Vladimir Gligorov

Serbia:
Slow recovery with depreciation

Unlike most other Balkan countries, Serbia's actual exchange rate regime is a managed float. As a consequence the central bank could let the dinar depreciate rather strongly from the beginning of the crisis: above 30% since August 2008. Initially, that had a stronger impact on imports, but it may be supporting the growth of exports since late 2009. In any case, exports have been growing by somewhat less than 20% while imports are still declining by just above 2% year-on-year in the first five months of 2010. This seems to be affecting industrial production, which is growing by somewhat less than 4% this year. These developments may have been enough to produce a 1% growth of GDP in the first quarter. Investments are declining, however, and so is private consumption. Public consumption, on the other hand, is increasing faster than planned and the fiscal deficit should be higher by somewhat less than 1% of GDP, mainly due to lower than envisaged revenues, for the year as a whole. The current forecast, agreed on by the government and the IMF, is for 1.5% of growth of GDP this year and 3% growth next year. This presents a downward revision from 2% in 2010 and may prove to be somewhat optimistic. Still, numbers put aside, the recovery is clearly slow and the risks are biased on the downside.

The key risk is the state of the balance sheets of the corporations. They are under pressure from declining consumption and rising costs due to exchange rate depreciation. The hardest hit is construction. That activity is depressed and there is scant chance that it might recover any time soon. Credit has dried out so it is hard to build and even harder to sell the already built apartments and offices. Similarly, falling retail trade is presenting problems for the companies in that line of business. Indeed, the whole services sector is facing tough times, and services are the major part of the economy.

Labour market problems are also mounting. Loss of employment in 2009 was quite strong and labour shedding has been continuing in the first half of this year too. Additional job losses are planned with the reduction of government employees. Furthermore, wages have been frozen since the beginning of the crisis and are declining in real terms and also in euro due to the devaluation. Similarly, real pensions are declining for the same reason.

Given that the number of pensioners is not much lower than the number of employed people, the overall fall of income in real terms is quite significant.

Dinar depreciation has not speeded up inflation all that much; indeed inflation is slowing down. If it were not for the upward adjustment of administered prices and some contribution from higher import prices, deflationary pressures would be quite strong. In any case, the slowing down of inflation has made it possible for monetary policy to be more accommodative. The central bank reduced its policy rate from somewhat below 20% before the crisis to 8% in early June 2010 and further cuts are possible if there is no spike in the rate of inflation.

Fiscal policy has been accommodative with deficits above 4% of GDP in 2009 and 2010. Not much of a fiscal stimulus can be attributed to these deficits, however, because they mostly reflect the shortfall in public revenues. As public sector wages and also pensions have been frozen and public investments cannot be increased within a short period of time, it is hard to attribute much growth support to fiscal policy. Monetary policy has been more active with the central bank reducing the reserve requirements in addition to lowering interest rates. This has had some effects on the availability of credit, but mainly for government debt. Indeed, there are some indications that the credit exposure of the, mostly foreign-owned, banks is being reduced. In early 2009 these banks signed up to the Vienna Initiative, that is to a commitment that they will not reduce their exposure to the Serbian financial market. At the beginning of this year, however, this commitment was relaxed and it was agreed, implicitly, that they could reduce their credit exposure by as much as 20%. This may be one of the reasons why the dinar exchange rate continues to depreciate in euro terms.

The prospect is for a slow recovery mostly driven by an improvement in the trade balance. That has a limit, however, because the tradable sector is rather small and with declining investments, export capacity is quite limited in the short run. The government intends to sell the Telecom and use the money to invest in infrastructure with the hope that this will lead to increased foreign investments in the tradable sector. As wages are quite low in euro terms, better and cheaper access to external markets could support a speed-up in growth. The risk is, however, that pressure to support current consumption may lead to the privatization income to be spent and not invested. In any case, in the medium run, slow recovery if not stagnation seem the most probable prospect.

