Weekly *Economic* Bulletin

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ANALYSIS

Economic Trends in Serbia

(Part I)

1.1. Global Assessment of the Economic Situation

In January, the business environment in the Serbian economy was extremely unfavorable. Apart from the external factor in the form of the reduction of the foreign demand due to the debtor crisis in the euro zone, this was also considerably the result of the internal structural weaknesses. These weaknesses are primarily reflected through the non-transformed public sector in its entirety. Namely, the present public sector is only aggravating the country's foreign trade and balance of payments position, it is additionally tightening the debtor noose around its neck and it is the source of corruption. It is, therefore, also an obstacle to the continual stronger inflow of investments into our market. Over the past four years we were witnesses, not only of the fact that there were no essential moves in the restructuring of the public sector, but rather that this public sector additionally grew and burdened the state coffer. Thus, a large number of unsuccessfully privatized companies was turned into state ownership without any special analysis that would show the economic justification of such a procedure. The long-lasting active presence of the state in these companies (1.Maj Pirot, the Fabrika Vagona train car factory in Kraljevo, the Staklara glass factory in Paraćin, the Methanol-Vinegar Complex, Petrohemija, and since recently the former Sartid as well), indicate that the state has no clear vision, i.e. an idea about the direction in which to develop their business operations, but rather most of the moves boil down to the preservation of social peace through the ensuring of credits from someone else's sources of financing, whose guarantor is the state, this aggravating the budget deficit and the level of the state's credit exposure to foreign creditors. This also creates unequal relations on the market, since the state is benevolent to certain players on the market, but malevolent towards others. This is especially visible by the fact that, it is turning a blind eye when it comes to certain state companies, or those that have been turned into state-ownership, settling their obligations towards the state, such as, for example, the payment of funds for health insurance. When, apart from the new companies that form the chain of the public sector, one also takes into account the public companies which have been transformed only cosmetically or not at all, and whose losses, like in the case of the Jat airline company or the Železnice railway company, are, through the borrowing of the state, also being covered at the expense of future generations, it is clear that the state has anchored itself within the Serbian economy and that it is the one prompting the processes of corruption and of monopoly-cartel structures, inflation and illiquidity, as well as financial non-discipline. In a way, we are witnessing the process of metastasizing which is additionally weakening the already bad business climate in Serbia, i.e. its competitive position in the world. That process is being supported by the non-transformed judiciary and the public administration at all levels, as well as the passivity of various state institutions in punishing non-market or socially irresponsible conduct on the market, such as the abuse of the monopoly position. Realizing that the current economic policy of the Serbian government is a road without an economic and social future, the IMF has also frozen the arrangement out of precaution, waiting for a new government, which, in the present bad economic situation will be forced, for the sake of preserving the already fragile semblance of macroeconomic stability and of the efforts for this no longer to be a semblance but a reality, will have to call the IMF as support and a guarantor of the realization of the badly needed serious cuts in the public sector.

In January 2012, negative trends among the analyzed economic indicators were predominantly registered. Apart from the pronounced impact of the season, this was also contributed to by internal economic weaknesses accompanied by a drop in the foreign demand. Thus, a negative dynamics is evident among the following: industrial output, overall orders, retail trade, average net wage and total foreign currency reserves. The latest data for the foreign debt and exports refer to December 2011 and according to them, these two economic indicators are also in the group of indicators with a negative sign. The foreign debt grew primarily owing to new state borrowings, so that Serbia is very close to facing the Greek scenario. Exports are dropping and already January will indicate that it will experience a dramatic collapse, especially after the considerable drop of production in the former Sartid. Thus, Serbia's balance of payments position will also deteriorate, which will make additionally difficult the regular servicing of the previously taken credit obligations. This will require new borrowings, and in view of the frozen arrangement with the IMF, the price of borrowing could be higher, and investors themselves could steer clear from concluding credit arrangements with the state, primarily in the issuing of state bonds. Therefore, Serbia is galloping towards the theater stage where a play will start being performed according to the Greek scenario, but at a somewhat lower level and in a milder form, because the debts are lower and the country is smaller. However, this therapy will have all the characteristics of a shock therapy, as a result of the irresponsible economic policy in the previous period and the masking of the realistic gloomy picture of the domestic economy and its future.

In January 2012, it is only the turnover in tourism that registered a growth in its dynamics, while inflation registered stability in its trends.

The increase in the tourist turnover is the result of the more flexible price policy of tourist workers and primarily the result of a sports event of European proportions (the European Handball Championship). For this reason, at issue is only a growth on a short-term basis. With the limiting of margins on some of the basic foodstuffs conditions were created for inflation to grow in January by a negligible 0.1% at the monthly level. However, the increase in the price of oil on the world market and the depreciation of the dinar will lead to the swelling of inflationary trends in the next two to three months. Nevertheless, if the further major plunge of the domestic currency is halted and if the escalation of the price of oil on the global market is calmed down, in view of the low domestic demand, one can expect inflation to finish this year at the upper projected limit of 5.5%.

Analytical Assessment of Economic Trends

Observed by certain economic and monetary indicators, at the end of January 2012, the following trends were registered in the Serbian economy:

- As is already the tradition in the first month of each business year, 2012 also registered a drastic drop of the production activities in the Serbian industry compared to December of the preceding year, at a rate of as much as 21.6%. At issue is a pronounced negative impact of the seasonal factor, since January is recognizable as a month with a smaller number of workdays due to the New Year and religious holidays. However, even when the impact of the season is excluded, it becomes evident that this steep drop of the physical volume of industrial production at the monthly level is also the result of the drop in the inflow of overall orders, especially those from abroad, and, due to this, the drop in the degree of the usage of production capacities. A sufficiently illustrative example is the closing down of a blast furnace of the former Sartid in Smederevo and the American owner's final decision to leave the factory. Thus, when January 2012 is observed in deseasonalized terms compared to the preceding month, a drop is production activities is registered at a rate of 0.3%. The fact that, apart from the impact of the season, which was indisputable in the course of January, the factor of the unfavorable economic situation on the domestic and European markets was also present is also attested to by the results from January last year. Namely, in the first month of 2011 compared to December 2010, a drop in production was registered by 18.7% (a milder drop than in January 2012), while, unlike this year, in deseasonalized terms, it registered a growth by as much as 3.2%. Therefore, it is absolutely clear that the present negative dynamics cannot be based only on the season and the season cannot be an excuse, but rather the consequence of both the drop of the domestic and foreign demand, on the one hand, and the non-restructured economy, non-transformed public sector and the lack of new investments that would bring a broader and better production and export assortment of the Serbian industry, on the other, which would, at the same time, improve the country's economic performances.

Dynamics of industrial production by commodity groups in Serbia

-Indices-

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Energy	106.2	114.9	105.1
Intermediary products, except energy	103.2	74.6	96.8
Capital goods	102.2	66.7	81.2
Durable consumer goods	83.8	56.4	91.6
Non-durable consumer goods	99.0	69.8	91.0
Industrial production – total	**102.1**	**84.0**	**97.3**

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

At the annual level (January 2012 / January 20122), the physical volume of industrial production was reduced by 2.7%. Therefore, at the very start of the business year of 2012, the dynamics of production activities took a steep negative direction, which will additionally deteriorate in February. Just as countries of the euro zone are sliding into recession, the inflow of orders from abroad will continue to drop, which, along with the internal weaknesses of domestic industrial capacities, will result in the total negative dynamics of industrial production this year, most probably ending in the negative zone.

(to be continued)