SCHEDA PAESE

SERBIA

SACE

COUNTRY REPORT

SERBIA

Economic Research and Public Affairs
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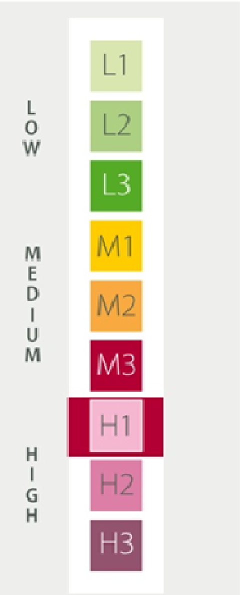
Capital: Belgrado
Population (2010): 7.4 million
Nominal GDP (PPP, 2010): USD 80 billion



RISK: H1

OUTLOOK: stable

EXECUTIVE SUMMARY

Political risk. The difficult economic situation is fuelling the public's discontent with the government. The status of Kosovo continues to be a key political issue, both within the country and in its international relations. Serbia is gradually moving down the path towards integration into Europe.

Economic risk. The country's economic performance improved in 2010, but certain weaknesses persist, such as the high budget deficit and indebtedness in foreign currency (euro). In April 2011 Serbia signed a € 2.9 billion stand-by arrangement with the IMF.

Financial and operational risk. The financial system has some weaknesses and, in particular, is vulnerable to exchange-rate risk as most of its debt is in euros. The operational environment is improving.

SELECTED ECONOMIC INDICATORS

	2008	2009	2010e	2011f	2012f
Real GDP (% change)	5.5	-3.1	1.5	3.0	5.0
Consumer prices (% change. average)	12.4	8.1	6.2	9.4	4.8
Central government balance/GDP (%)	-2.6	-4.3	-4.9	-4.1	-2.8
Balance of payments					
Exports ($ bln)	7.4	6.0	7.2	8.2	9.9
Imports ($ bln)	-15.0	-11.1	-12.1	-12.9	-14.2
Trade balance ($ bln)	-7.6	-5.1	-4.9	-4.7	-4.2
Current account balance ($ bln)	-6.1	-2.1	-2.7	-2.8	-2.4
Current account balance/GDP (%)	-17.6	-6.9	-9.3	-8.6	-7.0
Total external debt ($ bln)	21.8	22.9	23.3	23.3	25.4
Total external debt/GDP (%)	65.2	76.5	79.5	73.1	72.7
Debt service ratio (%) *	30.8	32.3	21.4	26.5	28.1
Reserves ($ bln)	8.2	10.6	9.4	9.7	10.7
Reserves (months of imports)	7.7	7.8	7.9	7.5	-
Exchange rate RSD/USD (annual average) *	55.8	67.6	78.6	83.3	83.8

Source: IMF, December 2010; EIU – Bureau van Dijk. February 2011
e: estimates; f: forecasts

OPERATIONAL BUSINESS INDICATORS

Business Climate Indicators	Current	Previous
Doing Business 2011	89/183	90/183
Index of Economic Freedom 2011	101/183	104/183
Corruption Perceptions Index 2010	78/178	83/180

Agreements and Treaties	
Convention of Washington	In force
Convention of New York	In force
Bilateral agreement on the promotion and protection of investments	-
Bilateral agreement to avoid double taxation on income	-
Transferability of SACE policy	Yes

RATING

Standard and Poor's
BB-
Moody's
-
Fitch
BB-

SACE TERMS OF COVER

OECD Category: 6/7	
Sovereign risk	with conditions
Bank risk:	without conditions
Private risk:	without conditions

SACE GUARANTEES 31 MARCH 2011

Serbia	
Committed (€ mln)	155.1
Outstanding (€ mln)	150.0
- of which issued (€ mln)	149.4

RISK: medium

OUTLOOK: stable

POLITICAL RISK

Domestic affairs. The pro-European coalition "For a European Serbia" led by Boris Tadic's Democratic Party is under pressure due to the country's financial problems. The fiscal austerity package implemented in order to comply with IMF requirements has given rise to public discontent. Although Belgrade maintains its stance towards the status of Kosovo and refuses to recognise its independence, talks have started in recent months, in part due to pressure by the EU. The next elections will be held in 2012.

International relations. On 17 February 2008 Kosovo declared independence from Serbia, which refuses to recognise its status. Serbia has made significant progress down the path towards integration into Europe. The interim trade agreement between Serbia and the EU officially came into effect on February 1st 2010, pending implementation of the broader Stabilisation and Association Agreement. In December 2009 visa restrictions were lifted, allowing citizens to travel freely within the Schengen area and, at the same time, Serbia formally submitted its EU membership application. It will take at least four years before the hand of EU membership extends to Serbia and the road will not be easy. However the country demonstrated a desire to cooperate with the International Criminal Tribunal for the former Yugoslavia (ICTY) by capturing war crimes fugitive Mladic. The last remaining fugitive wanted by the ICTY to allow Serbia's to join the European Union is the former Croatian Serb wartime leader Goran Hadžić.

