solutions which would include the insurance sector and provide new competence. The banking system has been “changed” under outside pressure and the threat of a collapse, but instead of digging deeper into the financial system and launching initiatives for the development of the capital market, particularly of medium-sized companies, we keep seeking “culprits” among those who worked on solutions and not for the triggering of the crisis that impoverished the country for at least ten years of progress; a crisis experienced at the same

time by comparable EU member states such as the Baltic countries or the Czech Republic and Slovakia.

Other examples include excesses in management and corporate governance in companies from before the crisis, which finally accumulated in non-performing loans in bank balance sheets and were back in the form of “invasions” in Petrol or Telekom. The post office, an entity which guarantees the interconnection of information systems in any country, is a saviour of other companies of national importance (Mladinska knjiga, Intereuropa) on the one hand, while on the other, the implementation of its public function is under pressure to produce short-term profitability and dividends. After a decade spent building motorways, the country faces a general traffic jam, a dysfunctional railway infrastructure and, in the wake of the final bankruptcy of Adria Airways, limited air transport connections with the world; not to mention the absence of any sensible regulation of information-providing media during the digital transition. It is only in ecological disasters (Kemis) and civil initiatives (in the case of Lafarge or Termit) that systemic deficiencies are unveiled. The list goes on and on, but let us just add that, typically, each such “problem” sooner or later turns into an emergency task of the ruling government, which eventually takes on the duty to assume responsibility for it, often when it is too late.

In this issue of Outlook, we attempt to place the issue of institutions into a broader context, beyond “institutions”, and discuss it from the aspect of the functioning of the rule of law, respect for private property and free entrepreneurial initiative. Professor Verica Trstenjak and other authors (Irena Prijovič, Vojko Čok, Sergej Simoniti and Andrijana Bergant) shed light on the reasons for systemic deficiencies and the preconditions required for the efficient management of the country. As well as seeking reasons and emphasising systemic deficiencies which could be eliminated by introducing best practices from other EU member states, they point out and explain the lack of awareness of, and “desire” for, the rule of law within ourselves. The critical reflection is supplemented by a feature by Dr Ali Žerdin on the perception of limited goods.



## Creativity, meritocracy and the perception of limited goods

In an atmosphere awash with focus on the zero-sum game, knowledge is a mental barrier, creativity is a waste of time, and the transparency and regulations of the rule of law sooner or later become a burden. Newcomers are suspicious, as are people who have left and want to return. Infinite solidarity seems to be commanded for people who gain from knowledge and work. Others gain in other ways. How can a dialogue about development be held in such an atmosphere? This could be an effective way to introduce Žerdin's discourse.

**The issues of meritocracy and the rule of law are pointed out as fundamental preconditions for a dialogue on development that should result in a development agreement; target institutions and fundamental centripetal forces of social cohesion.** Best practices of Slovenian management are the main consideration of the Managers' Association, the publisher of this publication, and are therefore placed as the main contrast to the undesirable phenomena described above. These practices are distinguished by the progressive leadership of award-winning individuals and teams, their strategic mindset, and the knowledge and skills to create new value and a positive deviation from the average through an open dialogue and in transparent organisational structures, which are branded as the fragmentation of "feuds" between small social "annuitants" who perceive limited goods as absolute, and the complete management of a country is equated with division, not creation.

For this reason, we wonder: do these individuals receive enough attention and understanding from the public, and the support of institutions and, most importantly, followers? Best management practices are introduced by Saša Mrak, Executive Director of the Managers' Association.

## Ambition and choice of direction

Ambition is the motto of enlightened management, which called for a motivational agreement for better salaries and reduced workload at the beginning of the year. The ambition to do away with backwardness stems from the enlightened awareness of everyone who has spoken in favour of a development agreement, which could put an end to the universal weakness of Slovenian development orientation, as reflected in a short-term focus on the (re)allocation of resources. In a situation in which every country may get lost in populisms, and the transition from convergence to divergence before the next generation arrives is due to a lack of ambition and awareness, ambition is a must. This was addressed by Aleksander Zalaznik, President of the Managers' Association and editorialist of Outlook 2020, at the beginning of 2019.

Support for a development agreement from the leaders of partners in industrial relations and other representatives of stakeholders, included in a dialogue with us within the Managers' Association and the expanded Observatory of the Managers' Association, shows that awareness has matured. But how to achieve it and promote it in social institutions? A development agreement is precisely what this Outlook is dedicated to. It is perceived as an unwritten convention, and particularly as the master institution of a society with an inherent ambition to make the world a better place for current and future generations.

Where we wish to go is important. The Chamber of Commerce and Industry and the Government of the Republic of Slovenia have made it their mission for the Slovenian economy to halve the backlog in added value per employee in comparison with Austria by 2025. Slovenia has several ambitious goals, but they are not discussed enough. The Slovenian Development Strategy 2030 was devised according to the bottom-up approach and sustainable development principles, and defines measurable objectives and their pursuit. It is the basis for the Smart Specialisation Strategy, which is the fundamental document for the allocation of measures and initiatives for innovations focused on development objectives. Following its adoption by

the government of Miro Cerar, no significant public discussion on its implementation has taken place. How to sensibly update and amend it has been debated even less. Let us remind ourselves that its adoption was accompanied by uncalled-for criticism and even ridicule. Does it even have an administrator? Or better still: whoever has the courage to be its administrator should come forward!

## Path to a development agreement

In 2019, Outlook expressed the need for a development agreement and promoted dialogue between social partners and other stakeholders, highlighting five aspects, most of which comply with the recommendations and warnings in Mramor and Sambt's feature article. Firstly (1), we need to maintain and increase the employment rate despite the ageing population; and (2) we need to radically boost investment in education and science. We should follow the example of Ireland, Estonia or Finland, nations that have managed to pull off a generational breakthrough and achieve competitive positioning through investment in the knowledge of their people and newcomers. Good schools, institutes and development centres foster investment in innovation and start-ups, which is a lever for redirecting the talent drain to a developmental influx. We should add that education is a critical area in Slovenia, particularly due to the lack of lifelong learning, which is the only thing that supports the desires of workers for flexibility.

Sustainable transition, and technological skills and knowledge must be promoted (3), since this is about pan-European competitiveness, not only Slovenian competitiveness. This is followed (4) by the establishment of an efficient judicial system, which will safeguard agreements and private property, and distinguish between public and private interests. Finally (5), a thorough transformation of the tax policy and initiatives, and the harmonisation of regulatory measures, are required to foster convergence in the other four areas. This Outlook deals in depth with all five areas, with a focus on the first and fourth, while

we do not dwell much on taxation. The reader will not fail to notice that the highlighted five areas are in fact closely related to the objectives of the Slovenian Development Strategy 2030.

The path to a development agreement consists of five stages. Initially, an agreement between social partners must be reached, which should be supported by as many stakeholders and social groups as possible. It is crucial to define the contribution of each social group and the long-term benefits for each, both of which must be justified in a clear matrix. Furthermore, the Slovenian Development Strategy must be upgraded with a development agreement that enhances the vision of the Strategy. The government's "on-call duty" must distance itself from forced crises and shift towards an active conversion of the strategy and the development agreement into development-oriented policies. The role of parliament is essential for the moral firmness of the commitment, particularly the role of the National Council, which must mature, in terms of content, into an administrator of a long-term development ambition for the well-being of future generations.

Last but not least, a moral commitment is needed from each social group to assume responsibility for the implementation of the development agreement and manage its active role within it. The awareness of each individual that they are part of a society with a common ambition is also required. Only then may everyone be eligible for the benefits arising from the agreement. All this may happen only in an open and supported social process.

The ambition is still open to conclude, follow and upgrade the agreement, and continually translate it into consistent development policies. We must seize this last chance if we do not wish to waste an entire generation and miss the opportunity provided by economic stabilisation after overcoming the economic crisis. This means that a development agreement boosts competitiveness in itself.

# "Since you've got more, I've got less" –

## The principle that excludes innovators

Is the quantity of goods in a certain society limited and given in advance?

When it comes to the issue of social inequality, in the background of any reflection are three more or less thought-through belief systems.

The first belief stems from the analytical assessment that asymmetries occur during production – to put it simply, let us say that these are ideas with a strongly emphasised social undertone, based on Marx's philosophical premises. To put it very simply again, people who produce value as workers are paid less for their work than those who have invested capital in the production receive by selling products or services.

The second belief – let us call it meritocratic – understands the issue of inequality, if I may put it very simply again, as a natural state; those who work more, have more. Those who are more skilful have more than those who are less skilful. This belief is an important mechanism of economic development, but it is not possible to explain real inequalities only at the analytical level, even with great skill and diligence.

The third belief, which is also critical of social inequality, is less well known, but is perhaps more rooted in the common social perception of the world than the century-and-a-half-old criticism of inequality by Marx. It is a belief discussed by American anthropologist George M. Foster in his 1965 article, "Peasant society and the image of limited goods". Since this is a lesser known system of beliefs, we should take a closer look at it.

**While conducting anthropological research in Mexico, Foster encountered the idea, rooted in the peasant population, that the quantity of goods – land, crops, and knowledge, as well as affection, friendship and love – is limited and provided in advance.** Foster mentioned reports by other field researchers who encountered similar notions in other parts of the world. The idea of a limited quantity of goods leads to the logical conclusion that if some have more, then others have less. To have more is not only an offence against a specific person, who is supposedly directly affected because the first person has more. To have more is an offence against the community as a whole, because the entire community will be affected by the one who has more. These ideas about limited goods were taken so far that, in the peasant community studied by Foster, even copying technological innovations

## Ali Žerdin

in pottery was considered an offence. A potter "taking" a technological innovation of another potter meant that the innovator lost out.

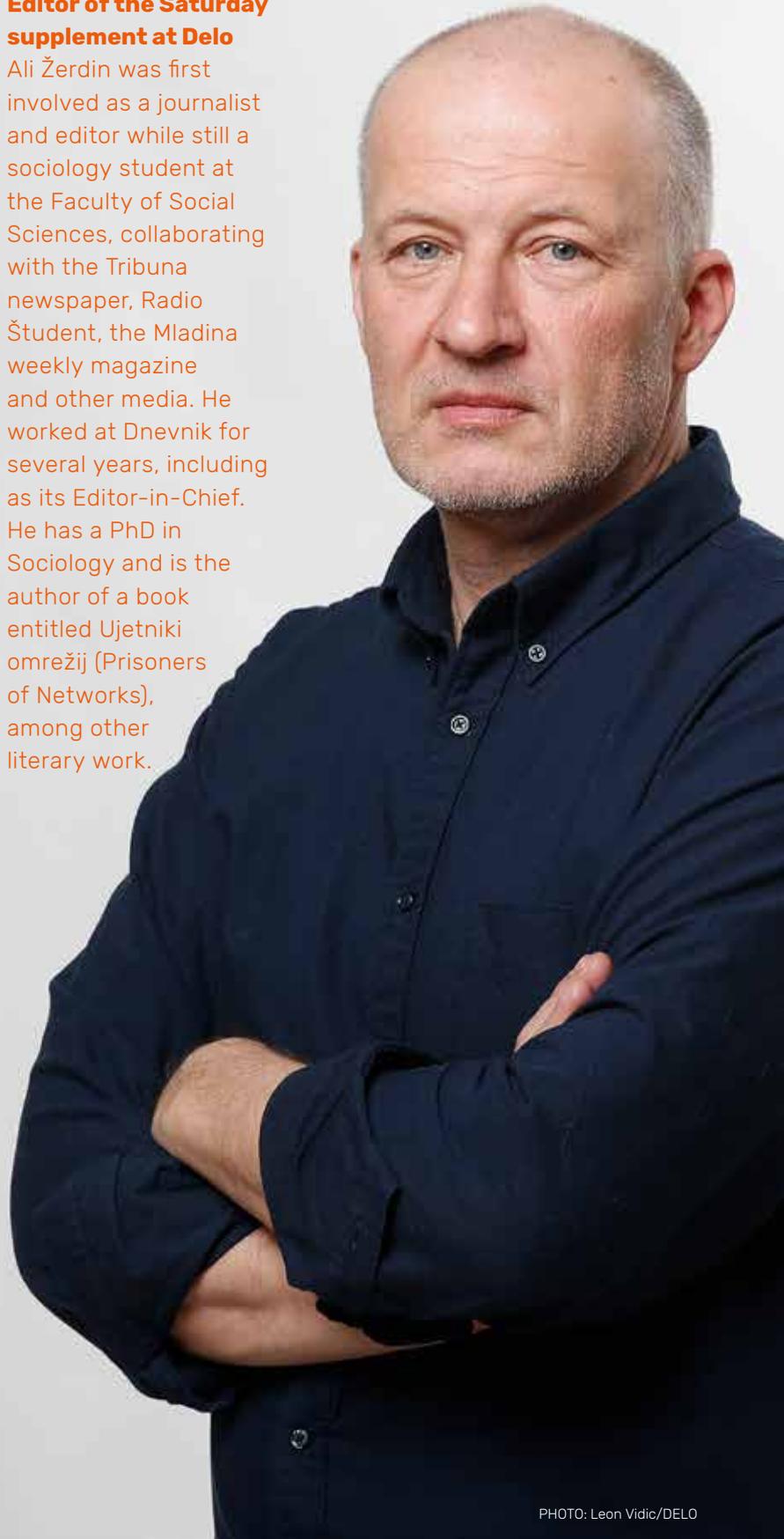
While commenting on the ideas about limited goods, Foster was not patronisingly critical, but was analytical in finding the causes of these concepts. It was true, as Foster established, that the quantity of land, as the most important production factor, was limited. Since it was limited, it is hard to imagine that more than had naturally been given could grow on a specific area of land. Even if more effort were invested in production on a limited area of land, this would not result in higher crop yields. Due to the absence of information, agricultural production had not changed for centuries. Due to soil degradation, there was even a very high risk of crop yield becoming even worse over time, despite a greater effort being made. Since there had been no innovation and progress for several centuries, things remaining unchanged seemed the natural state of things.

### Misconceptions about limited goods and the inability to cooperate

A world in which a community is held together by an implicit assumption about a limited amount of goods provided in

### Editor of the Saturday supplement at Delo

Ali Žerdin was first involved as a journalist and editor while still a sociology student at the Faculty of Social Sciences, collaborating with the Tribuna newspaper, Radio Študent, the Mladina weekly magazine and other media. He worked at Dnevnik for several years, including as its Editor-in-Chief. He has a PhD in Sociology and is the author of a book entitled *Ujetniki omrežij* (Prisoners of Networks), among other literary work.



advance is a world without cooperation. The family or the individual are the key units of society. As cooperation requires leadership, it is hampered, because the person who leads, by increasing the amount of their power, takes some of the others' power away, which is not permissible. An ideal human makes no effort to lead a broader community. As the community is not being led, there can be no progress, either. As an increase in property is understood to be something which has been gained at the expense of others, people only display as much property as other people have. If they displayed more, they would give the impression that this had been gained at the expense of others. A society governed by the idea of limited goods is a society of mutual distrust.

All those who deal with organising society, or organising economic cooperation in society, are faced with particular distrust. On the other hand, the principle exists that humans must rely on themselves and on their families.

**The starting question is, in what way is inequality perceived in modern Slovenia?** Do we understand it as a consequence of differences and asymmetries which occur during production, a consequence of the fact that some are more hardworking and skilful; or do we perceive inequality as it is perceived in traditional farming communities, which were held together by implicit assumptions about a limited quantity of goods? In the absence of a thorough empirical analysis, I may only offer hypotheses, but empirical conclusions show that we must not underestimate the extent of the underlying ideas about the limited quantity of goods.

### Perception of limited goods, a meritocratic view of inequality, and social development

The meritocratic belief that inequality is a consequence of differences in abilities and diligence is relatively rare. The belief that inequality is a consequence of differences in abilities is analytically





PHOTO: Uroš Hočevar/DELO

A world in which a community is held together by an implicit assumption about a limited amount of goods provided in advance is a world without cooperation.

insufficient, as it fails to take into account the fact that individuals also gain advantages by using disreputable practices, exploiting the labour force, establishing monopolies, restricting competition, inherited or political privileges, corruption and so on. Nevertheless, the meritocratic belief is important for social balance, as it emphasises the importance for development of an individual’s own efforts. If meritocratic values are promoted in an environment which takes the rule of law very seriously, such a system of beliefs is favourable for social and economic development.

If the idea that inequality is a consequence of differences and asymmetries in production was dominant in Slovenia, it would be relatively simple to answer the question of how to manage social inequality. It is possible to seek balance within political institutions and within institutions dealing with tripartite social dialogue. In other words, if the ideas about inequality are based on the perception that inequality occurs within production, the potential conflict may be resolved within political institutions. The problem may be solved by taxation, the instruments of a welfare state, and other political tools.

However, if it turned out that the prevailing ideas were about inequality arising from the adoption of a limited quantity of goods provided in advance, this would cause several difficulties. If the perception of inequality is based mostly on the idea of limited goods, political tools cannot be successful. In this context, debate is no longer conducted in the political framework, but the ideas become fuel for the spreading of populism.

There are several elements which lead to the assessment that the idea about limited goods is

strongly anchored in Slovenia. "They have stolen everything," is a sentence frequently uttered in debates in bars or online discussions. The comment "they have stolen everything" is universal – it relates both to events which have realistic criminal backgrounds, and the perception that someone has more than others because they are skilful. The fact that someone has more than others is, in the context of bar gossip, proof that that someone has been stealing and making gains at the expense of others. But the implicit assumption of such viewpoints is the belief that goods are not generated by production, or the more or less fair distribution of profit between workers and investors, but that the quantity of goods is limited and provided in advance.

### Trust in institutions as a reflection of the perception of limited goods

There are some other pieces of direct evidence which may support the hypothesis that the perception of a limited quantity of goods is characteristic of Slovenia. A survey by the pollster Valicon, published in January, shows that institutions may be divided into five categories in terms of the level of trust in them. Trust is lowest in the current institutions that regulate society, such as opposition parties (the lowest trust), the National Assembly, the parties of the ruling coalition, the government, the European Commission, and the courts (the courts have improved their score the most in relative terms compared to a survey from 2014).

Financial intermediaries (banks and insurance companies) are somewhere in the middle of the list.

Public sector institutions (education, healthcare, the public broadcaster RTV Slovenija) enjoy a slightly higher level of trust. Two law-enforcement institutions – the police and the military – are almost at the top of the list.

People have the greatest level of trust in small companies (the highest mark) and the companies in which they themselves work.

What was also characteristic of the egalitarian syndrome was antiintellectualism, anti-professionalism, the perception that division is more important than production, a disdainful attitude to entrepreneurship, and so on.

Translation: People trust themselves the most (their own company, small companies). They trust law-enforcement structures – perhaps because they have not had negative experiences with them – and understand them as institutions which prevent them from suffering direct damage. The level of their trust in institutions of knowledge – education, healthcare – is medium-high. On the other hand, they do not trust institutions of key importance for the organisation of economic activity (banks, insurance companies), and institutions in power.

The picture is also changeable when it comes to trust in professional groups. People have the greatest level of trust in the professions which prevent damage being inflicted on goods (e.g. firefighters). Nurses are trusted more than doctors; both professional groups deal with preventing damage to important goods i.e. health. People trust teachers more than university professors. Those they trust the least are politicians (the lowest mark), ministers, priests, state officials, trade unionists, and company directors – the professional groups which organise society; groups with a higher level of authority or power.

This information about who we trust corresponds to a certain extent with the orientation of a society based on the idea of a limited quantity of goods. This could mean that we are in trouble. There is a low level of trust in professions and institutions which coordinate the functioning of society and make decisions important to the community.

However, on the other hand, a high level of trust is expressed in scientists, which relativizes to the hypothesis about the dominance of values that are

not inclined to development. Trust in scientists has, by itself, a precious development potential. But we should also be careful in this area. We trust teachers more than university professors, which points to a certain level of anti-intellectualism. We trust nurses more than doctors; this too points to anti-intellectualism. When we choose from people who work in similar fields, we put more trust in those who were educated for a shorter time and finished less demanding studies. Let us repeat: even knowledge may be perceived as provided in advance, as limited goods. Under the idea of limited goods, some have more knowledge because they have gained it at the expense of those who have less knowledge.

When it comes to values, we find that these are not equally distributed among the population. Part of the population advocates meritocratic values, and part advocates social values. Either way, division of values in society is by no means bipolar. We also need to pay attention to the section of the population which has the implicit idea about a limited quantity of goods provided in advance, i.e. to the part of the population which is convinced that some have more because others have less.

While the American anthropologist Foster found that the idea about limited goods was prevalent in the Mexican countryside, the Croatian sociologist Josip Županov put this idea at the core of the egalitarian syndrome characteristic of the former Socialist Federal Republic of Yugoslavia. What was also characteristic of the egalitarian syndrome was anti-intellectualism, anti-professionalism, the perception that division is more important than production, a disdainful attitude to entrepreneurship, and so on.

### The assumption about limited goods does not enable dialogue

Although a dialogue between the social and meritocratic views is relatively difficult, it is possible, as both views put production at their core. The social view of inequality finds that asymmetries

occur during production, while the meritocratic view emphasises that more productive people have more than less productive ones. Dialogue is possible within the political system and is regulated by the instruments of the rule of law. If the meritocratic and social views are schematically translated into political party categories, we may say that the meritocratic view is partially consistent with the liberal political orientation, and the social one with social democracy. Both views are compatible in the framework of a functioning rule of law within the concept of a welfare state.

What is much more difficult is a dialogue with those who hold an implicit assumption that the quantity of goods is provided in advance and thus limited. It would be a mistake to attribute such a view to modern social democracy; the imperative of production is important for social democracy. The viewpoint that an individual can get rich only at someone else’s expense is in a way archaic, as it dates back to times when there were no political parties. However, we may still find traces of this mindset in modern populist groups and movements.

If managers are the pillars of the meritocratic mindset, it would be wrong for them to see those who use social arguments and warn about the asymmetries they detect in production as their key opponents. The meritocratic view feeds from the modern slogan about freedom, while the social view feeds from the modern slogan about equality and brotherhood.

What is a considerably greater threat to a meritocratic society based on the rule of law is the implicit assumption that the quantity of goods is limited and provided in advance, as this view disregards the aspect of productivity. This idea is pre-modern, and it neglects the aspects of production, productivity and innovation. At the same time, we must acknowledge that traces of such ideas are strongly anchored in the current perception of the world held by part of the population.

# Does the Slovenian social market model have a chance of survival?

In last year's publication of the Managers' Association, Outlook 2019 (see Mramor and Sambt, "Resolving the Aging Problem in a Sustainable Way", Outlook 2019, Managers' Association, 2018), we analysed the medium and long-term economic challenges of Slovenia in the light of the extremely severe economic crisis it had experienced, and the more than excellent economic movements after 2014. Based on our experience in the crisis, we also took into account the impact of the projected state of the economy on social stability, and its repercussions on the economic performance of Slovenia. We arrived at the conclusion that the extremely rapidly ageing Slovenian population is the greatest challenge for Slovenian society.



## Dušan Mramor

President of the Observatory of the Managers' Association, and full Professor of Finance at the Faculty of Economics of the University of Ljubljana Dušan Mramor was Minister of Finance of two governments of the Republic of Slovenia; in the government of Anton Rop (2002-2004), during which Slovenia joined the EU and the ERM 2, and that of Miro Cerar (2014-2016). The Banker magazine of the Financial Times Group named him Finance Minister of the Year 2016 for his contribution to Slovenia's finding a way out of the great economic crisis. He was the first President of the Council of the Securities Market Agency and has been a member of the council of the National Bank of Slovenia, a Vice-president of the Strategic Economic Council of the Slovenian government, and an adviser to the President of the Republic and to other expert academic and advisory panels. He also served as a World Bank consultant and in the supervisory bodies of several companies and banks. Mramor was the Dean of the Faculty of Economics (2007-2013) and Chair of the Board of the University of Ljubljana, as well as a visiting professor and member of staff at several universities in the EU and the USA (for example, at Indiana University). He has been an accredited senior appraiser with the American Society of Appraisers since 1995. Mramor was also a Vice-president of the European Finance Association and the European Institute for Advanced Studies in Management.



