



Serbia: Political & Economic Profile

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This note provides a political and economic overview of the current situation in Serbia. It looks at the halting progress which Serbia is making toward integration into the EU, held up to a large extent by Serbia's failure to cooperate fully with the International Criminal Tribunal for the former Yugoslavia, and at the dynamic political landscape of 2008 with both presidential and parliamentary elections. Serbia continues to have difficult relationships with some of its neighbours, particularly Kosovo and is awaiting the outcome of the International Court of Justice ruling on the legality of Kosovo's February 2007 declaration of independence. The note also looks at the current economic situation in Serbia. While Serbia had seen strong growth since 2000, accompanied by the implementation of reforms, following the conflicts and crises of the 1990s, Serbia has suffered under the global financial crisis, primarily because of its large current account deficit. Serbia also suffers from high levels of unemployment and poverty.

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Political Overview

1.1 Recent Political History

The decision to extradite Slobodan Milošević in 2001 to stand trial at the UN War Crimes Tribunal in the Hague marked an important turning point in Serbia's international prospects although it did little to end political instability within Serbia itself. The assassination only two years later in 2003 of the then Serbian Prime Minister, Zoran Đinđić, carried out by Serbian intelligence officers served to highlight the dangerous divides within and between Serbia's ruling political and security elites.

The election of Boris Tadić to the Presidency in 2004, along with his commitment to EU integration, helped to ensure that by 2005 Serbia's political and international fortunes were looking better, aided in no small measure by the European Commission's decision to open negotiations on a Stabilisation and Association Agreement—an important first step towards EU integration. However, the EU's subsequent decision to suspend talks on 3 May 2006 because of Serbia's failure to co-operate fully with the International Criminal Tribunal for the Former Yugoslavia (ICTY), by capturing or identifying the whereabouts of former Bosnian Serb military commander Ratko Mladić, was a significant blow to Serbia's progress.

On 21 May 2006 Montenegrins voted by 55.5% to 44.5% to terminate their three year State Union with Serbia. The Union had been formed in 2003 from the break-up of the former Yugoslavia with the option for both parties to leave after three years.¹ Nevertheless the result came as a shock to the people of Serbia, and their leaders, and added another layer of complexity to Belgrade's already turbulent political set-up. While Serbia's President Boris Tadić congratulated the Montenegrins, the Prime Minister Vojislav Koštunica was unhappy with result.² Montenegro's formal declaration of independence on 3 June 2006 and Serbia's formal declaration of independence on 5 June ended what was effectively a loose political confederation.

Although tensions and differences between the Serbian President and Prime Minister predated the referendum, the break with Montenegro aggravated existing grievances. It also served to shift the political focus away from everyday policies onto constitutional issues, personnel changes and elections, thus removing any residual momentum for internal reform which had already slowed following the EU's decision to freeze the Stabilisation agreement.³

In October 2006 Serbia agreed a new constitution by referendum.⁴ Over the next year Serbia faced further difficulties. On 26 February 2007 the International Court of Justice announced its ruling on Serbia's role in the 1992-95 Bosnian war. The Court cleared Serbia of direct involvement in genocide during the war, but ruled that Belgrade had breached international law by failing to prevent the 1995 Srebrenica genocide, and for failing to try or transfer the persons accused of genocide to the ICTY, in order to comply with its obligations under the UN's genocide convention, in particular in respect of General Ratko Mladić. The decision stated:

"Serbia has violated the obligation to prevent genocide, under the Convention on the Prevention and Punishment of the Crime of Genocide, in respect of the genocide that occurred in Srebrenica in July 1995, [...] Serbia has violated its obligations under the

¹ BBC, "Montenegro chooses independence", 22 May 2006, <http://news.bbc.co.uk/1/hi/world/europe/5003220.stm>

² 'A Tale of Two Slavic States', *The Economist*, 1 June 2006

³ "Serbia's Choice, *TOL*, 13 June 2006

⁴ Rare unity over Serb constitution, 30 October 2006, <http://news.bbc.co.uk/1/hi/world/europe/6097558.stm>

Convention on the Prevention and Punishment of the Crime of Genocide by having failed to transfer Ratko Mladić, indicted for genocide and complicity in genocide, for trial [...] Serbia has not committed genocide, through its organs or persons whose acts engage its responsibility under customary international law [...] Serbia has not conspired to commit genocide, nor incited the commission of genocide; Serbia has not been complicit in genocide."⁵

In the 2007 National Assembly elections, the nationalist Serbian Radical Party (SRS) became the largest party in parliament, winning 81 of the 250 seats. However, it was not able to form a government on its own. Consequently in May, a coalition government was formed that comprised the Democratic Party (DS) of pro-European President Tadić, the moderate nationalist Democratic Party of Serbia (DSS), the New Serbia (NS) party and the "G17 Plus party". The coalition controlled 130 seats in all. The new government was led by Prime Minister Koštunica of the DSS.⁶

Central to Serbia's political life in 2008 has been the status of Kosovo and its relationship with Serbia. The Final Status Talks on Kosovo to determine Kosovo's future governance arrangements started in Vienna in 2006 under the auspices of the UN.⁷ During the talks Serbian negotiators stuck to their original position, as outlined in Serbia's amended 2006 Constitution, that Kosovo—which many Serbs regard as the cradle of their heritage and civilisation—was entitled to substantial autonomy as an autonomous province of Serbia, but not full independence. With a negotiated settlement unlikely and Kosovan authorities threatening to issue a unilateral declaration of independence, Maarti Ahtisaari, who was chairing the negotiations, presented a proposal for the future status of Kosovo in February 2007. The "Comprehensive Proposal for the Kosovo Status Settlement" recommended a form of independence for Kosovo supervised by the international community.⁸ On 3 April 2007, at the beginning of a debate in the UN Security Council, Prime Minister Koštunica declared that Serbia rejected the Proposal (following a vote in the Serbian legislature in February), and requested that a new mediator be appointed. On 5 April Ahtisaari's plan was approved by 100 of 101 votes cast in the Kosovo Assembly.