RISK : high

OUTLOOK: stable

ECONOMIC RISK

Economic activities. Following the slowdown in 2009 caused by the global crisis (-3%), GDP turned positive in 2010 (1.5%), driven by an increase in imports and investments. Growth is forecast to continue in 2011 (3%), but is unlikely to recover to the pre-crisis levels before 2012/2013, as the reduction in salaries in real terms and restrictive lending criteria continue to hold back domestic demand. The transition to a more sustainable growth model requires measures capable of downsizing the public sector and expanding the private sector in order to create a more favourable business climate.

Fiscal policy. The budget deficit widened again in 2010 (4.9% of GDP), reflecting an increase in public spending. Under the new finance bill, which was approved at the end of 2010, the deficit should gradually narrow in 2011-12.

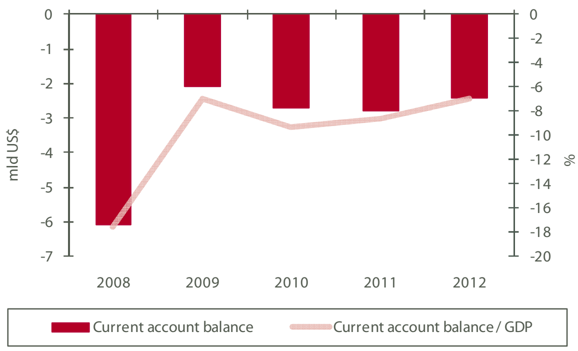
Inflation. The deflationary trend that started in 2009 as commodity prices and interest rates have gradually fallen is expected to end in 2011 (9,4%).

Balance of payments. The decline in imports in 2009 as a result of the crisis led to a reduction in the current account deficit, which moved back up in 2010 (9.3% of GDP). The support of international financial institutions (IMF, WB and EU) and of foreign banks that have intervened to sustain their Serbian subsidiaries is fundamental.

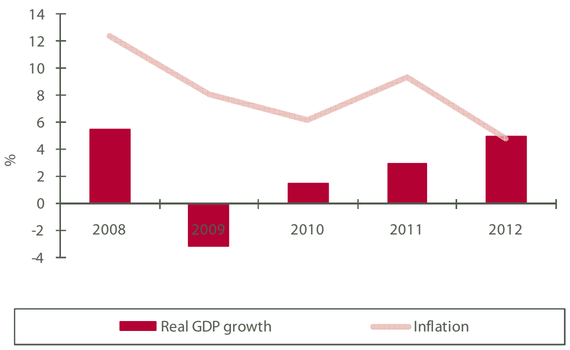
External debt and international reserves. In 2010 Serbia's external debt was equal to approx. 80% of GDP, of which 52% of GDP referred to private debt. As forecasters predict the recovery of the global and domestic economies, tests performed by the IMF indicate that the foreign debt-GDP ratio will not improve until 2012. International reserves are high (€ 9.4 billion at the end of 2010, equal to 7.9 months of imports).

Exchange rate. The Serbian dinar came under further pressure in 2010 due to instability on financial markets and, above all, the Greek debt crisis and tensions in the eurozone. However, currency depreciation has made Serbian exports more competitive. External factors combined with the uncertainty surrounding the approval of reforms might result in further depreciation during 2011-2012.

Current account balance



GDP growth and inflation



RISK : **high**

OUTLOOK: stable

FINANCIAL RISK

Structure. Serbia's financial system is dominated by the banking sector, which manages 90% of total financial assets. The banking sector consists of 33 commercial banks, 21 of which are foreign-owned (mainly by Italy, Greece and Austria), which manage 80% of total assets, 8 are Serbian state-owned banks and the remainder are private national banks. The main three banks are: Banca Intesa Belgrad (which recently merged with Panoska Bank, a subsidiary of San Paolo IMI), Komercijalna Banka and Eurobank EFG. They represent 31.4% of the national banking market. Some banks are still partially state-owned.

Performance. The banks are well capitalised with a high level of liquidity, also due to measures adopted by the central government to restore stability. However a gradual withdrawal of deposits and a notable increase in non-performing loans (16.9% of the total at the end of 2010) are recorded. Serbian banks are also extremely vulnerable to exchange rate risk, since around 66% of bank loans are denominated in a foreign currency, mainly the euro. The main foreign banks that dominate the sector have confirmed that they will continue to sustain their Serbian subsidiaries in 2011.

RISK : **high**

OUTLOOK: stable

OPERATIONAL RISK

Legal system. Serbia is currently overhauling its legal system. Since the fall of the Milosevic regime, reforms of the justice system have made the courts more independent, although corruption continues to be a serious problem. The prospects of EU membership and negotiations in view of Serbia's accession to the World Trade Organisation might foster improvements within the operational context.

