Serbia

Key developments and challenges

The global economic crisis has reduced foreign investor interest and hampered privatisation of remaining state-owned assets. Nevertheless, it is important that efforts continue to prepare viable companies for sale once international prospects improve.

Financial stability in the banking sector has been maintained after a difficult period in late 2008, but lending conditions are tight. Close cooperation among regulators, domestic and foreign banks and international financial institutions (IFIs) is essential to ensure that banks continue to meet businesses' and households' needs.

The economic crisis has led to a sharp drop in public revenues and has highlighted the need to lower spending on public administration and benefits. It is crucial that the government sticks to its commitments under the International Monetary Fund (IMF) agreement to keep the budget deficit under control.

Country data

Population (in millions)	**9.9**
Area ('000 sq km)	**102.0**
GDP (in billion US$, 2008)	**50.1**
Average transition score (scale: 1 to 4.33)	**2.89**

Progress in structural reform

Liberalisation and privatisation

Since signing the Stabilisation and Association Agreement (SAA) with the European Commission (EC) in 2008, Serbia has begun unilaterally to implement an Interim Trade Agreement with the European Union. However, implementation from the EU side remains blocked (as of August 2009) because of Serbia's perceived lack of full cooperation with the International Criminal Tribunal for the former Yugoslavia (ICTY) in The Hague. Nevertheless, the EC has recommended to the Council of Ministers that Serbian passport holders receive visa-free access to the Schengen zone from January 2010. Negotiations on membership of the World Trade Organization (WTO), which began in 2005, are at an advanced stage.

The privatisation programme suffered set-backs over the past year, partly because of the global crisis. The government's attempts to privatise several major companies, including the mining complex RTB Bor, JAT Airways and JAT Tehnika, failed. The government is, however, searching for a strategic partner to acquire 40 per cent of RTB Bor, with the possibility of extending to a majority stake over time. It is also unclear when major infrastructure companies such as Telekom Srbija and the state-owned power company EPS might be offered for sale. However, progress has been made in other, non-infrastructure areas. For example, the government plans to tender and sell a 70 per cent stake in the major pharmaceutical company, Galenika, in early 2010.

Business environment and competition

Successive governments have made several efforts to improve the business environment, although significant problems remain according to cross-country surveys. Serbia was ranked 88th in the World Bank's *Doing Business 2010* survey. In the 2008/09 Business Environment and Enterprise Performance Survey (BEEPS IV), enterprises identified tax rates, competition from the informal sector and lack of access to finance as the main obstacles to doing business. The government has established a "guillotine" project to promote regulatory reform and, as of mid-2009, an inventory of existing regulations has been prepared. In addition, a one-stop shop for company registration began operating in May 2009 in order to reduce the time needed to register companies from 23 days to five.

A new competition law was adopted in July 2009 and will enter into force in November 2009. One of its main aims is to strengthen the authority of the Competition Commission by giving it enhanced powers to impose penalties (of up to 10 per cent of revenues) on companies that fail to comply with the law. In addition, a new law on control of state aid, in line with EU law, has been adopted (effective from January 2010) under which any state aid that distorts competition is ruled out except under certain restricted conditions.

Infrastructure

In July 2009 the government signed a loan agreement with the World Bank to receive US$ 388 million for construction work on the major highway, Corridor 10. Several large projects have also been signed with IFIs to help restructure the state-owned railway company, Zeleznice Srbije.

Earlier in 2009 the dominant state-owned power company, EPS, launched expressions of interest for the construction of a new unit at a thermal power plant and for the completion of another power plant. The winning bidders will be selected by the end of 2009 and will acquire majority stakes in the ventures.

Financial sector

The banking sector was initially affected by the global financial crisis, but the authorities took firm steps to restore stability and confidence. A number of banks suffered high deposit withdrawals in the final quarter of 2008, estimated at €1 billion (about 20 per cent of total deposits). In response, the government raised the level of deposit insurance substantially in October 2008 from around €3,000 to over €50,000. The National Bank of Serbia (NBS) has also taken a number of measures to ease liquidity in the market. As a result, the deposit base gradually recovered and the banking system remains sound, well-capitalised and liquid. According to the central bank, stress tests, based on mid-2009 results, point to adequate capital and liquidity buffers in the 10 largest banks. Foreign banks, which own approximately 70 per cent of total banking assets, remain committed to their operations in Serbia. In March 2009 the 10 largest foreign-owned banks in the country promised to maintain their exposure in Serbia and to provide adequate support to their subsidiaries during the crisis.

