INTERNATIONAL MONETARY FUND

IMF Country Report No. 18/375

REPUBLIC OF SERBIA

December 2018

FIRST REVIEW UNDER THE POLICY COORDINATION INSTRUMENT—PRESS RELEASE; AND STAFF REPORT

In the context of the First Review under the Policy Coordination Instrument, the following documents have been released and are included in this package:

- A **Press Release**
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on a lapse of time basis, following discussions that ended on October 4, 2018, with the officials of the Republic of Serbia on economic developments and policies underpinning the IMF arrangement under the Policy Coordination Instrument. Based on information available at the time of these discussions, the staff report was completed on December 7, 2018.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
PO Box 92780 • Washington, D.C. 20090
Telephone: (202) 623-7430 • Fax: (202) 623-7201
E-mail: publications@imf.org Web: http://www.imf.org
Price: $18.00 per printed copy

International Monetary Fund
Washington, D.C.

INTERNATIONAL MONETARY FUND

COMMUNICATIONS DEPARTMENT

Press Release No. 18/491
FOR IMMEDIATE RELEASE
December 21, 2018

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Completes First Review Under the Policy Coordination Instrument for the Republic of Serbia

- The implementation of Serbia's economic program is largely on track.
- The 2019 budget safeguards the major fiscal adjustment made in recent years and foresees a further decline in public debt.
- Serbia is committed to advancing structural reforms needed to foster private sector-led growth and faster convergence towards EU income levels.

On December 21, 2018, the Executive Board of the International Monetary Fund (IMF) completed the first review under the Policy Coordination Instrument (PCI)[1] for the Republic of Serbia. The Executive Board's decision was taken without a meeting.[2]

Serbia is the second IMF member country to request a PCI. It was approved on July 18, 2018 (see Press Release No. 18/299) and aims to maintain macroeconomic and financial stability, while advancing an ambitious reform agenda to foster rapid growth, job creation and improved living standards.

Serbia's strong economic performance continues, supported by the recovery of private consumption and robust foreign direct investments (FDI) and exports. Economic growth is projected at 4.2 percent in 2018 (partly reflecting a rebound from the effects of drought in 2017) and 3½ percent in 2019. Program implementation is broadly on track. Inflation remains below the mid-point of the National Bank of Serbia's (NBS) inflation band, while the NBS has kept interest rates on hold since April. Bank lending growth and private sector wages are strengthening. Fiscal performance remains sound, modernization of the tax administration has accelerated, and public debt has fallen sharply. The Serbian dinar has remained broadly stable

[1] The PCI is available to all IMF members that do not need Fund financial resources at the time of approval. It is designed for countries seeking to demonstrate commitment to a reform agenda or to unlock and coordinate financing from other official creditors or private investors. (see https://www.imf.org/en/About/Factsheets/Sheets/2017/07/25/policy-coordination-instrument).

[2] The Executive Board takes decision without a meeting (based on lapse-of-time procedures) when it is agreed by the Board that a proposal can be considered without convening formal discussions.

against the euro, with the NBS refraining from significant intervention in the exchange rate as appreciation pressures have eased in recent months.

The 2019 budget safeguards the major fiscal adjustment made in recent years and foresees a further decline in public debt, while accommodating higher investment spending and unwinding of crisis-era temporary measures. Steps to increase the use of the Serbian dinar in bank lending and deposits, and reduce reliance on the euro, are gradually yielding results. The authorities are committed to making further progress on structural reforms in 2019, which are needed to foster private sector-led growth and ensure Serbia is put on a faster convergence towards EU income levels. Their plans include measures to reduce the size of the shadow economy, strengthen public administration, as well as reform and restructure state-owned utilities, enterprises, and financial institutions.

REPUBLIC OF SERBIA

December 7, 2018

FIRST REVIEW UNDER THE POLICY COORDINATION INSTRUMENT

KEY ISSUES

Recent economic developments. The program is broadly on track and the economy is growing strongly, supported by private consumption, investment, and exports. Fiscal performance remains sound, modernization of the tax administration has accelerated, and public debt has fallen sharply. Inflation remains below the mid-point of the NBS inflation band, while the NBS has kept rates on hold since April. Both credit and private sector wage growth are strengthening.

Program performance. Quantitative targets (QTs) for end-September 2018 were met, apart from a minor deviation on the QT for domestic arrears. Most reform targets (RTs) have been implemented, albeit some with delays. Staff recommends completion of the first review under the Policy Coordination Instrument and modification of QTs for end-March and an establishment of end-September 2019 QTs.

Policy Recommendations

- **Fiscal policy.** The 2019 budget safeguards the 2015–18 fiscal adjustment and foresees a further decline in public debt, while accommodating higher investment spending and unwinding of crisis-era temporary measures. Tax policy and tax administration reforms aim to support growth and job creation. It will be important to focus reforms on reducing uncertainty and administrative burdens as well as increasing transparency.

- **Monetary and financial sector policies.** Financial sector reforms should focus on reforming state-owned financial institutions in a transparent manner, strengthening financial safety nets, and addressing AML/CFT shortcomings. The authorities are taking steps to reduce euroization of the economy, but greater two-way exchange rate flexibility would also help.

- **Structural reforms.** Complete the reform of large public enterprises and develop a strategy for SOE governance. Continue to advance efforts to reduce the grey economy, including through improved inspection and closure of loopholes in special tax regimes.

Risks. Risks to the program are considered moderate. Serbia remains vulnerable to spillovers from regional developments and market volatility. Domestic risks center on resistance to structural reforms or weakening of fiscal discipline, while delay in addressing AML/CFT weaknesses could undermine investment attractiveness.

Approved By
Thanos Arvanitis (EUR) and Petya Koeva Brooks (SPR)

Discussions were held in Belgrade during September 24–October 4, 2018. The staff team comprised James Roaf (head), Christine Richmond, Marina Marinkov (all EUR), Pietro Dallari (FAD), Rachid Awad (MCM), Sebastian Sosa (resident representative), Desanka Obradović and Marko Paunović (Belgrade office). Vuk Djoković (OED) attended some discussions. HQ support was provided by Daniela Marchettini (SPR), Min Kyu Song and Brett Stewart (both EUR).

CONTENTS

TABLES

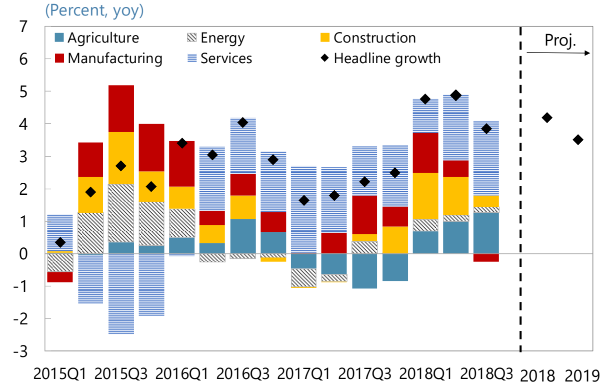
APPENDIX

RECENT DEVELOPMENTS

1. Strong economic performance continues (Figures 1-7). Real GDP growth in 2018H1 was the fastest in 10 years and continued at 3.8 percent yoy in Q3, supported by the strong recovery of private consumption and robust FDI and exports. Growth is now projected at 4.2 percent in 2018. Revised annual national accounts (2015–17) were released in October, resulting in about 6 percent higher nominal GDP and tilting the composition of growth away from net exports (Box 1). Continued improvements in labor market participation are supported by robust employment growth in the formal sector and declining unemployment. Average net wages are rising, up 5.5 percent yoy in September, and an increase in the minimum wage of 8.6 percent will take effect from January 1, 2019. Overall, real wage growth remains restrained (Figure 7).

Contributions to growth

(Percent, yoy)

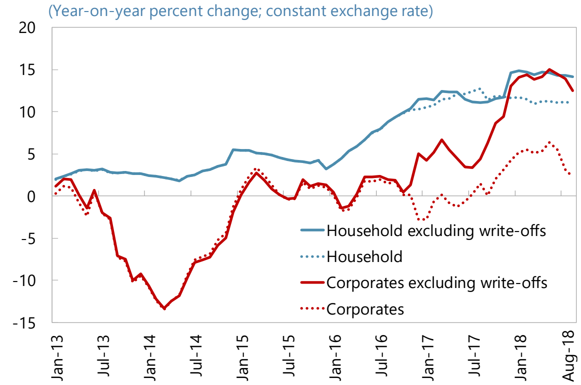


Sources: SORS; and IMF staff calculations and projections.

