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## **Serbia: Slow and unbalanced recovery**

***GDP growth this year is expected to be 2.5%. Next year, it should accelerate to 3%. An inflation rate of more than 10% has raised concerns as to stability. Much will depend on the outcome of the general elections next year. Social pressures and unrest usually accelerate in the run-up to the elections; they have already become more than apparent. It is also expected that negotiations on EU membership will start next year: something that should have a stabilizing effect.***

GDP growth is expected to be 2.5% this year. Next year, it should accelerate to 3%. These are official forecasts, backed by the IMF though. The initial estimate of the first-quarter GDP growth is also 3%.

There is, however, significant uncertainty about the accuracy of the growth rates in the last two years and thus also concerning those of the current estimates and forecasts. The reason is that the final figure for the decline of GDP in 2009 is 3.5%. However, doubts are raised from within the statistical office about the accuracy of that figure and some expect that it will be corrected to a decline of 6.5% in 2009. The final assessment of GDP growth in 2010 is still to come anyway and initial estimates of quarterly GDP growth are notoriously unreliable. Without even doubting the currently released figures, such large uncertainties about the real GDP growth figures do not inspire confidence in the official pronouncements and forecasts.

There are two additional considerations. For one, the output gap is hard to assess because potential output growth, and thus level, are not known while the reported real growth rates are not reliable. That makes it difficult to reconcile official estimates of GDP decline in 2009 and its recovery in 2010 and 2011 with the much greater reduction of employment. From October 2008 to October 2010 employment declined by about 15% (about 400,000 jobs lost). This is consistent with a huge loss in potential output – certainly larger than that implied by the reported figures of actual real GDP decline.

For another, inflation has accelerated since mid-2010 and the headline inflation rate is currently close to 15% annualized. The central bank is arguing that this is mostly due to one-time price increases and that inflation will come down without too much monetary tightening, though the reference rate of the central bank has been increasing in the last year or so. It is still negative in real terms at least at headline inflation but most probably in terms of inflationary expectations too. In addition, the dinar has appreciated by about 10% against the euro and there are further pressures in the same direction. Currently, therefore, there is appreciation with accelerating inflation. If it turned out that some stabilization measures proved necessary, growth might disappoint next year. That seems to be what is expected because parliamentary elections will be held in the first half of next year and the next government will have to assess the measures it needs to take to stabilize the economy.

Even if the current forecasts prove correct, recovery will have to be considered slow because growth of employment cannot be expected to be strong. In fact, at the projected growth rates, the output gap will continue to widen, which also means that the labour market will continue to be depressed. In addition, there are structural changes that need to take place and will keep both the growth of GDP and of employment low. Jobs in the services sector are not coming back and jobs are being lost in agriculture too. Manufacturing has declined significantly in this crisis and is recovering very slowly. Whatever growth there is in manufacturing, it is connected with the growth of exports, which has been quite strong since the end of 2009. However, exports are driven mostly by sectors and companies that have been export-oriented before the crisis. Those have been helped by the strong depreciation of the dinar in 2009 and 2010. Investments in new production for export have been few and may not be forthcoming given the appreciation of the dinar. Much hope is being put on the revival of the automotive industry due to investments by Fiat. The scope and the scale of that investment still remain to be determined.

The prospects for this and the next few years are that GDP growth will be between 3% and 4% and that stability will be preserved. Much will depend on the outcome of next year's general elections. Social pressures and unrests usually accelerate before the elections and this is already happening. The aim is to secure as good a starting point as possible before the new government comes in and starts to work on a programme of stabilization and reforms. In the last two elections that was enough to basically block incoming governments from taking any austerity and reform measures. This time around those measures may prove to be unavoidable and, when taken, they will determine the medium-term prospects.