Macroeconomic performance

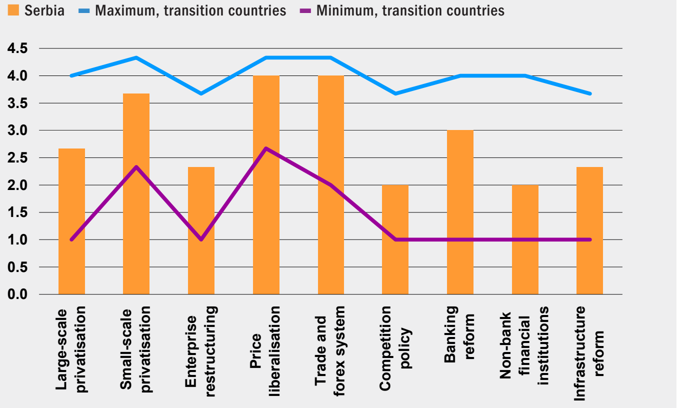
Following real GDP growth of 5.4 per cent in 2008, the crisis was increasingly felt in the first half of 2009, when the economy contracted sharply. Figures for the first half of the year showed a year-on-year fall of 4.1 per cent, while industrial output was down 17.4 per cent relative to the same period last year. Credit growth has slowed significantly from the rapid rates seen in recent years, and interbank interest rates stood at more than 13 per cent as of July 2009. The dinar depreciated sharply at the end of last year and the start of 2009, necessitating central bank intervention to prevent even greater falls, but has since stabilised. The NBS did not intervene further in the foreign exchange market between late February and September.

The authorities have responded to the crisis in several ways. Macroeconomic policy is now set in consultation with the IMF, following the signing of two agreements in 2009. A precautionary stand-by arrangement was agreed in January, but was replaced in May by an extended and significantly augmented arrangement (covering more than two years) to the value of around €3 billion. In February 2009 the government allocated €1.3 billion to stimulate production and exports by improving liquidity in the economy and purchasing power. The central bank also eased liquidity by scrapping reserve requirements for new foreign borrowing and by progressively lowering the key policy rate in a succession of cuts, the latest being from 12 to 11 per cent in October 2009. However, the government is struggling to keep to the commitments under the new arrangement with the IMF. In early September the IMF mission and the authorities agreed that the government deficit target for 2009 could be increased from 3 per cent to 4.5 per cent of GDP, but completion of the second review of the stand-by arrangement was delayed, pending further steps by the government to make firm commitments to reduce spending in 2010 and to implement reforms in health, education and pensions.

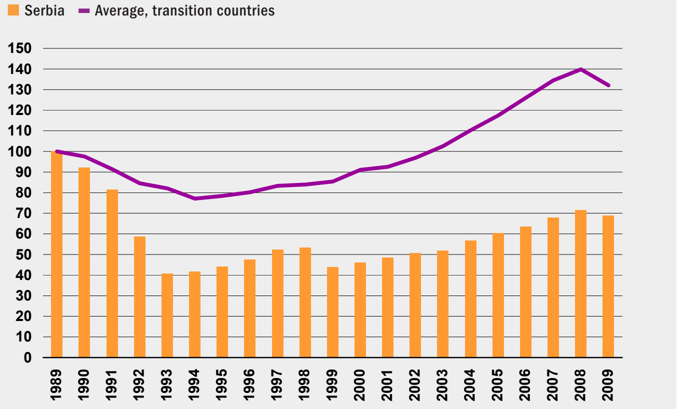
Outlook and risks

GDP is expected to contract by about 4 per cent in 2009, with a modest recovery in 2010. The main macroeconomic challenge is on the fiscal side, as the authorities try to control pressures for greater spending. On the external side, the key risk lies in the expected sharp reduction in foreign direct investment (FDI) this year, which will make it harder to finance the current account deficit (over 17 per cent of GDP in 2008, although falling sharply in 2009). While there is still a significant pipeline of privatisation projects, it may be difficult to obtain a politically acceptable price for these assets in the present environment. Furthermore, banks are reluctant to lend, especially to small and medium-sized enterprises, even though adequate funds are available. More positively, the country enjoys strong support from IFIs and from parent banks of subsidiaries in Serbia, and this is expected to continue. Over the medium term, prospects for further integration with the European Union should contribute to the country's good potential for resuming high growth rates.