2. Headline inflation has slowed, while core inflation remains low and stable at around 1 percent. CPI inflation decelerated to 2.2 percent yoy in October mainly due to food prices. The NBS has kept its main policy interest rate at 3 percent since April, citing uncertainty in international financial markets. Lending interest rates continue to decline (albeit gradually) and credit growth is strengthening due to greater risk appetite of banks, increased banking sector competition, and the positive economic outlook. However, credit dinarization has stalled as corporates continue to rely on forex borrowing.

Credit Growth

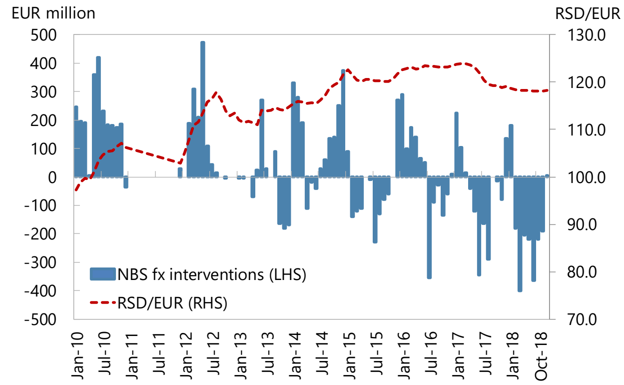
(Year-on-year percent change; constant exchange rate)



Sources: National Bank of Serbia.

3. The external position remains sustainable on account of robust FDI and other capital inflows. Although the current account deficit is projected to remain broadly unchanged at 5¼ percent of GDP this year, the trade deficit is expected to widen by 1½ percent of GDP due to strong import growth. The increase in imports continues to be driven by investments in the industrial and construction sectors and also reflects higher fuel prices and US dollar appreciation. Exports of intermediate goods and agricultural products are increasing compared to 2017, but not enough to offset strong imports. Vulnerabilities associated with the high deficit are partly mitigated by the favorable import composition, mainly tilted towards capital imports, and the fact that the current account remains fully financed by non-debt-generating inflows. Private and total external debt will remain flat in 2018. Exchange rate appreciation pressures eased beginning in 2018Q3 and more recently the NBS has occasionally sold foreign exchange. However, in net terms the NBS has purchased more than EUR1.5 billion foreign exchange from the market since January.

NBS FX interventions and exchange rate movement



Sources: NBS; IMF staff calculations.

4. **Strong fiscal performance continued in the first nine months of 2018.** The general government registered an overall surplus of about 1.1 percent of GDP in January-September, outperforming the program target (after adjustors) by RSD 5.6 billion. Tax revenues grew in line with nominal GDP, while large one-off dividend payments and receipts from securities issued at a premium boosted non-tax revenues. On the expenditure side, investment execution increased by around 60 percent yoy, and is projected to remain strong until year-end. Current spending, including mandatory spending on wages and pensions, grew in line with projections. General government debt fell below 57 percent of GDP at end-September. Despite volatility in many EMs, yields on government securities remain near all-time lows.

Serbia: General Government Fiscal Operations, RSD billion

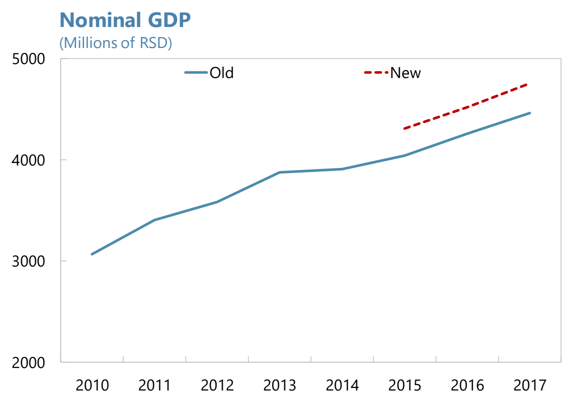
	January - September 2018		
	Prog.	Act.	Diff.
Total revenue	**1,511.7**	**1,537.6**	**25.9**
Tax revenue	1,333.2	1,341.7	8.5
of which: VAT	362.5	375.6	13.1
of which: Social security contributions	446.9	449.7	2.8
of which: Excises	222.0	210.6	-11.4
Non-tax revenue	168.5	190.2	21.7
Capital revenue	0.0	0.0	-
Grants	8.6	5.7	-2.9
Total expenditure	**1,480.4**	**1,483.1**	**2.7**
Current expenditure	1,347.9	1,338.8	-9.1
Capital expenditure	112.4	122.5	10.1
Net lending	8.2	6.2	-2.0
Amortization of activated guarantees	11.9	15.6	3.7
Fiscal balance	**31.3**	**54.5**	**23.2**
Memo:			
Wage bill	349.4	349.2	-0.1
Primary current expenditure of the Republican budget	648.7	639.8	-9.0
General government debt (percent of GDP)	57.5	56.7	-0.8

Sources: Ministry of Finance, IMF staff calculations.

Box 1. Revisions to National Accounts

The Statistical Office of the Republic of Serbia (SORS) published the revised annual estimates of GDP for the period 2015–2017 in October. This constitutes the first phase[1] of a multi-year project to enhance the national accounts compilation process and reflects improvements required for producing more robust and accurate GDP estimates. These improvements include better coverage of the grey economy[2] and the agricultural sector, the use of improved data sources for mining and energy production, as well as reclassification of certain institutional units. The new GDP calculation is also a step towards aligning the system of national accounts with the European System of Accounts (ESA 2010) and is consistent with recommendations from the IMF Statistics Department and other technical assistance providers.

Notable revisions include changes in the level of nominal GDP and in contributions to real growth. Preliminary results show that the revised GDP over 2015–2017 is about 6 percent higher in nominal terms relative to the old GDP series.[3] Around half of this increase is attributable to better coverage of the grey economy in GDP calculations. The real GDP growth rate in 2016 is about ½ percentage point higher relative to the old estimates, driven by larger contributions of consumption and gross fixed capital formation, as well as a lower contribution of imports to GDP. Real GDP in 2017 is almost unchanged relative to old estimates, although there are significant differences in the contributions to GDP, specifically from government consumption, gross fixed capital formation, and imports.



Source: Statistical Office of the Republic of Serbia (SORS)

Growth composition
(percent)

	New 2016	New 2017	Old 2016	Old 2017
Real GDP growth	**3.3**	**2.0**	**2.8**	**1.9**
Contributions to GDP				
Consumption	1.2	2.2	0.8	1.9
Government	2.5	3.7	2.3	1.0
Gross fixed capital formation	5.4	7.3	5.2	5.9
Exports of goods and services	11.9	8.2	12.1	9.9
Imports of goods and services	6.7	11.1	9.0	10.8

Sources: SORS, staff calculations

[1] Subsequent phases include producing quarterly GDP estimates along with backdated estimates up to 2005 (published in November), as well as the compilation of definitive GDP for 2015-2017 under a supply and use framework.
[2] The revised GDP estimates include for the first time estimates of sales of small-sized and micro enterprises and the value of production of self-employed persons.
[3] This data revision affects key macroeconomic ratios to GDP, including the debt to GDP ratio which is now lower.

PROGRAM PERFORMANCE

5. **The program is broadly on track (PS Tables 1-2).** The authorities reiterated their commitments to all program objectives and targets.

- **End-September Quantitative Targets (QTs) were observed, excepting a minor deviation in the QT on domestic arrears.** The September fiscal deficit ceiling for the general government was met as well as the ceiling on current primary expenditure of the Republican budget. While inflation remains below the NBS target, it was within the lower band limit of the inflation consultation clause. The end-September QT on the ceiling on accumulation of domestic arrears by the consolidated general government was missed by a slight margin due to arrears of the Ministry of Justice.

- **Most Reform Targets (RTs) have been implemented, albeit with some delays.** The government submitted the draft Law on Charges to parliament in November (**end-October RT**) and also adopted amendments to the Law on Inspection Supervision in December (**end-September RT**). However, the authorities have not adopted a decree specifying the wage coefficients under the new public wage system (**end-September RT**) due to concerns about domestic political reception. Further, the authorities did not adopt a government decision to launch a privatization tender for Petrohemija (**end-September RT**) but continue to discuss parameters with potential buyers and intend to launch the privatization tender by end-February 2019.

- **The authorities have made good progress in the RTs for end-December.** In October the authorities launched the first phase of the tender for the sale of a EUR240 million portfolio of bad assets held by the Deposit Insurance Agency (DIA); the NBS completed a draft update of their Dinarization Strategy; and amendments to the Law on Public Debt were submitted to Parliament in November.

OUTLOOK AND RISKS

6. The economic outlook remains positive, supported by the continued reform momentum (Tables 1-8).

- **Real GDP growth** is projected at 4.2 percent in 2018 (partly reflecting a rebound from the effects of drought in 2017) and 3½ percent in 2019 due to base effect, with the output gap closed in 2018. Taking into account the baseline macro-policy settings, growth is projected to strengthen modestly to 4 percent over the medium term, with the output gap remaining closed. Structural reforms envisaged under the PCI represent an upside risk to medium-term potential growth.

