

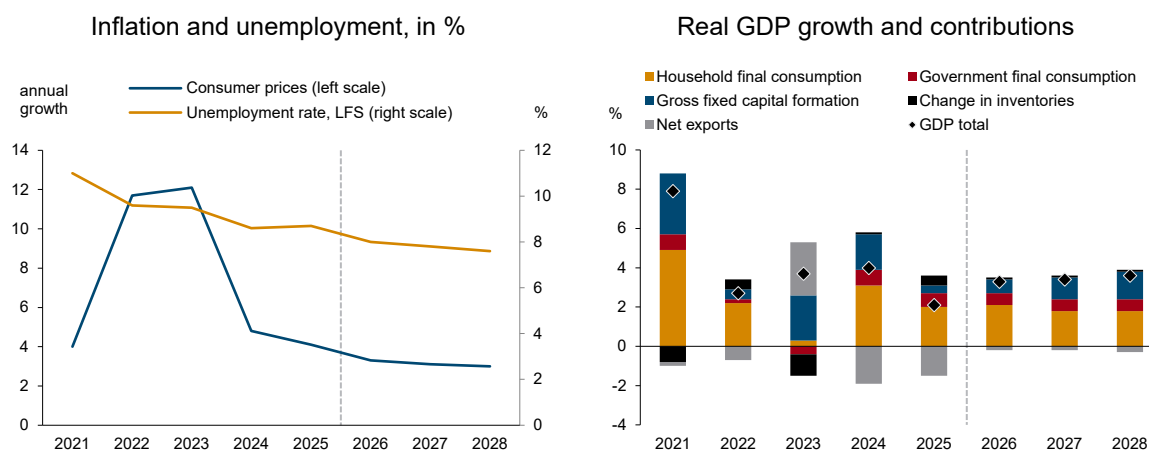


SERBIA: The moment of truth

BRANIMIR JOVANOVIĆ

The long-awaited parliamentary elections will take place on 25 October, at a moment when Serbia's economy is finally catching its breath – inflation is close to 2% and GDP growth is at its highest for two years. Long-time leader Aleksandar Vučić faces the Student List, which emerged from two years of protests against corruption and bad governance. The atmosphere is tense, and the result is likely to be razor thin – and will probably be contested by whichever side loses. If Vučić stays in power, economic policy will continue as before, though most likely with a tighter authoritarian grip. If the Student List wins, policy is likely to shift towards supporting domestic companies and higher value-added activities, with a stronger focus on democratic standards and the rule of law.

Figure 3.19 / Serbia: Main macroeconomic indicators



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

On the face of it, Serbia's economy seems to have improved; but scratch the surface and a more nuanced picture emerges. GDP grew by 3.8% year on year in Q2 2026, the healthiest rate for two years. However, this solid growth was driven mainly by more robust private consumption, which rose by 4% year on year in Q2, supported by lower inflation and higher incomes. Both of these owe much to government intervention – the cap on fuel prices and the big increases in public-sector wages and pensions. Both can be criticised as populist measures ahead of the coming elections.

Moreover, the fact that growth is driven mainly by consumption raises questions about its durability and sustainability. The other GDP components performed less well. Gross fixed investment grew by 3.3% year on year in Q2, while foreign direct investment (FDI) and public investment both declined. FDI fell by 5% in nominal terms in Q2, bringing the decline for the first half of the year to around 25%. This appears to have been largely driven by global factors, with FDI declining across the CESEE region amid heightened geopolitical uncertainty, although Serbia's domestic political crisis may also have played a role. Public investment was also weak in Q2, falling by 18%, although a strong first quarter meant that it was still up by 15% for the first half year and remained the main driver of overall investment activity. Exports grew by only around 4%, despite the resumption of production at the Stellantis factory in Kragujevac, while imports rose more rapidly, by 5%, so net exports made a negative contribution to growth.