Table RS

Serbia: Selected Economic Indicators

	2006	2007	2008	2009 [1)]	2009	2010	2010	2011	2012
					1st quarter			Forecast	
Population, th pers., average	7411.6	7381.6	7350.2	7320.0	.	.	7300	7280	7250
Gross domestic product, RSD bn, nom.	1962.1	2302.2	2722.5	2953.5	.	.	3200	3400	3600
annual change in % (real)	5.2	6.9	5.5	-3.0	-4.1	0.6	1	2	3
GDP/capita (EUR at exchange rate)	3100	3900	4600	4300	.	.	.	.	.
GDP/capita (EUR at PPP - wiiw)	7700	8300	9000	8700	.	.	.	.	.
Consumption of households, RSD mn, nom.	1492.7	1714.0	2023.6	.	.	.	.	.	.
annual change in % (real) [2)]	5.4	6	6	-2	.	.	0	2	2
Gross fixed capital form., RSD mn, nom.	412.8	552.3	632.4	.	.	.	.	.	.
annual change in % (real) [2)]	15.2	12	8	-5	.	.	0	3	4
Gross industrial production									
annual change in % (real)	4.7	3.7	1.1	-12.1	-15.7	2.8	2	3	3
Gross agricultural production									
annual change in % (real)	-2.6	-8.0	9.0	5.0	.	.	.	.	.
Construction output total [3)]									
annual change in % (real)	7.7	10.8	4.6	-17.1	-14.0	.	.	.	.
Employed persons - LFS, th, Oct [4)]	2630.7	2655.7	2821.7	2616.4	.	.	2510	2510	2510
annual change in %	-3.8	1.0	.	-7.3	.	.	-4	0	0
Unemployed persons - LFS, th, Oct [4)]	693.0	585.5	445.4	503.0	.	.	.	.	.
Unemployment rate - LFS, in %, Oct [4)]	20.9	18.1	13.6	16.1	.	.	22	22	22
Reg. unemployment rate, in %, end of period	28.0	25.4	24.0	24.8	25.1	26.2	.	.	.
Average gross monthly wages, RSD [5)]	31745	38744	45674	44147	41933	44326	.	.	.
annual change in % (real, net) [5)]	11.4	19.5	3.9	0.2	2.6	1.4	.	.	.
Consumer prices, % p.a.	11.7	7.0	11.7	8.6	9.4	4.3	6	4	4
Producer prices in industry, % p.a. [6)]	13.3	5.9	12.4	5.6	5.3	11.1	.	.	.
General governm.budget, nat.def., % GDP									
Revenues	43.8	42.4	41.0	39.5	.	.	.	.	.
Expenditures	45.4	44.3	43.5	43.7	.	.	.	.	.
Deficit (-) / surplus (+), % GDP	-1.7	-1.9	-2.5	-4.2	.	.	-5	-3	-3
Public debt, nat.def., in % of GDP	37.3	29.8	27.9	32.6	.	31.1	35	36	36
Discount rate of NB, % p.a., end of period	8.5	8.5	8.5	8.1	8.5	8.1	8	7	7
Current account, EUR mn	-2356.0	-4614.4	-6089.7	-1743.4	-978.6	-724.9	-2700	-3100	-3100
Current account in % of GDP	-10.1	-16.0	-18.2	-5.5	.	.	-9	-10	-10
Exports of goods, BOP, EUR mn	5109.0	6382.0	7415.0	5978.0	1291.0	1470.6	6300	6900	7600
annual growth rate in %	27.4	24.9	16.2	-19.4	-22.8	13.9	5	10	10
Imports of goods, BOP, EUR mn	10090.0	13020.0	14964.0	10760.0	2755.4	2622.0	11300	12400	13600
annual growth rate in %	21.8	29.0	14.9	-28.1	-20.8	-4.8	5	10	10
Exports of services, BOP, EUR mn	1839.0	2304.0	2741.4	2500.1	568.1	537	2500	2800	3100
annual growth rate in %	39.3	25.3	19.0	-8.8	-17.4	-5.5	0	10	10
Imports of services, BOP, EUR mn	1880.0	2557.7	2913.9	2477.3	606.9	554.8	2500	2800	3100
annual growth rate in %	41.9	36.0	13.9	-15.0	-6.9	-8.6	0	10	10
FDI inflow, EUR mn	3392.4	2512.6	2017.5	1410.1	644.7	333.2	1000	1500	1500
FDI outflow, EUR mn	70	692	193	38	1.4	49.7	100	200	200
Gross reserves of NB, excl. gold, EUR mn	8857.9	9440.7	7938.5	10277.7	7864.5	10093.4	.	.	.
Gross external debt, EUR mn	14884.4	17789.4	21800.5	22787.0	21445.2	23278.4	.	.	.
Gross external debt in % of GDP	59.9	61.2	70.9	74.0	69.6	74.9	.	.	.
Average exchange rate RSD/EUR	84.19	79.98	81.47	93.92	93.8	98.6	103	110	115
Purchasing power parity RSD/EUR [7)]	34.42	37.66	41.04	46.55	.	.	.	.	.

1) Preliminary. - 2) wiiw estimate. - 3) Gross value-added. - 4) From 2008 extended survey as of April and October. - 5) From 2009 methodological changes of survey. - 6) Domestic output prices. - 7) Benchmark results 2005 from Eurostat and wiiw estimates.

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