In August 2007, after Russia obstructed the adoption of a resolution based on Ahtisaari's plan at the UN Security Council, a further series of negotiations began between the Serbian and Kosovo delegations, with mediation by the USA, the EU and Russia. On 7 December, shortly before the deadline stipulated by the UN, it was announced that the negotiations had failed to result in an agreement. On 26 December the Serbian legislature approved a resolution urging the Serbian Government to "reconsider" diplomatic relations with any Western country that recognized Kosovo as independent. Relations between Russia and Serbia were consolidated in early 2008, with the signature of an agreement whereby Serbia was to join Russia's South Stream pipeline project, and Gazprom, the large Russian gas company, acquired a 51% share in the Serbian state-owned oil enterprise, Naftna Industrija Srbije. Emboldened in particular by Russia's strong international support, Serbia saw no reason to compromise.

In the meantime, Kosovo's position had also hardened, in part due to the election on 17 November 2007 of Hashim Thaçi, a former Kosovo Liberation Army (KLA) military

⁵ "Serbia condemned for Srebrenica despite acquittal on genocide charge," *The Guardian*, 27 February 2007.

⁶ Serbia: National Assembly, http://www.ipu.org/parline-e/reports/2355_E.htm

⁷ For further information on the Final Status Talks process see Standard Note 3390 'Grasping the Nettle: Kosovo's Final Status Talks'

⁸ The proposal can be found here: <http://www.assembly-kosova.org/common/docs/Comprehensive%20Proposal%20.pdf>

commander, to the post of Kosovo's Prime Minister. Taçi's election campaign included a promise to declare independence if the talks failed. However, under diplomatic pressure from the US and EU, Taçi was persuaded not to declare independence until Kosovo's supporters were more certain that they could garner broad international support for independence.

Ultimately, Kosovo declared independence on 17 February 2008. A Resolution of the Assembly of Kosovo declared Kosovo a sovereign state independent from Serbia. The decision was based on Ahtisaari's Comprehensive Proposal for the Kosovo Status Settlement in accordance with UN Security Council Resolution 1244 of 1999.

Serbia, with the continued support of Russia, immediately protested that the declaration of independence contravened international law and demanded that it be annulled. On the following day the Serbian Ministry of the Interior issued arrest warrants for treason against Taçi and other Kosovo government officials. The NATO Kosovo force, KFOR, reinforced the border with Serbia, after the destruction of two border posts by Serb protesters and reports that Serbian security forces had entered northern Kosovo.

Several states, including Albania, France, the USA and the United Kingdom, extended recognition to Kosovo on 18 February, followed by others; Serbia immediately recalled its ambassadors based in those countries. On 21 February Serb protesters rioted in Belgrade, attacking several embassies, including that of the United Kingdom and the USA.

1.2 Developments in 2008

2008 was a politically tumultuous year for Serbia. Provincial, parliamentary and presidential elections plus the loss of Kosovo, the arrest of Radovan Karadžić and difficult discussions over EU membership have all stretched the political capabilities of the governing parties.

Serbia now finds itself at a political crossroads and a pawn in the increasingly bitter dispute between Russia and the EU over their respective spheres of influence. Russian patronage, particularly over the issue of Kosovo, has been, and continues to be, vital to Serbia, providing much needed international support as well as domestic investment. Yet, the EU's renewed offer of a Stabilisation and Association Agreement (SAA)—an important step towards Serbia's gaining EU Candidate Status—proved too good to refuse for pro-EU voters in the May 2008 parliamentary elections. As one commentator has noted, "There is no longer any room for delaying this choice or for finding some sort of compromise that would embrace Russia and the EU. No such compromise exists that would not result in the further dismemberment of the country."⁹ However, finding a resolution to this issue or, perhaps more realistically, coming to an amicable way of agreeing to disagree about Kosovo, is a major challenge for the government. Also under scrutiny, and key to the full implementation of the SAA, will be an assessment of Serbia's co-operation with the International Criminal Tribunal for the Former Yugoslavia following the July 2008 arrest of Radovan Karadžić.

Presidential Elections: Tadić's Close Call

Presidential election were held on 20 January 2008, shortly before Kosovo declared independence from Serbia. Incumbent Boris Tadić of the pro-Western Democratic Party (DS) faced Tomislav Nikolić from the nationalist Serbian Radical Party (SRS) as well as several candidates from smaller parties. Nikolić won 40% of the vote while Tadić came second with 35.4%.¹⁰ As no candidate gained a majority, a run-off was held between Tadić and Nikolić on

⁹ "Serbia's Second Chance to Embrace the West", Nenad Pejic, *Radio Free Europe*, 30 July 2008

¹⁰ The Presidential election results can be found here: <http://psephos.adam-carr.net/countries/s/serbia/serbia2008.txt>

3 February which was won by Tadić by a narrow majority of 51.2% to 48.8%. The results were welcomed by the EU. Javier Solana, the EU's foreign and security policy representative, said: "The results for me at least signalled the wish of the majority of the people in Serbia who want to continue the path towards Europe, and I'd like to say Europe is very happy with that."¹¹

Parliamentary Elections: Towards the EU - Just

By March 2008 the coalition government created in May 2007 was in difficulty, with the nationalist Prime Minister Koštunica of the DSS and the new President Tadić of the DS unable to forge a common position on Europe after Kosovo's declaration of independence on 17 February. The disagreements between Koštunica and Tadić predate the Kosovo declaration but the decision of 22 EU Member States to recognise Kosovo made the issue of closer ties to the EU the issue which challenged the already fragile coalition.¹² While both parties stood firmly against Kosovo's independence they differed on the issue of whether this should influence Serbia's quest for EU membership.¹³ The International Herald Tribune reports on a disagreement in February 2008:

Tadic, who supports closer ties with the European Union and Washington, also is vehemently opposed to Kosovo's independence. But he made it clear during his election campaign that he was not willing to sacrifice Serbia's European future.

"The EU's proposal to sign a political agreement with Serbia while at the same time sending a mission to break apart our state is a deception aimed at getting Serbia effectively to sign its agreement to Kosovo independence," Kostunica said.¹⁴

In March Prime Minister Koštunica resigned and President Tadić called early National Assembly elections for 11 May 2008.