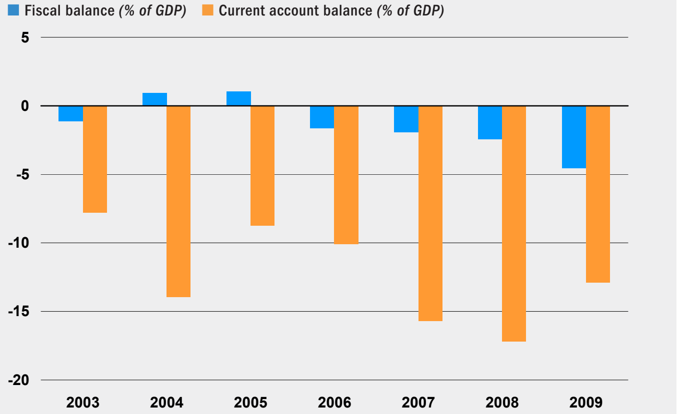
Transition indicators 2009



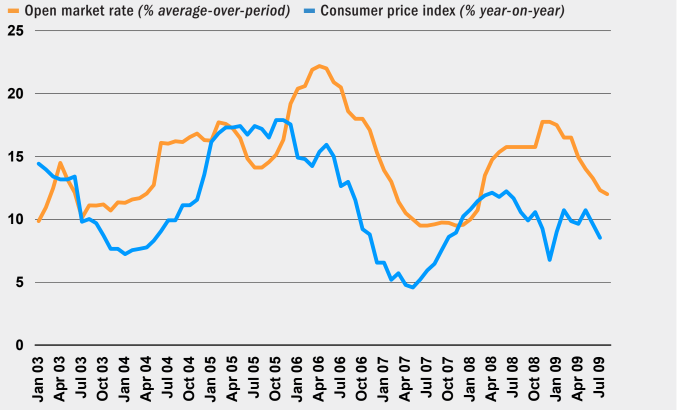
Real GDP (1989=100)



Fiscal balance and current account balance



Interest rates and inflation



Liberalisation and privatisation	Business environment and competition	Infrastructure	Financial sector	Social reform
Current account convertibility – **full** Controls on inward direct investment – **no** Interest rate liberalisation – **full** Exchange rate regime – **managed float** Wage regulation – **no** Tradeability of land – **limited de jure**	Competition office – **yes** Quality of insolvency law – **medium** Secured transactions law – **modern/some defects**	Telecoms regulatory assessment compliance – **low** Independence of the electricity regulator – **partial** Separation of railway infrastructure from operations – **no** Independence of the road directorate – **no**	Capital adequacy ratio – **8 per cent** Deposit insurance system – **yes** Private pension funds – **yes**	Share of population living in poverty – **na** Government expenditure on health – **5.7 per cent of GDP** (2008) Government expenditure on education – **3.8 per cent of GDP** (2008) Household expenditure on power and water – **9.3 per cent**