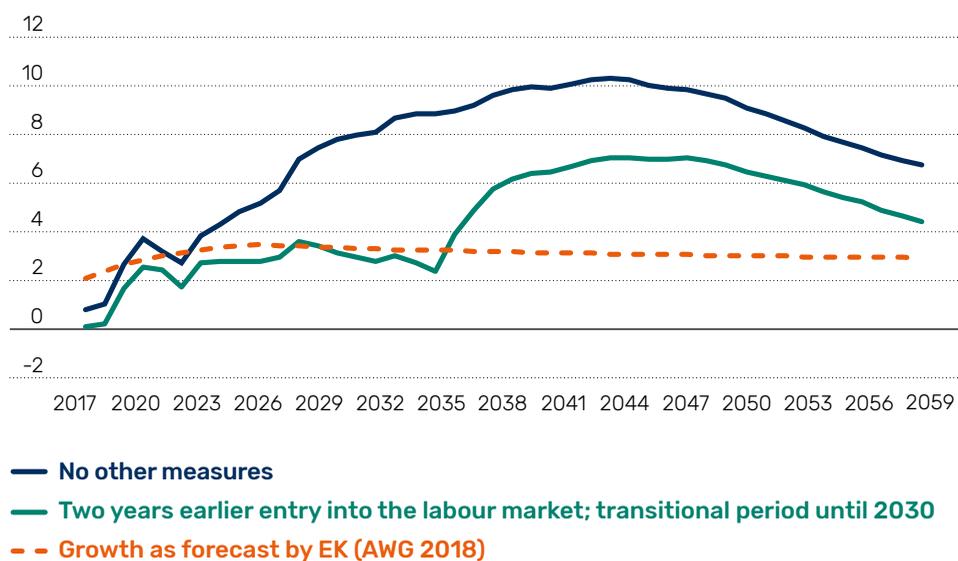
We reject the simplified explanations of the necessary “structural reforms” in regard to the focus on ways of reducing the risks involved in an ageing population, which require severe government expenditure cuts per capita in Slovenia to maintain their share of GDP unchanged. We argue that this way of “resolving” the problem would cause social instability that could lead to relative or even absolute economic decline. Such a large reduction in pensioners’ rights, for example, (one of the proposals is a unified 500 euro a month) would, in accordance with the logic of the “downward spiral” movement, increase social instability and the consequently negative economic trends, and the cycles would be repeated at an ever lower level. In the light of our experience in the last very long crisis, such negative trends are very difficult to reverse, as they gain in strength and thus become increasingly long-term.

## Jože Sambt

### Associate Professor at the Faculty of Economics of the University of Ljubljana

Jože Sambt’s research areas include relations between generations, the impacts of demographic changes on the long-term sustainability of public finance, and labour economics. One of his many articles was published in the world’s top scientific journal, “Science”. He is the leader of the Slovenian team of an NTA international research project ([www.ntaccounts.org](http://www.ntaccounts.org)).

Figure 1: **Annual labour productivity growth rate required to maintain government pension expenditure at the same percentage of GDP (faster entry into employment and later retirement)**



Source: Various sources (European Commission, Statistical Office of the Republic of Slovenia, EUROSTAT, Pension and Disability Insurance Institute of Slovenia, etc.) and authors’ calculations



PHOTO: Leon Vidic/DELO

## Logic and the results of last year's analysis

We decided to look for ways to maintain the stability of the parts of government finances that are significantly affected by demographic change, without or with minimum cuts to the rights to public funds. In doing so, we focused on government pension expenditure, which represents a major proportion of these finances. Initially, we presented an empirical analysis to put productivity at the centre of the study for the first time, and to answer the question of how much labour productivity should be increased to counteract the impact of an ageing population on the increase in the percentage of government pension expenditure in GDP.

How can we reduce the required productivity growth without significantly affecting pension rights? The most important "reserve" is in population activity.

The analysis, which presupposed the given pension scheme and EC and Eurostat forecasts, showed the need for unachievable gains in annual productivity: for instance, from 2023 onwards over 3% annually, higher by nearly half as much again than the 2% growth forecast by the EC, and in the range between 6-10% growth between 2027 and 2060, which Slovenia has never achieved in even one year.

Of course, the question immediately arose as to how we can reduce the required productivity growth without significantly affecting pension rights. The most important "reserve" is in population activity. In the younger age cohort, we assessed the impact of an increase in activity with earlier entry into the job market by shortening full-time education, and in the older age cohort with a significant extension to working lives; both at the level of the most successful EU countries. The impact on reducing the required productivity growth proved to be very large, reaching the EC forecast level by 2037, after which it would increase to a maximum of 6% (around 4% on average) annually, as shown in Figure 1.

In certain shorter periods, Slovenia reached much higher annual productivity growth, over 4% (see Figure 5 in the datasheet), than during the long-term growth anticipated by the EC by 2060. According to our experience and past analyses of the effects of individual economic policy measures and system changes on GDP growth, we have proposed a set of challenging measures and systemic changes that together would have the effect of significantly increasing growth in annual productivity, roughly estimated at over 3% a year.

If we were to increase activity and productivity to the levels shown, in theory other measures would hardly be necessary. Increasing population activity and labour productivity are changes that address the problem of population ageing through a corresponding increase in GDP; in short, by producing more. We have also shown the positive effect of addressing the ageing issue in this way on the well-being of all residents – both working and retired people.

However, from the experience of Dr. Ali Žerdin (see his article in this publication) and his excellent analysis of the way priorities are formulated in Slovenian society, we cannot count on this. So, we also analysed and estimated changes in the division of GDP, including growth in wages lagging behind that of labour productivity, and reducing the indexation of pensions, that could be used in combination with increased activity and productivity. Both changes in the model proved to be very effective in maintaining fiscal sustainability, but we recognise the difficulties of achieving them, as they reduce the income rights of workers and/or pensioners.

### Last year's "window of opportunity" for Slovenia

As we know, in Slovenia it is extremely difficult to achieve changes that increase work effort or reduce rights for a particular group. In the meantime, unfortunately, changes have taken place, or, in the last stages of adoption, amendments have turned in the opposite direction to those that we identified and assessed as technically reasonable and necessary by

analysis. However, in order to make the necessary changes, a special **development agreement**, which was proposed in the first quarterly edition of Outlook in the pages of the Delo newspaper, would be necessary (see Mramor, “The society of agreement to avoid the black scenario,” Delo, 17 April 2019). According to Mramor, “A social agreement should, in the long term, commit key social groups to the implementation of these necessary changes, regardless of the mandate of individual governments. In the first phase, an agreement between the state, employees and employers would make the most sense. The commitments of each side should be verifiable and measurable, with benefits linked to results with regard to work activity and productivity growth.”

It has been estimated that now is the right moment due to the excellent economic performance, which bring greater possibilities for the state to respond to the pressures on financing, and consequently, reduced social tensions. This was confirmed by the social partners’ representatives in the second quarterly edition of Outlook 2019 (see Delo, 10 July 2019).

Unfortunately, it is likely that this “window of opportunity” has more or less closed, as the measures and systemic changes carried out have focused almost exclusively on reducing the pressure from individual social groups, without simultaneously achieving the necessary changes for the medium and long-term sustainability of the system. Thus, they have prepared and/or adopted amendments that mostly go in the opposite direction to those required, and which far exceed the available government financial resources to alleviate the pressures, as shown by the results of our analysis this year.

### Did we close the “window”?

In Scheme 2 to this article, we summarise the proposals for action we made last year and the actions we have taken, partly through our own experience and partly through empirical analysis. A rough comparison of last year’s proposals with the actual changes and the measures taken since then worryingly reveals not

only the failure of the vast majority of the proposals, but changes in the opposite direction to those required; this is the direction that Ali Žerđin describes in his article in this publication as a “perception of limited goods”, regarding it as a problem.

1. First, let us look at our cluster of proposed amendments intended to increase the activity of the population, which we have called “Work pays off.” Apart from the incentives for later retirement, there are no other positive changes. As we demonstrate in this analysis, all other amendments increase pension expenditure tremendously in the long run, far more than they are reduced by the later retirement age. Other amendments in the form of increasing or re-establishing numerous social rights contribute significantly to the work “not paying off,” and are crowned by an amendment that requires seniors to pay a penalty if they work more than they are allowed to. Nothing happened to increase young people’s activity, except for an increase in the minimum hourly rate of student work, which of course further prolongs the time before arrival in the central labour market and extends the duration of studies, among other things. Only migration has made us more lenient, due to the shortage of personnel at low unemployment rates, as is apparent from the data. Of course, this is carried out with the same extreme administrative obstacles and thus lower work productivity in companies.
2. The second proposed cluster relates to an increase in investment where it has the greatest impact on GDP. Last year, we had a unique opportunity to direct this cash flow into urgently needed investments for the long term, due to the large increase in budget revenues with a record-high fiscal surplus. This did not happen, as we directed our cash flow primarily into social rights, pensions, and wages for a longer period ahead.

This missed opportunity was particularly stressed by the European Commission, assessing the high

risk of long-term fiscal sustainability, and the Fiscal Council of the Republic of Slovenia, which *inter alia* wrote: “The Fiscal Council recalls that the draft budget for the years 2020 and 2021 represents a continuation of fiscal policy management without an outlined comprehensive set of policies to adequately ensure the long-term sustainability of public finances, especially in relation to the costs of an ageing population. Recently, measures have been taken, or are currently being prepared, which could structurally impair the position of public finances in the future. In the past, the lack of room for manoeuvre of the fiscal policies has often led to shrinking government investment. In a period of moderate economic growth, a restrictive fiscal policy designed in this way would be inadequate, and would also impair long-term economic prospects.”<sup>1</sup>

In our opinion, such an investment also means additional investment in health care, both (gross) investment due to the high write-off of fixed assets, and in the form of (net) investments in capacity expansion, due to the increase in the number of patients, and in the form of increased costs, due to additional required healthcare workers. The dramatic increase in sick leave, the cost of sick leave and the consequent negative impact on growth in labour productivity could significantly reduce such investments. Velimir Bole estimates that it is necessary to gradually increase the percentage of health care resources in GDP by 1 percentage point.<sup>2</sup>

The reorganisation would achieve all possible savings on the one hand, and cover real deficits on the other. These are additional resources, which would be allocated in parallel with the reorganisation of the sector. The current discussions lead to a reduction in existing funding through the abolition of supplementary health insurance and restrictions in it.<sup>3</sup>

3. No progress can be found in the proposed measures to increase overall factor productivity,

1 Fiscal Council of the Republic of Slovenia: “Fiscal Council Assessment: Compliance of the Draft Budgets of the Republic of Slovenia for 2020 and 2021 with the fiscal rules”. 22. 10. 2019

2 Velimir Bole: “The scope of the health system – where is Slovenia?” GG, September 2017.

3 These are not expert discussions based on the results of certain studies claiming that there are too many resources in the Slovenian health system, even up to 25% (Medeiros & Schwierz: Efficiency estimates of health care systems. European Economy, Economic Papers 549, June 2015), but are based on ideological factors.

as shown by the third proposed cluster. On the contrary, the state proposes some changes which go in the opposite direction, e.g. a change in the capital investments management strategy of the state, and a change in the fiscal rule.

4. After a year of opportunity, we do not have a development agreement that outlines the necessary changes to avoid the "black" scenario. The outline of logic and areas is shown in Scheme 1 at the end of this article. The social partners welcomed the initiative in words, but took the opposite direction.

### What do this year's calculations show, and is there anything else that can be done?

In order to determine whether medium and long-term stability and growth in Slovenia can be achieved in the context of significantly changed circumstances compared to last year, we decided to update and extend the analysis by:

1. Taking into account the latest Eurostat demographic projections.
2. Taking note of this year's amendments to the pension legislation and assessing how they increase the already significant problem in the pension sector.
3. Adding public healthcare and long-term care expenditure, which are also highly dependent on demographic trends, to government pension expenditure, and repeating the analysis of productivity growth needed to maintain fiscal stability.

#### Latest Eurostat demographic projections

In this year's demographic projections, Eurostat assumed a slightly lower net immigration for Slovenia than three years ago, and a slightly lower birth rate. With respect to the future mortality trend, the continued extension of longevity, however, retained virtually the same assumptions as the last projection update three years ago. The results suggest that, under these assumptions, the ageing of the population would be slightly stronger than in the projections of three years ago. The proportion of people aged 65 and over

in the population is expected to increase from 19% in 2018 to 31% in 2050. The assumption is that about 4000 inhabitants are expected to immigrate rather than emigrate each year during this period; however, in the absence of these positive net migrations, the projections point to an even greater increase in the proportion of the population of people aged 65 or older of 34%.

Increasing the proportion of people aged 65 or older to about one third of the population will result in strong demographic pressures on economic sustainability. Appropriate changes must therefore follow, notably in the pension scheme, the healthcare system and the long-term care system. Below, we outline expenditure projections in each of these areas and some measures to curb the pressures on financial sustainability. At the same time, we show the scope of the gains in productivity in dealing with these pressures.

### Effects of amendments to the pension scheme

In the calculations presented in 2018, we identified the necessary productivity gains to maintain government pension expenditure on pensions relative to GDP at the 2016 level of 10.9% (Mramor & Sambt, 2018). Meanwhile, amendments to the pension legislation have come into the public debate:

- 1) An increase in the vesting percentage for calculating the amount of the pension for men. These are expected to gradually increase from the current 26% to 29.5% for the first 15 years of the retirement period by 2025, and for the retirement age of 40 years of service (which is the full retirement age) from the current 57.25% to 63.5%. However, the increase in percentage for retirement years between the ages of 16 and 39 will also be between 3.61 and 6.14 percentage points, which is between 13.2% and 11.0% higher. This will have a strong negative impact on the sustainability of the pension fund. Arresting the decline of vesting percentage for women will also have an impact on higher pension expenditure. According to the existing pension legislation, women's vesting

percentage for the full pension period (40 years) should be reduced to 60.25% by 2023, while according to the proposal for pension amendments, they should remain at the current level, i.e. 63.50%.

- 2) The additional vesting rates for carers of children in their first year of age, given that in the current retirement group there are in most cases women. For each child, up to three children, whether born or adopted, they can receive an additional vesting percentage of 1.36 when claiming a pension. This will also put additional pressure on the sustainability of the pension fund.
- 3) After completing 40 pensionable years without buying extra years of service, and at least 60 years of age, every six months of completed pensionable years are valued at 1.5%, which is 3% annually (in the current system, this amounts to 1% for every 3 months, which is a total of 4% per annum) for up to three additional years of insurance. If an individual remains employed after qualifying for retirement, they will receive a substantially higher pension after retirement than they would otherwise. At the same time, while still in employment, under the

existing legislation, an individual receives 20% of the pension they would have received if they had retired, and the amendment proposal includes an increase of that percentage to 40%.

Table 1 shows how much each of these measures contributes to pension expenditure as a percentage of GDP. The third measure does not include the effect of the proposed amendment (reducing the vesting percentage for three years of additional work from 4% to 3% annually, and increasing the payment of part of the pension from 20% to 40%), but an overall effect of this measure compared to the situation if there were no more incentives for the longer retention of workers. As can be seen in the Table, the first of the three measures described above has by far the largest impact – an increase in the government pension expenditure relative to GDP will have increased to as much as 16.5% of GDP by 2060, i.e. 1.3 percentage points more than under the current arrangement. The scenario of additional vesting percentage for each additional child increases the result in 2060 by 0.3 percentage points. The third of the above measures initially has a positive effect on the sustainability of the

Table 1: **Government pension expenditure (% of GDP); projections up to 2060**

Government pension expenditure (% of GDP)	2020	2025	2030	2035	2040	2045	2050	2055	2060
Current arrangement	10.1	10.4	11.5	12.7	13.9	14.9	15.4	15.5	15.2
Vesting % for 40 years: to 63.5 for both genders	10.1	10.6	11.8	13.2	14.8	16.0	16.7	16.9	16.5
Additional 1.36 vesting % for each child	10.1	10.6	11.8	13.3	15.0	16.3	17.0	17.1	16.8
40/3*	9.9	10.3	11.7	13.3	15.1	16.5	17.3	17.5	17.2

\* Note: Compared to the results if this option were not available (it is not only about an impact of the proposal)

Table 2: **Necessary growth in labour productivity by individual scenario to maintain government pension expenditure as a percentage of GDP at the 2016 level**

Growth in labour productivity	2020	2025	2030	2035	2040	2045	2050	2055	2060
AWG Assumptions	1.6	2.2	2.1	2.0	1.9	1.8	1.8	1.7	1.7
Existing pension arrangements	2.6	3.8	7.2	8.4	9.7	10.0	9.1	7.4	6.0
Including proposed amendments to the pension legislation	-0.6	4.0	8.7	11.5	13.8	13.9	13.0	11.2	9.4

Source: European Commission, 2018; calculations made at the Institute for Economic Research within the framework of the operation "Upgrading analytical models for the needs of the pension system", financed from the European Social Fund by the Republic of Slovenia and the European Union

pension fund (-0.2 percentage points of GDP), since we pay individuals only 40% of the usual pension instead of paying them a full pension. Over time, however, pension fund expenditure begins to increase, as more and more pensioners receive a significantly higher pension – 9 additional per cent for 3 additional years, which means a 14.2% higher pension (72.5% instead of 63.5%).

**Figure 2: Necessary growth in labour productivity by individual scenario to maintain government pension expenditure as a percentage of GDP at the 2016 level**

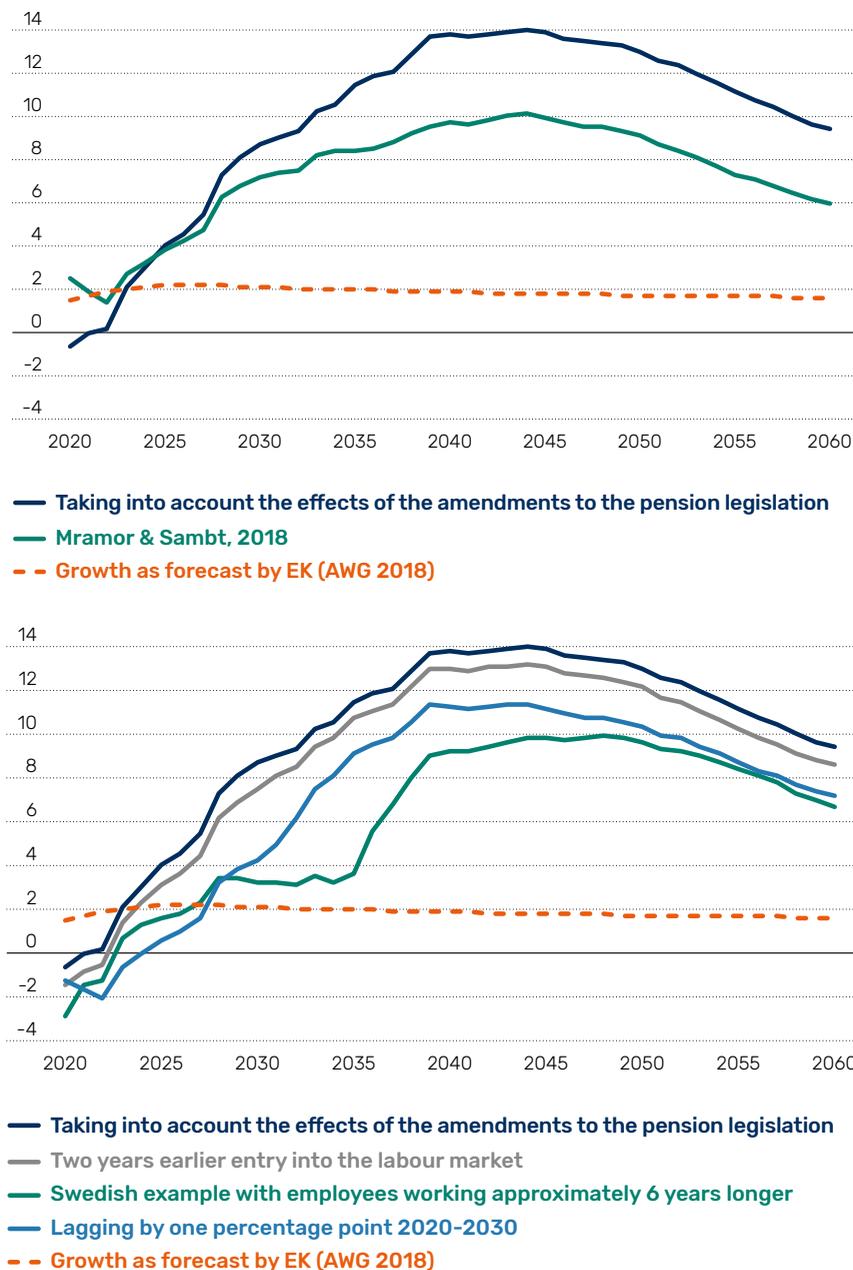
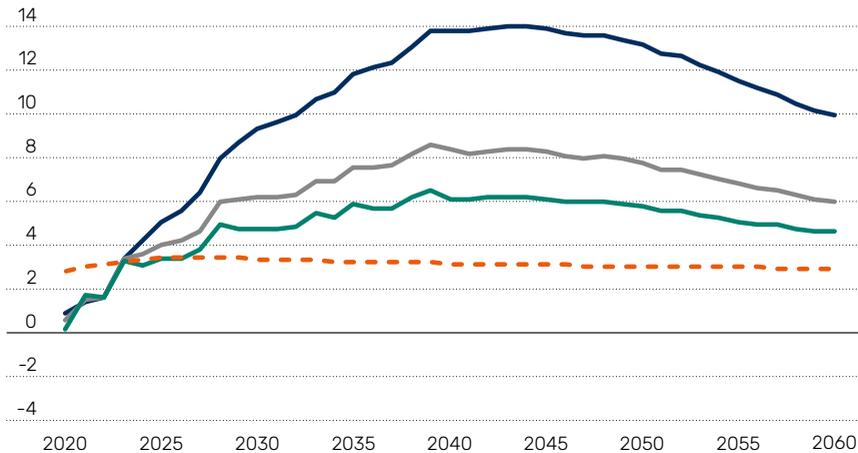


Table 2 and Figure 2 show the required labour productivity growth for maintaining government pension expenditure as a percentage of GDP at the 2016 level, taking into account the projected amendments to the pension scheme and demographic projections. Figure 2 shows the same image of individual scenarios as presented in last year’s article; this time, however, we use the new Eurostat

demographic projections (EUROPOP2018) and the effects of the proposed amendments to the pension legislation.

As we can see, significantly higher growth in productivity would now be required to maintain the percentage of government pension expenditure relative to GDP at the 2016 level. In some of these Figures, we show how much this required growth in labour productivity would decline if the measures were introduced individually, namely, entering into the labour market two years earlier, working approximately 6 years longer (7 years in total to be in line with Sweden, but the third element of the pension legislation amendment already provides for approximately one year longer stay in employment), lagging wage growth behind productivity growth by one percentage point in the period 2020-2030, and indexation (30% or 0% real indexation instead of the current 60%).

With higher productivity, it is possible to improve the sustainability of the pension scheme, since higher productivity is not fully reflected in higher pensions. In



- Taking into account the effects of the amendments to the pension legislation
- Indexation 30 : 70 (wages : CPI)
- Indexation 0 : 100 (wages : CPI)
- - Growth as forecast by EK (AWG 2018)

With higher productivity, it is possible to improve the sustainability of the pension scheme, since higher productivity is not fully reflected in higher pensions.

Source: European Commission, 2018; calculations made at the Institute for Economic Research under "Upgrade of analytical models for the needs of the pension system", financed by the Republic of Slovenia and the European Union from the European Social Fund.

existing pension arrangements, for already retired individuals, higher productivity is reflected in a real pension increase at 60% indexation of the real wage increase. Higher productivity, and thus higher wages for the individuals who are still working, will lead to higher pensions with a delay (when they retire), and gradually, since the calculation of the pension base takes into account the 24 best consecutive years.