The election campaign was dominated by the issues of Kosovo, the EU and the Government's previous record. Just as opinion polls were suggesting that Boris Tadić's pro-EU Democrats may lose the election, the EU offered a carrot in the form of an agreement to implement a Stabilisation and Association Agreement. As the *Economist* noted, "The bribe worked: Mr Tadić's party won."¹⁵ With only 39.25% of the vote and 102 seats in the 250 seat parliament the victory of the pro-Western "For a European Serbia" bloc was unexpected. Among the other parties the Radicals won 30.1% of the vote and 78 seats. The nationalist Democratic Party of Serbia "New Serbia list" received 11.87% of the votes and 30 seats. A bloc led by the Socialist Party of Serbia (SPS) won 7.75% of the votes and 20 seats. The pro-Western Liberal Democratic Party won 5.35% of the vote and 13 seats. The remaining seven seats went to parties representing Hungarian, Bosnian and Albanian ethnic minorities.¹⁶

The turnout (including Serbs voting in Kosovo) was 61.35%. Following a number of complaints submitted by the Serbian Radical Party (SRS), the electoral commission announced that voting was to be repeated in three constituencies on 18 May, owing to

¹¹ "Serbian election result muddies waters for Kosovo independence," *The Guardian*, 4 February 2008.

¹² Setting a Westward course, *The Economist*, 4 February 2008, http://www.economist.com/world/europe/displaystory.cfm?story_id=10635380 ;

¹³ EU Awaits Serbian Election, *Balkan insights*, 24 March 2008, <http://www.balkaninsight.com/en/main/news/8838/>

¹⁴ "Angry EU officials attack Serb's blocking of pact with Brussels", *International Herald Tribune*, 6 February 2008

¹⁵ "Arrest of a Bearded Man", *The Economist*, 24 July 2008

¹⁶ The May election results can be found here: http://www.ipu.org/parline-e/reports/2355_E.htm

irregularities. Neighbouring states, the EU and the USA welcomed the election results (which had followed predictions of success for the SRS) and urged the rapid formation of a new administration.¹⁷

Despite the success of the DS-led bloc in the May elections, its ability to form a government was not a forgone conclusion. There was speculation that Koštunica's DSS might be able to form a nationalist and anti-EU coalition government with the Radicals (SRS) and the Socialists (SPS). However, on 7 July, following the decision of Slobodan Milošević's old party, the SPS to ally itself with the main pro-EU bloc rather than the nationalist parties, a new pro-European government was formed. Led by the Democratic Party, it consists of ten parties including the SPS and the "G17 Plus" party, and has 27 cabinet ministers. Former Economist Mirko Cvetković, who is not a member of any party, but who is close to the DS, was appointed as Prime Minister.¹⁸

1.3 Co-operation with the ICTY

Radovan Karadžić's capture in Belgrade in July 2008, only weeks after President Tadić was elected and a new secret service chief was appointed, was a major boost to Serbia's EU aspirations. In the past Belgrade had arrested some alleged war criminals but the 2003 assassination of the then Serbian Prime Minister, Zoran Đinđić, by members of the security forces, which was partly a response to the arrest of Slobodan Milošević, meant that subsequent governments were far more cautious about taking on suspected war criminals. On balance, says Tomas Valasek, Director of Foreign Policy and Defence at the *Centre for European Reform*, "Tadić's pursuit of war criminals seems genuine. It strengthens his domestic political position and it improves Serbia's standing in the eyes of the EU."¹⁹ While many had hoped that Karadžić's arrest would immediately lead to the unfreezing of the SAA, the EU has been more circumspect, praising the Serbian government but arguing that it must wait on a progress report from the ICTY before deciding on its next step. Ratko Mladić remains at large. Recent reports suggest that western intelligence agencies have stepped up their efforts, in cooperation with Serbian authorities, to find Mladić.²⁰

2 Economic Overview

By Ian Townsend, Economic Policy and Statistics

The conflicts and crises of the 1990s hit Serbia's economy hard, but since then the country has seen a sustained period of economic growth. However, the current financial crisis has exposed Serbia to economic uncertainty, primarily because of its large current account deficit. Serbia also suffers from high levels of unemployment and poverty. **Serbia's economy**

A Foreign Office profile notes that since 2000 "Serbia's economy has been going through recovery from conflict and isolation in the 1990s".²¹ The Economist Intelligence Unit states that Serbia has seen "a succession of crises after the break-up of the former Yugoslavia in 1991, which also severed established economic links; the imposition of international

¹⁷ Recent History (Serbia), in Europa World online. London, Routledge.

¹⁸ "Serbia approves pro-Western government", *International Herald Tribune*, 7 July 2008

¹⁹ Thomas Valasek, "The EU will want more from Serbia than Arrests", *Centre for European Reform*, 25 July 2008

²⁰ Hunt intensifies for Serbian war criminal, Ratko Mladić, 17 February 2009, <http://www.guardian.co.uk/world/2009/feb/16/ratko-mladic-hunt-intensifies-serbia>

²¹ [Foreign & Commonwealth Office](#), Serbia profile

sanctions; and the damage to industry and infrastructure caused by the 11-week air bombardment by NATO in 1999.”²²

Unemployment is also a key issue, with a rate of over 20%. As well Serbia’s current account deficit and unemployment (which it puts at 14% of the labour force on an internationally comparable basis), the World Bank also highlights the country’s external debt, at around 60% of GDP “as private external liabilities continue to grow quickly.” It also notes that while 6.6% of the country is below the poverty line, a third are “barely above” that level, “and remain in danger of slipping into poverty if any adverse economic developments occur.”²³

As European Commission report noted that Serbia’s²⁴

growing level of external debt creates important external financing needs requiring significant capital inflows. To that extent, the external imbalances render the Serbian economy vulnerable to possible disruptions in capital flows. The risks of a sudden stop or reversal of capital flows have recently grown and/ higher risk premiums and refinancing costs could put further pressure on the external side. In particular, a decline in cross-border lending, which has become an important financing source for the domestic corporate sector, could be affected.

Size of economy

Serbia had the 72nd largest economy in the world in 2007 according to the International Monetary Fund (IMF), with Gross Domestic Product (GDP) valued at \$39.9 billion. This is slightly larger than the economies of Bulgaria and Lithuania. On a per capita basis, the IMF ranked Serbia’s economy 75th globally.²⁵

The World Bank classifies Serbia as an ‘upper middle income’ country based on a per capita Gross National Income (GNI) of \$4,730 in 2007, ranking 95th in the world on this measure.²⁶ On total economic output, the World Bank ranks Serbia 69th in the world (\$41.6 billion).²⁷

World Bank data on the structure of Serbia’s economy are limited to the period from 2000 to 2005, but over that period there was a gradual decline in the contribution of agriculture and industry to the Serbian economy (from over 19% to under 13% for agriculture, and from around 30% to 25.5% for industry, while services’ share increased from 51% to nearly 62%.