Attitude towards foreign investors. Foreign investments in Serbia are regulated by the law on foreign investment passed in 2002, which establishes equal rights and responsibilities of foreign and domestic investors. Transfer and repatriation of profits are allowed. Foreign investors may buy real estate provided that, according to the principle of reciprocity, Serbian investors would enjoy the same rights in the investor's country of origin. Compensation is provided in case of expropriation. There are six free trade zones in Serbia (Pirot, Uzice, Sabac, Subotica, Zrenjanin, Novi Sad). Privatisation is still underway. Excessive bureaucracy is a hindrance to entrepreneurship.

Infrastructure, safety and natural disasters. The process of rebuilding Serbia's infrastructure, destroyed by bombing raids in 1999, continues thanks to international aid. The country is involved in the construction of the Corridor X road network that will link Salzburg and Thessaloniki via Budapest and Belgrade. The declaration of independence by Kosovo has heightened tension, particularly in the south of the country along the border with Kosovo, a region populated by a large Albanian minority.

RELATIONS WITH IFIs

International Monetary Fund. Serbia signed a € 2.9 billion stand-by arrangement with the IMF in April 2011. The country recently started discussions on a new precautionary credit line (PCL).

World Bank. The 2008-2011 Country Assistance Strategy for Serbia sets out three main objectives: 1) to create a more streamlined and efficient public sector; 2) to create a bigger and more dynamic private sector; 3) to reduce poverty among the population. At November 2010 there were 12 ongoing projects in Serbia, worth a total of US$ 845.8 million, mainly addressing the infrastructure and transport sectors.

European Bank for Reconstruction and Development. 159 projects have been approved, worth a total of € 5.5 billion. 45% of investments are directed towards the private sector.

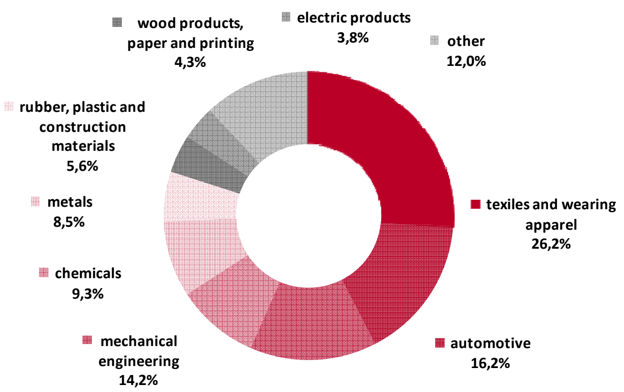
European Investment Bank. The EIB has financed projects for over € 2.3 billion for 2010-2011: these regard the financial, infrastructure and transport, education, energy and R&D sectors.

BUSINESS RELATIONS WITH ITALY

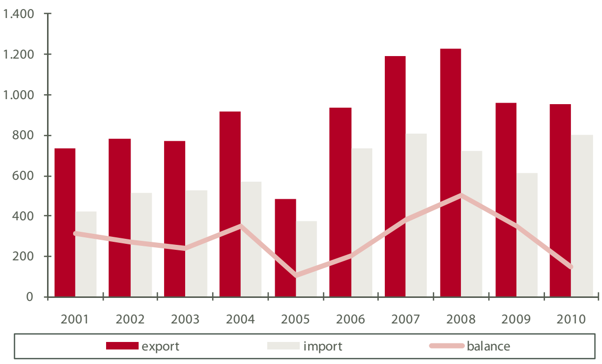
Trade. In 2010 Italy was ranked third in terms of exports to Serbia, behind Russia, its main supplier of gas and oil, and Germany. Serbia's trade balance amounted to around € 150 million. Italian exports to Serbia were valued € 950 million, falling by 0.7% compared to the previous year. Fashion (26% of the total) and motor vehicles (16%) drove exports, followed by mechanical engineering (14%) and chemicals (9%). Italy was Serbia's biggest export market. Imports were valued at € 802 million and the main sectors were steel and iron, non-ferrous materials, electrical machinery, cereals, fruit and vegetables.

Foreign direct investments. According to a joint report by the Italian Institute of Foreign Trade (ICE) and the Italian Ministry of Foreign Affairs (MAE), FDIs in Serbia amounted to € 1,117 million. The biggest investors are the Netherlands (€ 264 million), Austria (€ 193 million) and Slovenia (€ 108 million). In terms of sectors, the manufacturing industry accounts for the biggest share of FDIs, followed by the financial sector and wholesale and retail trade. In recent years the number of Italian enterprises that have invested in Serbia has almost trebled. Italian companies rank second in the number of companies acquired under the government's privatisation scheme.

Italian exports to Serbia (2010, %)



Italy - Serbia trade balance (2001-2010, mln €) *



* Data up to May 31, 2005 include Serbia and Montenegro

Last update: July 2011