The values presented in Table 2 are very high. In the past, high productivity growth has been recorded by countries that have been in the process of catching up with developed countries, and only for a limited period of time. For European countries, for example, in recent decades such a period of high growth occurred between 1997 and 2007, when transition countries had particularly high growth rates. The highest average annual GDP growth rates in this 10-year period were recorded by Latvia (7.9%), Estonia (7.4%), Ireland (7.0%), Lithuania (6.8%), Luxembourg (5.2%) and Slovakia (5.0%).

### The effect of healthcare and long-term care

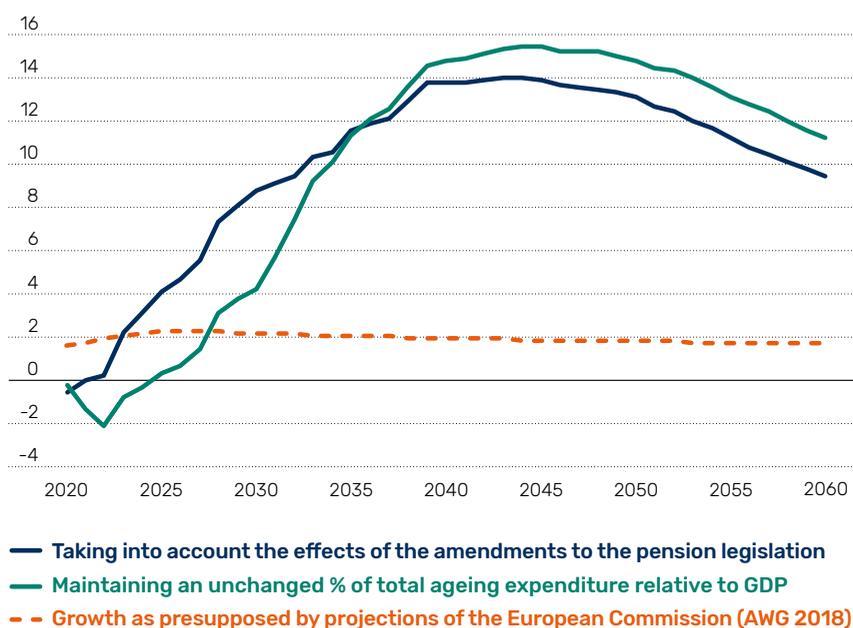
In healthcare and long-term care systems it is impossible to solve economic sustainability with

higher productivity. According to the European Commission's assumptions, in the case of healthcare unit costs basically increase with an increase in GDP per capita. If productivity increases, it is assumed that GDP, which depends on productivity and the number of workers, will increase by the same percentage. Higher productivity thus increases GDP per capita by the same percentage (the population does not change due to higher productivity), so the sustainability of the healthcare system does not improve.

Similarly to the healthcare system, it is also true for the long-term care system that higher productivity cannot solve the problem of sustainability, as unit costs are assumed to increase with growth in productivity. The argument for this assumption lies in the labour intensity of long-term care, since most of the costs are labour costs. Higher productivity therefore translates directly into higher long-term care costs through higher wages.

Thus, in our calculations, we assumed that the increase in unit costs is not related to productivity growth or GDP growth rate per capita, but wage growth. In the basic version of the model, wage growth was directly linked to productivity growth, but we have now changed this; in the period 2020-2030, we assume one percentage point lag in wage

Figure 3: **Labour productivity growth required to maintain the sum of general government expenditure on ageing (pensions + healthcare + long-term care) as a percentage of GDP at the 2016 level**



It is likely that this “window of opportunity” has more or less closed, as the measures and systemic changes carried out have focused almost exclusively on reducing the pressure from individual social groups, without simultaneously achieving the necessary changes for the medium and long-term sustainability of the system.

Table 3: **Necessary wage growth lag after productivity growth in order to maintain government expenditure on healthcare or long-term care as a percentage of GDP at the 2016 level (in percentage points)**

	2020	2025	2030	2035	2040	2045	2050	2055	2060
Healthcare	0.7	0.8	0.5	0.4	0.2	0.1	0.1	0.0	15.2
Long-term care	1.5	2.3	2.4	2.6	1.9	2.3	0.9	0.4	16.5

Source: European Commission, 2018; authors' calculations

growth each year behind productivity growth. This nearly halves the increase in health expenditure, expressed as a percentage of GDP. With regard to the increase in long-term care expenditure, the impact of this assumption is small, as with regard to GDP, this expenditure more than doubles in projections. According to the European Commission projections, they will increase from 0.94% of GDP in 2016 to 1.79% of GDP in 2060, and will go even slightly higher (1.87%) according to the new population projections currently being used. On these assumptions, Figure 3 shows the necessary productivity growth for pension, healthcare and long-term care expenditure together to maintain the same percentage of GDP over the entire projection period as that of 2016.

The results indicate that, at the beginning of the projection period, the annual growth in labour productivity is sufficiently lower in this case, since it has a strong positive effect on the sustainability of wage growth lagging behind the growth in labour productivity. However, after 2030, all expenditure on ageing, in addition to pensions, begins to increase, due to healthcare and long-term care. However, the problem of growth in this expenditure is not solved by higher productivity, so it is necessary to further reduce pension expenditure so that all expenditure on ageing remains unchanged. We emphasise that such extremely high rates of productivity growth are not considered in the least realistic, but serve only as a measure of the size of the sustainability problem of the fiscal system.

This is also clearly shown in Table 3, which shows the necessary but unachievable wage growth lag after productivity growth in order to maintain government expenditure on healthcare or long-term care as a percentage of GDP at the 2016 level.

## Conclusion

From the results of the analysis, we conclude that good solutions are becoming more and more difficult to implement because the additional required increase in labour productivity by more than five percentage points annually is by no means achievable, due to changes in the pension legislation and taking into account the effect of healthcare and long-term care. The longer the delay, the greater the necessary cuts to all kinds of rights, which can lead to intergenerational conflicts, great dissatisfaction, and sharp political changes, especially in the direction of the extreme. The social partners (including the National Assembly, which we deem extremely important) have not only closed the “window of opportunity”, but continue to take actions that make the situation even worse. Thus, in the future we see the dangers of a black scenario of increasing risk of poverty (especially for pensioners) and social instability, with all their negative consequences.

Already the current social market model of social order is not sustainable, and we are further deepening it by the logic of “solving”, for instance, the economic situation of pensioners by increasing pensions, which is financed by reducing investment in assets (e.g. infrastructure) and knowledge, and in times of stagnation or recession, we will also have to borrow funds. Increasing pensions is justified by GDP growth, although pensions should not increase with GDP growth, which is a result of a more active population. This increase in goods belongs primarily to the additional active population, and the remainder to the additional pensioners.

In short, we are spending today and not investing for tomorrow. As in the case of environmental issues, the disenchantment may be very painful.

## **SCHEME 1:** HOW TO REACH THE DEVELOPMENT AGREEMENT

Each social group commits itself to the implementation of certain measurable steps over a period of time and is rewarded for increasing (or reducing the required increase in) productivity. In the first phase, the social partners include employers, employees, the state. Some illustrative commitments (limited to three) for productivity growth:

### **EMPLOYERS:**

1. Improving the leanness of the organisation;
2. Capital investment,
3. Investing in company-specific knowledge and training of employees.

### **EMPLOYEES:**

1. Productivity-linked pay system;
2. The labour market with flexicurity and work pays off;
3. Lifelong education (including for retraining).

**STATE:** in addition to measures to increase work activity:

1. Rapid improvement in the health of the population;
2. Complete and accelerated removal of administrative burdens;
3. Accelerated improvement in management of state-owned companies and the rule of law.

### **EXTENSION OF THE MOST EFFECTIVE COMMITMENTS TO OTHER STAKEHOLDERS.**

## **SCHEME 2:**

### UNUSED RESOURCES TO INCREASE GDP LEVEL

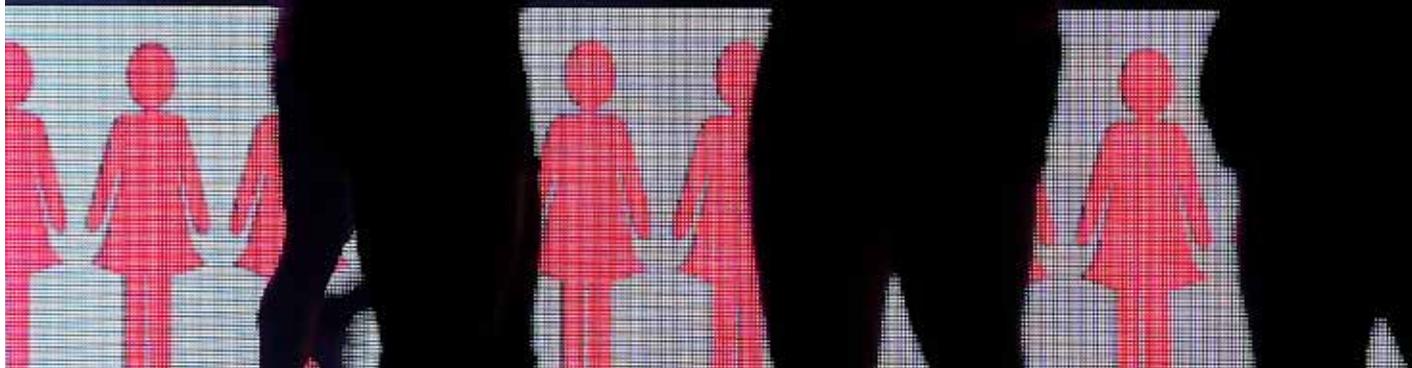
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#### **I. CHANGES IN WORK ACTIVITY: LET WORK PAY OFF!**

1. Increasing employment rates in older age classes:
  - Pensioners allowed to work without loss of pension;
  - Between the ages of 55-64: A more appropriate active employment policy, social transfer policy should not indent into the attractiveness of work;
  - Arranging the labour market towards flexicurity;
  - Increase in the required retirement conditions.
2. Increasing youth employment rate for increasing the efficiency of education:
  - Abolition of graduate status;
  - Abolition of diploma theses at the first level;
  - Introduction of full tuition fees for studies beyond the number of years of the study programme;
  - Promotion of the equalisation of the old system and Bologna undergraduate programmes.
3. Higher net migration: poor demographic image of growth.

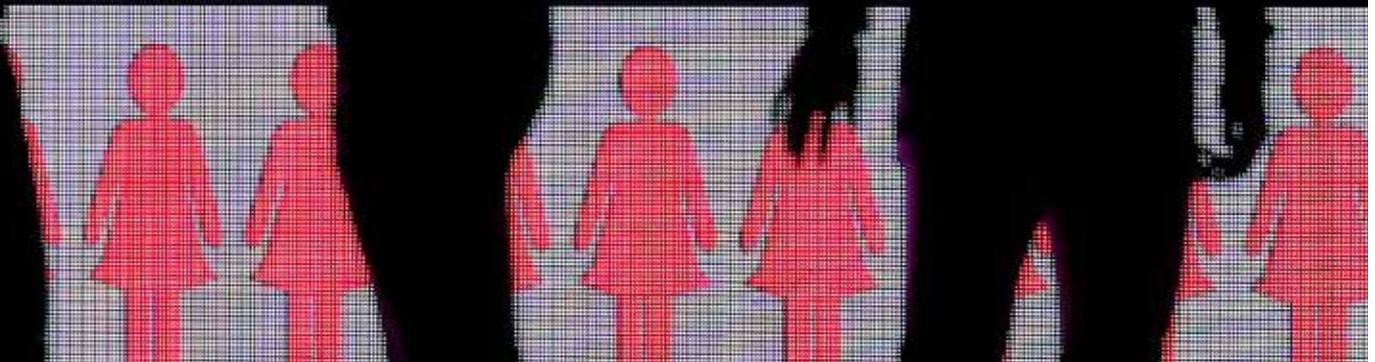
#### **II. CONTINUOUS INCREASE IN CAPITAL EQUIPMENT**

1. Accelerated investment in critical infrastructure (railways, scientific equipment and premises, regional roads, electricity distribution, 5G, etc.);
2. Promotion of private investment, especially in R&D;
3. A high-quality, professional financial system, institutions and markets;
4. Encouraging the introduction of artificial intelligence and robots for simpler work.



### III. CONTINUOUS INCREASE IN TOTAL FACTOR PRODUCTIVITY

1. Changes in political decision-making – long-term and effective;
2. Reducing political influence in state-owned companies;
3. Rule of law: rationalisation and measures to eliminate bias;
4. Sound public finances: (countercyclical)
  - Relatively low public expenditure;
  - Balanced budget;
  - Low public sector debt;
  - Competitive revenue structure and efficient expenditure;
5. Objective: highest quality staff in terms of knowledge, competence and culture;
6. Significant improvement in the sphere of R&D:
  - The "wise men" group directs technology research and development;
  - Forming nuclei of the best researchers and technologists;
  - Increasing R&D teams;
  - Merging of institutes with universities;
  - Proven cooperation with industry;
  - Reducing pedagogical obligations to the international level;
7. Improving public sector efficiency and reducing administrative barriers;
8. Encouraging the diversification of the economy towards high value-added products and services.



## Violeta Bulc

### **European Commissioner for Transport (2014–2019)**

Bulc earned a bachelor's degree in Computer Science and Informatics at the Faculty of Electrical Engineering, University of Ljubljana, Slovenia, as well as a master's degree in Information Technology at the Golden Gate University of San Francisco. She then worked as an expert for wide area networks performance analyses in California. In 1994 she returned to the then-independent Slovenia, where she worked, among others, in telecommunications, and from 2000 to 2014 as the founder and CEO of Vibacom Ltd, consulting on sustainable strategies and innovation ecosystems. She served as Minister without Portfolio responsible for Development, Strategic Projects and Cohesion and Deputy Prime Minister in 2014 before joining the European Commission.

# An invitation to the European Green Deal

As I was preparing to write this article, a question silently crept up on me: how did we arrive at this point in the first place? What point? you ask. The point where we must make GREEN the key objective in our social development. What has gone wrong? Which step in our development has led to a situation in which we are threatening our own existence? Which part of the human brain has gone mad, without inviting our hearts and souls to go along? Is it an aspect of evolution? Is it part of our mission? Have we really developed only to colonise the universe?

The latter would perhaps explain this exceptional focus of our civilisation on technological progress, individuality, reason, and accumulating wealth. Or, perhaps we are developing science and artificial intelligence at a fast-enough pace to save ourselves as a species in this time of major climate change?

Several ice ages have taken place on our planet Earth throughout its billions of years of existence, but in the relatively short span of time since the Industrial Revolution, humankind has been severely encroaching on natural processes. Through this behaviour, we are facilitating cycles of change which have become too fast, too violent and too terrifying for human beings to deal with. Are we still capable of adapting to them? The situation is serious.

## Entering a new civilisation paradigm

All the questions asked in the introduction will perhaps remain unanswered at the end of this article; they will continue to silently provoke many debates. My intention is to encourage us all to take a deeper look into GREEN. To move from problems to possible solutions and, by doing so, support our belief that we still have a chance to ensure a future on the Earth for human beings.

GREEN is not only the colour of nature, money and new European strategies; it is the colour of one of many possible future scenarios. In order to understand it and perhaps actively participate in its creation, we must feel it deep inside ourselves. We must look at it with an expanded consciousness, which dares to explore beyond the boundaries of the known and which directs our courage towards a new civilisation paradigm; one which ties development to responsibility and social welfare. One that

is prepared to accept that it is we who are the beginning of a new "eco-civilisation".

The changes ahead of us are too thorough to be implemented only by using common sense. They are too all-encompassing to be crammed into the existing strategies, into the existing political frameworks, into known models. Changes which we will be experiencing at the conscious and subconscious levels during one single generation are a new evolutionary challenge for human beings. In doing this, we will need planetary consciousness, understanding of the planetary sense. Even more than today, we will need breakthrough innovation in our behaviour, relationships, and social and political models, in business and technological solutions.

So let me encourage you to recognise the weak signals around us that will lead us to sustainable coexistence with the planet, so that we are able to detect the vibrations which announce a new evolutionary momentum in society, new ways to create value, governance, cooperation, co-creation, integration and co-determination. At the same time, I would like to express the belief that the sources of sustainable innovation are hidden in inter-structural connections in horizontal models connecting experience, knowledge, and findings from various fields, generations, continents and civilisations. All this calls for an expanded human consciousness that will increase the resistance and adaptability of us all.

## The EU and climate change

A four-year all-European survey and analysis of the situation in the European transport sector, by member state and by individual transport mode, clearly shows that the EU faces a trillion euro in negative consequences a year in this area alone. It could be called social damage, or the cost of development. The number represents 7% of the gross domestic product (GDP) of the European Union and includes the consequences of pollution and emissions, 25,000 people killed and 136,000 seriously injured on European roads, the consequences

of traffic bottlenecks and related losses, failed investments, and deficient maintenance of investments. It is clear from the analysis that traffic is the second largest polluter. It generates 30% of all emissions, with cars contributing a 60% share. At the same time, transport is one of the fastest-growing sectors in the EU, with 90% of consumed fuel still being based on petroleum.

The energy sector, which is still largely dependent on fossil fuels, remains the largest polluter. However, if energy losses due to inadequate construction of residential and industrial buildings, energy-hungry products, and the lack of efficient (smart) system management is added to this, we can detect opportunities in addition to problems. Agriculture is also placed close to the top of the list of the worst polluters, due to the lack of a long-term global strategy, which would enable farmers to restructure their farming activity by means of smart tools and services, understanding of biodynamic models, and appropriate analytical tools for efficient and nature-friendly management. We must also mention the pharmaceutical and beauty industries, which destroy oceans, rivers and land through "micro" influences that are mostly invisible to the human eye.

The oceans are the largest suppliers of oxygen on the Earth, while at the same time the most endangered. The European Commission has been successful with measures to reduce the use of plastic. The mandatory discharge of vessel waste in European ports, and the acceptance of old fishing nets and waste collected by fishermen at sea free of charge are just two examples. It is true, though, that human intervention in the oceans and forests has been so deep that we are justifiably concerned whether their regeneration, and humans continuing to coexist with them, is possible at all.

The "scream" by the young Greta Thunberg is completely justified – as is her message. Young people are showing us the problems; it is incumbent on us, the active population, to take measures, not only for the sake of economic goods, but for life itself. It must, therefore, come from the heart.

## “Vision Zero” by 2050

Examples show that we have “surrounded” ourselves by development, which brings with it something else besides progress. It is time for wisdom, science, action and political commitments fuelled by the energy of the heart. I believe that our negative impact on the planet may be compensated for by knowledge, behaviour and cooperation. The “Vision Zero” by 2050, which has been set by the European Union, is feasible, but only by means of technological progress and the previously mentioned innovation at all levels. But even this will not be enough. The challenges call for a universal social contract which would carry social justice at its core. The flow of climate refugees will continue to increase, as there will be ever more areas in the world where climate conditions will throw people into a state of desperation, and generally increase susceptibility to extremist movements.

Of course, several scenarios are possible. I will leave it to you to allow yourself to dream about the different paths. I personally pursue the one about the co-creation of an “eco-civilisation” based on a global awareness of the Earth as our common home. In the remainder of the text, I will think along with you about GREEN in the European Union, in Slovenia and the world.

## A “Green Deal” for a carbon neutral Europe

Together with the European Council and the European Parliament, the European Commission built foundations during the term of President Barroso, enabling the Juncker team to assume the role of global promoter and leader of the GREEN transformation. The president of the new Commission, Ursula von der Leyen, has set a “Green Deal”, together with “Digital Europe”, as her two main priorities, so that Europe can become the first carbon neutral continent.

According to a survey, more than 90% of European citizens demand solutions for climate change management. The political framework is clear, and so

is the will of the people. Now we need the open and honest cooperation of everyone so that the “Green Deal” will also be inclusive, and that we will ensure social justice while at the same time maintaining an open market economy based on respect for multilateral agreements and non-discriminatory and mutual rules. The EU is, without any doubt, capable of realising the objectives set by the “Vision Zero” by 2050, but we will need more than eight member states to make the commitment to reduce emissions by 55% by 2030. I invite Slovenia to recognise the green agenda as its strategic lever and join the first group of countries to adopt the relevant legislative commitments towards this objective.

Establishing and promoting global commitments will be a greater challenge. Pollution does not respect national borders; this is why only global solutions are sustainable. The US president, not being inclined towards multilateral global agreements and turning a blind eye to climate change, brings unnecessary obstacles to the search for global solutions. The very poor starting positions of China and India, which are still suffocating as their air quality continues to deteriorate, reduce the ambitions and impede the reactions of the global community. The same applies to Brazil and Turkey. What we would also like to see is a more active and inclusive Russia, which is on its own in looking for solutions to the catastrophic consequences of the warming of the Siberian tundra and taigas.

Thankfully, there is scope for global action. More than ever, the United Nations is the key facilitator, motivator and supervisor, bringing even diametrically opposed opinions to the same negotiating table. The first results are already here. In the field of transport alone, in the last three years we have reached historic agreements for the reduction of pollution and emissions in aviation and maritime transport (ICAO, IMO); gradually, but ambitiously, with a commitment to a constant increase in development ambition and innovation. If the EU wants to lead a GREEN transformation, then it must establish a global “Green Deal” in addition to the European “Green Deal”. The time is right.

## What can we do today?

Where should we start, and where should we continue? Let me illustrate the contents of the "Green Deal" in the field of transport, since I have been actively co-creating them for the past five years. In transport, legislative and operational changes take place at three levels:

Firstly, in the "front loop", which includes the production of vehicles, vessels and aircraft with alternative propulsion systems or renewable fuel, we envisage the construction of an infrastructure for access to renewable sources of energy; the development of services connecting public transportation with models from the sharing economy on the basis of need; innovation in the behaviour of passengers, with a transition from the ownership of assets to the use of services; and a transition to automated and autonomous transport in order to increase the efficiency of the use of resources and time and the smart planning of cities, which at a fundamental level reduces the need for mobility, or provides integrated transport services from door to door. We have already created basic regulatory frameworks and standards for all fields, which will be further strengthened in the new mandate.

Secondly, in the "reverse loop", which includes the production of electricity, we plan a transition from petroleum sources to renewable sources, combined with nuclear energy, and a reduction in the EU's energy dependence on third countries.

Both loops have a completely different time horizon. While major changes in the first of these may be expected in 10 years, the second loop needs at least 30 years.

Thirdly, in the mutual close cooperation of the telecommunications, energy and transport sectors as a single ecosystem, we will encourage the provision of smart solutions which will reduce the need for mobility by better planning, and improve the efficiency of energy use, for example, with smart dynamic energy and digital networks. The latter is

also an innovation in the proposed new EU budget for the 2021-27 period, which envisages more than 70% of all investment being in GREEN transport, with the highest rate of co-financing being intended for projects which include partners from all three infrastructural fields.

It is investment and innovative breakthroughs that will ensure the implementation of the European Green Deal. During my term, almost 70% of investment in transport, out of a total of 240 billion euro, was intended for the reduction of sound and air pollution and the finalisation of cross-border connections for efficient logistics and passenger services. An emphasis was placed on the modernisation of the railways and digitalisation. A legislative proposal which would bind public institutions to using green mobile solutions is still awaiting confirmation by the European Council. It is public institutions which are able to lead the green transition at the local level and, by example, enable the economy of scale needed to lower the prices of green vehicles.