Economic growth

While economic growth data from the IMF are only available from 1999 onwards, the Serbian economy suffered under UN sanctions in the early 1990s, and by 2000 the economy was 40% of its pre-war size.²⁸ After a 10% contraction of Serbia’s economy in 1999 it has seen continuous real GDP growth averaging 5.4% in each year between 2000 and 2007.

²² EIU, [Serbia ‘Factsheet’ page](#) (dated 28 Jan 2009).

²³ World Bank [Serbia profile](#) “Economic” section

²⁴ European Commission [Staff Working Document, Serbia 2008 Progress Report](#) [accompanying the Communication *Enlargement Strategy And Main Challenges 2008-2009* (Com(2008)674)], pp 24

²⁵ IMF, *World Economic Outlook* database, [October 2008](#)

²⁶ Using the Atlas method, rather than a PPP basis (as shown in this note’s main statistical table), and excluding Kosovo and Metohija. See the World Bank’s [rankings](#) and [country classification](#) pages.

²⁷ Using World Bank [GDP rankings](#) (Atlas method); see also rankings on a [purchasing power parity basis](#).

²⁸ Central European University (Hungary) Center for EU Enlargement, [Serbia report \(executive summary\)](#), p1

Serbia: Real GDP, annual % change, 1999-2008



Source: IMF, *World Economic Outlook* October 2008 database

IMF projections for Serbia's economy from October 2008 suggested that it would grow by 6% in 2008 to reach GDP of \$52.2 billion. However, the financial crisis has developed since that time (see part 2.5 below), and growth may therefore be lower than previously expected. Indeed, IMF staff forecasts released in January 2009 suggest 3.5% growth in 2009 and 4.5% in 2010,²⁹ compared with previous forecasts of 6% and 6.5% in those years. This suggests that the next IMF *World Economic Outlook* forecasts due in April will see growth revised downwards.

In January 2009 the Economic Intelligence Unit was forecasting real GDP growth of 1% in 2009. This is one sixth of the rate projected by the IMF back in October 2008, and reflects the likely effects on Serbia of the global economic crisis. The EIU suggested that economic growth would be seen in 2010, with 3% forecast.³⁰

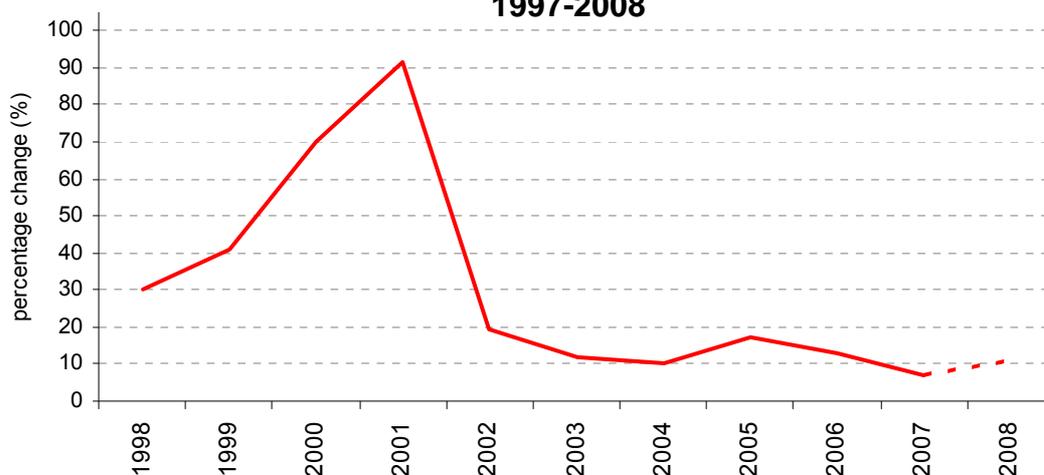
Inflation

Having experienced consumer price inflation of over 90% in 2001, Serbia has since brought inflation under control, and it averaged 6.8% in 2007.

²⁹ "IMF Approves €402.5 million Stand-By Arrangement for Serbia", IMF Press Release 09/12, 16 January 2009

³⁰ EIU, [Serbia 'Forecasts' page](#) (dated 28 Jan 2009).

Serbia: Consumer price inflation, annual % change, 1997-2008



Source: IMF, *World Economic Outlook* October 2008 database

In October 2008, the IMF forecast inflation to increase in 2008 to 10.7%, then to fall to below 8% thereafter.³¹ The Economic Intelligence Unit notes that annual retail price inflation fell in December 2008 to 6.8%, the third monthly fall in a row (down from 9.2% in November and 10.5% in October). The EIU also forecasts inflation at the end of 2009 to stand at 7%, then 5.2% at the end of 2010, although it notes risks “related to the impact of dinar depreciation.”³²

Trade, investment & external balances

The share of Serbia’s trade in goods as a proportion of the country’s GDP increased between 2000 and 2005, from 60.4% to 65.1%. Taken together, exports of goods and services as a share of GDP increased from under 17% in 2000 to 28% in 2007. Over the same period, imports of goods and services as a proportion of GDP more than doubled (from 24% to over 48% in 2007).

