

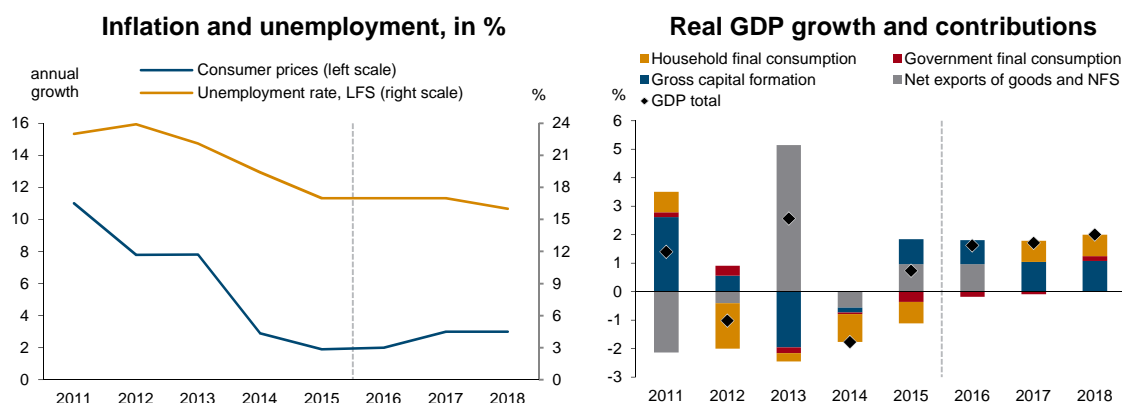


SERBIA: Early elections and reforms

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Slow recovery in tandem with investment and export growth is to be expected over the medium term. Growth over the next three years or so should reach 2% or slightly more, if the fiscal consolidation programme and structural reforms are put into effect. Industrial production, in particular manufacturing, should grow, as should certain exportable services. Growth in wages and consumption, however, should be only relatively slow.

Figure 53 / Serbia: main macroeconomic indicators



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

After a slow recovery last year, some acceleration is expected in the medium term. In 2015 the economy saw a return to growth – the preliminary rate is 0.7%. This, if it survives revisions, is higher than forecasted due primarily to somewhat higher investments. Still, this was mainly due to the rather deep recession in the previous year. Besides investment, net exports contributed positively to growth, while consumption was down on account of fiscal consolidation efforts and the decline in real wages by about 2.5% year on year. On the supply side, industrial production increased, though less due to manufacturing and more because of the recovery of production of energy, which had been strongly affected by the floods in the previous year. The rest of the economy stagnated at best.

Employment continues to increase, and unemployment to decline. Informal employment is apparently growing, but so is the formal one. The unemployment rate has declined substantially in the last years or

so. With recession in 2014 and almost stagnation in 2015, new employment indeed needs to be taking place in activities with below-average productivity. The unemployment rate remains high at around 17%.

The government would like to see growth accelerating to above 3% by 2018. The forecast remains rather cautious in the medium term mainly because consumption is not expected to increase due to continued fiscal consolidation and the announced reforms of the public sector, which will mean declining employment and additional pressure on wages and compensations. The speed-up of growth has to come from investment and exports. The former should increase by 6% per year on average, while there is uncertainty about the development of net exports. Imports tend to increase significantly with the acceleration of growth especially if it is financed by foreign investments. Even if exports are mostly aimed at, it will take some time before that translates into continued contribution of net exports to overall growth. Also, exports of commodities will continue to face low world prices, which will affect negatively exports of raw materials and agricultural products.

Public investments are to increase. So far, as in some other countries in the region, public investment has underperformed. The government is unable to spend all the money that it sets aside on infrastructure investments primarily. This may change in the medium term, and that would certainly contribute to growth and employment.