We have also developed numerous innovative financial mechanisms that attract private and institutional investors, such as, for example, the introduction of clean buses in public transportation, the development of multi-modal logistics and passenger hubs, micro-mobility services, and tolling. Investment will also be key in facilitating the development of breakthrough innovations, such as, for example, electricity storage facilities, a new generation of recyclable batteries, signalling systems for better management and utilisation rates, new propulsion systems, artificial fuels, autonomous solutions, artificial materials and intelligent sensors for proactive maintenance and prevention of accidents. An important green development impetus has also recently been provided by the European Investment Bank (EIB), which announced the start of a process of transformation into a green bank and a shift from investments related to fossil fuels. The latter will also have a strong influence on the development of national promotional banks, such as, for example, SID Banka in Slovenia.

## What about people?

Not technology, but people are the focus of a green transformation. For this reason, the development of competence, expansion of new knowledge, new forms of participatory co-determination for empowered people who will be capable of recognising opportunities, and the implementation and adaptation of projects is included in all efforts. In the field of transport, for example, there is a social partnership in the maritime sector, where social partners and industry have concluded an agreement on the development of new knowledge for the needs of green and autonomous maritime transport, and on transferring numerous operations from shops and ports to digital offices. This positive experience is already making its way into other areas.

## And where is Slovenia?

Slovenians are environmentally aware. We are one of the most successful EU member states in recycling. Our national flag is green, and cleanliness is one of the first impressions of Slovenia noted by tourists. Numerous companies are adding environmentally friendly solutions to their socially responsible elements of operation, and energy efficiency is one of the most frequent mechanisms for reducing costs.

What is lacking is an umbrella project which would enable every craftsperson, entrepreneur or manager and every citizen to be involved to the best of their abilities for the common good. The time has come to create an umbrella "strategic story" of Slovenia, in which green, health and love could perhaps be part of the leading integrated content. Slovenia has not yet managed to find its place in the EU with content with which it can connect other member states as a leading partner. Perhaps it is precisely this green and healthy approach, imbued with people's love of nature and life, that could be installed in the heart of Europe. Industry could thus inspire common values in all its products and services. Schools could encourage the use of environmentally aware know-how in support of the common story. It would then be easier to reach

a consensus that we need a modern railway network, which enables speeds of up to 200 km/h at least between major cities and airports; to establish green zones, in particular in our Triglav National Park; to develop efficient public transportation combined with sharing economy services, both in cities and villages; to adjust legislation to favour ecological products in schools, kindergartens, and public institutions; to sort materials more innovatively, which would make it easier to introduce them for re-use; and to implement "green legislation", which rewards those who successfully implement green solutions and effectively penalises violators. It is time to transform opportunity into concrete value and create a framework and mechanisms in our space which help people decide where to direct their investments and be educated for the future, and how to engage their creative capital.

## We can come out of the climate crisis as winners

All activities at the level of the European Union lead to the realisation of a sustainable society that recognises the circular economy as the foundation of the future economic model. The "Green Deal" and a clear "Vision Zero" by 2050 provide political and long-term strategic frameworks which ensure predictability and are necessary for the transparent and effective integration of whole ecosystems. But for humans to continue to coexist with all the other creatures on this beautiful Earth, we will need, in addition to reason, to also courageously activate the heart, spiritual and social dimensions. Only when we, as individuals, get to comprehensively understand ourselves as humans, and allow ourselves to personally develop, will we contribute to society, living to the fullest and shining in a better, inclusive and sustainability-oriented world. I believe that we are on the right track. We should thus support each other in our everyday efforts so that GREEN will not only be a part of our strategies, but an element of everything that we are. It is true that sometimes we only need an incentive to dare to be on the right side of history and also co-create it by doing so. I am on board. Are you?



## Verica Trstenjak

### **Professor of European Law and Civil law**

A former advocate general of the Court of Justice of the European Union (2006-2012) and a former judge of the General Court of the European Union (2004-2006); as advocate general she significantly contributed to European law, particularly in the fields of consumer protection, intellectual property, public procurement, state aid, asylum, and fundamental rights and freedoms in the EU, among other things. She is a lecturer in European Law in Vienna, Ljubljana and Maribor. She was a visiting professor at several universities in the EU and worldwide (for example, in Hamburg, Ferrara, Zürich, The Hague, Amsterdam, Montreal, Sydney, Los Angeles, San Francisco, New York, and Kyoto), and gives lectures at various international conferences. She has published several books and over 250 articles, most of them abroad. She is a member of the Executive and Management Board of the European Union Agency for Fundamental Rights in Vienna and member of the Permanent Court of Arbitration in The Hague.

# The rule of law and private property – what do they mean for the economy?

A discussion on the rule of law in society is necessary for the sake of everyone, not (only) the politicians, officials, judges and others who make decisions about us and our rights. Although the rule of law has functioned quite well in Slovenia, there are areas which must be improved.

Only an effective rule of law will also ensure the efficiency of the economy. As an effective rule of law requires an efficient, independent and impartial judiciary and administration, as well as the active exercise of rights (for example, social rights), there is no place for corruption. The rule of law must be present at all times, night and day, when the sun shines and when it rains. The authorities should not be making excuses that there is a shortage of officers, that there are too many applications, and so on; they are the ones who must make sure that the rule of law functions and that its principles are respected by everyone.

Businesses must demand the effective and trustworthy functioning of the rule of law, and the state must provide a clear and predictable legal system and an efficient judiciary, state administration and legal security, as well as protecting investments, property and freedom of contract. Businesses have a legitimate objective – profit – but they also have to take social responsibility for people and their dignity (including by providing appropriate pay), as well as responsibility for the environment, so that our planet is preserved for future generations. Only a successful economy can provide for a wealthy, successful and welfare-oriented society, and the state must provide the conditions for this and let businesses operate under market principles.

I would also like to discuss the rule of law in relation to the EU. The rule of law is one of the fundamental values of the EU, listed in Article 2 of the Treaty of the European Union. The values of the EU include respect for democracy, equality, the rule of law and human rights. If a member state violates these rights, the EU may launch proceedings against it (as is the case with Poland), and high financial penalties may eventually be imposed on that member state. The EU may also initiate a political procedure which does not involve the European Court of Justice, where political sanctions could be possible (for example, stripping a member state of its voting rights).

What should I say to businesses and managers in relation to the rule of law? As we celebrate the 10th anniversary of the Charter of Fundamental Rights of the European Union on 1 December, let me first focus on the rights listed in the charter that are most relevant to businesses. It was this charter that gave the fundamental rights their importance in European constitutional law. It deals with certain rights which are of specific relevance to businesses, among which the right to property and free economic initiative should be particularly emphasised.

The **right to and respect of property** is one of the foundations of society and the rule of law in democratic systems. In some systems which had to make a transition to a democracy in which all human rights are respected, the right to property is still sometimes subjected to unnecessary limitations or is, at least, not respected enough. Apart from providing us with the opportunity to be independent and creative as individuals, the right to property is also crucially important for the economic development of society. Neither your neighbours nor the state may encroach upon your property. The right to property is important for business entities, and it is

also important in the area of intellectual property; for example, brands, patents, and copyrights. Private property also means property that we manage and dispose of independently. The judiciary is the system that ultimately prevents possible interventions or abuse of property, as is the case for all aspects of the protection of rights.

The EU Charter of Fundamental Rights contains another right which is of exceptional importance for businesses: **freedom to conduct a business**. Companies refer to this right in numerous procedures. The state must refrain from unnecessary limitations and must prevent this right from being violated. Of course, it must be remembered that this right is not absolute; there is almost always a conflict of interest between several rights. One example of this is Google, which refers to this right when it publishes personal information, while ordinary people, responding, refer to our rights to privacy and protection of personal information. It is the courts that decide which right outweighs the other in this and any other conflict. At the national level, this is a Slovenian court, including the Constitutional Court, while at the European level, the European Court of Justice prevails. The European Court of Justice has stressed the importance of free economic initiative, which includes the right to carry out an economic activity, freedom of contract and free competition, on several occasions.

## Businesses and the public sector

Businesses take responsibility for development – both their own and that of society as a whole. However, the political system, and in particular the entire public sector, must create an appropriate and, especially, a stimulating environment for this development by levying appropriate taxation, facilitating respect for private property and free economic initiative, and by being more efficient. Businesses and the private sector, meanwhile, ensure development and enable the functioning of the public sector, healthcare and education systems, and transport infrastructure, as this is provided by the taxpayer. This is why it is necessary to have a cooperative effort in which

the public sector provides, through its work, an appropriate and stimulating environment for economic development. The entire public sector must ensure that the rule of law is respected and that business rights are protected.

## The importance of an efficient public sector

Around the end of the last year we mentioned the **problem of the new Karavanke Tunnel** and the fact that, while Austria was already building it, procedures to select the contractor were still taking place in Slovenia. What has changed since then? Austria is continuing to build the tunnel, while procedures in Slovenia are still ongoing. An optimist would say that this is because legal protection in Slovenia is at a higher level – and that trust in the law is necessary. A realist would also warn about trust in the law, but additionally be concerned that regulations and their implementation must not only be lawful and just, but also effective. Why? The process of public procurement, which is involved in the construction of the Karavanke Tunnel, is regulated at the EU level by directives which apply equally to Austria and Slovenia. Both countries must respect them; they have adopted laws and they must implement them. A pessimist would say that nothing works in Slovenia and that abuse and corruption are everywhere. So why is Austria already engaged in building the tunnel? Where regulations are effective, authorities apply them efficiently and make decisions impartially and independently, and the people trust the bodies which implement them. If someone violates the regulations, they do not call on the assistance of an acquaintance or friend from a political party, but, if a violation is established, they are held responsible and, consequently, face a prison sentence. The fact that the contractor selection procedure is still ongoing in Slovenia does not mean that the rule of law is at a higher level here, but that our procedures are more complicated and inefficient. This is not a criticism of the current authorities which are implementing the procedures, but more of the entire system, from laws and other regulations to the organisational structure and lack of responsibility, all of which make procedures take so long.

Too many times we focus only on the judiciary when it comes to the functioning of the rule of law. But **efficient public administration is what an economy needs to be effective.** It is in this area that many foreigners point to problems, in particular in relation to the construction of commercial buildings and permits for activities. Public administration should be there for the people, and not vice versa. The Office of the Human Rights Ombudsman has warned that lengthy procedures are not only a consequence of overload, but also of arrogance. Other supervisory bodies also need to contribute major input to ensuring the rule of law; here let me mention **inspection services.** Another aspect of the rule of law is that those who violate regulations must be held accountable. The public administration must be organised and function in a way that ensures that violations are identified, legally sanctioned and eliminated. In Slovenia, the most often asked question is not who committed the violations in the first place and what the penalty will be, but who informed whom that the regulations were being violated, and who was responsible for pointing them out? If a violation takes place in Austria, the perpetrator is punished, possibly with a prison sentence, as was the case recently with an abattoir in Styria which sold meat unsuitable for sale or consumption. The person responsible is now in detention.

The inefficient way in which regulations are implemented in Slovenia is shown by the case of a reader who forgot to collect their cash from an ATM. The person who found the cash handed it over to the police – who took months to return it to its rightful owner. Or when someone points to what are, in my opinion, aggressive business practices, or at least unfair contractual terms, when it comes to paying an internet service provider after the subscriber's death, and inspectors say that they cannot take measures. In foreign countries, proceedings against a company which pursues aggressive business practices are launched by an inspection or consumer organisation, making sure that such practices are changed or abandoned. Another example is counterfeits of renowned brands being sold in the middle of Ljubljana, which hurts not only the companies which own the brands, but also Slovenia's reputation. Protection of ownership rights, including

that of intellectual property, is one of the foundations of the rule of law. Finally, let me also mention the inefficiency of the Slovenian state administration in drawing on European funds, at which we are one of the least successful countries.

**The public sector must also take its share of responsibility.** Since responsibility in the public sector is not as direct as it is in the private sector, where you can lose (your own) revenue or even go bankrupt as a result of mistakes, there are frequent attempts to blur it. The case which prompted me to point out that it is the people who have done something wrong that need to be held accountable, and not those who have warned about it, is (again) the case of arbitration on the border between Slovenia and Croatia. We are yet again discussing where and how a Slovenian agent and an arbiter talked to each other. The point is that a judge, or in this case an arbiter, must be independent and impartial. They must make sure that no one influences them. Who is responsible for us making a mess of the arbitration and being humiliated in front of the whole of Europe? It was not Brussels or the Croatians, but us, because our arbiter and our agent talked to each other. Then someone is saying that they did not violate the rules because they talked over a "standard" phone line. Any student at a faculty of law would recognise that it is inconceivable for a party to call a judge! I cannot imagine an official ordering an arbiter to make a specific decision in a 'normal' country. It is true that the mistake was sanctioned during the arbitration procedure (with a new arbiter being appointed). But who should be blamed for the additional costs related to the new arbiter, for the procedure becoming prolonged, and for Slovenia losing some of its reputation among international and arbitration jurists? Media hold up a mirror to those who are unable to look at themselves in it!

## Adria and the rule of law

What has Adria to do with the rule of law? Some time ago, when Adria Airways was not yet in receivership, we read in the newspapers that one of its aircraft had been temporarily seized in Vienna

until compensation was paid to a passenger for a delay or flight cancellation. This was possible because the Austrian legal system works, because court proceedings there are fast, and there is trust in legal protection. Specifically, every passenger has the right to compensation in the event of the delay or cancellation of a flight. This is stipulated by both the EU's passenger rights regulations and case law of the European Court of Justice.

Exactly this happened to me a few years ago, in 2013. When I requested compensation from Adria (which was still state-owned at that time), my request was rejected, with the argument that – to put it simply – it was not bound by EU law. I got the same answer from the Civil Aviation Agency. Since the law was not being respected and damage was being done to Slovenia's reputation, I sent a letter to the office of the then Prime Minister. They got rid of the problem there and then by forwarding my letter to the relevant ministry (solving a problem by making it someone else's problem is a frequent practice in administration in Slovenia). If I had been a resident of Austria at the time, I would have sued the company in the Austrian courts, which could order Adria to pay compensation, as in the case of the passenger in Vienna – who managed to ground an Adria aircraft with the threat of a lawsuit! Since I knew that the procedure in Slovenia would take too long and cost me too much time and energy, I did not sue – because my trust in legal protection was not as high as it would have been in Austria.

## The judiciary and the rule of law

Last year I wrote about the **judiciary** and its influence, not only on the state of the rule of law, but also on the economy. Although statistics for the judiciary are showing a constant improvement, there is an urgent need for further advances. The statistics showing that Slovenia has the highest number of judges and highest costs per capita are still valid. I think that we do not need additional judges, but more efficient ones. I have warned several times that justice delayed is justice denied (*tarda iustitia non est iustitia*). But I see real problems in the lack of understanding of

independence and impartiality. A judge must have that as a fundamental guideline, in addition to fairness and justice. If judges do not have these values, they are not suitable for the job, which is also true of the Constitutional Court. A lie is a lie, even at the level of the Constitutional Court. **A judge's impartiality is the essence of the rule of law, and a judge's lie is a matter of the moral and ethical suitability of that person to be a judge.** Who would continue to trust such a judiciary?

I frequently ask my students what values are important for judges. They do not mention fairness and impartiality. Although they are in their final year of studies at the Faculty of Law, they have not yet seen the Code of Conduct for Judges. They are learning articles by heart, instead of learning about modern interpretations of law and what values a judge should have. However, the judiciary must also be provided with material conditions for work, and appropriate pay.

Like independence, the impartiality of a judge is also the essence of the rule of law, and violation of the principle of impartiality is a violation of a principle of the rule of law and the EU Charter of Fundamental Rights. Article 47 expressly stipulates the right to be tried by an independent and impartial court. In addition to the currently topical issues, what has proved to be a problem in Slovenia on several occasions has been judges commenting on political events, even though such comments were not made by them in their judicial capacity. The evaluation of the impartiality of a judge has a strong bearing on whether or not this should be allowed.

In a country where the judiciary enjoys a good reputation, trust in it is extremely important. In Austria, for example, the judiciary itself ensures that a judge who violates the principle of impartiality is sanctioned. The judge who expressed a political opinion on social networks about a former Austrian politician ("Why does Germany not have politicians of the Grasser type?" [Author's note – the former Austrian Minister of Finance]), was disciplined and had to pay a fine amounting to a month's salary. It was the decision of the Supreme Court of Justice of

Austria. In Slovenia, judges comment on political affairs even when they are ruling in a related case, and even attend political rallies related to parties involved in their cases. What needs to be established in such instances is a balance between freedom of political expression and ensuring impartiality. The judiciary must rebuild its reputation in society by itself; it is not people or politicians who have tarnished this reputation. But I must emphasise that politicians must express their opinions about the judiciary in a respectful manner, and criticism of the judiciary in society must be kept at a professional level. The judiciary will gain a favourable reputation by responding to mistakes that are drawn to its attention and eliminating them, not by sweeping them under the carpet. Even if the currently topical case at the Constitutional Court does not draw a response, this will not improve the reputation of, and trust in, the judiciary, but further reduce it, including in the Constitutional Court, which must be the home and pillar of law and justice, providing everyone with the reassurance that they live in a law-governed state.

### Trust in law, legal security, fairness

In Slovenia, the problem of trust in the law, in the work of state bodies and the related level of legal security lies not with the EU, our neighbours, the Croatians or President Trump. The problem is in the quality of laws which we write ourselves, in the non-implementation of laws and regulations, in their being by-passed, and in the lack of sanctioning of their violations by state bodies. The problem is that those who violate regulations are frequently regarded in society as heroes, not villains. People like this should instead be despised and ostracised by our society. What we also lack are higher moral standards that can be upheld against people who violate the law; against those who, as we would say, are “resourceful”. Such people deserve to be legally punished in accordance with the law, and to receive additional moral punishment by being excluded and despised, because they are taking something away from your children, not from the state or someone else.

### The state as a saviour?

Who or what is the state? Every now and then you may hear claims that the state will do something, that the state is responsible, that the state has failed to do something. Who or what is the state?

Everyone needs to take their share of responsibility. While we have mentioned several areas where improvements need to be made, there are also many which makes us proud of being Slovenians. There are numerous successful companies, researchers, artists, athletes – the list goes on. We can be proud, if I may say so, of the good and gentle Slovenian heart when we help those in need (including on the occasions when the state or the public sector has failed). This is also where our character shows a little bit. A Slovenian (unfortunately) does not condemn a Slovenian who does not pay taxes, but they do condemn one who does not donate to a humanitarian cause. When they start condemning both, the rule of law will be functioning more effectively. Then we will be closer to our ideal, Switzerland; the country where corruption and the failure to pay taxes is almost as despised in society as murder.

### We as a saviour!

The state is actually made up of the bodies that we have elected. If a (written-off) debt to the state gets paid by the state, the debt will actually be paid by you and your children and grandchildren. If successful managers have been replaced by the state, this has been done by politicians who have been elected by you or by voters who are not reading this. Only we, and no one else, can change things. We have the right and power to decide because we live in a democracy. This is why we must demand our rights, and exercise them, too. When we vote in an election, we exercise our rights. Just as we fought for an independent Slovenia ourselves, we can also make Slovenia even better. I wish you a lot of courage, success and love (to your homeland) in 2020.

## Vojko Čok

**President of the Honorary tribunal of the Managers' Association and Honorary Reward receiver at its 30<sup>th</sup> Anniversary.**

Long-time Chairman of the Management Board of Banka Koper (today Intesa Sanpaolo Bank) and later its Chairman of the Supervisory Board.



PHOTO: Arhiv ZM

Ethics, property and free entrepreneurial initiative together as a prerequisite for a thriving economy

A thriving economy is a fundamental condition, although not in itself sufficient, for prosperity and a flourishing society. There are many answers to the question of which criteria must be fulfilled in order for the economy to be successful. Many are contradictory, but they may still be correct because of the assumptions on which they are based. The answers for which there are no major differences concern private property and free entrepreneurial initiative; factors that significantly shape the competitive environment.

With regard to the authority of property, how it was acquired is important, while respect for the public interest is essential for free entrepreneurial initiative. Under the rule of law, both are important starting points in assessing the credibility of the legal system. This builds economic confidence, not least among the citizens.

Unfortunately, it is often shown in practice that trust in the rule of law can be a perishable relationship, even when there are not always clear legal reasons for this. It is most often generated by socially unacceptable or at least controversial practices that deviate from ethical norms. This is proof that the legal system and ethical norms make a whole, without which it is difficult to imagine a coherent and sustainable social coexistence.

If it is true for legal regulation that everyone is equal before the law, then it is true for ethical principles that example is an effective teacher and that power is established from the top down.

With the changes in the socio-economic system in Slovenia, the institutional attitude towards private property in the pursuit of economic activity has also changed. With privatisation processes, private property has begun to grow rapidly in ways and forms that were not widespread before, although certain basics had already been established. Managerial structures and managers were also significant drivers of these changes.

The higher an individual is on the social ladder, the greater the importance of their attitude towards moral and ethical norms – and managers are very high in these rankings. The social standing of managers gives particular weight to their attitude towards morally

ethical norms. The greatest guarantee of their respect, and this is confirmed in practice, is appropriate transparency of operation, which is a crucial safeguard against temptation. Morally ethical norms are also a constant in business life.

In the absence of experience and legal solutions, which had many gaps or inconsistencies, and with an unadjusted legal system and initially with an uninvolved public, forms and methods of privatisation developed. This initially aroused attention and concern, mainly due to inconsistency in the general ethical principles, especially the principles enshrined in the Code of Ethics of the Managers' Association.

This has raised considerable concern and dissatisfaction in members of the Managers' Association (ZM), especially the younger ones, and has undermined and compromised the reputation and credibility of the Association, its members and the managerial profession itself among the general public. For this reason the ZM Honorary Tribunal declared that there were ethical deviations in the privatisation procedures, although not in the concept of privatisation per se; decisively and publicly declared them unacceptable; and acted accordingly. It should be emphasised that business results were not a criterion for assessment. This is the responsibility of other authorities. The basic guideline of the Honorary Tribunal in assessing the conduct of the members of the Managers' Association was respect for the Association's Code of Ethics. This stance by the ZM Honorary Tribunal was assessed by both the public and members as correct, which contributed to the restoration of ZM's reputation, its members, and the managerial profession. It also consolidated ZM's high position among the most respected and recognised institutions and professional associations in Slovenia.

The experience cited above confirms that the **active involvement of civil society**, especially if it grows into an organised movement, is crucial to the effective functioning of the rule of law in safeguarding the authority of private property, and for maintaining a private entrepreneurial initiative as important components of a competitive environment. By taking this stance, ZM confirmed that organisations in this field could be an important and credible carrier.