Structural and institutional change indicators

	2003	2004	2005	2006	2007	**2008**	**2009**
Enterprises							
Privatisation revenues (cumulative, in per cent of GDP)	6.9	7.7	10.2	17.4	20.2	**21.4**	**na**
Private sector share in GDP (in per cent)	na	na	na	na	55.0	**60.0**	**60.0**
Private sector share in employment (in per cent)	na	na	na	na	na	**na**	**na**
Budgetary subsidies and current transfers (in per cent of GDP)	3.7	3.2	3.3	2.8	2.7	**2.7**	**na**
Share of industry in total employment (in per cent)	29.7	27.4	25.9	24.4	23.1	**22.1**	**na**
Change in labour productivity in industry (in per cent)	10.9	12.5	9.0	14.2	14.3	**14.0**	**na**
Investment/GDP (in per cent)	22.7	37.8	26.5	27.1	27.0	**28.0**	**na**
EBRD index of small-scale privatisation	3.0	3.3	3.3	3.7	3.7	**3.7**	**3.7**
EBRD index of large-scale privatisation	2.3	2.3	2.7	2.7	2.7	**2.7**	**2.7**
EBRD index of enterprise reform	2.0	2.0	2.3	2.3	2.3	**2.3**	**2.3**
Markets and trade							
Share of administered prices in CPI (in per cent)	11.2	11.2	9.2	9.9	5.7	**5.8**	**na**
Number of goods with administered prices in EBRD-15 basket	3.0	3.0	2.0	3.0	3.0	**3.0**	**na**
Share of trade with non-transition countries (in per cent)	79.3	79.0	65.6	52.1	51.8	**49.5**	**na**
Share of trade in GDP (in per cent)	54.0	62.0	60.6	64.6	65.9	**65.3**	**na**
Tariff revenues (in per cent of imports)	7.4	6.0	5.7	5.3	5.5	**5.2**	**na**
EBRD index of price liberalisation	4.0	4.0	4.0	4.0	4.0	**4.0**	**4.0**
EBRD index of forex and trade liberalisation	3.0	3.0	3.3	3.3	3.3	**3.7**	**4.0**
EBRD index of competition policy	1.0	1.0	1.0	1.7	2.0	**2.0**	**2.0**
Financial sector							
Number of banks (foreign-owned)	47 (16)	43 (11)	40 (17)	37 (22)	35 (21)	**34 (20)**	**na**
Asset share of state-owned banks (in per cent)	34.1	23.4	23.9	14.9	15.7	**16.0**	**na**
Asset share of foreign-owned banks (in per cent)	38.4	37.7	66.0	78.7	75.5	**75.3**	**na**
Non-performing loans (in per cent of total loans)	na	na	na	na	na	**na**	**na**
Domestic credit to private sector (in per cent of GDP)	21.0	24.8	30.7	30.8	35.3	**39.7**	**na**
Domestic credit to households (in per cent of GDP)	2.6	4.9	7.6	10.1	12.6	**13.9**	**na**
– Of which mortgage lending (in per cent of GDP)	0.4	0.7	1.4	2.4	3.8	**5.7**	**na**
Stock market capitalisation (in per cent of GDP)	6.8	13.7	23.1	33.3	54.4	**27.0**	**na**
Stock trading volume (in per cent of market capitalisation)	na	na	na	16.3	14.6	**6.9**	**na**
Eurobond issuance (in per cent of GDP)	0.0	0.0	0.0	0.0	0.4	**0.0**	**na**
EBRD index of banking sector reform	2.3	2.3	2.7	2.7	2.7	**3.0**	**3.0**
EBRD index of reform of non-bank financial institutions	2.0	2.0	2.0	2.0	2.0	**2.0**	**2.0**
Infrastructure							
Fixed-line (mobile) penetration rate (per 100 inhabitants)	32.1 (na)	27.1 (47.8)	25.6 (55.9)	27.7 (67.6)	30.5 (86.0)	**31.4 (97.8)**	**na**
Internet users (per 100 inhabitants)	na	15.3	7.9	14.2	15.3	**24.0**	**na**
Railway labour productivity (2000=100)	127.7	161.6	199.6	251.9	282.4	**247.1**	**na**
Residential electricity tariffs (USc kWh)	4.7	5.3	5.1	5.8	7.5	**8.8**	**na**
Average collection rate, electricity (in per cent)	90	94	94	95	93	**94**	**na**
GDP per unit of energy use (PPP in US dollars per kgoe)	na	na	na	na	na	**na**	**na**
EBRD index of infrastructure reform	2.0	2.0	2.0	2.0	2.0	**2.3**	**2.3**
– Electric power	2.3	2.3	2.3	2.3	2.3	**2.3**	**2.3**
– Railways	2.3	2.3	2.3	2.3	2.3	**2.3**	**2.3**
– Roads	2.3	2.3	2.3	2.7	2.7	**2.7**	**2.7**
– Telecommunications	2.0	2.0	2.0	2.3	2.3	**2.7**	**2.7**
– Water and wastewater	2.0	2.0	2.0	1.7	1.7	**1.7**	**1.7**

Macroeconomic indicators[1]