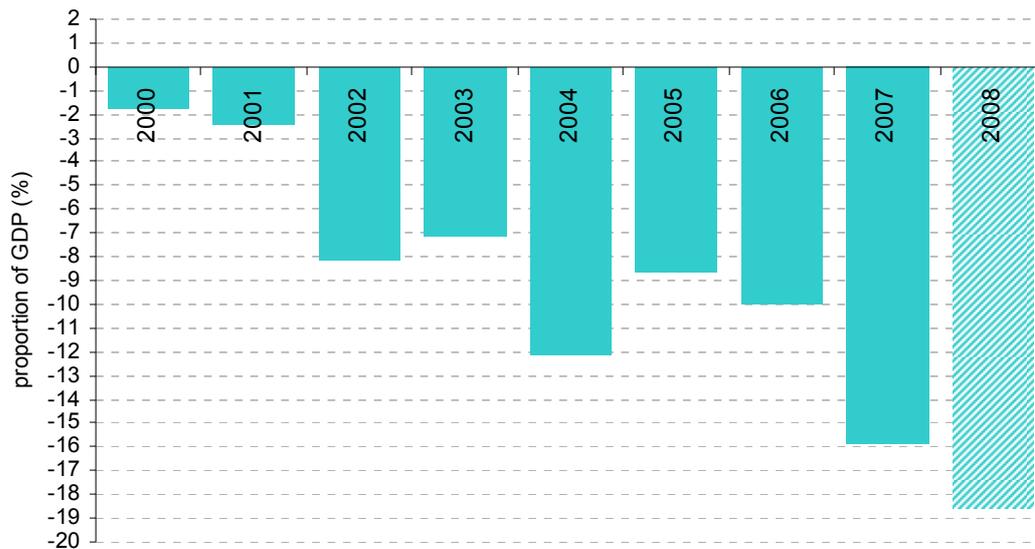
Serbia has been running a current account deficit since at least 1998 (the earliest year for which IMF data are available). This deficit has grown from \$500 million in 1998 to a forecast \$9.7 billion in 2008. As a share of GDP (see chart below) the deficit has gone from 1.8% of GDP in 2000 and was expected to reach almost 19% in 2008.

October 2008-based IMF forecasts were for the deficit to widen in 2009 to over 19% of GDP, then to narrow gradually to reach 15.4% of GDP by 2013.

³¹ IMF, *World Economic Outlook*, October 2008 database

³² EIU, [Serbia ‘Forecasts’ page](#) (dated 28 Jan 2009).

Serbia: Current account deficit, % of GDP, 2000-2008



Source: IMF, *World Economic Outlook* October 2008 database

Serbia's external debt has increased from \$10.6 billion in 1997 to \$16.3 billion in 2006, and then fell back to \$13.8 billion in 2007. Net inflows of Foreign Direct Investment (FDI) have also risen since 2000 – annual FDI inflows were less than \$1 billion before 2003, and this increased in recent years to reach \$5.1 billion in 2006 (no data available for 2007).

Table 2

Selected Economic Indicators: Serbia

		1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
IMF data (a)													
Gross Domestic Product (GDP)	(\$ billions, current prices)	..	..	..	8.7	11.5	15.3	19.8	23.8	25.4	29.7	39.9	52.2
GDP, constant prices	(annual % change)	..	..	-10.2	4.5	5.4	3.6	2.8	8.2	6.0	5.6	7.1	6.0
GDP per capita, current prices	(\$)	..	2,047	1,451	1,160	1,536	2,036	2,640	3,186	3,408	4,009	5,387	7,054
Inflation, consumer prices	(annual % change)	..	30.0	41.1	70.0	91.8	19.5	11.7	10.1	17.3	12.7	6.8	10.7
Current account balance	(\$ billions)	..	-0.5	-0.5	-0.2	-0.3	-1.2	-1.4	-2.9	-2.2	-3.0	-6.3	-9.7
Current account balance	(% of GDP)	..	..	..	-1.8	-2.5	-8.2	-7.2	-12.1	-8.7	-10.0	-15.9	-18.6
World Bank data													
Population	(millions)	7.6	7.6	7.5	7.5	7.5	7.5	7.5	7.5	7.4	7.4	7.4	..
Population growth	(annual % change)	-0.8	-1.1	-0.4	-0.3	-0.2	0.0	-0.3	-0.2	-0.3	-0.4	-0.3	..
Gross National Income per capita	(\$ PPP, current prices)	..	..	5,500	5,880	6,330	6,680	7,000	7,810	8,540	9,350	10,220	..
Time required to start a business	(days)	..	..	..	..	..	..	51.0	51.0	23.0	23.0	23.0	..
Merchandise trade	(% of GDP)	..	..	..	..	..	..	..	60.4	59.1	61.7	65.1	..
Exports of goods and services	(% of GDP)	16.7	22.6	17.1	23.0	20.7	18.7	21.4	22.7	25.2	27.0	28.0	..
Imports of goods and services	(% of GDP)	24.1	29.6	27.3	39.1	38.3	38.3	40.2	46.3	47.3	46.8	48.3	..
External debt, total	(current \$ billion)	10.6	10.9	10.9	11.5	12.4	11.6	14.4	14.7	16.3	13.8	..	..
Foreign Direct Investment inflows	(\$ billions (BoP), net)	0.7	0.1	0.1	0.0	0.2	0.1	1.4	1.0	1.5	5.1	..	..
Agriculture (value-added)	(% GDP)	..	..	..	19.4	19.7	15.9	14.4	14.2	12.7	..	..	..
Industry (value-added)	(% GDP)	..	..	..	29.6	27.6	26.7	26.2	28.1	25.5	..	..	..
Services (value-added)	(% GDP)	..	..	..	51.0	52.7	57.4	59.3	57.7	61.8	..	..	..

Note: (a) IMF data are estimates after 2006 (2003 for per capita GDP); ".." = not available

Sources: World Bank, *World Development Indicators* database, & IMF, *World Economic Outlook* database, October 2008

Table 3

Serbia: IMF GDP, inflation & current account balance forecasts

		2008	2009	2010	2011	2012	2013
GDP, constant prices	(annual % change)	6.0	6.0	6.5	6.5	6.0	5.5
Inflation, consumer prices	(annual % change)	10.7	7.5	7.8	7.9	7.7	7.5
Current account balance	(% of GDP)	-18.6	-19.3	-18.8	-17.5	-16.4	-15.4

Sources: IMF, *World Economic Outlook* database, October 2008

2.2 Economic reforms

Economic reforms to liberalise the economy, have been implemented, but political uncertainty in the country limited their impact. The EBRD has referred to the 1990s as “the lost decade” due to the delays in reform, in contrast with other Balkan countries.³³ Even so, the World Bank ranked Serbia as the “top reformer” in its *Doing Business 2006* report (covering reforms in 2004-2005).³⁴

A privatisation programme, running from 2000/2001 and expected to be completed in 2009, has transferred state-owned companies to the private sector. Some 80% of Serbia’s banking sector is now foreign-owned.³⁵ In 2008, the Serbian government unveiled a three-year, \$44 billion programme of privatisation.³⁶ This encompasses the state telecommunications company (Telekom Srbija), an electricity utility (EPS), the national airline (JAT) and a pharmaceutical company (Galenika).

