

# Weekly *Economic* Bulletin

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Issue No. 799

Thursday, February 9, 2012

## ANALYSIS

### *Economic Trends in Serbia*

*(Part I)*

#### 1.1. Global Assessment of Economic Situation

The dissatisfactory business climate on the Serbian market is the hostage of the disorganization of the state and its large interference, either direct or indirect, into the developments in the economy. That direct role is reflected through generous subsidies which have been granted for quite some time now to potential new investors, i.e. to state-owned companies or those that have become state-owned, and the indirect role through the excessively large administration and numerous procedures and paperwork, which induce the appearance of corruption. This creates unequal rules of the game for market players, which, in conditions of a non-transformed and inefficient judiciary, as well as the passive role of regulatory bodies, such as those for fighting corruption or for the protection of competition, are only additionally stimulating such inequality on the market. For this reason, those who are not close to the invisible cabinet hands have more difficult working conditions, and, at the same time, consumers are also suffering the consequences through prices that are higher than healthy competition relations would allow, and ultimately the state itself, i.e. its citizens, because the state is borrowing too much so as to help correct unsuccessful business moves, mostly by large domestic businessmen, and the pumping of money into their companies or into the still non-restructured socially-owned companies, doing little to enable them to play the market match, independently, with professional management.

Furthermore, an avalanche of clerks at all the state levels and the entire non-transformed public sector represent a big burden for the weakened Serbian economy and population to support. Instead of reform processes in that sector being seriously launched, creating an environment of a more efficient administration, a more efficient judiciary and, through the restructuring of public companies, space for attracting new investments and, thus, their gradual removal from the state budget, political and economic officials opted for something less painful on a short-term basis, this being the conclusion of financial obligations towards creditors, mostly towards foreign creditors. This provides only for a semblance of macroeconomic stability and social peace, while problems are accumulated and are being left aside, all of them threatening soon to come out onto the main stage and, with eruptive force, to cause serious disturbances in the Serbian economy. With a continuation of the present economic practice, and upon the sale of the remaining state "silver", these disturbances would bring Serbia into the position of having to dance a Greek folk dance.

*Observed by certain economic indicators, in December 2011, a positive dynamics was registered among the following: the tourist turnover, retail trade, average net wages, total foreign currency reserves, producer prices and inflation.*

*Contrary to this, negative trends in December 2011 were registered among the following analyzed economic indicators: the physical volume of industrial production, total orders, exports, the foreign trade balance, the foreign debt and the unemployment rate.*

#### 1.2. Analytical Assessment of Economic Trends

*Observed by certain economic and monetary indicators, at the end of December 2011, the following trends were registered in the Serbian economy:*

- **The physical volume of industrial production was lower by 2.1% at the monthly level. And if the seasonal factor is excluded from the analysis, we also get a drop in the dynamics of production activities in the Serbian industry (-0.5%). Therefore, the trend of the drop in industrial production since the beginning of 2011 has not been**

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interrupted and as the inflow of both domestic and foreign orders has been dropping, one should expect an additional deterioration of the negative dynamics of production activities, with a serious intimation that this economic indicator could slide towards the recession zone. This situation could somewhat be improved with the launching of the production of Fiat automobiles in Kragujevac, but as one swallow does not make spring, this swallow will not bring more sun in 2012 than there was in 2011, primarily because at issue is the very beginning of the launching of production activities in this company. One should also bear in mind the fact that the former Sartid (which accounts for around a fifth of the Serbian exports) works with almost a two times smaller capacity and that the state has taken over the management of this company after the departure of the American owner, so as to prevent the closing down of this company in the hope that it could soon find a strategic partner from the same field of production. Furthermore, a more favorable environment has not been created for the more massive arrival of foreign investors, so that the inflow of investments is proceeding in a sporadic ad hoc rhythm, far below the dynamics which the Serbian economy needs, i.e. the renewal of its outdated production capacities. And how badly the Serbian industry needs new investments is also sufficiently attested to by the fact that the domestic economy is on the 130th position in the report of the World Economic Forum of October 2011 among the 142 analyzed countries, from the standpoint of company investments in research-development projects.