# The economic aspects of the absence of the rule of law

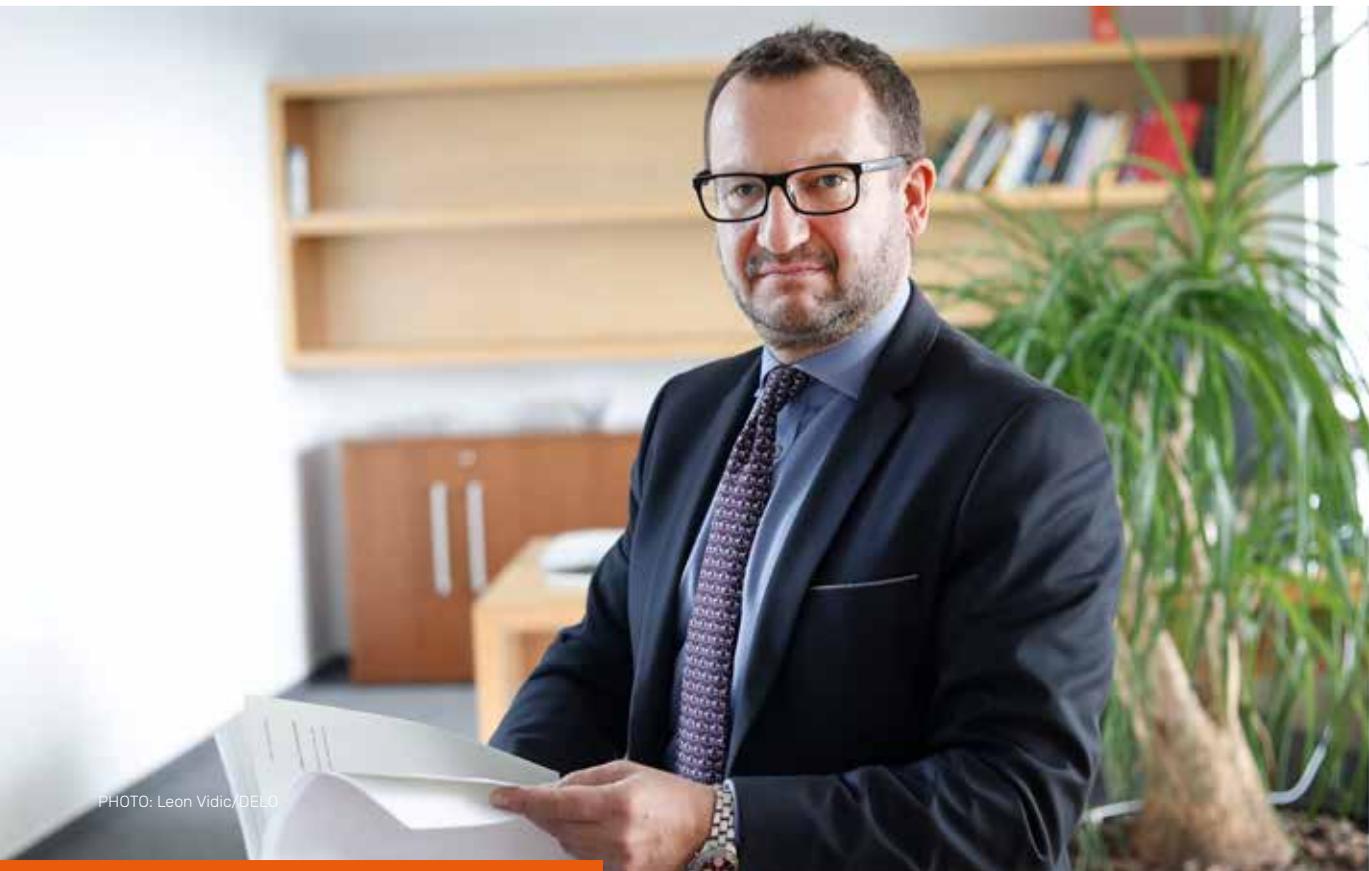


PHOTO: Leon Vidic/DELO

## Sergej Simoniti

**President of the Management Board of Coface PKZ, first credit insurance, and former Director of the Insurance Supervision Agency (2011–2017)**

This article serves to highlight some aspects of the (non-)functioning of the rule of law in Slovenia, especially in the field of economics. I am proceeding from the thesis that the key problem in Slovenia is not the existence of a rule of law, or the degree of the rule of law of a state as opposed to a non-legal or unlawful state, but rather that the economic and wider social environment in Slovenia is characterised by a state of absence of the rule of law.

It is not, therefore, a question of labelling the opposition to the rule of law, in which the legislator, the courts and other stakeholders act in conflict with the principles or procedures of the rule of law. I point to the absence of the rule of law in its positive or negative occurrence. Moreover, I believe that key stakeholders in society (the legislator, decision-makers and, above all, entities, either natural or legal persons) do not, in fact, expect that the rule of law will hold, and abandon their own will to enforce it.

I do not believe in the existence of a "hydra", a para-state, an organised "mafia", or a "string-puller in the background" who runs the economy in Slovenia with their grand plan. However, I do believe in a lack of will for the existence of the rule of law in a large part of Slovenian society. I see it primarily in the wish of the major part of the electoral body that the state should provide for them, and in a complete lack of reasonable expectation that certain institutions of the rule of law will function. In my opinion, respect for, and the authority of, the institutions of the rule of law in Slovenia are at an extremely low level, from the perspective of both the legislator and the decision-making bodies. In many instances, the courts do not have the courage to "materially," in terms of content, decide on matters of conflict; the revenue service prosecutes the little people with meticulous attention to detail, yet often is unable to inspect the sources of the unusually excessive wealth of certain individuals; and illegal construction is our national pastime. I would like to draw attention to the individuals who use the interests of this country for their own purposes, be it individuals who take advantage of state ownership to intimidate the management of state-owned companies, rent-seekers in one form or another that find support in the National Assembly, or anybody else. All of these are symptoms of the absence of the rule of law.

### EU competition rules and the happiness of citizens

The rule of law denotes a set of mutual relationships that exist in society. The fact is that there are many

I would like to draw attention to the individuals who use the interests of this country for their own purposes, be it individuals who take advantage of state ownership to intimidate the management of state-owned companies, rent-seekers in one form or another that find support in the National Assembly, or anybody else. All of these are symptoms of the absence of the rule of law.

countries in the world today that do not conform to the Eurocentric liberal ideals of the rule of law, but this does not necessarily affect the greater satisfaction of their citizens. The present nostalgic flirting with the socialist social order of the past in our local environment is essentially a desire to abolish the rule of law.

The "tragedy" of the Slovenian environment is that we consciously opted for a liberal market economy, and consciously and with great pleasure joined the European Union in 2004. It must be remembered that the basic principle of the EU is the free movement of people, capital, and goods, and that its objective is competitiveness. The metathesis is that EU citizens will be happier if there is a greater degree of competition in the EU market. In the case of the free movement of people, any national of any country can compete in any labour market within the EU. In the field of economics, the EU is trying to minimise national influence, which is where we encounter the absence of the rule of law in Slovenia.

Due to the nationalisation of the banks during the last recovery plan, we were faced with restrictions to the operation of banks that received state aid. Throughout the debate on bank rehabilitation, the arguments regarding the injustice or otherwise of the European Commission's measures were constantly repeated. It is extremely rare in this public debate to hear the contention that illicit state aid leads to a distortion of competition, and that effective competition is beneficial to the Slovenian consumer. Indeed, the rule

of law is not a necessary and universal condition for civil and broader human happiness in our country; yet it is an absolute prerequisite for the functioning of a competitive economy.

Later in the article, we focus on the views, positions, actions, and, in the broadest sense, the state of mind of the following major stakeholders: the legislator, the decision-makers and individual entities, either economic operators or consumers. By legislator, I mean any state body that decides on abstract general legal acts, most often the parliament; and by decision-makers, I mean all bodies that have jurisdiction over making decisions in specific instances, particularly the courts and administrative authorities. I assert that for the successful functioning of the rule of law in all three categories of stakeholders the following four traits are more or less necessary: courage or uprightness, awareness of one's place in the system or competence (procedural aspect), adequate knowledge or understanding of one's rights and obligations (material aspect), and integrity.

### Regulations that are not enforced or are over-regulated, and the problem of social rents

One major sign of the absence of a rule of law at the level of the legislator is the adoption of regulations that are either over-regulated or not enforced at all. Let me give an example from everyday life. A few months ago, I was on my way to the Union Hotel, where the Three Seas Initiative was taking place, and a regional political summit was present. Security was tight and the police officer required identification to be presented prior to entry. Unfortunately, I was not carrying my identity card. The police officer warned me that I should have been fined for this offence. I asked him whether the situation would have been the same if I had been jogging in Rožnik or swimming from the shore to Bled Island without an ID. He answered both questions in the affirmative. Here we have a regulation that we both violated: I, due to negligence; the police officer through maladministration, because I was not fined for the

offence, an action that he probably should have undertaken at his own initiative.

The following example illustrates the misunderstanding of the content adopted by the legislature, and the consequences. In Slovenia, we have a well-established system of worker co-management in companies, which is predominantly based on the German model. The system prescribes the mandatory representation of employees on the supervisory boards of companies. In order to fulfil their duties, workers' representatives must be properly trained to function appropriately in the interest of the company and to represent the interests of the workers. However, the provision that the workers' representatives can only be employees of the same company has crept in, which significantly reduces the pool of potential candidates. Looking at the annual report of a German insurance company, I see that retired insurance salespeople, auditors, lawyers and other highly qualified people representing workers' interests can be found on the supervisory board as employees' representatives. In Slovenian everyday life, instead of a high level of competence for a supervisory function, the starting point is to solve the problem of finding an employee representative who does not have a conflict of interest and fulfils the conditions of relevance and competence.

The absence of the rule of law in the relationship between the economy and the legislator is also reflected in the number of regulations requiring certificates, compulsory training, and mandatory insurance for economic operators, presumably by providing greater security for businesses, employees or consumers. I would argue that the vast majority of these regulations are intended to provide rents to contractors, restrict competition and generally dampen the economy. In reality, this is a general, systemic violation of the constitutional principle of free economic initiative.

This reminds me of a case about ten years ago when I worked in one of the largest insurance companies in Slovenia. I met with a person authorised by the state, an "rent seeker", who came to check the dangers of employment at an insurance company

in accordance with the regulations on occupational safety. We obtained the relevant study on occupational safety and all the employees passed the required test, with the “rent seeker” providing considerable help to us in supplying the correct answers. We then had to monitor our knowledge continually, which meant we took the same test every two years. Because the “rent seeker” nicely provided the answers, we kept her as a contractor. Meanwhile, an occupational safety expert worked to find the dangers, while we pretended to learn about occupational safety, and then we all pretended together to take the test. I wonder if the legislator estimated how much more expensive the insurance policy would be for the Slovenian consumer due to this regulation and its means of implementation.

### Lack of decision-making according to content, and lack of courage and knowledge

The decision-maker, in this case the court or the administrative body, must have the appropriate authority, courage and knowledge to make substantive decisions on a case-by-case basis. My experience in the case of the Financial Administration of Slovenia’s (FURS’s) tax exemption proceedings reminds me of the absence of these virtues, which I have come across too many times. FURS did not treat a stepchild’s inheritance in the same way as it would have if they were in a mother-daughter relationship. The law did not provide for such a case. The Administrative Court (Case I U 941/2017) fortunately established the unconstitutionality of such an approach and annulled the decision.

FURS also fails in some obvious everyday cases of illegality. Years ago, I took my children for a swim at Atlantis one Saturday. A gentleman at the checkout in front of me was settling a bill for a children’s party. He asked the friendly cashier to put it on his “business account”. I seriously wonder how FURS can recognise the cost of a children’s party taking place on a Saturday as a tax-deductible expense. Similarly, I wonder how it is possible for a father to bring a child to kindergarten in a BMW X6, and the mother

apply for a subsidised kindergarten. In my opinion, the failure of administrative bodies, such as tax authorities, represents the absence of a rule of law.

### The integrity of the individual, the will to the rule of law, and understanding the benefits of it

When I worked in insurance supervision, my colleagues at an international level often wondered what the content of the condition of relevance and suitability of a board member or a member of a supervisory board of an insurance company was, particularly in the case of personal characteristics. The views were very diverse; from a purely legalistic approach, from the conditions being fulfilled by anyone who has not been finally convicted, to a completely subjective approach that an individual must have an appropriate “lifestyle” to fulfil this condition. After consideration, we established the substantive criterion that a person in the assessment procedure must not have characteristics that would be incompatible with the conduct of the insurance company in accordance with the regulations. In particular, from the point of view of insurance supervision, it is impermissible for an insurance company to avoid the fulfilment of its obligations. We therefore considered an example to be whether a person who is a member of the board of directors or supervisory board of an insurance company avoids the settlement of their debts by transferring assets to relatives or in other similar ways. When the Insurance Supervision Agency conducted an inquiry into a population of senior executives about the possible evasion of assets, the reactions were, in fact, complete astonishment and bewilderment: “Who does this insurance supervisor think he is?”

The rule of law requires the active conduct of key stakeholders, who must also have certain qualifications: responsibility and competence for such behaviour and, above all, integrity, awareness of their role or competence in the economy, professionalism, and, last but not least, the courage to exercise independence in making their own decisions.

# Silence is not about neutrality, but support for the current state of affairs

We can all agree that good corporate governance is important for the competitiveness of companies.

This quality of management is, in fact, a key risk factor in the future of a company, regardless of the type of ownership of the business or its governance system. This is clearly demonstrated in the case of bad management practices and scandals.

At the heart of quality governance is competent and long-term sustainable management and effective control. Both management and supervisors must act with due diligence and for the benefit of companies, while putting aside their personal or other interests. Good practice can only be pursued by detecting irregularities and pointing out real problems. The current state of mind reflects a worrying decline in corporate governance culture in the public discourse – as if we had not taken significant systematic steps over the last decade to move away from bad practices and the excesses of the more distant past.

This is why the World Bank and the OECD require countries to provide assurances of appropriate legislation and standards in this area, as well as legal certainty, in order to ensure a globally secure flow of capital. The same goes for the European Union and its legislative framework, which the member states must comply with. However, since the most important challenges lie in the actual practice of corporate governance, that is, in its culture and the security of legal transactions, the functioning of the judicial system is crucial to investing in a particular country.

Irena Prijović

Executive Director,  
Slovenian Directors' Association



PHOTO: Mateja Jordovič Potočnik

When investing in an individual company, in addition to its financial assessment, the quality of its corporate governance becomes a decisive factor. All this is necessary in order for capital, which is a timid bird, to flow into the company and remain there at all.

## Supervisors' competencies, opportunity losses, and trading with influence

In Slovenia, where a large proportion even of listed companies are still state-owned, such risks are particularly high, despite well-regulated legislation and recommendations for good practice. The appointment procedures of supervisors are still subject to a certain array of influence, despite the numerous regulatory

measures imposed to prevent interference, such as nomination, accreditation and human resources committees, and the related transparency of procedures. Of these, the most obvious are political influences through a system of “political quotas” which allow winning parties to distribute their influence. This means that supervisors do not become experts, but political friends, executors of instructions, and traders with power. Certainly, the original sin is that someone even wants such a supervisor, who is like a puppet in a puppet theatre, with invisible strings to be pulled up with a hand when voting on the supervisory board, and at the first important decision of the board, such as appointing or recalling the board members or selling the company, it can lend its voice.

If we have “puppets” from the puppet theatre of politics on the supervisory board, it is very likely that it is not the candidate who is most competent and independent who will be appointed to the company’s management, but someone whose most important attribute is that he is also attached to the same invisible strings. In this way, the appointed management board will pursue the interest of the company following their own concerns of job protection, through the satisfaction of particular interests guided by politics in the guise of a state stakeholder, or by other interest groups. The same is true, of course, for businesses owned by municipalities and local communities, which are somewhat less in the spotlight. The consequences for these companies will initially be lost opportunities, which may be less tangible, but within a few years they will typically result in a serious negative impact on their competitiveness.

### From my personal experience towards a Code of Conduct for dealing with political and other pressures

As a supervisor myself, I have recently been the subject of political pressure. I was called by the secretary general of the ruling political party concerning the “expectations of the state” of the appointment of a director in a state-owned company, where I am Chair of the Supervisory Board. Despite my response that we, as members of the Supervisory Board, would act for the benefit of the company with due care in choosing the most suitable

candidate, a request to directly receive information on the election process going by the authorised state asset manager (the Slovenian Sovereign Holding) was clearly stated. In my personal reflection after this event, I came to the conclusion that the consciousness of our actions so far in the local environment has most often been limited to choosing between doing nothing, or following the expectations of a “personalised state”. In order to protect the selection process and to change these established practices in the selection processes, I decided on a third option; I reported to the Slovenian Sovereign Holding, as the authorised asset, that I, as the first supervisor, was subject to pressure that could affect my independent decision-making. I also filed a denouncement to the Anti-Corruption Commission with a call for it to act and to formulate its position on this very case.

I believe that, as Harari says in his book “21 Tips for the 21st Century”, silence is not about neutrality, but about supporting the existing situation. This is why, based on my experience, the Association of Supervisors of Slovenia, which I lead, has cooperated with the Anti-Corruption Commission to prepare a Code of Conduct for members of supervisory boards in the face of political and other pressures and unethical influence on independent decision-making. This protocol is primarily intended to encourage members of supervisory boards to end the culture of silence, and to serve as a handbook on how to act in such cases. In reality, the same applies to management board members, who may also be subject to such influences and pressures to meet the requirements of stakeholders, politicians, or even any of the supervisors.

### Workers’ roles in management, trade secrets and conflicts of interest

Besides the significant influence of state ownership, another characteristic of Slovenian corporate governance is the participation of workers in the management and governance of companies. After Independence, we followed the German model of workers’ roles in management. This came into being in the transition from one socio-economic system to another, and is therefore logically characterised by the former culture of self-management. The law on

workers' participation in management from 1993 is still in force today, even though it is long overdue for an overhaul, despite some minor updates. This is a law that no government has wanted to tackle so far, and it is systematically overlooked, since it maintains the political status quo.

Evidence from research and identified problems in practice show that the greatest challenge to the current framework derives from the fact that workers' representatives on supervisory boards are perceived as delegates of the labour councils. As a consequence, the protection of company trade secrets becomes an issue. The second challenge is the overlap of trade union and supervisory functions in one person, which places these individuals in a conflict of interest in decision-making on a supervisory board which is difficult to handle in practice. Although "labour" supervisors are perceived as independent from management, thanks to the effects of other related legislation, it is precisely their subordination to management that causes the distorted dynamics of labour supervision. They can therefore be extremely passive, and the reverse can also be true in the case of influential trade unionists who are directly represented on Supervisory Boards as a strong opposition to the Management Board's efforts.

### A dangerous setback to corporate governance culture

If all of these challenges are key to our competitiveness and attractiveness to investors, we should be concerned about any setback in the culture and practice of corporate governance. However, the deterioration in practice is reflected in opaque appointment procedures and frequent changes of supervisors and boards, and consequently in the problem of the duality of the corporate-legal and labour-legal relationship of the management board with the company, which bears the risk of legal proceedings with the former management boards in case of dismissal. This is therefore resolved by severance payments to former members of the management boards. All this results in a distrust of shareholders and other stakeholders in such decisions, and a deep gap in the continuity of management.

In this way, we lose the trust of our employees in the company, which is crucial for its future development.

The responsibility for the setback in the culture of corporate governance in the public discourse primarily lies with the governing politicians and the media. It is unbelievable that not only new but also experienced politicians demonstrate complete oblivion, and effortlessly speak in public about management issues in state-owned companies to justify their actions, as if the legal separation of politics from state-owned companies did not exist, and as if in the whole of the last ten years there has been no progress in the development of corporate governance at all. Some media outlets do not respond critically to such statements, or even become conducive platforms that facilitate the justification of these considerations. It is the duty of all experts involved in corporate governance to draw attention to this, which becomes a great challenge if a culture of silence prevails, as it is a high risk for those who expose themselves; while in the case of disclosing and reporting disputed influences and practices, retaliatory culture wins out by exploiting the media with the clear intention of discrediting the profession.

These are dangerous acts that should not be underestimated, especially if they gain non-critical media support. Some time ago, given the social progress in the field of corporate governance, I would have been inclined to believe that regression was no longer possible. Now, I often recall how, in the futuristic novel *The Handmaid's Tale* by Margaret Atwood (1985), the regression of an entire democratic society began when people simply believed that rights, once acquired and enforced, could be eternal.

Only the further knowledge and competence of all those involved in corporate governance processes can save us from a deterioration in practice, which also holds for the political elite, because competent and independent supervisors are not enough. It is necessary to move beyond the scandals, which should be replaced by a well-argued public debate with the scope of raising awareness of the real problems. A prerequisite for effective change in this area lies in the strong basis of the rule of law and in ethical and socially responsible media.

# Integrity and leadership

The purpose of companies today must be to create value for all stakeholders, to contribute to a better society, and to preserve the natural environment (ref: *Business Roundtable, World Economic Forum*) if the business world is to maintain the social legitimacy of its operations and for all of us together to cope with the growing global imbalances. In achieving this ultimate goal, generating profit and improving productivity are important tools and must be a natural consequence of socially responsible, honest and innovative business.

The described change in the perception of the purpose of the company is related to new trends in the economy and society, highlighting inclusive and divisive business models, socially responsible and ethical business, green companies, the circular economy, smart technologies and smart organisations, and the decentralisation of everything, including money transfer, decision-making, data management, and other resources. It seems that neither politics nor the traditional, yet dominant part



PHOTO: Arhiv ZM

**Andrijana Bergant**

**President  
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compliance and business ethics**

of the economy, nor education, seem to follow in this direction. Nevertheless, with these tides of change, new business models are getting underway and, with them, new management and leadership approaches that present both unimaginable opportunities and a number of challenges.

In spite of all the changes that are to come, the basic postulates of humanity, ethics and modern democracy will not change substantially. Neither will the fundamental constitutional principles of our country, which say that Slovenia functions under the rule of law and is a social state, and that it allows free entrepreneurial initiative, freedom of speech, the right to private property and other freedoms, while at the same time restricting our rights and the freedoms of others. It seems that in the new models of the functioning of society and the economy, these freedoms and values are only becoming more prominent. A closer look at the situation shows us that in our environment there are currently more threats directed against social rights than against prosperity; nor has any critical element of the rule of law been well established in our republic. The right to live in a healthy environment cannot be fully enforced, and many feel it is being reduced.

When it comes to new social arrangements and ways of increasing productivity, a strategic and systematic approach is necessary, and we need to move this further to the implementation level in a way that will be in line with current global trends. The aim should not only be to preserve the scope of social rights, but to enhance social well-being and strengthen the rule of law.

The challenge of enforcing the principle of the rule of law begins in the process of drafting and adopting regulations, which often does not provide sufficient opportunity, time, and space for quality discourse between stakeholders, even before submitting legal proposals. As a result, the legislation is flawed, and much has already been written about it. An important, but not yet sufficiently exposed, problem of enforcing the rule of law is that the anticipated financial effects of new legislation

are often underestimated or completely ignored, and thus often we do not allocate the necessary financial resources to successfully enforce the law. Consequently, the adoption of the regulations is not followed by effective preparation for the implementation of the laws or supervision. This, in turn, creates poor motivation in the business environment for companies to invest in internal compliance assurance mechanisms, because even the external, institutional mechanisms of safeguarding legality do not work effectively.

Companies in our environment, which nevertheless invest in internal compliance and ethics programmes, typically operate at higher, international standards, or in line with the expectations of their stakeholders, thereby gaining some market advantage, but sometimes appearing to be worse off. Therefore, an effective institutional approach to the implementation of legislation and the control of legality with sufficient staff, specialists, and financial resources would help to level the market conditions, especially in the interests of those pursuing higher standards of responsible and ethical conduct.

The excessive presence of corruption and a lack of political will and prosecution in this area is another major obstacle to the implementation of the rule of law. The corruption factor has an extremely negative impact on market conditions, and on Slovenia's international competitiveness and attractiveness for investment, as has been evidenced by numerous studies.

**The business community, with managers at the helm, can turn the situation in Slovenia in a positive direction precisely by introducing, to the broadest extent, established international principles and good practices of managing compliance and ethics programmes into our organisations.** This would bring us closer to the performance standards of the most successful economies, which have long since become the norm for credible business relationships and trusted partners. This would certainly be seen on the world map, where the colour of Slovenia would become

greener at the traffic light of corruption, money laundering and the rule of law, and thus more attractive not only to investors and to strategic partners, but also to the young generation of talent and innovation.

To this end, the Managers' Association, in collaboration with the European Institute for Compliance and Ethics (EISEP), recently introduced a handbook: 5 Star Integrity Leadership. It outlines the principles of well-thought-out compliance management and business ethics through good leadership. We have also identified concrete indicators for each principle in the corporate integrity programme; what specific changes are to be made for it in business, citing numerous examples of good and bad practices, and various additional resources and tools. In doing so, we aim to bring Slovenian managers and other leaders closer to an important set of internationally established standards and good practices in the internal management of a company, in the direction of responsible, legal and ethical business, hoping that similar standards and practices will be adopted by state institutions and bodies. The five principles are summarised as follows:

**Strategy.** In a core business strategy, management addresses and considers risks and opportunities in the area of compliance and integrity. In connection to this, it sets strategic goals and activities, and integrates them into its mission and responsible business conduct.