2.3 The global financial crisis & Serbia

The spread of the global financial crisis to emerging economies from the latter half of 2008, and particularly in the fourth quarter, has caused problems for a number of Central and Eastern European countries, including Serbia. The country is frequently cited as being among the economies thought to be most at risk from the crisis, primarily due to its large current account deficit noted above.

As the Foreign Office profile observed, until recently “this gap has been covered with privatisation receipts and international credit. However, the tough economic crisis has deterred investors and made credit more expensive.”³⁷ The Serbian dinar has depreciated by 25% since October,³⁸ and on 23 December ratings agency Fitch revised their Serbia outlook to negative from stable because of the effects of the financial crisis and the country’s debt levels.³⁹

The economic pressure of the crisis on Serbia led it to seek assistance from the International Monetary Fund (IMF). After IMF advice, Serbia made budget cuts, limiting increases to wages and pensions and reducing state subsidies, reducing the budget deficit to 1.5%.⁴⁰ A stand-by arrangement of \$530 million in credits was also agreed as a precautionary measure to support the country’s foreign currency reserves, should circumstances require it. Two thirds of this (\$353 million) would be available immediately, although it was stated that Serbia were treating this as a precautionary measure, not to be used “unless the need arises.”

In February 2009, following a visit the IMF deputy managing director confirmed discussions would continue with Serbia, after noting that:⁴¹

Serbia is beginning to feel the full blow of the global economic crisis, with slowing GDP growth, falling exports, lower capital inflows, and reduced credit activity. There was

³³ EBRD [Serbia strategy overview](#) page

³⁴ World Bank [Serbia profile](#) “Economic” section

³⁵ All based on FCO Serbia profile.

³⁶ “Serbia to soothe vexed voters with share of Euros 30bn sell-off”, *Financial Times*, 22 February 2008, p6

³⁷ [Foreign & Commonwealth Office](#), Serbia profile

³⁸ “Crisis-hit Serbia needs more IMF help (update 3)”, *Reuters News*, 10 February 2009 (via Factiva)

³⁹ “Falling credit ratings in emerging Europe”, *Reuters News*, 10 February 2009 (via Factiva)

⁴⁰ [Foreign & Commonwealth Office](#), Serbia profile

⁴¹ [“Statement by IMF Deputy Managing Director Murilo Portugal at the Conclusion of his Visit to Serbia”](#), *IMF Press Release* 09/31, 10 February 2009

agreement that Serbia's macroeconomic environment has worsened compared to what was assumed in the precautionary arrangement.

Further reports suggest that Serbia is willing to agree a revised IMF package, and estimates of at least \$1 billion have been suggested by economists.⁴²

Also, international banks with operations in Central and Eastern Europe have sought additional backing from the European Union and the European Central Bank in non-EU countries in the region, following packages for Hungary, Latvia and Poland.⁴³

The crisis has led to calls from the Serbian government for the EU to implement the Stabilisation and Association Agreement with Serbia (see part 3.1).⁴⁴ Serbia has also opted to unilaterally implement an interim trade agreement, the trade aspects of the SAA,⁴⁵ effective from 30 January 2009.⁴⁶

2.4 Other sources

Additional information on Serbia's economy can be found online from:

- [Foreign & Commonwealth Office](#) and [UK Trade & Investment](#) profiles;
- Economist Intelligence Unit [Serbia pages](#);
- World Bank country profile ([economics](#)) and [Doing Business 2009 rankings \(full report\)](#)
- *Financial Times* [survey of Serbia](#) (from 2007);
- EuropaWorld [profile](#) (Parliamentary intranet only);
- European Bank for Reconstruction & Development (EBRD) [Serbia](#) pages.

2.5 The financial crisis and its effect on Serbia

The spread of the global financial crisis to emerging economies from the latter half of 2008, and particularly in the fourth quarter, has caused problems for a number of Central and Eastern European countries, including Serbia. The country is frequently cited as being among the economies thought to be most at risk from the crisis, primarily due to its large current account deficit noted above.

As the Foreign Office profile observed, until recently "this gap has been covered with privatisation receipts and international credit. However, the tough economic crisis has deterred investors and made credit more expensive."⁴⁷ The Serbian dinar has depreciated by 25% since October,⁴⁸ and on 23 December ratings agency Fitch revised their Serbia outlook to negative from stable because of the effects of the financial crisis and the country's debt levels.⁴⁹

⁴² "Serbia to seek additional IMF loan to counter financial crisis", *Associated Press Newswires*, 10 February 2009 (via Factiva)

⁴³ "Bankers seek help for eastern Europe", *Financial Times*, 22 January 2009, p4

⁴⁴ "Serbia asks EU to step up ties as crisis bites", *Financial Times*, 18 November 2008, p8

⁴⁵ Commission of the European Communities, Serbia 2008 Progress Report, COM (2008) 674, 5 November 2008.

⁴⁶ "Serbia adheres to EU trade rules", *Financial Times*, 31 January 2009, p2

⁴⁷ [Foreign & Commonwealth Office](#), Serbia profile

⁴⁸ "Crisis-hit Serbia needs more IMF help (update 3)", *Reuters News*, 10 February 2009 (via Factiva)

⁴⁹ "Falling credit ratings in emerging Europe", *Reuters News*, 10 February 2009 (via Factiva)

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3 Key Issues

3.1 Relations with the EU

Current Situation

Serbia has been a potential candidate country since June 2000, but its progress towards candidate status and eventual membership has been severely delayed by its failure to fully cooperate with the ICTY. The new Government has pledged to make EU integration a top priority. On 9 September 2008 Serbia's parliament gave its overwhelming backing to the Stabilisation and Association Agreement, ratifying it with 140 deputies in favour and 28 against.⁵⁷ The SAA is an important indicator that the EU wishes to establish a special relationship with a potential future candidate for membership in exchange for a number of reforms which align that country's legislation more closely with that of the Community. However, the Council of Ministers has stated that full cooperation with the ICTY, including all possible efforts to arrest and transfer indictees, is an essential element of the agreements

⁵⁰ [Foreign & Commonwealth Office](#), Serbia profile

⁵¹ ["Statement by IMF Deputy Managing Director Murilo Portugal at the Conclusion of his Visit to Serbia"](#), *IMF Press Release* 09/31, 10 February 2009

⁵² "Serbia to seek additional IMF loan to counter financial crisis", *Associated Press Newswires*, 10 February 2009 (via Factiva)

⁵³ "Bankers seek help for eastern Europe", *Financial Times*, 22 January 2009, p4

⁵⁴ "Serbia asks EU to step up ties as crisis bites", *Financial Times*, 18 November 2008, p8

⁵⁵ Commission of the European Communities, Serbia 2008 Progress Report, COM (2008) 674, 5 November 2008.