#### Dynamics of industrial production by commodity groups in Serbia

-Indices-

	<u>XII 2011</u> <u>XI 2010</u>	<u>XII 2011</u> <u>XII 2010</u>	<u>I – XII 2011</u> <u>I – XII 2010</u>
Energy	103.8	113.0	106.2
Intermediary products, except energy	91.7	97.0	103.2
Capital goods	103.6	86.6	102.2
Durable consumer goods	106.6	90.4	83.8
Non-durable consumer goods	96.9	95.6	99.0
<b>Industrial production – total</b>	<b>97.9</b>	<b>100.1</b>	<b>102.1</b>

Source: Data of the Republic Office of Statistics (RZS)

Still being offered to foreign investors, as the only, but quite attractive bait, are generous subsidies, which is a good measure on a short-term basis, but only if the business environment is transformed in that period in the sense of creating a stable and transparent judiciary and the mechanisms for its acting, simplifying and reducing the paperwork and the procedures for the issuing of various permits and making the state administration more efficient and effective through its reduction, with improvement and technologically more modern equipment. Without this, even the present investments, attracted by state subsidies, can very easily leave our market once the business interest disappears. For this reason, a transformed public administration and judiciary is the foundation on which, along with a developed transport and communication infrastructure, it is possible to attract new foreign investments. The fulfillment of these basic preconditions would also result in the reduction of corruption, as a socially deviant occurrence which is of an endemic nature in Serbia. This is also indicated by the report of the World Economic Forum, according to which, among 142 countries, Serbia is 128th according to the efficiency of its judiciary, i.e. 107th according to the skillfulness of the institutional fight against organized crime.

**Despite the drop of production activities at the monthly level, the December level of production was, nevertheless, larger by the almost negligible 0.1% than in the same month of 2010. Due to this, after the trend of the alleviation of the growth of production activities as of the beginning of 2011, this trend was noticeably interrupted in the last month of the reporting year, although not in the direction of an upward path, but rather only with the maintenance of the level of production from the January – November period of 2011. Namely, in the first quarter of this year compared to the same period last year, industrial output registered a positive move at a rate of as much as 6.4%, by 4.8% in the first half of the year, 2.5% in the January – September period of 2011 compared to the same period in 2010, only for this positive dynamics to drop to the point of 2.1% in the first eleven months of this year relative to the corresponding period in 2010, which was maintained at the end of 2011 as well.**

What is disturbing is the drop in production in the processing industry. At the monthly level it was reduced by 3%, and in the entire year of 2011, compared to 2010, by 0.4%. In this regard, at the annual level, despite a better agricultural crop, a drop of production activities by 2.8% was registered in the food industry. The largest negative blow was taken by the producers of other transportation facilities, except motor vehicles and trailers (-46.1%), furniture (-20.3%), coke and oil products (-14.3%) and textile (-11.8%). Therefore, at issue are non-restructured sectors, and in the case of the food industry, the textile and furniture industries also the population's low standard of living which, as a weight, is limiting the demand for products of these industries. Since, in 2012, expected, in the best of cases, is the repetition of the purchasing power level from 2011, and with a strong likelihood of it being at even lower levels than last year, these sectors of the processing industry will suffer even stronger negative effects of the population's thin wallets and of growing unemployment. Furthermore, the demand in the metal processing complex is dropping, whereby the pressures on the Serbian industry, in the sense of changing the direction of the dynamics of its production towards negative zones will be intensified.