- **Inflation** is projected to gradually increase, but remain in the lower half of the inflation target band during 2018 and 2019.

- **The current account deficit** is expected to remain at about 5¼ percent of GDP in 2018 due to investment-related imports in the manufacturing and construction sectors, and to decline to around 4¼ percent of GDP over the medium term.

7. Risks are broadly balanced. While the outlook is positive under the baseline, Serbia remains susceptible to spillovers from regional and global developments and market volatility, including potential increased risk aversion for emerging markets (EMs). To date, Serbia has remained insulated from turbulence in EMs. Complacency or political resistance in delivery on structural reforms, or failure to maintain fiscal discipline, could undermine confidence and reduce medium-term growth prospects. Failure to decisively address AML/CFT weaknesses identified by FATF could undermine Serbia's investment attractiveness. Moreover, contingent liabilities stemming from unfinished reforms of state-owned enterprises (SOEs) and banks could arise. On the upside, growth could again outperform projections if structural reforms succeed in rapidly improving the business environment or FDI raises export growth further.

PROGRAM POLICY DISCUSSIONS

A. Fiscal Policy: Advancing the Pro-Growth Fiscal Agenda

8. The general government is projected to post a fiscal surplus of 0.5 percent of GDP in 2018, consistent with the program request. While the overall execution is in line with expectations, the composition has changed to reflect developments through September, with non-tax revenues projected higher by (0.4 percent of GDP) due to one-off receipts and capital spending revised up (0.5 percent of GDP) to account for faster execution through September. Pension spending is expected to be broadly stable, as savings will offset increases introduced in November resulting from the unwinding of the crisis-era pension cuts and modest pension bonuses paid in December.[1] Public debt will end 2018 at around 54 percent of GDP, with an improved maturity profile and currency composition.

Summary Table on General Government Borrowing (RSD billion)

	2018 Original	2018 Proj.	2019 Proj.
Financing needs	457	423	416
Use of financing			
Budget	400	357	373
Project	57	66	43
Financing sources			
Short-term	22	21	0
Medium-long term	435	402	416
Deposits	0	0	0
Memo: Issuance of guarantees (EUR mn)	180	107	261

9. The 2019 budget targets a small deficit of around 0.5 percent of GDP, consistent with PCI objectives (prior action). The budget keeps the wage and pension bills constant as shares of GDP, provides space for increasing capital investment, and includes policy initiatives aimed at spurring medium-term growth while continuing the downward trajectory of public debt.[2] These include:

[1] The December IT on the overall budget deficit is revised to reflect the effects of changes in revenue composition on the adjustors, even though the headline deficit projection is improved.

[2] The 2019 budget implies a fiscal impulse of about 1 percent of GDP.

- **Labor taxation.** The employers' part of the unemployment contribution will be eliminated resulting in a ¾ percent reduction of the labor tax wedge, with a net cost of about 0.2 percent of GDP.

- **R&D and innovation.** A package of measures will be introduced to promote innovation and R&D. Staff called for the inclusion of sunset clauses and reporting tax expenditures in the budget.

- **Parafiscal charges.** The consolidation of charges and fees will increase predictability and transparency, while also generating some savings for businesses. In this regard, the draft Law on Charges was submitted to the National Assembly in November (**end-October RT**) and was approved with the budget.

10. The authorities are advancing preparations for fiscal measures agreed under the program, although some implementation delays have emerged.

- **Public wage system reform.** Despite completing consultations between the government and public sector unions regarding wage coefficients in October, the authorities reported that they were not ready to implement the new wage system as originally scheduled for January 1, 2019. The authorities stated that they intend to pass the decree specifying wage coefficients (**end-September RT**) in time for the preparation of the 2020 budget. As a result, wage increases for 2019 will be granted on a sectoral basis, while keeping the general government wage bill constant as a share of GDP.

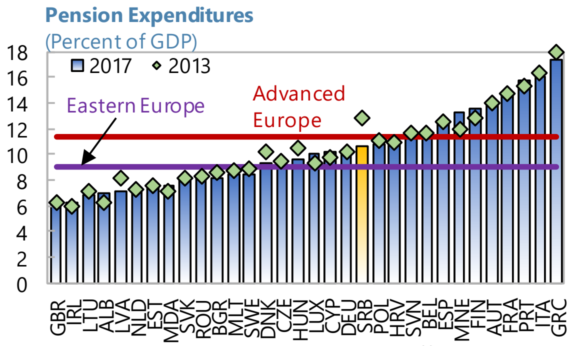
- **Public employment framework.** The authorities and staff discussed plans to replace the existing rigid employment framework with a more flexible system while containing fiscal pressures from the wage bill. The authorities agreed to adopt a decision on a new public employment framework for 2020 (**new end-September 2019 RT**).

- **Pensions.** Staff supported the authorities' decision to unwind the crisis-era temporary cuts to pensions and agreed to supplements for pensions below RSD34,000/ month, while ensuring that total pension spending does not rise relative to GDP. The authorities plan to reintroduce pension indexation for 2020 onwards, to ensure a more rules-based system (Box 2).

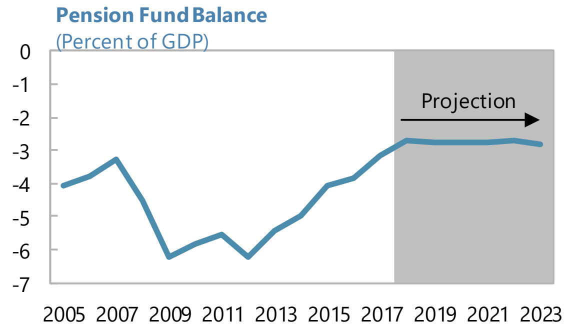
- **Review of direct taxes.** During 2019, the authorities aim to review the rates and structure of the direct taxation system, with the aim to increase progressivity, lower the tax wedge, and streamline intergovernmental fiscal relations, as well as to rationalize the presumptive tax system. Staff suggest the presumptive tax regime, which presents opportunities for tax avoidance and undue competitive advantage in certain sectors, should be limited to micro and small traders, the basis for taxation should be taxpayers' self-declared turnover, and that the administrative burden on the tax administration (STA) should be minimized.

Box 2. Pension Reform: Important Progress, but Continued Commitment Needed

Serbia's pension spending had been among the highest in Europe until recently. From 2005 to 2015 pension spending averaged 13 percent of GDP and generated sizeable deficits in the pension fund. High pension expenditures were driven by low statutory retirement ages and extensive general and occupational early retirement options, as well as demographic patterns.



Sources: IMF pension database; and IMF staff calculations.



Sources: MOF and IMF staff calculations.

Since 2014, a series of reforms to pension expenditures addressed some systemic issues. The government introduced temporary cuts of 22 percent to pensions above RSD 25,000, and 25 percent for those above RSD 40,000.[1] While these cuts did not affect the bulk of low-earning pensioners, pension income was reduced for about 40 percent of pensioners. Amendments to the 2014 Budget System Law legislated other parametric reforms, including the suspension of the indexation of pensions, the introduction of early retirement penalties, the gradual unification of retirement age for men and women, and changes to hardship, disability and survivor pensions. As a result, the pension fund deficit declined, and pension spending stabilized at around 10½ percent of GDP.

Underpinned by stronger fiscal and macroeconomic fundamentals, the government has unwound the temporary pension cuts. To allow an increase also in lower pensions, the government introduced a 5 percent supplement for pensions below RSD 34,000.[2] Based on staff estimates, this would help to redistribute a share of the overall pension bill towards the poorest pensioners. However, the proposed solution weakens the contribution-benefit links for lower pensions and poses the risk of arbitrary or targeted pension hikes in the future.

The long-term sustainability of the pension system depends upon continued commitment to containing pension increases and further reforms. The authorities plan to reintroduce indexation rules during 2019. To guarantee the long-term sustainability of the pension system, additional comprehensive parametric reforms need to be introduced (e.g., linking statutory retirement age to life expectancy, revising systems of "hardship" pensions and survivor benefits), and underlying revenue-side issues need to be addressed (e.g., increase labor force participation and employment rates, suppress underreporting of contribution-liable earnings).

[1] The "Law on Temporary Provisions for the Administration of Pension Payments" was part of a broader fiscal consolidation package adopted by the government at the onset of the 2015-18 IMF-supported SBA program.
[2] Under the proposal, this will be made possible by introducing a provision allowing for supplementary increases to the Pension Law, to be determined on an annual basis but capped at 0.3 percent of GDP.