Inflation declined to around 2% in July and August, well below last year's levels and lower than we were expecting in spring. This partly reflects strong domestic agricultural production and lower global oil prices over the summer, but it is still primarily driven by government price controls. After the US attack on Iran at the end of February, the government cut excise duties on motor fuels and began setting maximum retail fuel prices at below the market level. As a result, the price of diesel has since risen by around 20% – far less than elsewhere in the region. However, inflationary pressures may be starting to build again. Consumer prices rose by 0.5% in August compared with the previous month – equivalent to around 6% on an annualised basis – and the recent increase in global oil prices is likely to add further pressure in the coming months.

As with GDP growth, the labour-market data look good at first sight, but the devil is in the detail. Unemployment fell to 7.2% in Q2, the lowest on record and 1.3 percentage points lower than a year earlier. However, this owes primarily to a shrinking active population, not to rising employment: the number of people employed actually declined by around 46,000 year on year. But the active population fell even more – by around 93,000, meaning that the number of the unemployed dropped by around 47,000. Roughly two thirds of the decline in the active population reflected more people moving out of the labour force, and one third a shrinking working-age population (partly due to emigration). Since the fall in unemployment was not driven by job creation, it is unlikely to last: as some of those who left the labour force start looking for work again, we expect the unemployment rate to edge up somewhat over the remainder of the year.

Wages, meanwhile, continue to grow strongly, supported to a large extent by government decisions to raise public-sector wages and the minimum wage. Real wages increased by around 8% in the first half of the year, and the further increases announced ahead of the elections should keep wage growth elevated in the coming months and continue to support household consumption. However, wage growth can only support the economy up to a point.

These dynamics point to the limits of Serbia's current growth model, which rests on three pillars: public investment in infrastructure, FDI and rising incomes. On each of these, Serbia has performed well. Public investment has averaged around 6% of GDP in recent years, including this year. FDI inflows were strong for many years, until the decline seen in the past two years, and incomes have grown solidly. Yet this has failed to translate into faster growth and convergence: Serbia's GDP per capita in PPS terms remains only marginally above 50% of the EU average. Growth has also proved highly volatile, with good years regularly followed by poor ones. Higher, more stable and more sustainable growth requires stronger

domestic private investment – and that has largely been missing in Serbia. This reflects both weak governance – a lack of rule of law and widespread corruption – and the government's near-exclusive focus on supporting foreign investors, rather than domestic companies. To break free of this pattern, Serbia needs a different policy mix: more support for domestic firms, an active industrial and innovation policy, and a shift towards more productive, higher value-added and export-oriented activities.

Given the better-than-expected inflation performance in the first eight months of the year, we are revising our average inflation forecast for 2026 down to 3.3%. At the same time, we are raising slightly our forecast for 2027, to 3.1%, as we expect the renewed inflationary pressures to prove somewhat more persistent than previously anticipated. We are also revising our GDP growth forecast for 2026 up to 3.3%, reflecting the stronger-than-expected results from the first half year. For 2027, we are revising the figure slightly upwards, to 3.4%, in the expectation that the post-election period will bring fresh momentum.

The parliamentary elections on 25 October have effectively become a referendum: Vučić or the students. Aware that his chances of losing were high, Vučić postponed the elections for as long as he could. He now seems to have concluded that there will be no better moment than the present. The economy is doing well, with GDP growth at a two-year high, strong wage increases and inflation kept low by price controls – and this is what his campaign is built on. He has also, in effect, been campaigning for months, and hopes to have caught the students on the hop. On top of that, he can count on the usual pre-election tools: one-off payments, control over the media, voters brought in from neighbouring countries, and other familiar forms of pressure. Regional developments are also playing into his hands. Ethno-nationalist tensions have been fuelled by the general elections in Bosnia and Herzegovina on 4 October, the death of Ratko Mladić and the prison sentence handed down to the former Kosovo president, Hashim Thaçi. Such tensions typically boost Vučić's support, as he presents himself as the only person capable of defending Serbia against its foreign enemies.