**Code of Conduct.** In a first-level corporate document, the management codifies the standard of conduct, continuously promoting it in words and by its own example, attends training in the areas governed by the Code, and establishes the same obligation for all managers and employees. The requirements of the Code become operational through individual policies, procedures and instructions.

**Reward and discipline.** The leadership promotes ethical conduct through a system of rewards and disciplinary action. Practice has shown that this

element has the greatest weight in the implementation of a strong culture of integrity. The company has predetermined forms and severity of violations and their consequences, regardless of who the offender is. However, the consistency, fairness, and effectiveness of responding to positive and negative cases is demonstrated by documented records.

#### **Recruitment and relationships with partners.**

Integrity is only as strong as the weakest link in the company's business chain. One of the PWC surveys found that contractors contribute 80% of all compliance risks; namely, inflated commissions, rewards to influencers, dirty money, and so on. They need intermediaries, and these, of course, need colleagues on the inside. Therefore, there is an urgent need for an equal focus on background checks and ongoing monitoring and training on compliance and business integrity for employees, as well as for contractual partners. The content and approaches to training are tailored to each target group and their powers, and are practically oriented and documented.

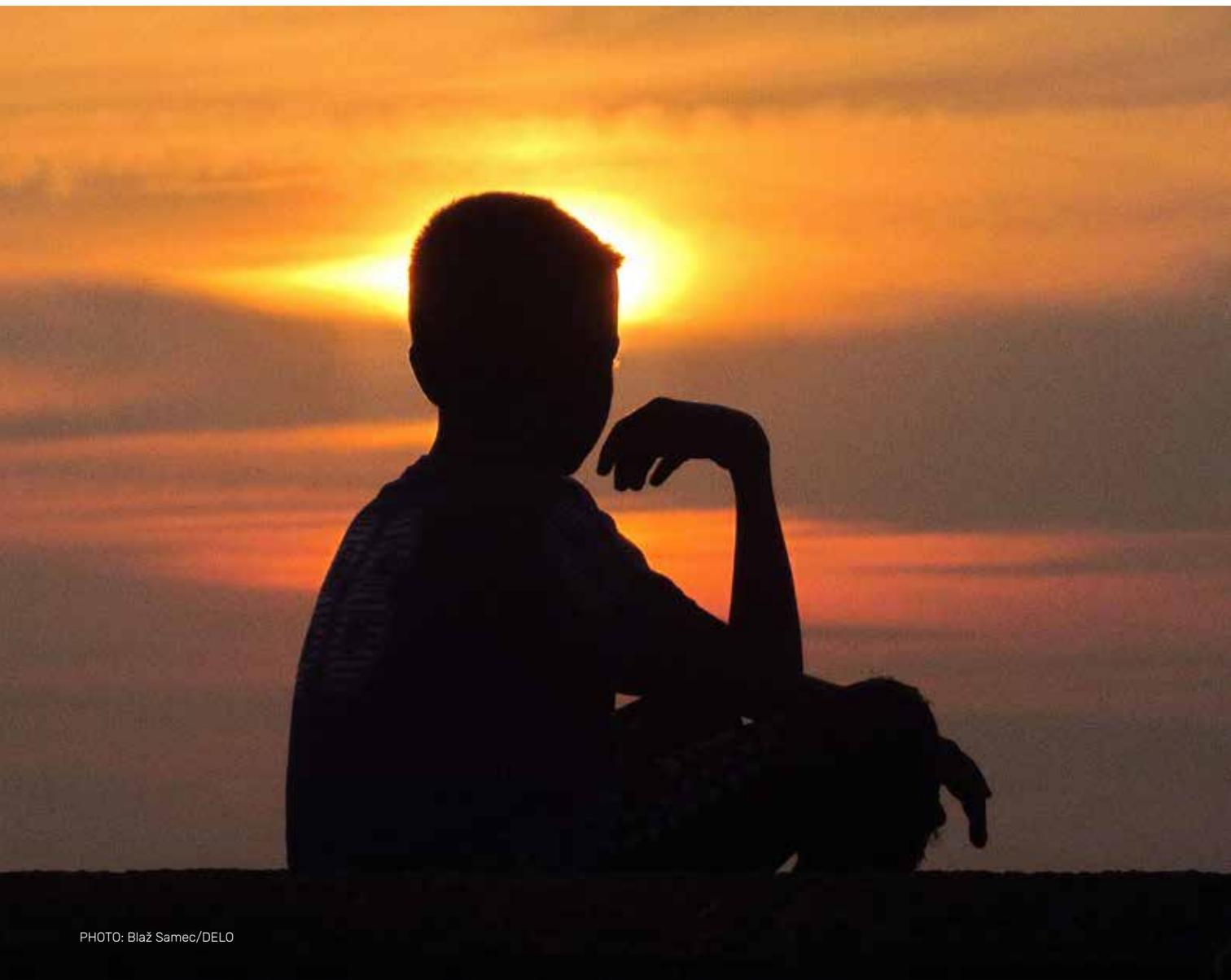
#### **Monitoring violations and responding to them.**

Setting up a compliance and integrity programme requires some time and energy. On the one hand, the state of integrity cannot be maintained without continuous operation, while on the other, the management's approach to detecting and responding to violations can, in a single moment, root the integrity of the company in the organisation's culture or degrade it. For the time being, the practice does not yet know a more effective mechanism for the early detection of violations, then the direct reporting system (whistle-blowing). If the company does not have any recorded violations, it means that the management has not effectively established this principle, or the managers and employees are completely unaware of it. A culture of open communication about violations is therefore the responsibility of responsible leaders, further raising the level of general trust and good relationships.

You can explore the content in more detail at [www.5stil.com](http://www.5stil.com).

# Good practices and support from the business environment: discrepancy or convergence?

Jurij Giacomelli and Diana Jecič



Who are the figures that the business world in Slovenia sets as an example and holds up to society as credible leaders? What examples of good business practice most directly address development challenges and can contribute to social wellbeing in the future? Most importantly: is the business and the broader institutional and stakeholder environment geared to good examples and creating opportunities for new breakthroughs and their followers?

Business Associations focus on identifying and promoting the best practices of managers in their profession. The results are reflected in innovative, growing, competitive companies. If we understand these practices well and learn from them, we can progress faster. This also applies directly to the managers themselves.

**Stakeholders** responsible for creating more of these experiences can help by creating increasingly favourable conditions for them. By this we refer to the country in the broadest sense, as a set of institutions that create an environment of rules, restrictions and incentives for entrepreneurial initiatives; these institutions bring high added value, and with their involvement in the local environment, can particularly contribute to increasing Slovenia's competitiveness. In the strictest sense, this also affects suppliers, customers, and consumers. Certainly, these examples deserve special consideration from social partners. Those of us who are not part of the economic and social world are really interested in how often, if at all, and from what perspective good examples are discussed at meetings of this body, as guides and positive comparisons for others.

What kind of people are the winners of the 2019 Business Association Awards? Sustaining as many winners as possible is about the application of the common good; a review of the winners shows

their capacity for innovation, a high level of internationalisation, and high added value. Reviewing this year's winners, we find that innovative and internationalised medium-sized companies are among them; those who succeed are well versed in the local environment and sustainable business practices.

At the beginning of the year, the **Chamber of Commerce and Industry of Slovenia** presented various managers of export-oriented medium and large companies with the oldest award for business leaders in Slovenia, honouring those who create achievements with lasting economic effects. They are: Rok Barbič, Chairman of the Board of STILLES in Sevnica; Tomaž Berginc, MSc, General Manager of ETI, in Izlake; Rudolf Horvat, Director of Saubermacher Slovenia in Murska Sobota; Srečko Jesenek, Director of JESENEK Printing House in Ljubččna; Peter Kosin, Chief Executive Officer of INEA, Ljubljana, who is also one of the Delo finalists; and Dušan Olaj, Director of DUOL in Brezovica.

#### **This year's Delo's Entrepreneurial Stars**

**Award** went to **Intra Lighting**, a family company founded by Marjeta and Marino Furlan, a lighting manufacturer and lighting solutions provider from Šempeter pri Gorici.

As the "factory of the year", **Finance newspaper** highlighted Ljubljanske mlekarne, and selected the aluminium producer Talum in Kidričevo as the most environmentally friendly company, following its energy transformation. **Edi Kraus**, an entrepreneur and manager from Trieste, is the winner of this year's Finance Award for Outstanding Economic Achievements, which is aimed at those organisations and individuals who have made a significant contribution to enhancing social wellbeing. Kraus is a long-serving director of Aquafil SLO, a nylon manufacturer, formerly Julon, part of the international family-owned Aquafil Group based in Arco di Trento, which is at the forefront of sustainable and circular innovation.

Three of the winners' stories, promoted by the Managers' Association of Slovenia, are highlighted in more detail below.

# From an indebted oil trader to a leading regional sustainable energy company

In nine years Tomaž Berločnik has succeeded in creating a regional energy company from an indebted petroleum products distributor – and it is now the largest in Slovenia. Petrol is no longer just an oil trader but a company of the future, setting new trends and business models in the field of energetics and trade across the wider regional area, and developing smart energy and mobility management solutions.

Berločnik successfully recruited employees who, among other abilities, emphasise visionary and persistent dedication to progress, as well as courage and openness. For Berločnik, a winning team which paves the way for outstanding business results is of the utmost importance.

2018 was the best fiscal year in Petrol's history and 2019 forecasts show a further double digit growth



PHOTO: Voranc Vogel/DELO

2019 Manager of the Year: **Tomaž Berločnik**, President of the Management Board at Petrol

in revenue and profitability, bringing the company closer to a net sales value of six billion euro. In 2018, the company generated 5.4 billion euro in net sales revenue, up 20% from a year earlier and up 92% from 2010.

The organisational culture introduced to Petrol by Berločnik is based on trust, accountability, and cooperation; it is stable and relaxed. Under his leadership, employee satisfaction increased and the number of those who were actively disengaged decreased. Among the business objectives of the directors and managers there was a proportion of assessment related to the organisational climate of their unit, demonstrating the importance placed on it. His closest associates appreciate his confidence, because he does not play "power" and knows how to empower others. He is learning-oriented and can take constructive criticism.

# From a student experiment, through space, to cancer treatment

In 2001, under the mentorship of Mark Pleško, a group of physics students at the largest Slovenian research institute, the Jožef Stefan Institute, founded Cosylab. Today the company has more than 180 employees and is the leading provider of hardware and software solutions for controlling nuclear accelerators and other large-scale physical experiments.

Cosylab has been operating globally since opening for business and has affiliates in the USA, Switzerland, China, Sweden, and Japan. Since 2001, in Chile, they have been involved in the development of a control system for radio telescopes, which have taken a unique photograph of a black hole. Today, the company is focused on proton therapy control systems, an advanced method for the treatment of cancer.

Cosylab Values: think bravely; be humble; work hard; enjoy life.

Igor Verstovšek developed as a leader as the company grew. He likes to point out that a zest for science, good ideas and playfulness can help in creating an interesting career path. He is an outstanding complexity manager and at the same time advocates a flattened and relaxed organisational culture.

Because projects in Cosylab can last for up to 10 years, it is important that the associates in the



PHOTO: Aleš Beno

**Igor Verstovšek**, Cosylab,  
Young Manager 2018

organisation feel good and stay with the company. Those interested in working for the long term are offered an attractive package for personal development, including business development, whether technical or managerial, involvement with the most interesting scientific projects around the world, travel and appropriate remuneration, and the many bonuses that make up the cultural mosaic of Cosylab – including pancakes on Mondays!

The net sales revenue of the Cosylab Group was just over 14 million euro in the last fiscal year (end-March 2019). A substantial proportion of this, 6.6 million euro, was generated in the EU market. From April 2018 to the present, an additional 45 people have been employed for development purposes, with the value added per employee exceeding 100,000 euro, which is almost 100% more than the industry average.

# Into a global niche and excellence with bold decision-making

KLS Ljubno manufactures gear rings for the automotive industry, incorporating them into the engines of as many as 28 different car brands.

It is one of the most automated and robotised companies in its sector in the world; 97% of production processes are automated and robotised, with about 150 robots already involved in production.

With 250 employees, the company has a 15% global market share, half of which is in Europe. As much as 96% of what they create is exported. Productivity has increased tenfold since 2000, which is reflected in exceptional profitability. **The value added per employee is 115,000 euro, which is almost three times more than the Slovenian average.** They are constantly increasing the number of employees and have salaries that are higher by a fifth than the Slovenian average and the highest Christmas bonus in Slovenian manufacturing.

The founder, director and majority owner, Bogomir Strašek, has been associated with KLS for 48 years. As a 26-year-old he was entrusted with running the SGP Gradbenik metal plant with clear instructions to create as many jobs as possible without incurring losses. When he started out, more than half the production was located outdoors or under a hayrack, and there was no heating in the winter, he recalls. All



PHOTO: Aleš Beno

**Bogomir Strašek**, KLS Ljubno,  
Lifetime Achievement Award 2018

the loads were carried manually by the workers as they had no machinery. But just five years later, the number of employees had increased from 33 to 87.

The products were sold all over Yugoslavia. In the early 1990s, they lost 90% of their customers, so they looked for new markets. In 1996, Strašek made the bold decision to narrow his specialisation to the production of gear rings. The good sense of this strategy is demonstrated today by the company's results.

Strašek is primarily a human being; a co-worker. In his relationships with employees, he emphasises interpersonal respect, which is the basis for the good functioning of the company and the achievement of business excellence. Even today, he feels a great deal of responsibility towards the employees whose work and income he provides, and towards the local environment.

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# Economic resilience in times of uncertainty

## Velimir Bole

### **Slovenian economist, mathematician and statistician**

Velimir Bole's macroeconomic analyses and projections have been deemed leading reference resources for decision-makers in relation to the Slovenian economy for three decades. He was a member of the Governing Board of the Bank of Slovenia (1992-2002), then a member of the Economic and Social Council of the Republic of Slovenia and a member of the Council of the National Bank of the Republic of Macedonia, as well as serving on numerous other expert advisory panels. He publishes and edits Slovenia's longest running macroeconomic magazine, *Gospodarska gibanja* (Economic Trends). After his graduation from the Faculty of Natural Sciences and Technology and the Faculty of Economics of the University of Ljubljana, Bole received his Master's degree at the Faculty of Science of the University of Zagreb. Since then, he has been working at the Economic Institute of the Law School (EIPF).

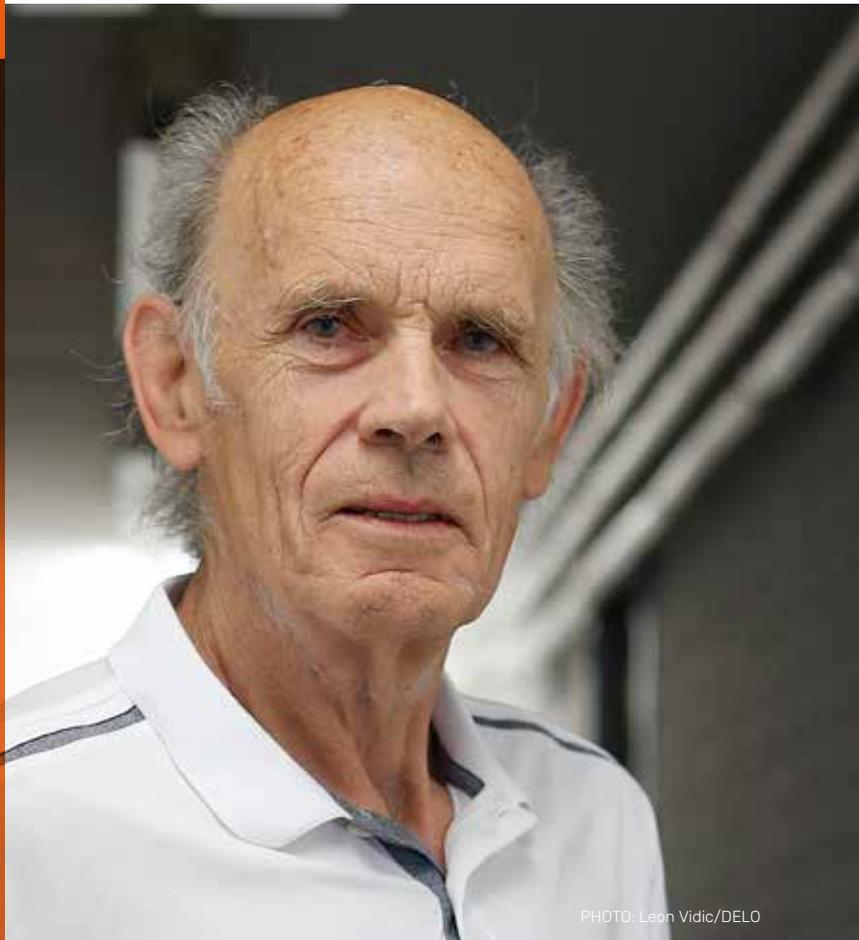


PHOTO: Leon Vidic/DELO

Similarly to that of Germany and France, the latest data across the entire eurozone for November reveals a better than expected picture of economic activity. The decline has slowed down in the third quarter of 2019, while interim growth remained at 1% annually, which is above expectations.<sup>1</sup> Can an upturn in the economic activity be expected?<sup>2</sup>

### **Uncertainty and economic activity.**

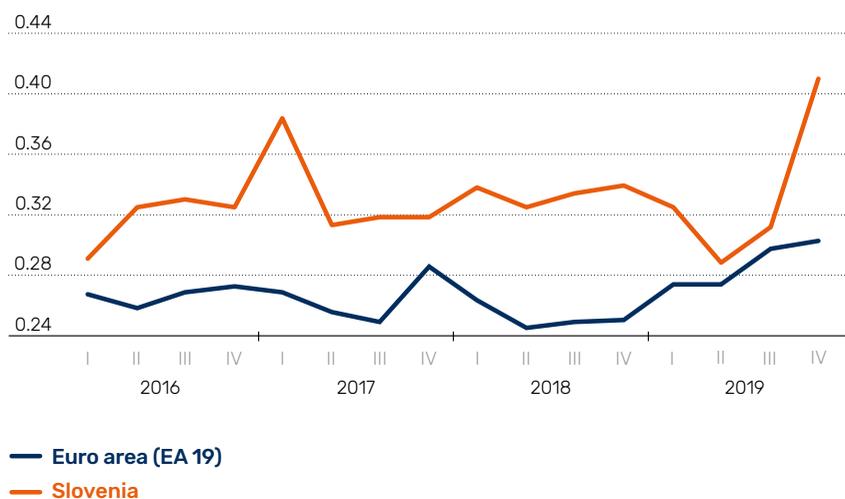
It seems that the bleak prospects for the future remain unchanged, despite the aforementioned November news, since the factors which generate them are still present. The slowdown in demand due to the cyclical decline in the USA and Asia, the trade barriers still impeding exports, and the continuing great uncertainty about trading conditions, particularly due to the shifting of customs and other trade barriers, in addition to the already low activity, are hindering investment.

The economic activity of the industrial sector is the most vulnerable. Prospects in the service sectors, which are particularly impacted by the domestic market, are still somewhat diminished in the short term, but it is likely only a matter of time before weak domestic demand also affects the industrial segment of economic activity, due to the decline in industry.

With such mixed fortunes in the (good and bad) news, the assessments of trend changes in the economy are increasingly becoming perishable goods, thanks to the great uncertainty and anxiety in the markets caused for the most part by plodding global trade orders and

The ongoing changing conditions in trade negotiations, uncertainties regarding Brexit, regulatory changes in the automotive industry, and ambiguous diagnoses of the current economic conditions (decline in economic activity) of the holders of monetary and fiscal policies in the EU (and Slovenia)<sup>4</sup> increase the uncertainty, not only of long-term but also of very short-term trading conditions. As shown in the graph below, which presents the level of uncertainty (variability) of expected industry export orders, the uncertainty of trading conditions has increased significantly in the eurozone and Slovenia in the past year and a half. The assessments/forecasts of activity trends are thus becoming even less reliable.

Figure 1: **Uncertainty of export expectations**



Source: European Commission – survey; author's calculations

Note: Uncertainty of export expectations; diversification (variance) of export expectations.

by Brexit. It is true that the forecast of an immediate breakdown "à la 2009" has become less convincing after more than two years, and that a cyclical decline in growth or a long-term slower growth in the eurozone, restricted by supply, are the most likely scenarios. A long-term decline in growth is not foreseen for the immediate future; however, a cyclical upturn is not anticipated until the end of 2020.<sup>3</sup>

Long-term economic growth prospects are also becoming less certain. As discussed above, the question is whether the current decline represents a regular cyclical slowing down of economic activity after a longer period of fast growth, or a significantly more long-term decline in economic growth that points to a systematic decline in productivity during the post-crisis recovery period. The number of unknowns is higher in the latter case. It is not clear what a systematically too low and structurally specific demand (for example, due to ageing) would mean for a long-term slowing down of growth. Furthermore, what is the impact of breaking value chains (due to current customs and other restrictions) and an increase in production costs on the decline in growth? Likewise, the issue of the consequences of technological changes (in the automotive industry, for example), and structural changes in China, also remains open.<sup>5</sup>

1 Eurostat, Newsrelease, "GDP and employment flash estimates for the third quarter of 2019", 14 November 2019.

2 See, for example, "Is Germany's economy over the worst?", Financial Times, 24 November 2019.

3 On long-term stagnation, see, for example, Rachel L. and L. Summers, 2019, "On Secular Stagnation in the Industrialized World", NBER, <http://www.nber.org/papers/w26198>; on the cyclical upturn, see ECB, "Survey of Professional Forecasters", 2019/IV.

4 Quantitative easing (and simultaneous restricting of consumer loans in Slovenia), launching the EDP procedure against Italy (simultaneously with the stagnation or contraction of the Italian economy), supporting fiscal interventions by the governor (and the blocking of the adoption of the budget in Slovenia), etc.

5 See, for example, R. Borg, M. Buti, O. Dieckmann, B. Döhring in A. Zeana, 2018, "A challenging path ahead: The Commission's Autumn 2019 forecast", CEPR.

**Leaving long-term uncertainty factors aside, the key question that arises in connection with the short-term ones is what action to take, or, what effect can the economic policies of Slovenia have on reducing the potential risks or mitigating the related costs of uncertainty at the level of the national economy?**

This is particularly true since Slovenia does not hold the basic monetary policy levers, and has very limited manoeuvring space when it comes to fiscal policy because of the European Commission's guidance and its own poorly calculated commitments. Undoubtedly these economic policies would achieve far less if a sudden financial and real collapse of trade in a significant section of the Slovenian economy occurred to the same extent as, for example, the one in 2009<sup>6</sup>, due to a hypothetical (usually one that cannot be foreseen) large financial turmoil (the bursting of a bubble) in any of the financial markets. However, it must be emphasised that such helplessness may also be expected in the course of normal, albeit very uncertain, developments.

Moreover, the economic policies of Slovenia would be of scant use, since it is not clear what the European Commission and the ECB would do in their current state (for example, with quantitative easing of the inflated balance and the ECB's negative interest rates burden), and particularly with their current commitments and formal restrictions (for example, countries' inability to borrow in their own currencies, negligible potential for direct fiscal intervention by the European Commission, and the obsession with the methodologically inadequate limiting of government spending), which were not eliminated even after the bad experience of the financial crisis.

### **What is the level of economic resilience at this time of increased uncertainty?**

Due to the narrow range of economic policies, the following question arises: **What is the level of economic resilience, i.e. the economy's endogenous ability to function sustainably in very insecure or**

**potentially even significantly worsened economic conditions supported only by weak economic policies?** A proper analysis of such resilience would involve a simulation of the consequences of hypothetical shocks in the environment, which would by far exceed the purposes of this article. Economic resilience in 2018<sup>7</sup> is thus illustrated only in comparison with resilience in 2008.<sup>8</sup> Since such a comparison allows only the illustration of changes and not the level of resilience as per the (likely) calibration of the ECB's policy and fiscal instructions by the European Commission, the comparison with 2008 has been made for **Slovenia, the eurozone and Germany.**

The eurozone is included because it illustrates the resilience against which (in the event of problems) the ECB's policy and the fiscal instructions of the European Commission will likely be calibrated. Germany was added as a reference since it made it through the financial crisis with significantly lower national costs than the eurozone average. Comparison with Germany thus reveals its resilience, which could possibly have positive effects on the ECB's and the European Commission's potential policy in Slovenia, and which would be calibrated against the eurozone.