11. In addition, the authorities reiterated their commitment to tax administration reform.

- **A working group (WG) to oversee reform implementation has been created comprising the MOF, STA, and other key stakeholders, and is meeting regularly to accelerate the pace of reform.** A consultant has been hired to assist the STA in producing a roadmap for the separation of core and non-core activities and additional support to manage the project implementation is expected by end-2018. The authorities also intend to prioritize the decision of a new IT system, by end-2018.

- **The authorities reported shorter VAT refund processing time.** STA committed to take additional measures to expedite refunds once VAT-management software modifications take effect in October. A new e-inspection software, supported by the EBRD, will be phased in to support audit and inspection activities. It was agreed to continue to monitor refund processing.

12. Despite improvements in capital spending execution in 2018, strengthening public investment management frameworks remains a priority. Spending execution has improved as backlogs have been reduced and more effective oversight introduced. As a result, investment is expected to remain strong in 2019. The authorities and staff agreed that strengthening public investment management (PIM) frameworks remains crucial for sustained progress in capital budget execution and to meet Serbia's large development needs. The EU has committed to technical assistance, focusing on project planning and assessment.

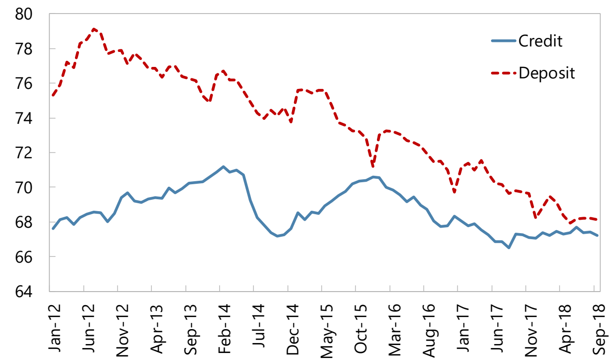
B. Monetary Policy: Strengthening Operational Frameworks

13. The current stance of monetary policy remains appropriate considering the domestic and external environment. Domestic and international inflationary pressures are low, and inflation expectations remain well-anchored. No upward pressure is expected from administered energy prices, after the authorities left electricity tariffs unchanged, while the minimum wage increase is expected to have a limited impact. The NBS and staff concurred that the strengthening of private sector credit growth was welcome, but recognized that risks associated with rising household cash loans—especially over longer maturities and variable interest rates—warrant close monitoring. The NBS noted that they were monitoring the situation and in October announced plans to limit retail lending over 5-year maturities and FX-indexed loans.

14. The authorities are strengthening their liquidity management framework to enhance the inflation targeting regime. The authorities agreed to (i) formalize communication between the NBS and MOF through a Service Level Agreement concerning single treasury account management and information provision; and (ii) establish a joint Consultative Committee on Liquidity Management aimed at strengthening the management and oversight of the Consolidated Treasury Account balance and improving the quality of liquidity forecasting.

15. The authorities' dinarization strategy is gradually yielding results, but further efforts are needed to mitigate entrenched fears of greater exchange rate volatility. While deposit dinarization is rising (31.9 percent in September), dinarization of credit has stalled since September 2017, due to increased forex borrowing by corporates and write-offs of dinar receivables. Dinar movement vis-à-vis the euro for the 12-months to October was less than 1 percent and has been classified by the IMF as a *de facto* crawl-like arrangement. The authorities plan to:

Deposit and credit euroization
(Percent)



Sources: NBS; IMF staff calculations.

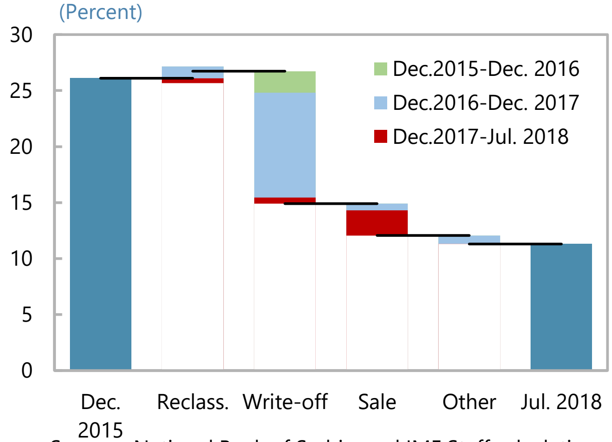
- **Update the dinarization strategy** (**end-December RT**). In this context staff recommend gradually moving to neutral liquidity conditions with short-term rates anchored around the key policy rate, strengthened monitoring of banks' FX exposures, fuller dissemination of information on risks of FX borrowing, and use of prudential measures to contain risks of unhedged FX borrowing, as well as allowing greater two-way exchange rate flexibility with interventions limited to smoothing excessive volatility. The NBS generally concurred with these priorities, but noted that relative exchange rate stability was important, especially with growing international market uncertainty, while reiterating that they do not target a specific exchange rate level. The NBS also introduced of a new instant payments system in October, which should encourage greater use of dinar mobile payments.

- **Strengthen public debt management.** In early-December Parliament approved amendments updating the legal foundation of debt management (**end-December RT**). The authorities will also: (i) establish the primary dealer system and develop adequate supervisory framework; and (ii) improve the Public Debt Agency's (PDA) operational framework and create a Debt Market Committee comprised of representatives of the PDA and MOF.

C. Financial Sector Policies: Enhancing Resilience

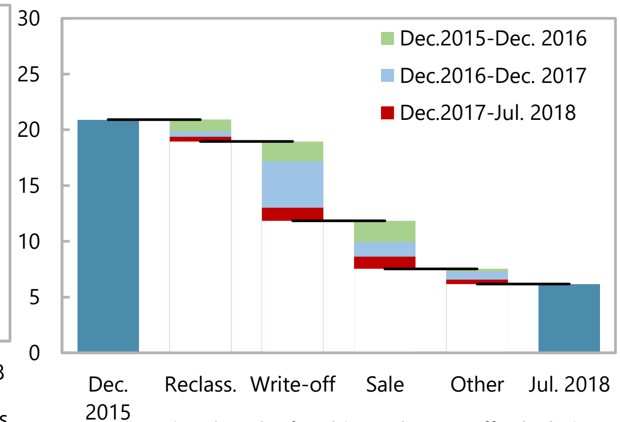
16. NPLs have fallen below 2008 levels to reach 6.4 percent in September 2018, but state-owned banks (SOBs) still lag. In private banks, significant NPL sales and mandatory write-offs helped lower NPLs to about 6 percent in September, below pre-crisis levels. The gross NPL ratio for SOBs has also decreased mainly due to write-offs, in addition to one significant sale, but it remains relatively high at 10.5 percent as of September. The authorities are currently updating their NPL resolution strategy, with the support of IFIs, focusing on measures to speed up NPL resolution in SOBs, while also broadening the scope to include the Development Fund (DF), export credit agency (AOFI), and assets managed by the DIA. This focus will help strengthen public financial institutions and reduce fiscal risks. In line with the strategy, the government and DIA will approve a time-bound action plan to resolve the higher-value parts of the DIA's portfolio of bad assets by end-2020 through a tendering process and will complete the first phase of the sale (**end-December RT**). The action plan will also include options to resolve the residual portfolio of relatively low-valued assets. The authorities launched the tender process for the first phase of assets sale in October, with bids due by December 7. They have also committed to issue tenders for the second phase of the assets sale (**new end-September 2019 RT**).

Change in Gross NPL Ratio, State-Owned Banks
(Percent)



Sources: National Bank of Serbia; and IMF Staff calculations.

Change in Gross NPL Ratio, Private Banks
(Percent)



Sources: National Bank of Serbia; and IMF Staff calculations.

17. Implementation of the state-owned financial institutions reform agenda is progressing, albeit unevenly:

- ***Komercijalna Bank.*** The authorities confirmed their intent to move ahead with the bank privatization process expeditiously, notwithstanding the expected exit of EBRD, IFC and other IFIs as shareholders in January. In October the authorities launched a tender to hire a privatization advisor for the bank. They will adopt a decision to initiate the privatization of the bank by end-February 2019, with a view to launch a privatization tender by end-June 2019 (**RT**) and complete the sale by end-2019.

- ***Banka Poštanska Štedionica (BPS).*** The bank decided to move forward with the implementation of its business plan and procurement of a new core banking system without the initially agreed assistance of the World Bank. As a result, BPS launched a public tender to acquire a new core IT banking system in September and signed the contract with the selected bidder in November. Staff urged the procurement and implementation of the IT system to be conducted in accordance with good practices and high-quality standards. Staff also urged the authorities to proceed quickly in the implementation of the bank's business plan (developed with the help of external consultants) and oversee its proper execution.

- ***Smaller state-owned banks.*** The implementation of the government strategy for smaller SOBs is moving ahead, but with some delays. The state shares in Jubmes Bank have been put up for sale and the transaction is due to be completed in 2019H1. However, the process to transform another SOB into a specialized financial institution is still facing delays.

