V.I.P. Daily News Report

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ANALYSIS

Government Pursues Electoral Economy

The International Monetary Fund is not behind the economic policy of the Serbian Government – foreign debt, unemployment, exchange rate, signals that sound an alarm for urgent turnaround measures.

Heavy snow and extremely cold winter have become the biggest problem of Serbian authorities and all media's news give most of their time to the issue. Snow has covered all other problems of Serbia.

There are no news on failed talks with the IMF, on the referendum in North Kosovo, or on the EU member-country candidate status. Snow has covered failures of Serbia's policy. The only problem lies in the fact that the bad weather will end soon, and spring sun will melt snow down.

Then the Serbs will be facing with reality of their economic and political situation. But, the authorities will not have the answers to the problems in which they have gotten themselves into. It is hard to believe that the successes in the arrest of Serb criminals will be good enough to please impoverished and unhappy Serbs. Particularly because contribution of Serbia's police in the arrest of the criminals is not significant. Their part in the operation comes down to sending and receiving photos and fingerprints.

Serbia's authorities will have to explain what has been happening in Serbia's economy. They should explain why they postpone making of painful decisions for the time after the elections in a new government, who ever will set it up, and in the meantime they accumulate debts to cover the over-high budget expenditures and close companies down one by one.

For the time being the state apparatus and companies without which day-to-day life could not go on are the only ones that have still been working.

Illusion of macroeconomic stability: Unsatisfactory business environment at Serbia's market is the result of non-organization of the state and her huge, direct or indirect, impact on economy. That direct role is reflected in high subventions that for a long time have been given to possible new investors, nationalized or state-run companies, and indirectly through massive administration and complicated and long procedures that induce bribe and corruption.

That also creates unequal rules of the game at the market. In the environment of non-transformed and inefficient judicature, in addition to the passive role of regulatory bodies, it only makes inequality at the market. So, the ones that are not close to the state or offices of the ministries work in more difficult conditions.

Large number of office workers at all state levels and the entire non-transformed public sector are great burden to Serbia's exhausted economy and people that has to be supported. Instead of the reform processes to be seriously conducted in that sector, the holders of political and economical power have chosen something that is painless in short run, and that is contracting debts mostly abroad.

By dong that, the authorities have been providing an illusion of macroeconomic stability and social peace, whereas the problems are accumulating successively and threat to erupt and cause serious disorders in Serbia's economy. These disorders, in continuation with the current economical practice, and after the sale of the remaining state's 'silverware', will lead Serbia to a situation similar to the one in Greece.

Private sector is more cautious than state: According to the official data of the National Bank of Serbia (NBS), in late November 2011, foreign debt of Serbia was EUR 23.8 billion. It was 0.3% higher than at the end of October, i.e. by 0.2% higher than in late December of 2010.

The increase in the overall foreign debt occurred primarily due to permanent contracting debts of the public sector. So, the state with the situation in November 2011 owed EUR 10.6 billion to foreign creditors, or 1.8% more than in October, i.e. 16.9% more than in late December of 2010.

One should keep in mind that the foreign debt of the public sector since 2008 - i.e. since the first wave of the recession hit the country and the current republic government came into power - has increased from EUR 6.5 billion to EUR 10.6 billion, with a trend of further indebtedness in order the current budget needs and accounts payable to be serviced.

So, in the period since 2008 till the end of November of 2011, the overall foreign debt of the public sector increased for a little bit more than EUR 4 billion.

On the other hand, the foreign debt of the private sector of approximately EUR 13.2 billion, was lower than 0.9% at a month level, i.e. 10% lower than in late December 2010. From almost EUR 14.6 billion – the amount of the private sector's foreign debt (banks and companies) in 2008 - it was reduced to EUR 13.2 billion in November 2011, which is a reduction of approximately EUR 1.3 billion.

It is obvious that there are opposite trends in dynamics of contracting debts of public and private sectors. Whereas the private sector has became more rational and cautious when it contracts new credit arrangements, the state acts irresponsibly, thinking about providing an illusion of macroeconomic stability by continuous credit infusions.