On the other side are the students, who launched their protests two years ago following the collapse of a canopy at Novi Sad railway station, which killed 16 people. What began as a demand for accountability grew into a mass movement against corruption and authoritarian rule, and for a better life more broadly. True to their direct-democracy approach, the students selected their electoral list through plenums, filling it with non-party candidates: university professors, experts and public figures. It is headed by Ilija Srdanović, a cardiologist and professor at the Faculty of Medicine in Novi Sad, who was relatively unknown to the wider public until now. The list includes numerous PhDs but relatively few economists, the most prominent being former National Bank governor, Dejan Šoškić. The campaign relies mainly on social media and touring the country. The students have published an 11-point programme, mostly concerning the rule of law. Only one point is devoted to economic development: it pledges a shift from a model based on cheap labour to one built on high value added, innovation and support for domestic companies. This is a welcome idea, though details on how it would be achieved remain scarce. So far, this is the only clearly stated economic difference between Vučić's government and a potential student-led government: whether domestic firms should receive more support.

The campaign is already intense, marked by tension and pressure. There have been numerous incidents targeting government critics, including the use of spyware against student and opposition activists. Reliable polls are scarce in Serbia, as most pollsters are seen as close to one side or the other – if not in intent, then at least in terms of who is willing to respond to them. Faktor Plus, seen as close to the government, gives the ruling coalition a clear lead (47% vs 32% in early September), while CRTA

and NSPM had the Student List ahead in July (45% vs 36% and 40% vs 38%, respectively). The betting platform Polymarket makes Vučić clear favourite in the race for prime minister. However, with a total trading volume of only around EUR 1mn, the market can easily be manipulated.

Our view remains that the students will win, thanks to the referendum-like atmosphere and what we expect to be the highest turnout in recent history, which should benefit the opposition. Global developments are also working in their favour, with Viktor Orbán's defeat in Hungary and Donald Trump's declining popularity in the US weakening Vučić's position. However, we acknowledge that the tide has shifted in Vučić's favour recently, thanks to the relatively healthy economy, heavy pre-election spending and regional tension. The result is therefore expected to be very tight, and tension is likely to run high once it has been announced and in the days that follow.

In our baseline scenario of a student victory, Serbia is likely to follow a path similar to Hungary's after Orbán's defeat. A student-led government is expected to focus on the rule of law and the fight against corruption. On the economic side, domestic companies will attract greater attention, as set out in the students' programme, possibly through industrial and innovation policy. The programme says nothing about EU accession – no great surprise, given how little the issue matters in Serbia at the moment – but a student-led government will likely be more pro-EU in spirit. Still, there will be no break with Russia: people from the Student List have clearly stated that they will seek to maintain friendly relations with Russia.

In the alternative scenario of Vučić staying in power, he is likely to double down on the repressive measures he has used so far. He can be expected to go after his critics and opponents, weaken the opposition further and consolidate his hold on power for years to come. Economic policy will remain unchanged, relying on attracting FDI and large-scale public investment – the very model whose limits are becoming increasingly visible. Foreign policy will also stay the same, with Serbia continuing to occupy several stools at once: the EU, the US, Russia and China. EU membership will remain the official goal, but there is no real interest in pursuing it.