18. Financial safety nets are being further strengthened. In October the DIA underwent an independent assessment of its compliance with the IADI core principles for effective deposit insurance systems. Once the assessment is finalized, the DIA and authorities will develop an action plan to implement its key recommendations. With World Bank support, the authorities will also review the parameters of the deposit insurance framework (including the target level, premium, and deposit base) based on good international practices. The findings of the assessment and the review will serve as inputs to amend the laws on Deposit Insurance Agency and on deposit insurance and introduce risk-based deposit insurance premia (**end-June 2019 RT**).

19. The authorities are making progress in addressing the deficiencies in the AML/CFT framework. Following the grey-listing of Serbia by FATF in February, the authorities have been addressing the shortcomings identified in the 2016 MONEYVAL AML/CFT mutual evaluation report through an inter-agency WG, with the aim to complete their work ahead of the January 2019 deadline agreed with FATF. Several laws, regulations, and guidelines addressing specific recommendations in the MONEYVAL report have been adopted, including on politically exposed persons, public notaries, correspondent banking, beneficial ownership, supervision of groups and foreign branches, and sanctioning regimes. The authorities expressed their commitment to fully implement Serbia's action plan to address the significant AML/CFT weaknesses identified by FATF (**end-February 2019 RT**).

D. Structural Policies: Improving the Business Climate

20. The authorities are moving forward with the reform of large public enterprises.

- **Strategic companies of the former Privatization Agency (PA) portfolio.** Since program approval the authorities reported significant progress, resolving 2 of the remaining 7 strategic companies in the former PA portfolio. The public tender for a strategic partner for copper mine RTB Bor was successful and the transaction will be completed by year-end. The privatization tender for dairy firm PKB was also successfully concluded and will be completed by year-end. However, the chemical company MSK failed to sell in the second offer and a third and final round will only be launched after exploring options with potential strategic investors. The authorities have not yet launched the privatization tender for Petrohemija (**end-September RT, proposed to be reset to end-February 2019**) but are continuing discussions with potential investors and plan to launch the tender by end-February 2019. The authorities committed to closely monitor the companies and not permit any accumulation of arrears.

- **Elektroprivreda Srbije (EPS).** The authorities, supported by the World Bank and EBRD, are working to enhance corporate governance, management, and procurement and planning frameworks of the national power utility. A time-bound action plan to improve management will be adopted by end-December. The authorities are committed to change the legal status of EPS to a joint stock company in 2020 and as an interim step in 2019 will adopt a government decision to establish ownership rights of all property and assets.

- **Srbijagas.** The authorities plan to adopt a capital expenditure plan in line with their new investment appraisal methodology by end-2018. Staff urged the authorities to phase out reliance on government support for debt servicing given Srbijagas' improved financial position.

- **Strategy for SOEs.** The authorities and staff agreed that developing an ownership and governance strategy for SOEs would complement on-going efforts to reduce and monitor fiscal risks and improve efficiency. The strategy, to be developed during 2019, would provide an integrated approach to oversight and monitoring of SOE operations, financial consolidation, restructuring or divestment for some strategic SOEs, and measures to improve governance and the institutional framework.

21. Reducing the footprint of the informal economy and improving the labor market are two priorities to raise growth prospects. The authorities identified three priority areas to combat the grey economy: (i) comprehensive transformation of the STA, including organization streamlining and capacity development; (ii) increased use of electronic fiscal services, facilitated by improved software utilized by the STA; and (iii) tightening the legal framework to prevent abuse of special tax regimes, in particular presumptive taxation. Staff saw scope to implement some measures in 2019 and urged the authorities to consider: (i) automatization of tax calculations (including presumptive taxes); (ii) issuance of electronic certificates for paid taxes and consolidation of tax debts; and (iii) digitalization of vehicle transfer taxes. Parliament adopted amendments to the Law on Inspection Supervision (**end-September RT**) in December to permit supervision of unregistered activities as well as improve coordination across inspections. The authorities have aligned all sectoral laws and plan to rollout the e-inspector electronic system to improve coordination across inspections. The authorities will also adopt the Law on Work Through Temporary Employment Agencies to eliminate unfair competition and support employment by end-2018.

PROGRAM MODALITIES

22. The program will continue to be monitored on a semi-annual basis. Serbia does not need the Fund's financial assistance under the baseline and is not seeking financial assistance from the Fund as the program is fully financed. Reviews are set out in Table 9. QTs for the key set of macroeconomic variables monitored under the PCI are set out in PS Table 1. RTs are reflected in PS Table 2, which aim to support the authorities' structural reform agenda in the areas of public financial management, tax administration, financial sector, and business environment.

23. Program conditionality is to be updated (PS Tables 1-2):

- One prior action is set for the completion of the first review: passage of the 2019 budget consistent with program objectives.

- Fiscal QTs for end-March 2019 are proposed to be modified and QTs for end-September 2019 are proposed, in line with the 2019 budget. The ceiling on the accumulation of domestic payment arrears is proposed at a de minimis level to accommodate very small, temporary deviations. The inflation consultation band has been re-centered to reflect changes in inflation projections.

- The end-September RT on the government decision to launch a privatization tender for Petrohemija is proposed to be reset for end-February 2019 to allow more time to discuss parameters with potential buyers.

- The following new RTs are being proposed: (i) adoption of a government decision on a new public employment framework for 2020 to improve employment flexibility while containing fiscal pressures; and (ii) issuance of tenders for the second phase of DIA asset sales, in line with the time-bound action plan.

24. Serbia has small sovereign arrears outstanding. It intends to resolve US$45 million in arrears to Libya, which arose in 1981 due to unsettled government obligations related to a loan for importing crude oil, after establishing the appropriate government counterpart. Staff urged the authorities to continue their efforts to resolve these arrears as soon as possible.

STAFF APPRAISAL

25. The authorities' program, supported by the PCI, is advancing. The hard-won macroeconomic improvement achieved under the previous program is maintained, with inflation within the target range, responsible fiscal policy producing rapidly falling public debt, and a current account deficit fully covered by FDI. The results supported the strong rebound in growth in 2018, broad-based investment growth, rising employment, financial sector soundness, lower interest rates and gradually rising use of the dinar.

26. The 2019 budget maintains the effort to reduce public debt while contributing to growth and unwinding crisis measures. The general government deficit target of 0.5 percent of GDP will bring public debt towards 50 percent of GDP by end-2019, continuing the impressive turnaround since the start of the last program. Increased infrastructure spending—coupled with improvements in public investment management—and reducing the tax burden on labor will help raise growth and employment. Unwinding the temporary cuts in pensions and public enterprise wages instituted in 2014 are also important normalization measures which reduce fiscal and legal risks.

27. Monetary and financial policies continue to support growth. Careful monetary policy implementation has contributed to confidence and growth. However, the recent IMF reclassification of the *de facto* exchange rate regime underscores staff's longstanding advice to gradually accustom the population and market participants to greater short-term fluctuation in the exchange rate.