⁵⁶ "Serbia adheres to EU trade rules", *Financial Times*, 31 January 2009, p2

⁵⁷ "Serbian Parliament Ratifies EU Pre-membership Pact", *The Star* (Belgrade) 9 September 2008

and as a result the SSA has been frozen until the ICTY issues its progress report. In practice, the EU is keen to encourage Serbia and has indicated that it could be offered candidate status in 2009.⁵⁸

The Serbian Parliament has nevertheless taken a decision to implement the Interim Agreement on Trade and Trade-related issues unilaterally as a sign of its commitment to European Integration, from 30 January.⁵⁹ In January 2009 the Serbian Foreign Minister, Vuk Jeremić, visited Brussels for talks with European Officials about Serbia's prospective membership of the EU. Serbia had previously called on the EU to step up the process in view of the impact of the financial crisis on the Serbian economy. According to reports, Belgrade plans to apply for candidacy during the Czech Presidency, which ends in June 2009, and hopes to begin membership negotiations during the Spanish Presidency in 2010.⁶⁰

Priority Areas for Action and Reform

In its November 2008 Progress Report the Commission highlighted a number of priority areas for action which are necessary to take forward Serbia's application for membership of the EU.⁶¹ Central to this is full cooperation with the ICTY, including the arrest of Ratko Mladić.

The Commission noted concerns about the slow pace of reform of the Constitution. In particular, concern was expressed about political party control over the mandates of members of parliament and the role of parliament in judicial appointments. The European Policy Centre notes that MPs who switch sides or vote with the opposition on important issues are thrown out of parliament.⁶² While there has been progress in adopting legislation for judicial reform, the Commission notes that further reforms in line with European standards are necessary.

Legislative reform has been limited and the Commission reports that the existing rules of procedure are inadequate for the smooth running of parliament. As a result, the Progress report says, parliament has failed to abide by legal deadlines for several appointments and continues to pass laws by urgent procedure with little public debate, using offensive and inflammatory language against political opponents and human rights defenders in parliament.

The Commission noted that the government continued to be occupied with issues relating to both Kosovo and the EU. However, following the legislative elections there has been greater consensus on the desire for EU membership. European integration support structures have consequently been strengthened and a National Programme for EU Integration was adopted in October 2008.

The Commission expressed its concern that while the Office of the State Ombudsman has been created and is very active, the Serbian authorities have not created the technical conditions necessary for its proper functioning. Similar comments are made of five other independent state bodies, criticising their lack of capacity, insufficient follow-up on recommendations and working conditions which undermine their independence.

⁵⁸ "EU Sees Candidate Status For Serbia In 2009", *Radio Free Europe*, 3 September 2008

⁵⁹ "Serbia adheres to EU trade rules", *Financial Times*, 31 January 2009, p2

⁶⁰ "Serbia renews push for EU membership", 25 January 2009 <http://www.eubusiness.com/news-eu/1232914621.65>

⁶¹ Commission of the European Communities, Serbia 2008 Progress Report, COM (2008) 674, 5 November 2008. http://ec.europa.eu/enlargement/pdf/press_corner/key_documents/reports_nov_2008/serbia_progress_report_en.pdf

⁶² S.Cvijic, "The new Serbia: fast forward towards the EU", European Policy Centre brief, January 2009

According to the Commission, corruption continues to be widespread and to pose a serious problem in Serbia. Despite the development of a fully-comprehensive anti-corruption policy there are insufficient independent and efficient oversight bodies and an anti-corruption agency has not yet been established.

Overall the Commission notes that civil and political rights are generally respected but have been affected by the political climate which deteriorated in the period immediately following Kosovo's declaration of independence. This was more pronounced in Southern Serbia.

3.2 Economic reform towards EU membership

The European Commission recently summarised Serbia's position on economic reforms:⁶³

The economy of Serbia continued to grow strongly. However, progress in macroeconomic stabilisation was mixed. The continuing reversal of fiscal consolidation added to macroeconomic risks. Structural reforms slowed down and the high level of unemployment, as well as rising inflationary pressures, remained major challenges. As regards the economic criteria, Serbia made some progress towards establishing a functioning market economy. Further efforts are needed to enable Serbia to cope in the medium term with the competitive pressures and market forces within the Union.

Consensus on the fundamentals of a market economy was broadly maintained. The new monetary policy framework of inflation targeting enabled Serbia to meet the inflation targets in 2007. There was some progress in privatisation. Financial intermediation continued to grow from a still relatively low level. Significant progress was made with the development of the non-banking financial sector.

However, external imbalances widened, the quality of financing deteriorated, foreign debt rose, and the degree of macro-vulnerability increased also in the light of the global financial crisis. Fiscal policy remained expansionary, contributing to growing external imbalances and resurfacing inflationary pressures in 2008. Despite high economic growth rates in recent years, unemployment remained a major challenge. At the same time, the economy suffered increasingly from a shortage of skilled employees. There was some progress with regard to the privatisation of state-owned companies and banks. Foreign investment has been affected by the unstable political climate.

A competitive and dynamic private sector has not yet been fully established. Excessive bureaucratic requirements and complex legislation continued to hamper market entry and exit. Legal predictability and trust in the legal system remained limited, in particular as far as the effective enforcement of property rights were concerned. Although having declined, state influence on competitiveness remained high. The large informal sector is fuelled by a weak regulatory framework, by inappropriate tax and expenditure policies, and by weaknesses in law enforcement, including the fight against corruption and organised crime. It remains an important challenge as it reduces the tax base and the efficiency of economic policies.