Certain trends of further debt accumulation, unemployment rate increase: Due to the fact that the year of 2012 is electoral one, one should not count on any changes in activities of the government in this year, which means that trends of further debt accumulation is certain without making any essential reform moves.

It has been confirmed by the failed talks with the IMF mission. The talks are frozen till the new government is set up in mid-2012, or even later on. The current authorities do not have political will to get to grips with the issue of high overall public debt which is at around 47% of the GDP, and by that it exceeded the limit of 45% of the GDP.

However, the amount of the public debt is not the biggest problem of Serbia's economy. The biggest problems are the structure of the debt and the situation in the real sector. The money is borrowed, it is not invested, but spent – on enormous state administration, wages, and pensions. Real sector, on the other hand, is in a very bad state and the production drops, which the image of Serbia's indebtedness makes worse.

In addition to that, the authorities do not take into account on the IMF's correction of economic growth of Serbia from 1.5% to 0.5% for 2012, whereas the Serbia's budget still envisages old and unrealistic projections.

The objective is, in addition to further accumulation of debts, making of an illusion of existing employment by making mostly unsuccessful companies (the latest example is the steelworks in Smederevo as well as the glassworks in Paracin, fertilizer factory in Pancevo, Methanol and Acetic Acid Complex – MSK, railway cars factory in Smederevo, Pirot-based "1 Maj" garment factory, etc.) as the state-run, to survive till the parliamentary elections in spring.

Economic crisis in Serbia has been escalating. The growing unemployment rate demonstrates how much the economy and the society are deep in crisis. The unemployment rate was lower than 16% in late 2008; a year later it was 16.6%; in 2010 it was 19.2% and in late 2011 it was 23.7%.

Increased business risk: Serbia is close to 80% of quantitative ratio between the overall foreign debt and the GDP. In the year of 2012, with a zero growth rate, or even with a negative growth rate (recession), keeping of the growing trend of accumulating debts of the public sector will certainly push Serbia into a group of highly indebted countries and it will affect her credit rating.

First strong alarming signals that Serbia is drawing closer to the so-called Greek scenario are sent by the RSD exchange rate, which has weakened dramatically against EUR over the past month. So, EUR 1 in late 2011 was RSD 104.64, but on February 10, 2012 it was RSD 109.18. If the NBS had not sold out EUR 68.5 million in a single day, RSD would have been even weaker. Weakening of the RSD occurred because the investors do not buy new NBS' securities, assessing that business risks at Serbia's market have been increasing.

The frozen dialogue between the IMF and the Serbian government indicated that. By that the IMF sent a clear message to local and foreign markets that it could not stand behind the Serbian government's economic policy, because it does not solve accumulated economic problems and it additionally complicates these.

Media are main electoral trumps: So, Serbia's authorities are waiting for launching of the election campaign (the parliamentary elections will be called in first half of March) with murky economic and social situation, but with complete control of media and political influence on judicature and the police. It is obvious that these will be the main instruments of power in the election campaign.

For the time being the authorities have not decided yet how the issues of Kosovo (the talks with Kosovo Albanians and the local elections in North Kosovo) and the struggle for the EU member-country candidate status would be solved. The authorities think only about the elections now and if they assess that to solve Kosovo issue will be larger damage than the candidate status will be an advantage, they will give up on the EU.

In addition to that, the authorities still do not know what they will do with the presidential elections, which will take place in 2013. They have to evaluate whether it is better for them to run at the presidential and parliamentary elections in May 2012, counting on popularity of the President Boris Tadic, or to leave the government to the Serbian Progressive Party (SNS) and a weaker coalition, and also to leave them problems of the current government, and to increase their popularity again due to that.

It will be clearer in a near future. One thing is more and more certain – parties of the governing coalition stand less and less chance of winning at the elections. Therefore they will have to seek for some other solutions. For that time the SNS will have to draft answers very fast for the chaos the current government will leave to them.

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