Table 3.19 / Serbia: Selected economic indicators

	2022	2023	2024	2025	2026	2027	2028
					Forecast		
Population, th. pers., mid-year	6,664	6,623	6,587	6,550	6,503	6,463	6,413
Gross domestic product, RSD bn, nom.	7,460	8,819	9,763	10,558	11,266	12,011	12,812
annual change in % (real)	2.7	3.7	4.0	2.1	3.3	3.4	3.6
GDP/capita (EUR at PPP)	16,140	18,600	20,620	21,920			
Consumption of households, RSD bn, nom.	4,822	5,436	5,954	6,389			
annual change in % (real)	3.5	0.5	5.1	3.3	3.4	3.0	3.0
Gross fixed capital form., RSD bn, nom.	1,784	2,061	2,320	2,374			
annual change in % (real)	2.2	9.7	7.7	1.7	3.0	5.0	6.0
Gross industrial production							
annual change in % (real)	1.9	2.6	3.2	0.8	2.5	3.0	3.5
Gross agricultural production							
annual change in % (real)	-8.9	6.4	-6.6	0.0			
Construction output							
annual change in % (real)	-8.2	7.9	3.3	-5.5			
Employed persons, LFS, th, average	2,819	2,842	2,898	2,870	2,860	2,860	2,870
annual change in %	2.3	0.8	2.0	-1.0	-0.5	0.0	0.5
Unemployed persons, LFS, th, average	296	296	272	272	249	242	236
Unemployment rate, LFS, in %, average	9.6	9.5	8.6	8.7	8.0	7.8	7.6
Average monthly gross wages, RSD	103,316	118,599	135,403	151,086	165,440	177,390	190,020
annual change in % (real, gross)	1.7	2.4	9.0	7.5	6.0	4.0	4.0
Average monthly net wages, RSD	74,933	86,007	98,143	109,462	119,860	128,520	137,670
annual change in % (real, net)	1.7	2.4	8.9	7.4	6.0	4.0	4.0
Consumer prices, % p.a.	11.7	12.1	4.8	4.1	3.3	3.1	3.0
Producer prices in industry, % p.a.	14.9	3.3	0.7	1.2	3.0	3.0	3.0
General governm. budget, nat. def., % of GDP							
Revenues	41.6	39.4	40.4	40.3	41.0	41.0	41.0
Expenditures	44.6	41.4	42.3	42.7	44.0	44.0	43.0
Deficit (-) / surplus (+)	-3.0	-2.1	-2.0	-2.4	-3.0	-3.0	-2.0
General gov. gross debt, nat. def., % of GDP	52.9	48.4	46.9	44.0	46.0	47.5	48.0
Stock of loans of non-fin. private sector, % p.a.	6.5	1.0	7.9	15.4			
Non-performing loans (NPL), in %, eop	3.0	3.2	2.5	2.1			
Central bank policy rate, % p.a., eop	5.00	6.50	5.75	5.75	5.8	5.3	4.8
Current account, EUR m	-4,162	-1,804	-3,788	-4,204	-3,880	-4,080	-4,250
Current account, % of GDP	-6.6	-2.4	-4.5	-4.7	-4.0	-4.0	-3.9
Exports of goods, BOP, EUR m	26,928	27,932	29,859	32,457	35,050	38,030	41,450
annual change in %	28.1	3.7	6.9	8.7	8.0	8.5	9.0
Imports of goods, BOP, EUR m	36,292	34,560	36,628	38,970	41,700	44,830	48,420
annual change in %	34.2	-4.8	6.0	6.4	7.0	7.5	8.0
Exports of services, BOP, EUR m	11,076	13,086	14,459	15,279	16,270	17,330	18,460
annual change in %	42.0	18.2	10.5	5.7	6.5	6.5	6.5
Imports of services, BOP, EUR m	8,761	9,982	11,639	12,916	13,500	14,110	14,740
annual change in %	36.9	13.9	16.6	11.0	4.5	4.5	4.5
FDI liabilities, EUR m	4,433	4,564	5,231	3,400	3,500		
FDI assets, EUR m	104	303	628	1,198	1,000		
Gross reserves of CB, excl. gold, EUR m	17,311	22,516	25,411	22,813			
Gross external debt, EUR m	41,506	44,090	48,673	51,044	56,620	62,110	66,920
Gross external debt, % of GDP	65.4	58.6	58.4	56.7	59.0	60.5	61.0
Average exchange rate RSD/EUR	117.46	117.25	117.09	117.20	117.4	117.0	116.8

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