The European Commission noted that the "functioning of market mechanisms [...] was hampered by distortions, heavy State involvement in production of private goods and lack of competition". However, it also saw increasing trade openness (goods and services exports and imports accounting for 78% of GDP in 2007, compared with 74% in 2006) and economic integration of Serbia and the EU. While the EU was already Serbia's main trade partner, the

⁶³ European Commission Communication, [Enlargement Strategy and Main Challenges 2008-2009](#), pp51-52;

share of total exports of goods and services to the EU rose to 56% in 2007 (from 53% in 2006), while the share of total imports from the EU reached 54% (49% in 2006).⁶⁴

Serbia is also part of the Central Europe Free Trade Agreement (CEFTA) with other South East European countries, a market of around 29 million people. Serbia also has a free trade agreement with Russia.

3.3 Kosovo

To date 54 states have recognised Kosovo including 22 EU Member States.⁶⁵ Both Serbia and Russia have however declared the declaration of independence illegal under international law.

Since the parliamentary election, comments by key Serbian government ministers have suggested a softening of attitudes towards the issue of Kosovo. The return of previously recalled Ambassadors to countries which recognised Kosovo is also indicative of a change in approach. However, this has been somewhat undermined by Serbia's request for an Advisory Opinion from the International Court of Justice on the legality of Kosovo's declaration of independence.⁶⁶

The motion to request an advisory opinion was passed in the UN General Assembly on 8 October 2008. Serbia had hoped that its success in the General Assembly would dissuade other states from recognising Kosovo before the ICJ judgement. However both Macedonia and Montenegro, Serbia's regional neighbours, recognised Kosovo the day after the vote.

Furthermore, after the Russian-Georgian war of August 2008, Russia decided to recognise the breakaway Georgian provinces of South Ossetia and Abkhazia as independent states. This placed Serbia in a difficult position—Russian patronage, particularly over the issue of Kosovo, has been, and continues to be, vital to Serbia, providing much-needed international support as well as domestic investment. The ICJ judgement could now take on a significance beyond Kosovo—if the ICJ rules against the independence of Kosovo this could be used against other breakaway states in the region and would place Russia in a difficult position, having sanctioned South Ossetia's and Abkhazia's independence.⁶⁷ Nationalist forces in Serbia remain strong. Crisis Group reports that while one section of this group may be willing to use diplomacy and other legal means to pursue their cause, another, significant section is prepared to approve of violence.⁶⁸

3.4 EULEX

While Serbia has repeatedly insisted that its potential EU membership and Kosovo are two separate issues, it brought the two head to head when it rejected the EU's Police and Justice Mission, called EULEX, in Kosovo. EULEX was intended to replace the UN mission in Kosovo, UNMIK, which had been established after the war in 1999. However both Serbia and Russia rejected this plan which was then rejected by the UN Security Council. The UN Secretary-General devised an alternative plan which would have seen police in Kosovo Albanian areas come under EULEX and those in Kosovo's Serbian areas under UNMIK.

⁶⁴ European Commission [Staff Working Document, Serbia 2008 Progress Report](#) [accompanying the Communication *Enlargement Strategy And Main Challenges 2008-2009* (Com(2008)674)], pp 29 & 30

⁶⁵ "Kosovo PM hails first year of independence", Association Press, 16 February 2009, http://www.google.com/hostednews/ap/article/ALeqM5h4nMqPzVvYkYkLv40-KAO6_zS8jmQD96CKC3O0

⁶⁶ For details about the Advisory Opinion Process see SN/IA 4846 [Serbia's bid to Secure a Legal Opinion on Kosovo's Independence](#)

⁶⁷ "Serbia's surprise embrace of Europe", *IJSS Strategic Comments*, November 2008

⁶⁸ Crisis Group, "Will the real Serbia please stand up", 23 April 2008.

Serbia originally approved this plan, but Kosovo rejected what it saw as the division of its territory. Eventually Serbia has come round and agreed to the EULEX mission for the whole of Kosovo, in part because it fears that otherwise the EU will place further blocks on its membership. The so-far-peaceful deployment of EULEX across the whole of Kosovo is a positive sign for the security of the political entity, although its presence in the north is currently largely nominal.

On 1 February 2009 EULEX took control of two customs posts in Serb-dominated northern Kosovo. The two checkpoints in question, at gates one and 31 near RaÛka and Zubin Potok, were destroyed in February 2008, after being set on fire by angry Serbs just days after Kosovo's unilateral declaration of independence last year. Local Serbs have protested at the checkpoints, blocking roads and arguing that the security situation had worsened since the arrival of the EULEX officers, but the protests have so far been peaceful.⁶⁹

3.5 NATO

By Claire Taylor, International Affairs and Defence Section

Full membership of the NATO Alliance has been a long term goal of the Serbian government. At the NATO Heads of State and Government Summit in Riga in November 2006, Alliance leaders agreed to offer membership of the Partnership for Peace (PfP) programme to Serbia, Montenegro and Bosnia-Herzegovina. As part of PfP membership, NATO has made clear that it expects both Bosnia and Serbia to co-operate fully with the ICTY. Serbia subsequently joined the PfP in December 2006 and is currently in the process of drafting its first Individual Partnership Programme. As part of that programme key areas of co-operation have been identified as security co-operation, defence and security sector reform, science and the environment and public information. Serbia is also considering establishing a diplomatic mission at NATO HQ as well as a liaison office at SHAPE. In October 2008 Serbia and NATO signed a PfP security agreement which will allow for the exchange of classified information. Although a standard PfP document, formalisation of the agreement is considered a sign that progress is being achieved. However, military reform is a key tenet of the PfP programme and the current divisions between the Serbian military and government over the pace and direction of those reforms could have implications for the progress of Serbian membership in the longer term.

4 Key events in 2008

3 February	Boris Tadić wins Presidency by a narrow majority in second round of elections
17 February	Kosovo declares independence from Serbia
11 May	Parliamentary elections held.
24 June	New coalition Government formed led by Boris Tadić's Democratic Party
7 July	Pro-EU coalition takes office
18 July	Radovan Karadžić is arrested in Belgrade

⁶⁹ "EULEX reaches into northern Kosovo", Jane's Intelligence Review, 12 February 2009, http://www4.janes.com/subscribe/jir/doc_view.jsp?K2DocKey=/content1/janesdata/mags/jir/history/jir2009/jir10582.htm@current&Prod_Name=JIR

8 October UN General Assembly agrees to Serbia's request to an Advisory Opinion from the International Court of Justice on the legality of Kosovo's declaration of independence.

December First EULEX forces arrive in Kosovo