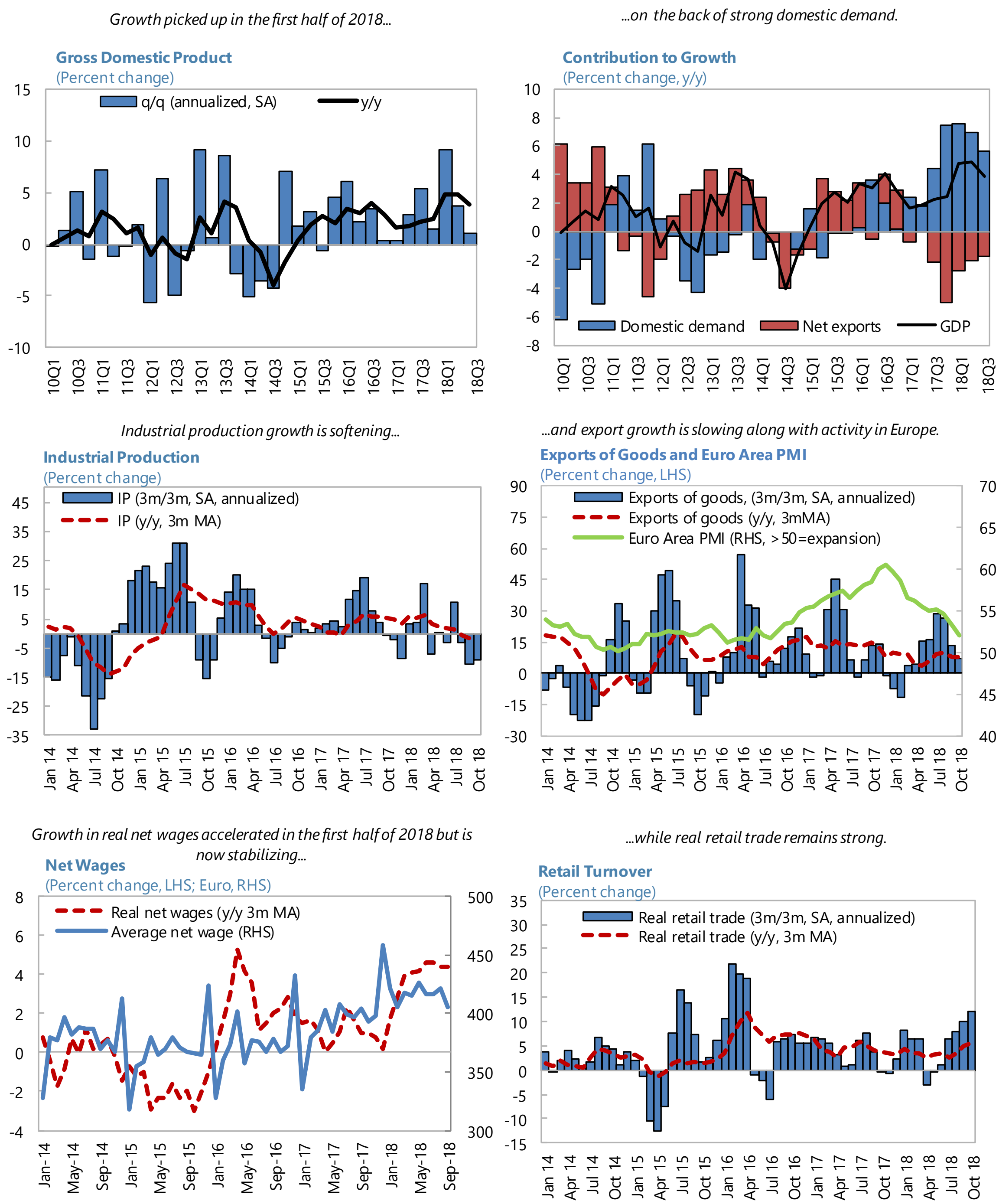
28. **Reforms of state-owned financial institutions are essential to improve efficiency and strengthen confidence and need to be implemented vigorously**. Given the notable progress in addressing NPLs especially in private banks, the program focuses on public institutions. Ensuring the DIA meets international standards will strengthen confidence and allow for a reduction in the burden of insurance premia on banks and their customers. Preparations for the privatization of Komercijalna Banka need to continue to ensure the successful sale of a controlling majority stake during 2019, while ensuring governance standards are maintained following the exit of IFIs as shareholders in January.

29. **Structural reforms are advancing, albeit unevenly**. Resolution of problem SOEs is progressing, helping increase efficiency and decrease fiscal risks. The new momentum in the tax administration reforms will be critical for strengthening collections and improving the business climate. However, the decision not to go forward with the wage system reform at this point is unfortunate and contrary to program understandings, and will delay the needed rationalization of public sector pay, including the catching-up of underpaid groups such as medical professionals and teachers. Determined efforts to reduce the grey economy and strengthen the business climate will be critical to Serbia's long-term growth and future competitiveness within the EU.

30. **Governance issues remain the Achilles heel of the Serbian economy**. Weaknesses in the judicial system stand out in surveys of the business environment, as well in as official-sector assessments. The authorities are working hard to implement the action plan agreed with the FATF to address identified shortcomings in the AML/CFT framework and its implementation. Improved transparency in public investment management, including for "government-to-government" contracts, full implementation of the tax administration reforms, and ensuring an open and competitive privatization process for Komercijalna Banka, will also be key indicators of the government's intent in this area. Broader governance reform of the state-owned sector would be a major step in achieving a level playing field for business, improving efficiency of public resource use and managing fiscal risks. Improved governance will also help advance the EU accession agenda.

31. **Staff supports the completion of the first review under the Policy Coordination Instrument.**

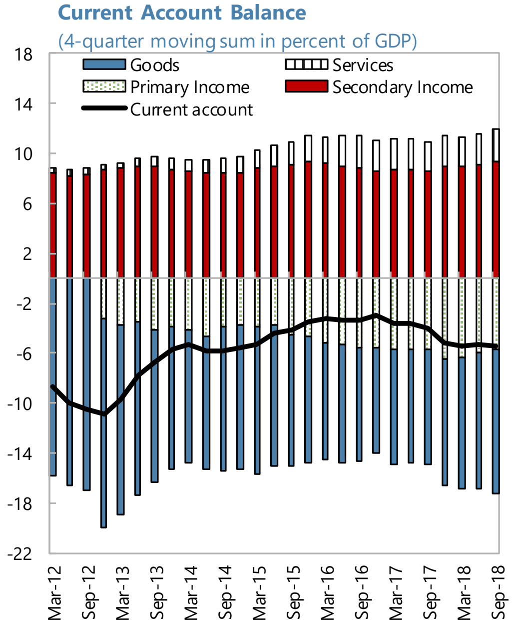
Figure 1. Serbia: Real Sector Developments, 2010–18



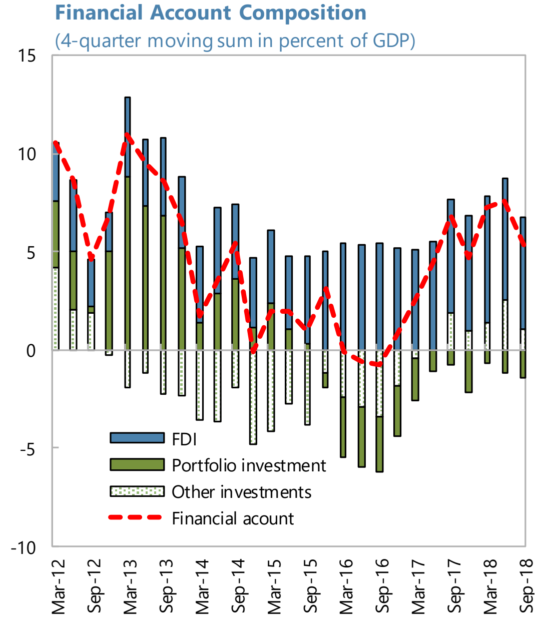
Sources: Haver analytics, SORS; and IMF staff calculations.

Figure 2. Serbia: Balance of Payments and NIR, 2012–18 1/

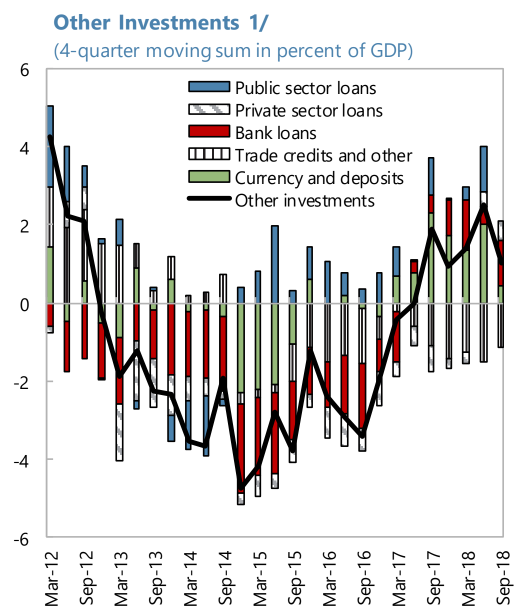
The current account deficit has stabilized…



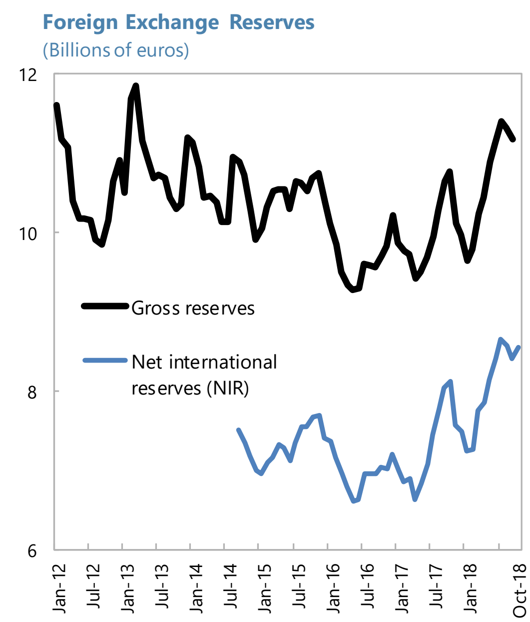
…and remains fully covered by FDI inflows.



Outflows in other investments continue to be driven by trade credits and private sector loans.



International reserves remain at comfortable levels.