The reforms as designed have not been popular. The Serbian reform programme has been praised because it has centred on fiscal consolidation and structural reform. When it comes to the latter, so far that just meant a change in the labour law to make firing (and hiring) easier. That has proved to be unpopular as expected, but as it affected the private sector it did not matter much because neither firing nor hiring have met with much legal rigidity under the old law either (with an unemployment rate at 24% at the time of the passing, the old law clearly did not provide for much workers' protection). Fiscal adjustment is another matter because compensations and pensions were cut nominally, by 10%, with an exemption for the recipients of low pensions. These unpopular measures made it well-nigh impossible to implement additional structural reforms in the public as well as in the private sectors. This is one problem with the strategy of fiscal consolidation cum structural reforms: if reforms come before austerity, the strategy may work, if not, the loss of support may kill them.

Early elections were announced to gain a mandate and time to restart the programme of structural reforms. The government enjoys popular support and in part the opposition is disorganised and without a political programme. It seems clear that the governing parties cannot do better if they waited for the regular elections in two years' time. In addition, they hope to strengthen the control on the provincial and local levels (local elections are held at the same time as the general one). If indeed the support is such that they will have a secure majority without the need to broaden the governing coalition, they will have four years to rekindle the reform programme.

In foreign policy, strategic ambiguity is to be followed. In the last few years, since 2012 in any case, the government has been strategically ambiguous with accession to the European Union being the main goal, but close relationship with Russia being also maintained. The latter was expected to be beneficial in economic terms, with hopes riding high that Serbian exports would benefit from the regime of sanctions and countersanctions. Serbia has a free trade agreement with Russia, though exports to that market were hardly ever above 10% of total exports. These hopes did not materialise due to a sharp drop of demand for imports in Russia itself. However, there is some political constituency for closer

political and military ties with Russia, so the ambiguity in foreign policy will remain, even though there is practically nothing that Russia can offer in return.

Regional recovery and the recovery in the EU should prove supportive of some speed-up of growth. The neighbouring countries are important trading partners, and not only those in the Western Balkans, but also Hungary and Romania. As most of them are expected to do better in the medium term, exports to these markets should help the recovery. The same goes for the EU, except that demand is less of a problem than supply of exportable goods when it comes to that market. Serbia is a very small economy, so the quantity of its exports to the EU, where its producers are price takers, is not really limited by market demand.