	2003	2004	2005	2006	2007	**2008 Estimate**	**2009 Projection**
Output and expenditure			*(Percentage change in real terms)*				
GDP	2.4	9.3	6.3	5.5	6.9	**5.4**	**-4.0**
Industrial gross output	-3.0	7.1	0.8	4.7	3.7	**1.1**	**na**
Agricultural gross output	-7.0	19.5	-5.3	-0.3	-8.0	**9.0**	**na**
Employment			*(Percentage change)*				
Labour force (end-year)	2.6	0.3	2.2	-1.1	-6.1	**-2.0**	**na**
Employment (end-year)	-1.3	0.5	0.9	-2.3	-1.5	**-0.1**	**na**
			(In per cent of labour force)				
Unemployment (end-year)	31.7	31.6	32.4	33.2	29.9	**28.5**	**na**
Prices and wages			*(Percentage change)*				
Consumer prices (annual average)	11.7	10.1	16.5	12.7	6.7	**11.7**	**8.3**
Consumer prices (end-year)	7.8	13.7	17.7	6.6	10.2	**8.6**	**8.0**
Producer prices (annual average)	na	na	na	na	na	**na**	**na**
Gross average monthly earnings in economy (annual average)	25.3	23.7	24.1	24.4	22.0	**17.9**	**na**
Government sector			*(In per cent of GDP)*				
General government balance	-1.1	0.9	1.0	-1.6	-1.9	**-2.4**	**-4.5**
General government expenditure	42.8	41.6	41.9	45.4	44.3	**42.9**	**na**
Monetary sector			*(Percentage change)*				
Broad money (M2, end-year)	12.6	17.1	31.4	45.2	40.0	**1.2**	**na**
Domestic credit (end-year)	24.6	43.3	44.4	15.3	32.5	**34.2**	**na**
			(In per cent of GDP)				
Broad money (M2, end-year)	11.0	10.6	11.4	14.1	16.5	**14.0**	**na**
Interest and exchange rates			*(In per cent per annum, end-year)*				
Discount rate	9.0	8.5	8.5	8.5	8.5	**8.5**	**na**
Money market rate	27.1	16.3	20.5	16.5	10.3	**18.5**	**na**
Deposit rate	2.1	3.6	3.7	5.1	4.1	**7.3**	**na**
Lending rate (long-term)	15.5	14.6	14.4	15.9	11.1	**18.1**	**na**
			(Dinars per US dollar)				
Exchange rate (official, end-year)	54.6	57.9	72.2	60.0	53.7	**62.9**	**na**
Exchange rate (official, annual average)	57.5	58.7	67.2	66.8	58.4	**55.7**	**na**
External sector			*(In millions of US dollars)*				
Current account	-1,532.0	-3,281.0	-2,194.0	-2,986.3	-6,334.9	**-8,721.3**	**-5,630.0**
Trade balance	-4,021.0	-6,469.0	-5,290.0	-6,271.0	-9,131.0	**-11,256.5**	**-7,400.0**
– Merchandise exports	3,319.0	4,082.0	4,970.0	6,442.0	8,755.0	**10,956.5**	**8,000.0**
– Merchandise imports	7,340.0	10,551.0	10,260.0	12,713.0	17,886.0	**22,213.0**	**15,400.0**
Foreign direct investment, net	1,365.0	966.0	1,550.0	4,264.0	2,523.2	**2,716.9**	**1,400.0**
Gross reserves, excluding gold (end-year)	3,411.0	4,096.0	5,628.0	11,648.0	13,892.0	**11,122.9**	**na**
External debt stock	13,575.0	14,099.0	15,467.0	19,606.0	26,236.0	**30,708.0**	**na**
			(In months of imports of goods and services)				
Gross reserves, excluding gold (end-year)	5.0	4.1	5.7	9.3	7.8	**5.0**	**na**
			(In per cent of exports of goods and services)				
Debt service	10.3	17.5	26.0	20.2	16.4	**17.3**	**na**
Memorandum items			*(Denominations as indicated)*				
Population (end-year, million)	7.5	7.5	7.5	7.5	7.5	**7.5**	**na**
GDP (in billions of dinars)	1,133.0	1,384.3	1,687.8	1,980.2	2,362.9	**2,831.0**	**2,985.0**
GDP per capita (in US dollars)	2,629.6	3,145.1	3,348.5	3,953.1	5,393.1	**6,773.9**	**na**
Share of industry in GDP (in per cent)	23.2	22.8	21.8	21.8	21.4	**20.7**	**na**
Share of agriculture in GDP (in per cent)	12.1	13.3	12.0	11.3	9.8	**10.1**	**na**
Current account/GDP (in per cent)	-7.8	-13.9	-8.7	-10.1	-15.7	**-17.2**	**-12.9**
External debt - reserves (in US$ million)	10,164.0	10,003.0	9,839.0	7,958.0	12,344.0	**19,585.1**	**na**
External debt/GDP (in per cent)	68.8	59.8	61.6	66.1	64.9	**60.4**	**na**
External debt/exports of goods and services (in per cent)	311.5	253.7	234.2	223.7	220.1	**204.9**	**na**

[1] All data exclude Kosovo.