### **Sustainability of internal and external balance.**

Economic resilience with regard to a possible severe worsening of economic conditions (financial or real shock) was illustrated by a comparison of the sustainability (stability) of the macroeconomic balance in the year of the turn of economic activity just before the onset of the crisis (2008), and the year of the turn of economic activity in the last economic cycle (2018), which occurred after a long period of upswing that began in 2013.

We have illustrated the sustainability of the balances which were of key importance for the transmission and increase of the national cost of the external shock which affected the economy after 2008. We have provided indicators for four characteristics of the sustainability of a (stable) macroeconomic balance, i.e. general government structural balance, current external balance, cost competitiveness, and the indebtedness of the basic institutional sectors of the economy.

<sup>6</sup> When the financial turmoil began in the market of subprime mortgage loans.

<sup>7</sup> That is, after the turn in economic activity at the end of 2017.

<sup>8</sup> The economic activity cycle reached its peak in the second quarter of 2008!

Table 1: **Macroeconomic balance**

	Slovenia		Eurozone		Germany	
	2008	2018	2008	2018	2008	2018
General government balance	-3.3	0.4	- 3.5	- 0.6	- 1.0	1.4
External positions	-5.3	5.7	- 1.5	2.9	5.7	7.3
Competitiveness	1.00	0.94	1.00	0.88	1.00	1.00

Source: IMF; author's calculations

Note: indicators of macroeconomic equilibrium; GDP rate; general government structural balance (year average); current external exchange balance (year average); competitiveness – effective exchange rate deflated by labour costs (last quarter of the year), normalised for 2008; **a decrease in the index shows an improvement in competitiveness.**

Table 1 presents the values of the structural deficit and current external balance in GDP rate and cost competitiveness for Slovenia, Germany and the eurozone, with the values of the indicators given for 2008 and 2018.

It is evident that Slovenia's general government balance, and particularly the current external balance, were noticeably better in 2018 – higher than before the financial crisis (in 2008) – since they are not only positive but also significantly higher. The structural balance has improved by almost 4 percentage points of GDP, and the current external balance by 11 percentage points of GDP (i.e. nominally by almost 5 billion euro). The suitable economic resilience to external shocks or long periods of decline in economic activity in Slovenia is currently significantly higher than it was in 2008, i.e. in the period when economic activity was declining just before the onset of the financial crisis. In the event of an external shock to the economy, the size of the general government balance and the current external balance are the key determinants of the economy's potential to manage the first phase of depreciating the shock (i.e. the phase of financing).

An increase in the sustainability of both balances also occurred in the eurozone and Germany after the financial crisis, while the structural fiscal balance and the current external balance improved; in fact, they greatly increased in Slovenia. In addition, the values in the table not only demonstrate the increase in resilience, but also its level. The level of current resilience (i.e. the sustainability of the stability of both balances) to extreme shocks is greater in Slovenia than in the eurozone, but less than that in Germany

(all conditions being equal). Resilience (as shown by the current value of the structural fiscal balance and the current external balance) to a greater worsening of economic conditions is as it was in Germany before the onset of the financial crisis in 2008.

The change in competitiveness from the end of 2008 to the end of 2018 is also presented in the table. **Following the onset of the financial crisis, the competitiveness of the Slovenian economy slowly worsened for about a year (it dropped by about 4%) and then systematically improved after the first quarter of 2012 until the beginning of 2017, when it stagnated until the end of 2018 and then began to decline noticeably, due to the outpacing of uniform labour costs.** At the end of 2018, competitiveness was higher than just before the onset of the financial crisis (the last quarter of 2008) by about 6%. Simultaneously, the competitiveness of the eurozone was higher by 12% when compared to the last quarter of 2008, while the competitiveness of Germany remained unchanged. Although competitiveness increased twofold in the eurozone by 2018 in comparison with Slovenia, the current external balance improved much more in Slovenia than in the eurozone, as is evident from the table.

**Indebtedness – national and economic sectors.** In the financial crisis, indebtedness was the key lever through which the shock in a small section of the global financial markets expanded and was transferred to the environments of individual economies. Banks, and later also countries, were initially unable to obtain suitable financing due to the blockage in the wholesale market of loan funds. Later, a limited range of banks

Table 2: **Indebtedness size and structure**

(%)	Slovenia		Eurozone		Germany	
	2008	2018	2008	2018	2008	2018
Country	23.2	77.5	72.3	97.9	68.4	67.5
Non-financial corporations	89.2	51.6	94.2	102.5	58.7	57.2
Financial corporations	23.5	6.7	126.6	126.7	97.5	63.9
Financial corporations – OMFI	44.0	5.2	60.0	40.3	58.7	34.6
Households	25.3	26.9	54.0	56.3	59.2	53.1

Source: Eurostat; ECB; author's calculations

Note: The size and structure of indebtedness in 2008 and 2018; indebtedness of national and economic sectors; loans and bonds; unconsolidated; annual average; GDP rate; state – general government; non-financial corporations – companies; financial corporations – banks, insurance companies, pension funds and other financial organisations; financial corporations – OMFI; short-term bank borrowing with deposits of other (resident and non-resident) banks; households – population.

(additionally reduced due to unsuitable intervention by regulators) caused a credit crunch in the high-volume mass market (between the banks on the one hand and companies, households and other financial organisations on the other), which halted new ongoing financing, renewal of loans and the activity of the sector. In this retransmission mechanism, the indebtedness of all the economic sectors, i.e. the state, banks, companies and also households (although to a minor extent) played a crucial role.

The question to be asked is: How efficiently could such a transmission mechanism of indebtedness function in the current period of economic cooling if a similar shock occurred in the financial markets? In other words, what changes have occurred in economic resilience in the period after the financial crisis to enable the economy to withstand external shocks through the transmission mechanism of indebtedness? Economic resilience to a potential financial shock in the current period of cooling of economic activity is thus illustrated by comparing the indebtedness of individual economic sectors just before the onset of the financial crisis (2008) and today (2018).

Table 2 shows the indebtedness of all national and economic sectors in Slovenia, the eurozone and Germany before the financial crisis (in 2008) and after the turn in economic activity (in 2018). Indebtedness is shown as a percentage of GDP. Short-term and long-

term loans and issued bonds were observed. Since a substantial part of short-term interbank borrowing is displayed in balance sheets as deposits, this short-term bank indebtedness is presented in a special line (OMFI), which is otherwise not shown in the indebtedness of financial corporations.<sup>9</sup>

It is evident that in the current period of decline in economic activity (after the turn at the end of 2017), the indebtedness of Slovenian companies and financial institutions is significantly lower than it was after the turn of the economic activity cycle before the collapse of 2008. In particular, indebtedness is greatly reduced (by multiple times) in financial institutions. Simultaneously, the indebtedness of households was unchanged, and general government indebtedness increased significantly due to the debts of rehabilitated companies and banks.

Changes after 2008 remained almost the same as those in Slovenia with regard to the indebtedness of households in the eurozone and Germany. In this period, household debt changed little for all three items.

The indebtedness of companies and financial institutions in Slovenia reduced more than that in Germany and especially in the eurozone, where no reduction in debt of companies and financial institutions occurred after 2008.

<sup>9</sup> The indebtedness of Slovenian banks usually involved borrowing from foreign banks, which is why the relatively high indebtedness of Slovenian banks could have been one of the most important reasons for the informal forcing of Slovenia into drastic recovery (substantial capital increase) of the banks. Considering the experience with Greece, such a recovery would result in "filling up" the banks with cash, and thus the safe return of loans to foreign, mostly European, banks would be guaranteed.

The increase in government debt in Slovenia after 2008 greatly exceeded that of the eurozone and particularly Germany, where government debt was even (somewhat) reduced by 2018.

In 2018, the level of indebtedness in all sectors was lower in Slovenia than in the eurozone, and it was also lower than in Germany, with the exception of the general government sector. Even the indebtedness of companies, which was significantly higher in Slovenia than in Germany in 2008, was lower in 2018.

Due to the change in debt, the resilience to shocks on foreign financial markets not only notably improved in all economic sectors after 2008, with the exception of the general government sector, but was also significantly higher than in the eurozone and Germany in 2018. This also applies to the total resilience of all national and economic sectors, since in 2018 the total debt of all sectors in Slovenia was 40% lower than in Germany and 60% lower than in the eurozone.

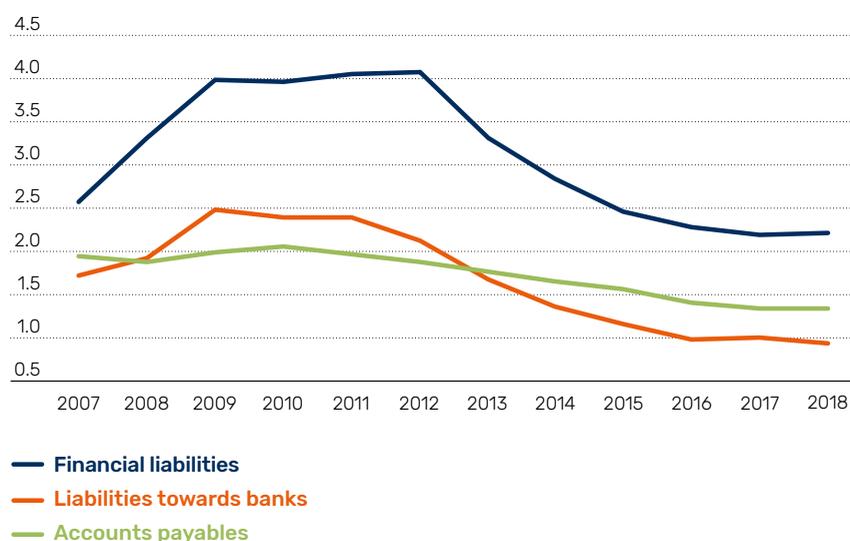
### Indebtedness of companies

– **distribution.** We learned in the previous section that the average debt of the national and economic sectors is significantly lower during the current decline in economic activity than it was at the time of the decline in economic activity just before the onset of the crisis (in 2008). It is also lower than in the eurozone and Germany (with the exception of the general government sector).

The range of companies that could be in danger after a potential financial and real shock due, for example, to the bursting of a bubble in any of the financial

markets, does not only depend on the national and economic average amount of debt documented in the previous section, but also on the dispersion of the debt's distribution of units (companies, households) and the nature of the debt (nature of creditors). With the same average (median) value, the section of population that is at risk increases with an increase in debt dispersion. Due to differences in the target function of creditors, the nature of the debt affects creditors' risk differently during financial or

Figure 2: **Indebtedness of companies**



Source: AJPES; author's calculations

Note: Indebtedness of companies by EBITDA unit; median of sectors of 5-digit classification; all financial liabilities; financial liabilities to banks; liabilities to suppliers.

real shocks. This particularly applies to companies that borrow extensively from highly regulated organisations, which may be more vulnerable during financial shocks due to the actions of the regulator (specific target functions).<sup>10</sup> We therefore provide evidence illustrating the impact of the size of debt dispersion and the nature of the creditor on economic resilience with regard to a possible financial shock during the current cooling of economic activity, in comparison with the period of the turn in economic activity before the onset of the financial crisis.

<sup>10</sup> See, for example, Bole V., J. Prašnikar and D. Trobec, 2014, "Policy measures in the deleveraging process: A macroprudential evaluation", *Journal of policy modelling*; see also Koo R., "The Holy Grail of Macroeconomics: Lessons from Japan's Great Recession", John Wiley & Sons.

Let us look at total (short- and long-term) financial indebtedness, applicable indebtedness to banks, and indebtedness (operating liabilities) to suppliers for companies from the industrial (i.e. processing activities and power, water and gas supply), construction and market services sectors.<sup>11</sup> The burden of indebtedness is presented by means of debt calculated per unit of net cash flow from regular operations (EBITDA), as is usual in macroeconomic analyses. In the short term, the changes in indebtedness measured in this way are particularly the result of changes to net cash flow from operating activities, and also the balance of debt in the long term. Since economic activity reached a peak in both periods being compared (2007-2008 and 2017-2018), we assume that reference (balance) values were concerned, which did not change significantly in the short term due to the financial shock.

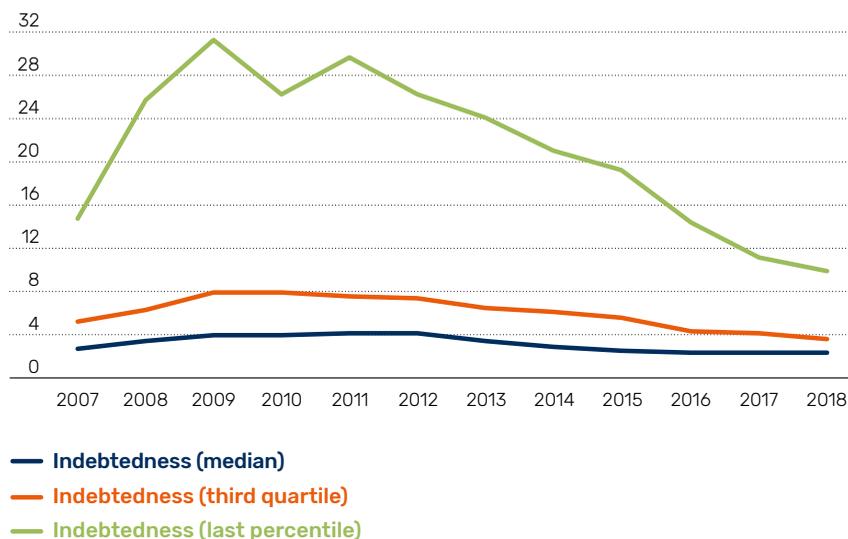
Figure 2 displays indebtedness in the 2007-2018 period. Total financial indebtedness, indebtedness to banks and operating liabilities to suppliers are presented. It is evident that the **indebtedness of companies at present, i.e. in 2018, is noticeably lower than just before the onset of the 2008 crisis**. It can also be seen that the debt burden quickly and severely increased after the start of the financial crisis, and that the level of indebtedness remained at this new level until 2012, when it began to rapidly decrease. Total financial indebtedness oscillated the most, as the EBITDA of 3 in 2008 increased to an EBITDA of 4 in 2009 and then dropped, by 2018, well below the initial value (to an EBITDA of 2.2). The relative increase in bank indebtedness at the onset of the crisis was somewhat lower, while the decrease after 2012 was significantly higher, as bank indebtedness had dropped by the end of the period, i.e. up to 2018, to an EBITDA of only 0.9. Although it is true that changes to the debt burden in the short term are particularly the result of changes to net cash flow, it must be pointed out that banks usually demanded prompt repayment of loans after the onset of the crisis.

**The graph clearly shows that banks are withdrawing from providing credit support to the business sector.** The great nominal reduction in domestic banks' loans to companies, which at the start of this year had already dropped to about 45% of the level it attained in 2008, was obviously not counterbalanced by borrowing from foreign banks or the non-banking sector, as overall indebtedness (financial and towards suppliers) had dropped well below the 2008 level by 2018, i.e. from an EBITDA of 5.3 to an EBITDA of 3.5. **At the onset of the current cooling, companies were thus much less vulnerable to possible financial shocks. This particularly applies to bank financing.**

However, the debt burden in 2018 is not noticeably lower (in comparison to 2008) for median companies, although it is lower across the entire distribution of companies. As shown in Figure 3, the reduction in debt burden is not proportionate, as the most indebted companies (at risk) in 2018 relating to 2008 are significantly less indebted than median companies. The figure presents the total financial indebtedness of median companies, companies from the third quartile and companies in the last percentile of debt distribution for the 2007-2018 period. The total financial indebtedness of the companies in the last percentile, i.e. companies with the largest risk due to loans, was 25.4 times larger than net cash flow (EBITDA) in 2008, while in 2018, the debt was only 9.9 times larger. The resilience of the companies with the largest risk is thus significantly better than that of median companies, i.e. the average of the business sector, in 2018 than compared to 2008.

The graph also clearly shows that the companies at the tail-end of the debt burden distribution are far more vulnerable than median companies in the eventuality of a financial shock. Their debt burden increased by an EBITDA of 5 in one year during the financial crisis, particularly due to the drop in net cash flow from operating activities. The burden of those from the third quartile increased by an EBITDA of 1.7, and of median companies by an EBITDA of only 0.7.

<sup>11</sup> The graph was drafted on the basis of sectors with five-digit activity classification.

Figure 3: **Total financial indebtedness – distribution of companies**

Source: AJPES; author's calculations

Note: Total financial indebtedness by EBITDA unit; median; third quartile and last percentile of sectors with five-digit activity classification; all financial liabilities.

The great reduction in median indebtedness and company debt dispersion for all the analysed forms of indebtedness (total financial indebtedness, indebtedness to banks and indebtedness to suppliers) is summarised in Table 3.

The values in the table clearly illustrate that the bank indebtedness of median companies is lower

by an EBITDA of 1 (53%), for companies from the third quartile by an EBITDA of 2.1 (55%) and companies in the last percentile by an EBITDA of as much as 11 (72%) in 2018 when compared to 2008. Indebtedness in the case of operating liabilities toward suppliers decreased least in 2018 in comparison to 2008; only by an EBITDA of 0.6 (32%) for median companies. However, the reduction in dispersion with regard to indebtedness towards suppliers was greater in 2018 when compared to 2005, as the indebtedness of the companies in the last percentile was only an EBITDA of 6 in 2018, i.e. by an EBITDA of 3.9 (40%) less than in 2008.

#### **Debt repayment – structure of companies.**

When analysing debt fluctuations, we frequently distinguish between three segments of companies: those with sufficient net cash flow to pay instalments (regularly pay off the loan); companies whose net cash flow from operating activities exceeds the required interest payments, but

Table 3: **Indebtedness – distribution of companies**

Year	Median	Third quartile	Last percentile
Total financial indebtedness			
2008	3.3	6.2	25.8
2018	2.2	3.6	9.9
Indebtedness with banks			
2008	1.9	3.9	15.3
2018	0.9	1.8	4.3
Operating liabilities toward suppliers			
2008	1.9	3.3	9.9
2018	1.3	2.3	6.0

Source: AJPES; author's calculations

Note: Debt by EBITDA unit; median; third quartile and last percentile of sectors with five-digit activity classification; total financial indebtedness; indebtedness with banks; operating liabilities toward suppliers.

Table 4: **Cash flow and debt repayment**

	<b>Lower than interest</b>	<b>Higher than interest and lower than servicing</b>	<b>Higher than servicing</b>
2007	3.0	0.6	96.5
2008	3.8	3.4	92.8
2017	0.3	0.2	99.5
2018	1.7	0.1	98.2

Source: AJPES; author's calculations

Note: Size of cash flow from regular operations; industry, construction and market services; sectors with five-digit activity classification; percentage of added value in the added value of all companies; cash flow does not suffice for the payment of interest; cash flow suffices for the payment of interest, but not for full servicing of financial liabilities; cash flow suffices for the servicing of financial debt.

not the return of the principal; and companies whose net cash flow fails to enable even the payment of interest. Minsky named the first ones "hedge borrowers", the second ones "speculative borrowers", and the third ones "Ponzi borrowers"<sup>12</sup>. The resilience of companies in 2018 in the event of a severe financial shock is also presented in Table 4 by means of a comparison of the suitable structure of companies in 2008 and 2018.

The table shows the structure of companies with regard to the size of their net cash flow from operating activities relative to the servicing of loans before the onset of the financial crisis (2007-2008) and in the current period of cooling economic activity (2017-2018). The percentages of added value of suitable segments of companies within the framework of total added value generated by all companies are shown.

It is evident that the share of "hedge borrowers" is much higher in the current period of decline in economic activity than in 2008. The share of "hedge borrowers" in 2008 amounted to 92.8%, but is 98.2% in 2018. The reduction in the share of "hedge

borrowers" following the turn in the economic activity (2007 and 2017) was also noticeably lower in the current period.

**Conclusion.** The economy continues to slowly cool down in an increasingly insecure environment. Economic policies have little manoeuvring space; those of Slovenia because its own commitments and formal possibilities, and those of Europe because of the current state of monetary policy and theoretical prejudices in the field of fiscal policy. The contribution of economic policies will thus not be modest if they manage to avoid contributing to major mistakes. The key question is how resilient is the economy with regard to possible further increases in tensions and uncertainties in trading conditions. The data reveals that resilience is much greater than before the onset of the financial crisis. It is also noticeably higher than the eurozone average.

12 See Minsky, H., 1992, "The Financial Instability Hypothesis", [http://digitalcommons.bard.edu/hm\\_archive/275](http://digitalcommons.bard.edu/hm_archive/275).

# Slovenia should not be caught off-guard, in the face of long-term economic and social challenges, by the budget surplus for the second consecutive year

## Overview of the Slovenian economic policy in numbers

Prof. dr. Dušan Mramor



PHOTO: Arhiv ZM

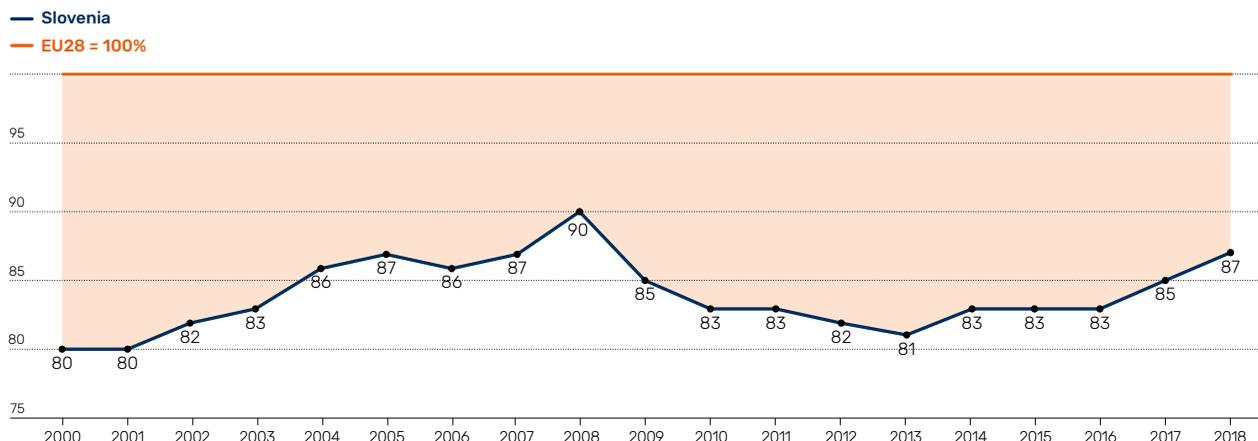
The selection of Slovenia's economic indicators for this year provides a clear and helpful illustration of the main highlights of the articles in Outlook 2020, which relate to long-term economic trends.

The graphs of the most important macroeconomic indicators enable the monitoring of the main economic development trends. In 2018, all the trends seemed extremely favourable:

- GDP growth was slightly lower than in 2017, but still more than double the growth in the eurozone;
- Slovenia's GDP per capita, adjusted for different levels of prices and relative to the EU average, was raised again, this time to 87% – last seen in 2008;
- We continued to see a large reduction in unemployment, especially for young people;
- There was a large reduction in all types of indebtedness (countries, economies, households, abroad);
- As a result, interest rates on Slovenia's government debt declined more than the eurozone average (interest rate spread);
- We maintained a huge surplus in the foreign trade operations shown in the current balance of payments.