Table RS

## Serbia: Selected Economic Indicators

	2007	2008	2009	2010 <sup>1)</sup>	2010 1st quarter	2011	2011 Forecast	2012 Forecast	2013
Population, th pers., average	7381.6	7350.2	7320.8	7300.0	.	.	7280	7250	7220
Gross domestic product, RSD bn, nom. <sup>2)</sup>	2276.9	2661.4	2713.2	3100.0	.	.	3500	3900	4300
annual change in % (real) <sup>2)</sup>	6.9	5.5	-3.1	1.8	0.4	3.4	2.5	3	3
GDP/capita (EUR at exchange rate)	3900	4400	4000	4100	.	.	.	.	.
GDP/capita (EUR at PPP - wiiw)	8200	9000	8300	9000	.	.	.	.	.
Consumption of households, RSD nn, nom. <sup>2)</sup>	1714.0	2023.6	.	.	.	.	.	.	.
annual change in % (real) <sup>2)3)</sup>	6	6	-2	2	.	.	2	2	2
Gross fixed capital form., RSD bn, nom. <sup>2)</sup>	552.3	632.4	.	.	.	.	.	.	.
annual change in % (real) <sup>2)3)</sup>	12	8	-5	-4	.	.	3	4	4
Gross industrial production									
annual change in % (real) <sup>4)</sup>	3.7	1.1	-12.1	2.9	1.1	5.6	3	5	5
Gross agricultural production									
annual change in % (real)	-8.0	9.0	5.0	0.0	.	.	5	5	5
Construction output total <sup>5)</sup>									
annual change in % (real)	10.8	4.6	-14.3	-10.0	.	.	0	5	5
Employed persons - LFS, th, Oct <sup>6)</sup>	2655.7	2821.7	2616.4	2396.2	.	.	2400	2400	2420
annual change in %	1.0	.	-7.3	-8.4	.	.	0	0	1
Unemployed persons - LFS, th, Oct <sup>6)</sup>	585.5	445.4	503.0	568.7	.	.	.	.	.
Unemployment rate - LFS, in %, Oct <sup>6)</sup>	18.1	13.6	16.1	19.2	.	.	20	20	20
Reg. unemployment rate, in %, end of period	25.4	24.0	24.8	25.9	26.4	26.8	27	27	27
Average gross monthly wages, RSD <sup>4)7)</sup>	38744	45674	44147	47450	44326	48803	.	.	.
annual change in % (real, net) <sup>4)7)</sup>	19.5	3.9	0.2	0.7	1.5	-2.3	.	.	.
Consumer prices, % p.a.	7.0	13.5	8.6	6.8	4.6	12.8	10	8	6
Producer prices in industry, % p.a. <sup>8)</sup>	5.9	12.4	5.6	12.7	11.1	18.2	.	.	.
General governm.budget, nat.def. % GDP									
Revenues	44.0	43.0	42.3	39.5	.	.	.	.	.
Expenditures	46.0	45.6	46.7	43.9	.	.	.	.	.
Deficit (-) / surplus (+), % GDP	-2.0	-2.6	-4.5	-4.4	.	-3.2	-5	-4	-3
Public debt, nat.def., in % of GDP	29.8	27.9	32.6	36.0	31.1	43.5	43	45	45
Central bank policy rate, % p.a., end of period <sup>9)</sup>	10.0	17.8	9.5	11.5	9.0	12.3	12	10	10
Current account, EUR mn	-5052.6	-7054.1	-2084.4	-2082.0	-759.8	-843.8	-2600	-3500	-3900
Current account in % of GDP	-17.7	-21.6	-7.2	-6.9	.	-11.8	-8.0	-9.9	-10.0
Exports of goods, BOP, EUR mn	6382.5	7416.0	5977.8	7402.5	1473.4	1951.6	8500	9400	10300
annual growth rate in %	24.9	16.2	-19.4	23.8	13.9	32.5	15	10	10
Imports of goods, BOP, EUR mn	13451.3	15917.2	11096.3	12175.8	2659.2	3268.9	13400	14700	16200
annual growth rate in %	33.3	18.3	-30.3	9.7	-4.8	22.9	10	10	10
Exports of services, BOP, EUR mn	2304.0	2741.4	2500.0	2667.1	536.7	631.4	2900	3200	3500
annual growth rate in %	25.3	19.0	-8.8	6.7	-5.6	17.6	10	10	10
Imports of services, BOP, EUR mn	2565.1	2926.1	2481.7	2661.9	554.8	603.9	2900	3200	3500
annual growth rate in %	36.4	14.1	-15.2	7.3	-8.6	8.8	10	10	10
FDI inflow, EUR mn	2512.6	2017.5	1410.1	1003.1	333.2	325.4	1500	1500	2000
FDI outflow, EUR mn	691.8	193.1	37.6	143.0	49.7	18.8	50	100	100
Gross reserves of NB, excl. gold, EUR mn	9440.7	7938.5	10277.7	9554.9	10093.7	9490.2	.	.	.
Gross external debt, EUR mn	17139.0	21088.0	22487.0	23786.4	22942.6	22671.9	.	.	.
Gross external debt in % of GDP	60.2	64.6	77.9	79.0	76.2	70.0	.	.	.
Average exchange rate RSD/EUR	79.98	81.47	93.94	102.90	98.60	103.99	108	110	110
Purchasing power parity RSD/EUR <sup>10)</sup>	37.59	40.41	44.49	47.07	.	.	.	.	.

1) Preliminary. - 2) According to ESA'95 (non-observed economy partially included). - 3) wiiw estimate. - 4) Quarterly data according to NACE Rev. 2. - 5) Gross value added. - 6) From 2008 extended survey as of April and October. - 7) From 2009 including wages of employees working for sole proprietors. - 8) Domestic output prices. - 9) Two-week repo rate. - 10) Benchmark results 2005 from Eurostat and wiiw estimates.

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