In 2012, there is the realistic danger of the Serbian industry setting foot into the zone of recession. Domestic presuppositions for this have already been created in the form of a low domestic demand and larger illiquidity with

unfavorable crediting conditions, while the possible plunge of the euro zone countries into recession, especially Italy, which has very developed business relations with the Serbian economy, only turn this realistic danger into practice;

- **The dynamics of the inflow of both domestic and export orders at the end of 2011 registered a drop.** This means that one should expect a declining dynamics of production and export activities, as well as the further growth of the number of unemployed persons. The negative dynamics of the demand from the domestic and foreign markets is present in all the commodity groups (means of labor, intermediary products and consumer goods);
- **The exceptionally low level of the population's standard of living and Serbia's non-recognizability as a tourist destination in international proportions, after the initial months in 2011, when it registered a considerable growth of the tourist turnover, primarily as a result of the introduction of more favorable prices in Serbian mountain centers at the start of the winter season, led to the formation of an alleviating positive direction in the dynamics of the tourist turnover in Serbia. This toning down of the initial positive results was increasingly pronounced with the passage of 2011. Thus, after the precipitate growth at a rate of as much as 17.9% in the first quarter of 2011, compared to the same quarter in 2010, as well as growth by 11.9% in the first half of the year, in the first nine months this growth in the number of the overnight stays by tourists in Serbia dropped to a single-digit rate of 6.9%, only for the point at which the growth of the tourist turnover held its position to drop to 4.5% in the first eleven months of 2011 compared to the same period last year. Finally, in the January – December period of 2011, compared to the corresponding period in 2010, the total number of tourists' overnight stays of around 6.6 million was registered, which represents the further lowering of the number of tourists' overnight stays in Serbia, so that the positive growth rate reached the level of 3.6%.**

#### Tourist turnover in the Republic of Serbia – number of overnight stays

	Total		Domestic		Foreign	
	I - XII 2011	$\frac{I - XII 2011}{I - XII 2010}$	I - XII 2011	$\frac{I - XII 2011}{I - XII 2010}$	I - XII 2011	$\frac{I - XII 2011}{I - XII 2010}$
<b>Republic of Serbia</b>	<b>6,644.738</b>	<b>103.6</b>	<b>5,001.684</b>	<b>100.8</b>	<b>1,643.054</b>	<b>113.1</b>
Belgrade	1,149.029	101.7	301,114	88.7	847,915	107.3
Novi Sad	213,549	126.9	70,926	104.0	142,623	142.4
Spa resorts	2,308.435	104.4	2,176.622	103.3	131,813	126.2
Mountain resorts	1,590.016	108.4	1,442.213	107.8	147,803	114.5
Other tourist places	1,172.675	95.3	847,263	89.1	325,412	116.4
Other places	211,034	101.9	163,546	103.0	47,488	98.1

Source: RZS data

As the main tone in creating the tourist turnover in Serbia is being given by domestic guests (around 5 million overnight stays, which, in 2011, accounted for 75.3% of the total number of tourists' overnight stays), due to the erosion of the domestic guest's already low purchasing power this factor became the main element in limiting the growth and development of tourism. That this is so is also attested to by the data on the trends in the number of overnight stays by domestic guests in 2011. In the first quarter of the observed year, compared to 2010, the rate of the growth of the tourist turnover induced by the overnight stays of domestic tourists reached the point of as much as 19.6%, only to drop to 10.2% at the six-monthly level, and when observed through the first three quarters of this year compared to the same cumulative period in 2010, to 4.6%, while in the first eleven months of 2011, relative to the January – November period in 2010, it reached the level of only 1.9%. Finally, the number of domestic tourists' overnight stays throughout 2011 was as much as 0.8% higher than in 2010. Therefore, as domestic guests are dominant in the realization of the overall tourist turnover in Serbia, the declining positive dynamics in the number of the domestic tourists' overnight stays leads to the weakening of the intensity of the growth of the overall tourist turnover. Unfortunately, such tendencies should be expected in the following year as well, in view of the population's poor purchasing power and the predominant dependence of the tourist turnover on the domestic guest, with certain positive seasonal oscillations, which will not disrupt such tendencies, seriously threatening to have tourism also enter the zone of recession in the year 2012.

*(to be continued)*