Let me mention in particular a result that will go into the annals of Slovenia's economic policy; not only was a budget surplus achieved for the second consecutive year, but there was also a large increase (from 0.1% to 0.8% of GDP) in the 2018

## GDP per capita in purchasing power parity (in %)



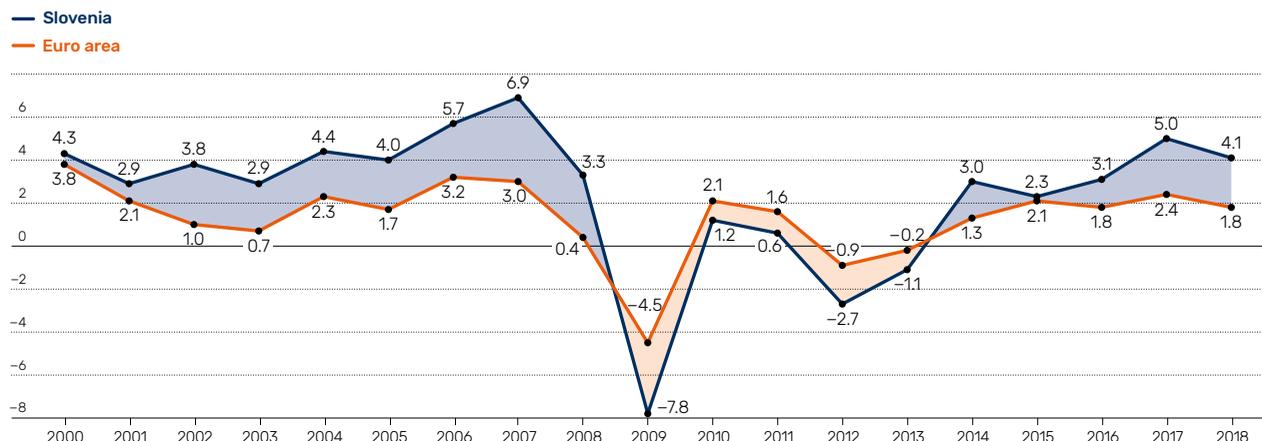
election year. Undoubtedly, in addition to strict monitoring of the legal constraints of the fiscal rule by the Ministry of Finance, Prime Minister Miro Cerar made a significant contribution by resigning rather than giving in to extreme pre-election pressure to increase all types of entitlements, and thus government expenditure. Labour costs again rose faster than in the eurozone, but less than the difference in GDP growth.

However, one must be aware that this was a short-term result, more or less at the top of the economic activity cycle. Slovenia faces very serious long-term economic and thus general societal challenges. From the current point of view, the most important challenges are the rapidly ageing population, i.e. demographic problems. I also tracked these in a selection of new graphs, and below I outline their content logic and the information they convey.

In our previous article, my colleague Jože Sambt and I show that solutions must first be sought to increase the working population and labour productivity. This is the only way we will be able to achieve

Let me mention a result that will go into the annals of Slovenia's economic policy. Not only was a budget surplus achieved for the second consecutive year, but there was also a large increase (from 0.1% to 0.8% of GDP) in the 2018 election year. Undoubtedly, in addition to strict monitoring of the legal constraints of the fiscal rule by the Ministry of Finance, Prime Minister Miro Cerar made a significant contribution by resigning rather than giving in to extreme pre-election pressure to increase all types of entitlements, and thus government expenditure.

## Real GDP growth (in %)



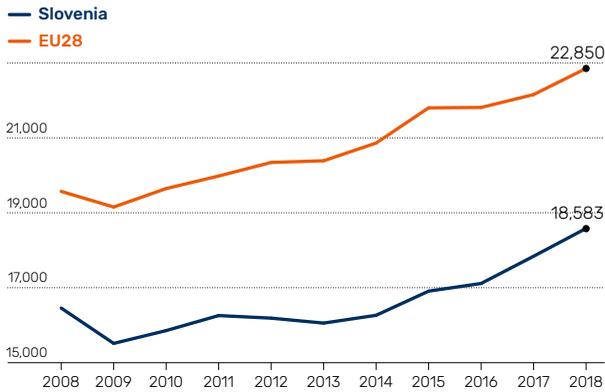
higher growth and thus higher disposable income per capita, which is a more appropriate indicator of social stability than GDP per capita. Disposable income per capita, adjusted for purchasing power, increased in value again last year, but not enough to grow compared to the EU average – it remained at 81%, well below the 87% EU average reached in GDP per capita. Such a low result correlates well with low levels of labour productivity (82.7% in the EU), while growth in labour productivity (1.5% in 2018) has also been far from satisfactory and even average from 2000 onwards (1.7%). These two indicators clearly suggest the necessary course of action, with private investment being the most important factor for productivity growth, and available equity (domestic and foreign) being the most important for private investment.

The macro indicator of return on equity invested in Slovenian non-financial corporations when compared to that of other eurozone countries could not be clearer. Entrepreneurial equity investments in Slovenia are unattractive, as their return over the years is far less than half that in the eurozone – hence the low productivity and consequent low growth.

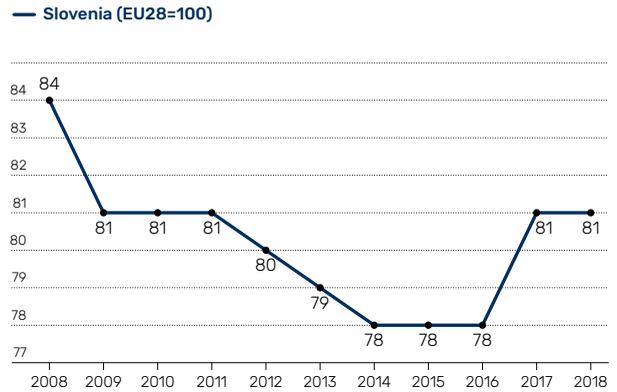
The overall overburdening of the economy with a levy on the public sector, which is expected to reduce productivity, cannot easily be ascertained, because since the peak of the crisis the percentage of public expenditure in GDP has been steadily falling, and was 3.3 percentage points below the eurozone average last year. The second question is, of course, the structure and effectiveness of the expenditure.

At first glance, it appears that the employment of the population, which was above the eurozone average in 2018 and its high growth (3%), is an exploited source of disposable income per capita. However, we should learn from the countries that have been most successful in activating the population into work (e.g. Sweden). From these, we find that we are seriously behind in the lowest and highest working age population segments, and in the proportion of those who earn enough by working without the aid of social transfers. There are considerable reserves here.

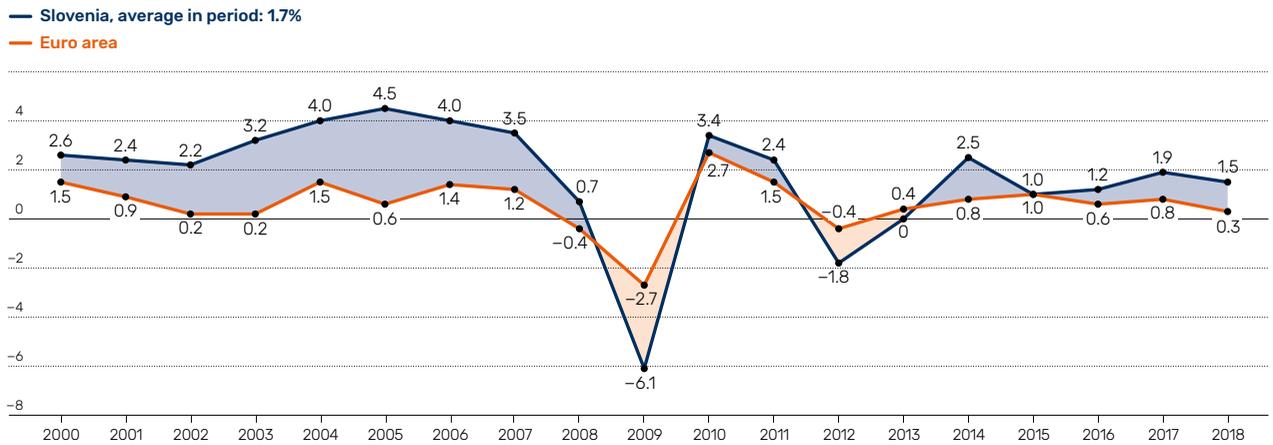
### Disposable income per capita in purchasing power parity (in €)



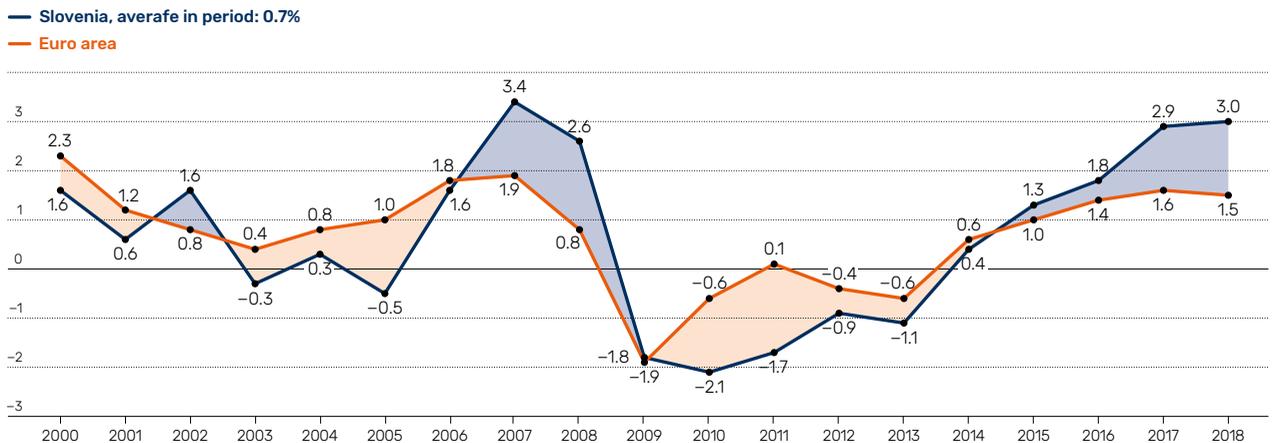
### Disposable income per capita to EU average in purchasing power parity (in %)



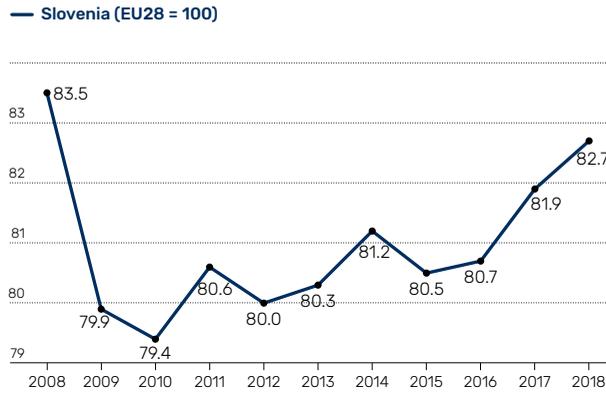
### Real labour productivity growth per person (in %)



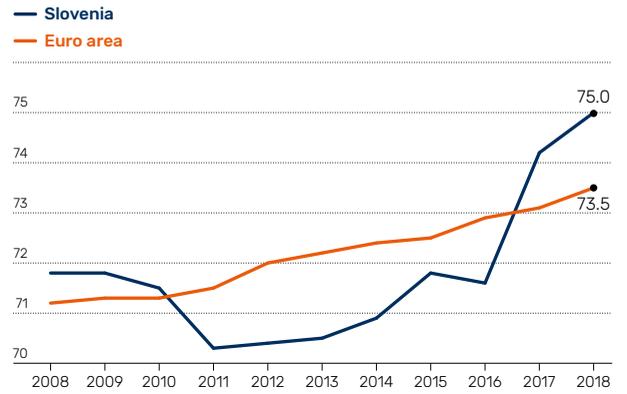
### Employment growth (in %)



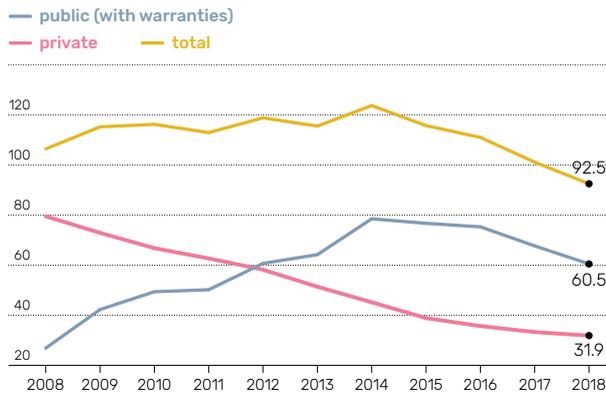
### Nominal labor productivity per person in purchasing power parity (in %)



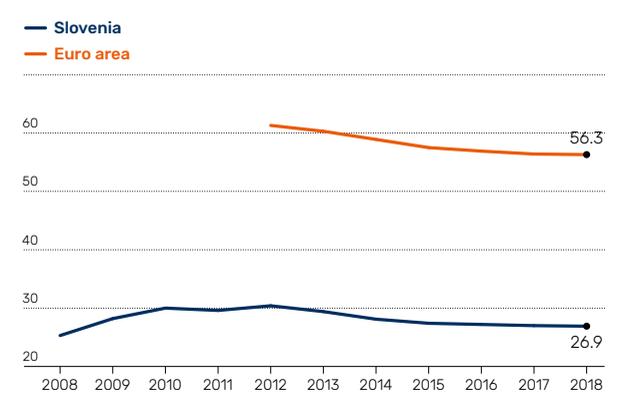
### Employment rate as % of total population in the age 15 to 64



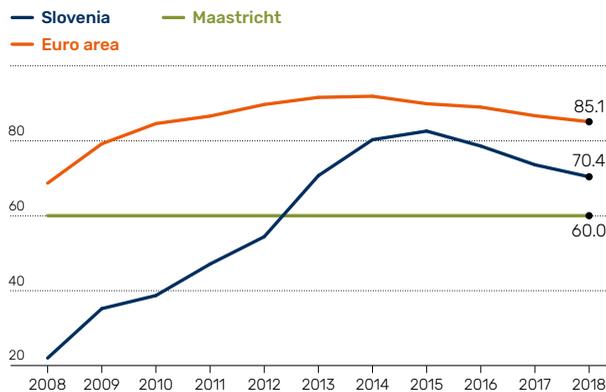
### Foreign debt (% GDP)



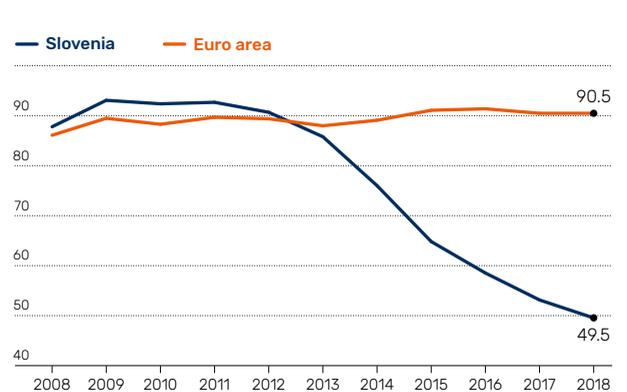
### Loans to households (% GDP)



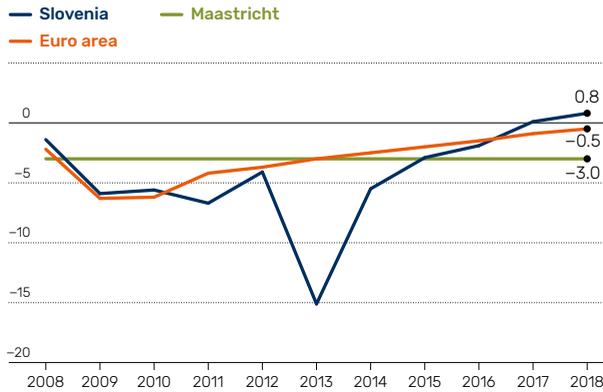
### General government debt (% GDP)



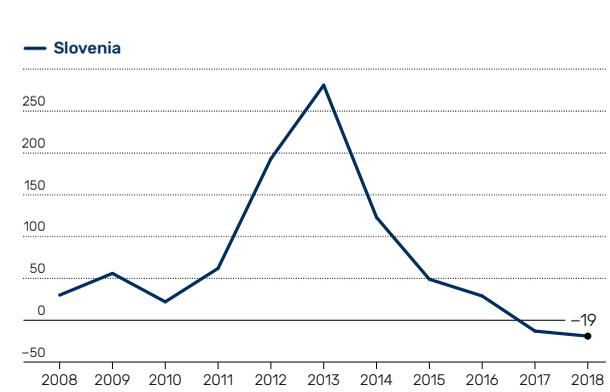
### Loans to non-financial corporations (% GDP)



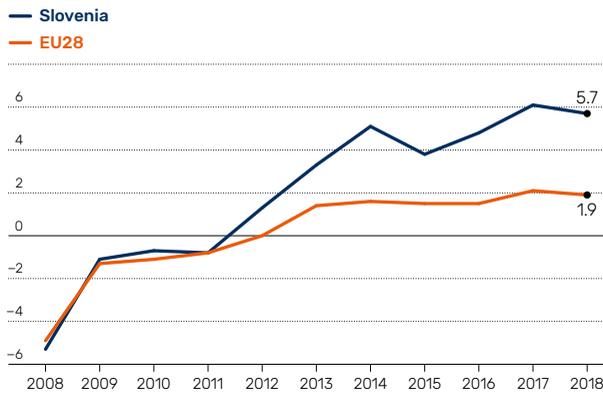
**Public finance deficit/surplus**  
(% GDP)



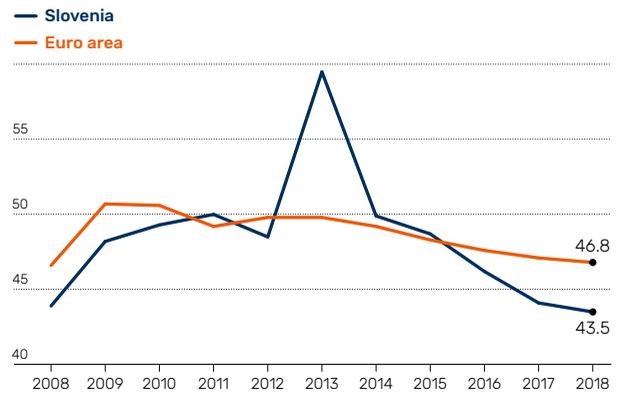
**Interest rate spread, 10yr government bond**  
in basis points to euro area



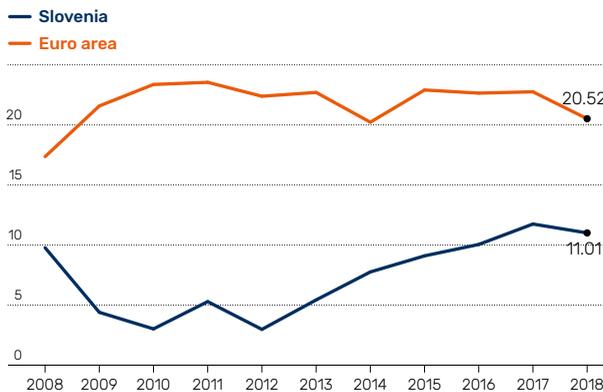
**Current account balance**  
(% GDP)



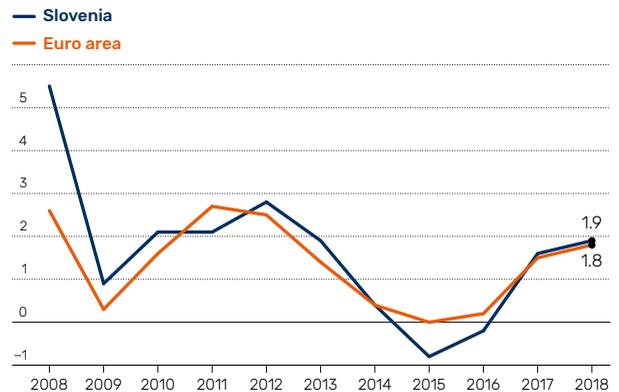
**General government expenditure vs GDP**  
(in %)



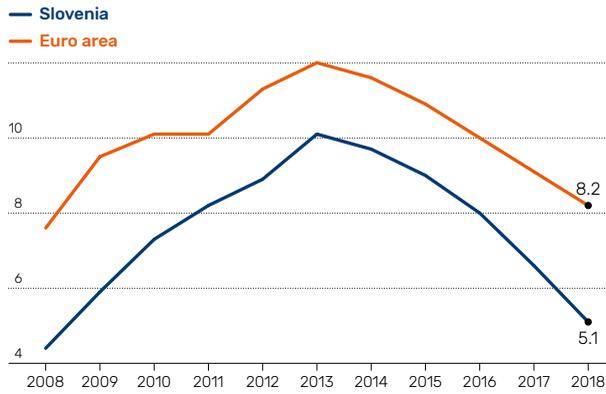
**Net return on equity**  
non-financial corporations, after tax (in %)



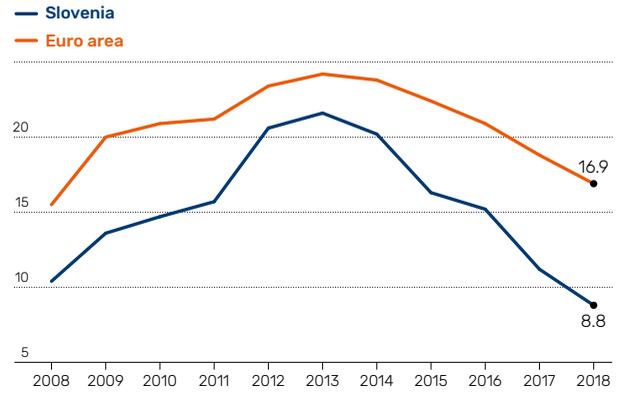
**Inflation**  
(in %)



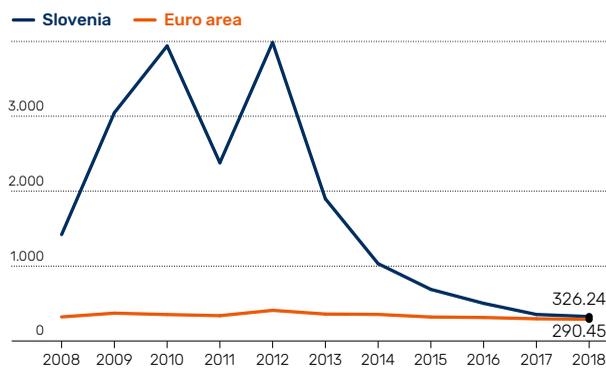
### Unemployment rate (% of active population)



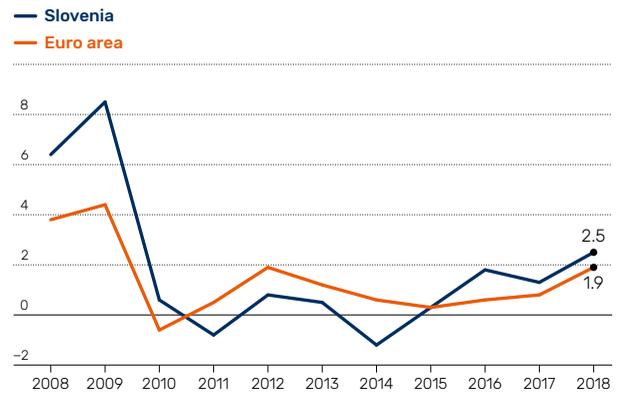
### Youth unemployment rate (% of active population in the age 15-24)



### Net debt to income of nonfinancial sector (in %)



### Nominal unit labour cost growth per person (in %)



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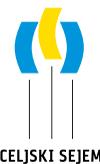
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A man with a beard and long hair is crouching in a field of tall grass, looking up at a child. The child is standing and reaching up to hold a large, colorful kite (red, orange, yellow, and blue) that is flying in the sky. The scene is set during sunset or sunrise, with a warm, golden light. The background shows trees and a clear sky.

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