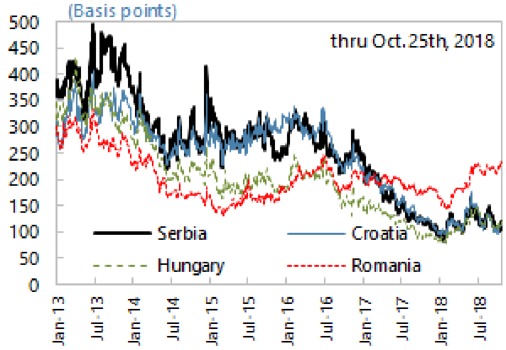


Sources: Haver; and IMF staff calculations.
1/ BPM5 data spliced with BPM6 going forward starting March 2013.

Figure 3. Serbia: Recent Financial and Exchange Rate Developments, 2013–18

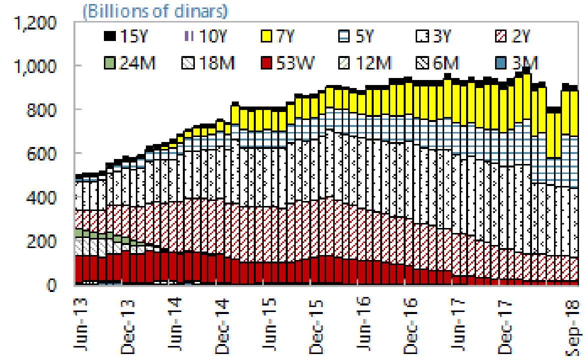
EMBI spreads remain near historic lows.

Sovereign Risk -EMBI spreads
(Basis points)



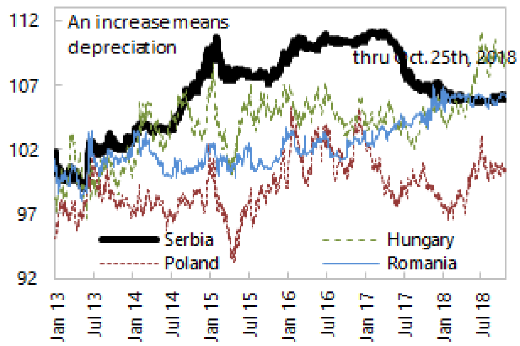
The authorities continue to lengthen the maturity of domestic securities.

T-Bill & T-Bond Stock 1/
(Billions of dinars)



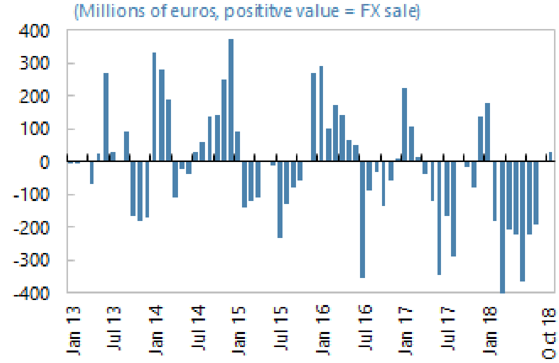
Exchange rate appreciation pressures eased...

Exchange Rates in the Region
(Index, end-May 2013=100)



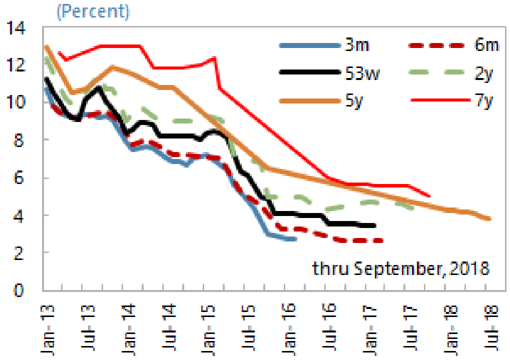
...and more recently the NBS has occasionally sold foreign exchange.

FX Interventions by NBS
(Millions of euros, positive value = FX sale)



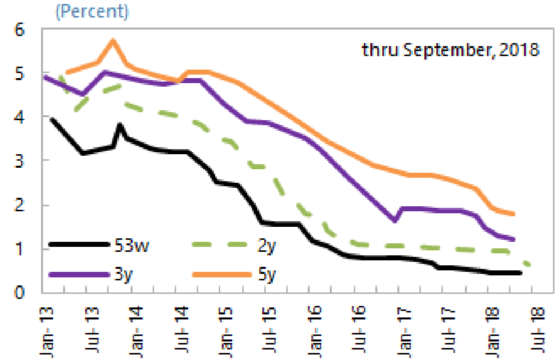
Yields in dinar denominated securities are near recent lows...

Yields on Dinar-Denominated Domestic Securities
(Percent)



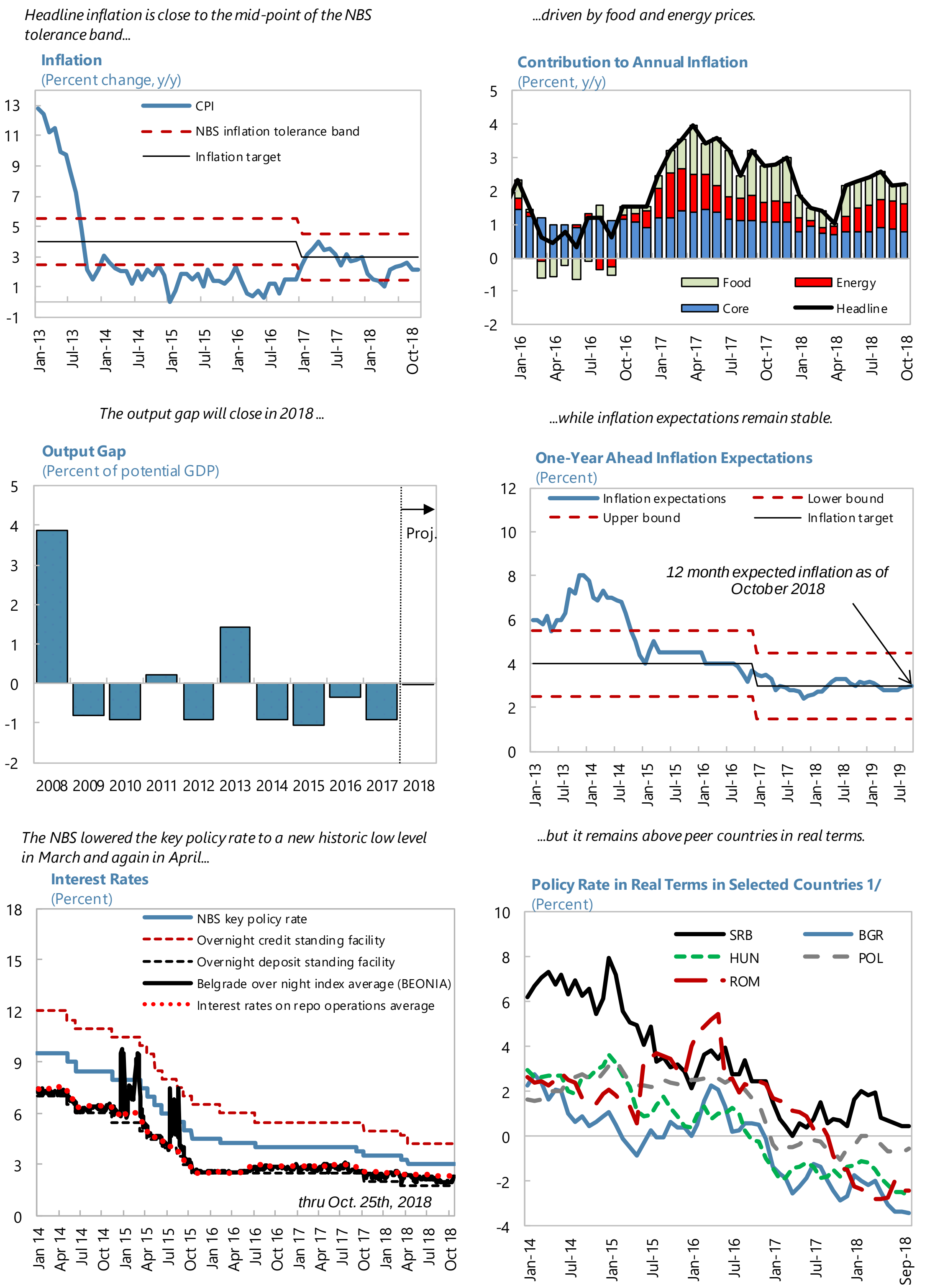
...as well as in euro-denominated securities.

Yields on Euro-Denominated Domestic Securities
(Percent)



Sources: Serbian Authorities; Bloomberg; and Haver.
1/ Sum of dinar and FX-denominated securities at current exchange rate.