Table 22 / Serbia: selected economic indicators

	2011	2012	2013	2014	2015 ¹⁾	2016	2017 Forecast	2018
Population, th. pers., mid-year	7,237	7,201	7,167	7,132	7,040	7,010	7,000	7,000
Gross domestic product, RSD bn, nom.	3,408	3,584	3,876	3,908	4,000	4,100	4,300	4,500
annual change in % (real)	1.4	-1.0	2.6	-1.8	0.7	1.6	1.7	2.0
GDP/capita (EUR at exchange rate)	4,600	4,400	4,800	4,700	4,700	4,600	4,800	4,900
GDP/capita (EUR at PPP)	9,500	9,800	10,100	10,200	10,700	.	.	.
Consumption of households, RSD bn, nom.	2,596	2,728	2,886	2,922	2,900	.	.	.
annual change in % (real)	0.9	-2.1	-0.4	-1.3	-1.0	0.0	1.0	1.0
Gross fixed capital form., RSD bn, nom.	627	759	668	652	700	.	.	.
annual change in % (real)	4.6	13.2	-12.0	-3.6	4.0	4.0	5.0	4.0
Gross industrial production ²⁾								
annual change in % (real)	2.5	-2.2	5.3	-6.5	8.2	5.0	5.0	5.0
Gross agricultural production								
annual change in % (real)	0.9	-19.5	21.7	2.1	-8.0	.	.	.
Construction output ³⁾								
annual change in % (real)	5.9	-9.8	-3.9	-1.5	20.5	.	.	.
Employed persons, LFS, th, average ⁴⁾	2,253	2,228	2,311	2,544	2,620	2,650	2,680	2,710
annual change in %	-6.0	-1.1	3.7	10.1	3.0	1.0	1.0	1.0
Unemployed persons, LFS, th, average ⁴⁾	671	701	656	613	530	540	550	520
Unemployment rate, LFS, in %, average ⁴⁾	23.0	23.9	22.1	19.4	17.0	17.0	17.0	16.0
Reg. unemployment rate, in %, end of period	27.6	28.6	29.1	28.4	28.0	.	.	.
Average monthly gross wages, RSD	52,733	57,430	60,708	61,426	61,145	63,300	65,900	68,600
annual change in % (real, gross)	0.1	1.0	-1.9	-1.7	-2.4	1.0	1.0	1.0
Average monthly net wages, RSD	37,976	41,377	43,932	44,530	44,432	45,800	47,600	49,500
annual change in % (real, net)	0.2	1.1	-1.5	-1.5	-2.1	1.0	1.0	1.0
Consumer prices, % p.a.	11.0	7.8	7.8	2.9	1.9	2.0	3.0	3.0
Producer prices in industry, % p.a.	12.7	6.8	2.7	1.3	1.0	2.0	2.0	2.0
General governm. budget, nat. def., % of GDP								
Revenues	40.0	41.1	39.7	41.5	40.0	40.0	40.0	40.0
Expenditures	44.8	47.9	45.1	48.1	45.0	44.0	43.0	42.0
Deficit (-) / surplus (+)	-4.8	-6.8	-5.5	-6.6	-5.0	-4.0	-3.0	-2.0
Public debt, nat. def., % of GDP	45.4	56.2	59.6	70.4	73.8	80.0	85.0	85.0
Central bank policy rate, % p.a., end of period ⁵⁾	9.75	11.25	9.50	8.00	4.50	5.0	5.0	5.0
Current account, EUR mn	-3,656	-3,671	-2,098	-1,985	-2,000	-2,100	-1,900	-2,000
Current account, % of GDP	-10.9	-11.6	-6.1	-6.0	-6.0	-6.0	-6.0	-6.0
Exports of goods, BOP, EUR mn	8,118	8,376	10,515	10,641	11,200	11,800	12,400	13,000
annual change in %	18.4	3.2	25.5	1.2	5.3	5.0	5.0	5.0
Imports of goods, BOP, EUR mn	13,614	14,011	14,674	14,752	15,200	15,700	16,300	17,100
annual change in %	17.6	2.9	4.7	0.5	3.0	3.0	4.0	5.0
Exports of services, BOP, EUR mn	3,027	3,093	3,422	3,810	4,200	4,400	4,600	4,800
annual change in %	13.8	2.2	10.6	11.3	10.2	5.0	5.0	5.0
Imports of services, BOP, EUR mn	2,873	2,981	3,109	3,344	3,600	3,800	4,000	4,200
annual change in %	7.6	3.8	4.3	7.6	7.6	5.0	5.0	5.0
FDI liabilities (inflow), EUR mn	3,544	1,009	1,548	1,500	700	.	.	.
FDI assets (outflow), EUR mn	225	256	250	264	100	.	.	.
Gross reserves of NB, excl. gold, EUR mn	11,497	10,295	10,734	9,351	9,812	.	.	.
Gross external debt, EUR mn ⁶⁾	24,123	25,645	25,738	25,741	28,000	29,000	30,000	31,000
Gross external debt, % of GDP ⁶⁾	72.2	80.9	75.1	77.3	84.5	89.0	89.0	90.0
Average exchange rate RSD/EUR	101.95	113.13	113.14	117.31	120.76	126	128	130
Purchasing power parity RSD/EUR	49.67	50.64	53.64	53.77	53.16	.	.	.

1) Preliminary and wiiw estimates. - 2) Excluding arms industry. - 3) According to gross value added. - 4) Until 2013 survey of April and October, quarterly thereafter. From 2013 based on census 2011. - 5) Two-week repo rate. - 6) BOP 5th Edition.

Source: wiiw Databases incorporating national statistics. Forecasts by wiiw.