V.I.P. Daily News Report

V.I.P. News Services, Čika Ljubina 6, 11000 Belgrade, Serbia
phone/fax: (381 11) 32 82 360, 32 86 140, 32 86 141
e-mail: ***office@vipnews.rs vipnews@sbb.rs***
Publisher: V.I.P. News Services Editor-in-Chief: Vladan Marjanović
News Desk Editors: Rade Stanić, Davor Lukač

Issue No. 4812 **Thursday, March 8, 2012**

ANALYSIS

Criticisms of NBS Governor: Government Seeks One to Blame for Drop of Dinar

The exchange rate of the Dinar (RSD) against Euro (EUR) has considerably dropped since the beginning of this year. It is a result of relaxation of restrictive course in pursuing the credit-monetary policy of the National Bank of Serbia (NBS) as well as of gradual leaving of investors from Serbia's market because of the announced instability. The IMF also warned about it when the organization made a decision that it could not back the economic policy of the government.

Thus, it is highly likely that the government will spend foreign currency reserves to defend RSD rate of exchange in the following period, and it probably will intensify the already restrictive credit-monetary policy in order to make investors to take the bite of securities with higher interest rates.

The question remains whether the investors will really take the bait in the current business environment, because such a policy of the government did not attracted investors back in late 2008, when Serbia's market was hit by the first wave of the global recession.

Depreciation of Dinar is something expected, because the RSD rate of exchange was unrealistically high, which suited importers, but discouraged production and export sectors. In addition, for the exchange rate is a mirror of an economy, and Serbia's economy has bad performances, it was evident that the Dinar was overblown as well as that the exchange rate would have to become more realistic.

Exchange rate fluctuation

	Worth of EUR against RSD
2010	
December	105,50
2011	
December	104,64
2012	
January	106,06
March 7	110,59

Source: NBS data

Anyway, weakening of the Dinar is not useful to very powerful import lobby, which has been trying to stop further weakening of Dinar.

In order strengthening of the RSD to occur realistically, it is necessary structural reforms in public sector to occur as well, and on the grounds of that to attract new investments which will boost the situation in real sector, i.e. production and exports. There is no sustainable economic growth without that. That is why Serbia-based press' articles that have been taking a rather critical view of indicating the NBS Governor Dejan Soskic as the one to be blamed most for the depreciation of Dinar is just distracting the public from the major culprit for the depreciation of the local currency – the government. For, the one who has not implemented thorough transformation of the public sector, decreased current public spending and stopped basing economic policy on galloping contracting debts in order to preserve virtual macroeconomic policy, is the government itself.

For the populist reasons, bearing in mind the forthcoming elections, the government turned deaf ear to IMF's objections regarding the very fact that the overall public debt exceeded 45% of the GDP, assessing that in the current situation the ratio, if Serbia sees the end of 2012 with the decrease in the GDP, will increase to approximately 55%.

According to that, the autistic economic policy of the government – which is, before the elections, accompanied by refusal to admit that there are problems created by the government itself – is the major reason of the increase of the foreign currency exchange rate.

In late January this year EUR 1 was RSD 106.06, which is 15% nominally and 0.3% realistically more than in late 2011. In relation to the situation in January the Dinar has depreciated 0.4% in nominal value, i.e. around 4% in real value. Further weakening of Dinar continued in February as well in early March. It only confirms conclusions that had been made and voiced earlier - the rate of exchange of Serbia's currency is not realistic, i.e. it is considerably overrated in relation to competitive potential of the local economy as well as that an illusion of its stability was preserved only through short-term financial operations initiated by the NBS and by the sale of treasury bills later on.

The depreciation of Dinar will be stopped for a short time, because of psychological reasons, due to the fact that Serbia has been granted the EU member-country candidate status. However, further weakening of Dinar will remain as general trend, regardless of temporary, seasonal fluctuations.

Real stability of Dinar can be achieved only through reform process of the public sector, an inflow of new investments and the IMF's guarantees that Serbia is on the path of economic recovering through implementation of more than necessary reforms. So, the exchange rate is just a signal of the occurrences and the situation within the economy and the depreciation of Dinar will be an issue till the country has bad production and export performances, i.e. till the country has over-enormous public spending.

Sustainable stabilization of Dinar in a long run would mean improvement of economic situation in the country, which would decrease pressure on Serbia's currency. The exchange rate only reflects the ill situation in the local economy and only serious cuts in the economy can pull the Dinar out from the crisis it is in right now.

Because it is hard to expect any serious moves of the government two months before the elections, the big job is waiting for a new government to be done. In the meanwhile, the outgoing government will do everything in its power to preserve the RSD exchange rate till the elections, in order to prevent further drop in the local currency and the psychological effect of it not to additionally decrease (the already dropped) rating of the governing coalition.

The orchestrated criticisms of the Governor these days, by the dailies close to the authorities, are just attempts all the blame for weakening of the RSD and the chain increase in prices to be put on the NBS. Soskic does not belong to the closest circles within the governing coalition and he is not a party representative, so he is a sacrifice which, if necessary, is easy to offer for the government's interests.