Figure 4. Serbia: Inflation and Monetary Policy, 2013–18

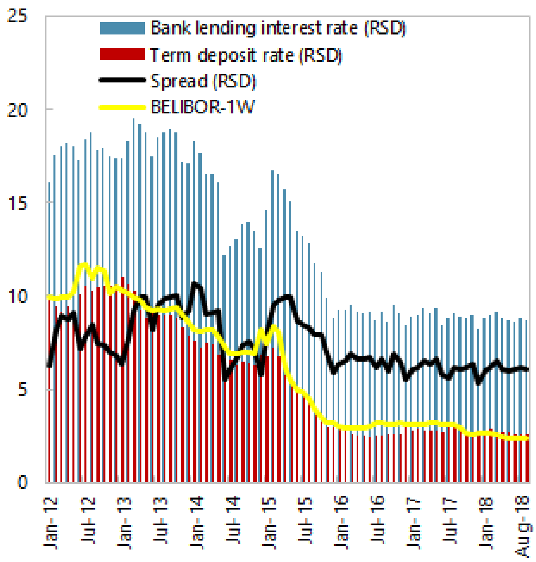


Sources: Haver; Bloomberg; National Bank of Serbia (NBS); SORS; and IMF staff estimates and projections.
1/ Nominal policy rate adjusted by inflation over the past 12 months.

Figure 5. Serbia: Selected Interest Rates, 2012–18

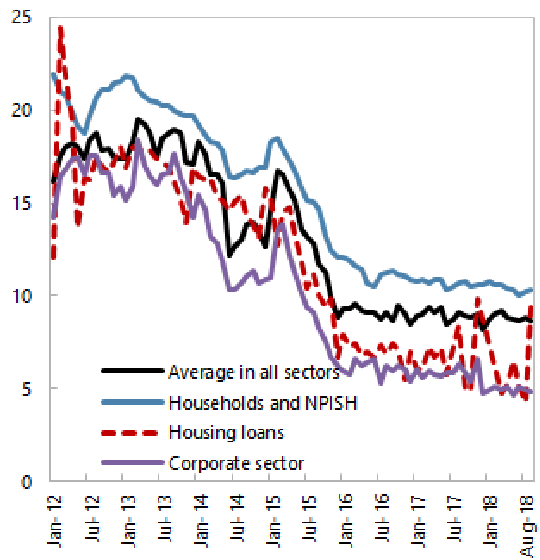
Easing of monetary policy has led to a decline in dinar interest rates...

Selected interest rates (RSD)
(Percent)



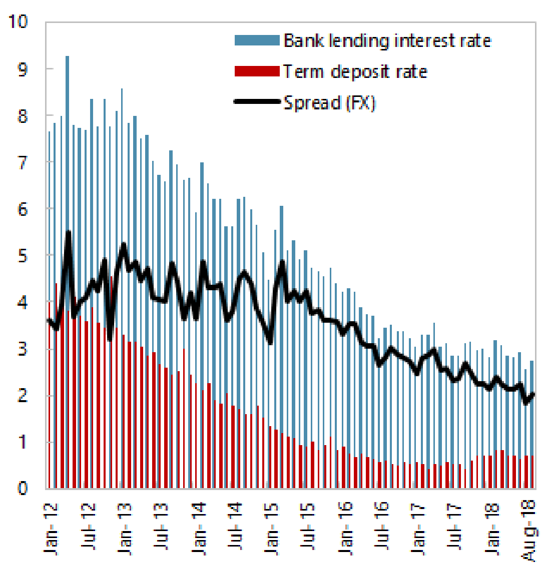
...in both corporate and household markets.

Bank lending interest rates: RSD
(Percent)



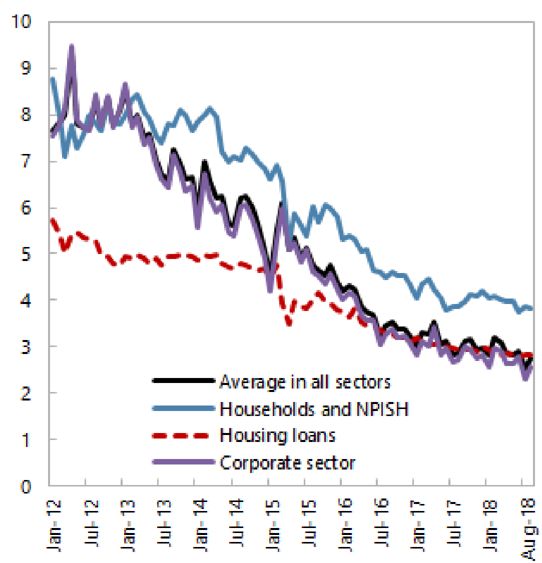
FX (or FX-linked) interest rates have been declining, too...

Selected interest rates (FX and FX-linked)
(Percent)



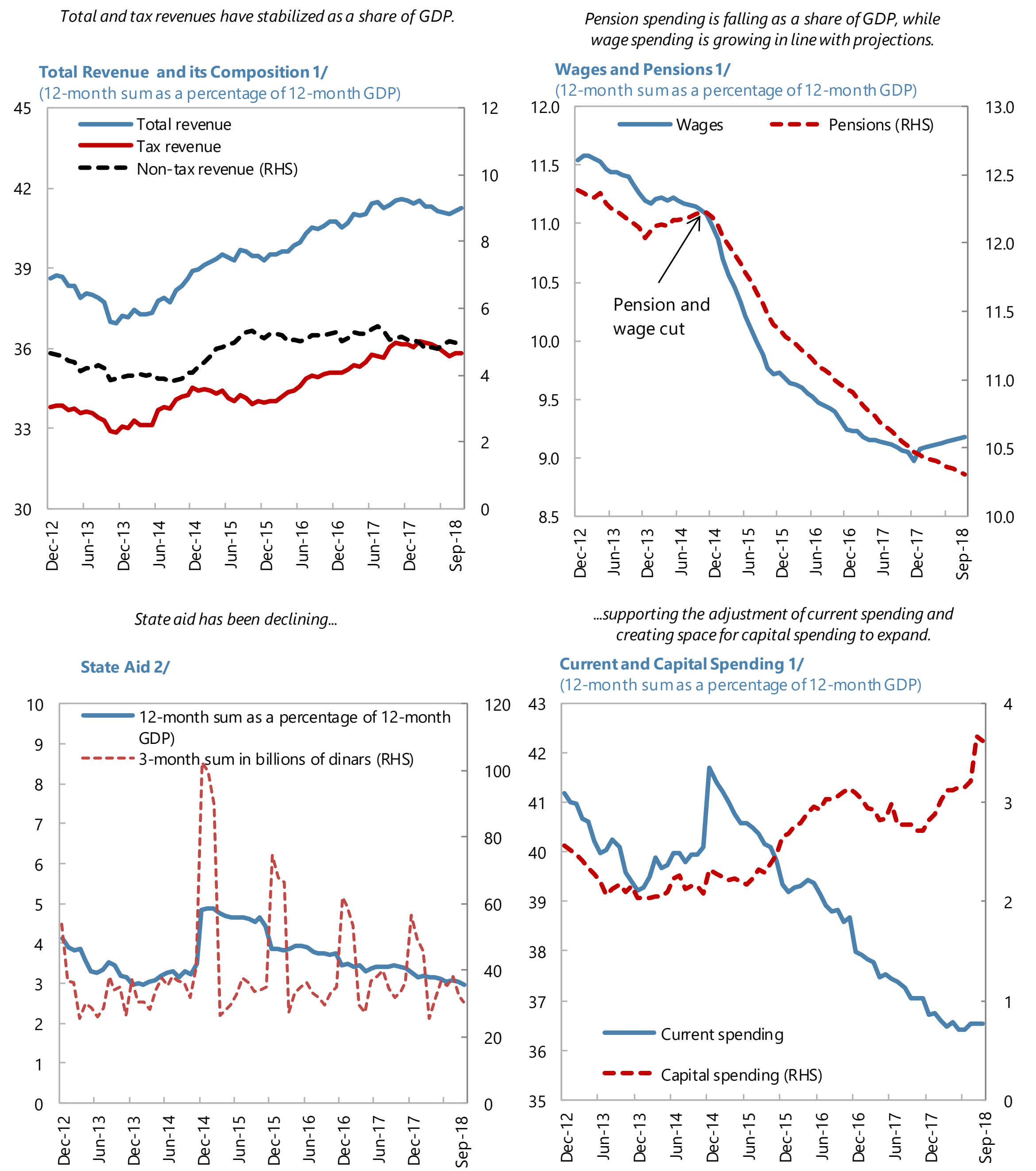
...most recently on account of lower lending rates to the corporate sector.

Bank lending interest rates: FX and FX-linked
(Percent)



Source: NBS.

Figure 6. Serbia: Fiscal Developments, 2012–18

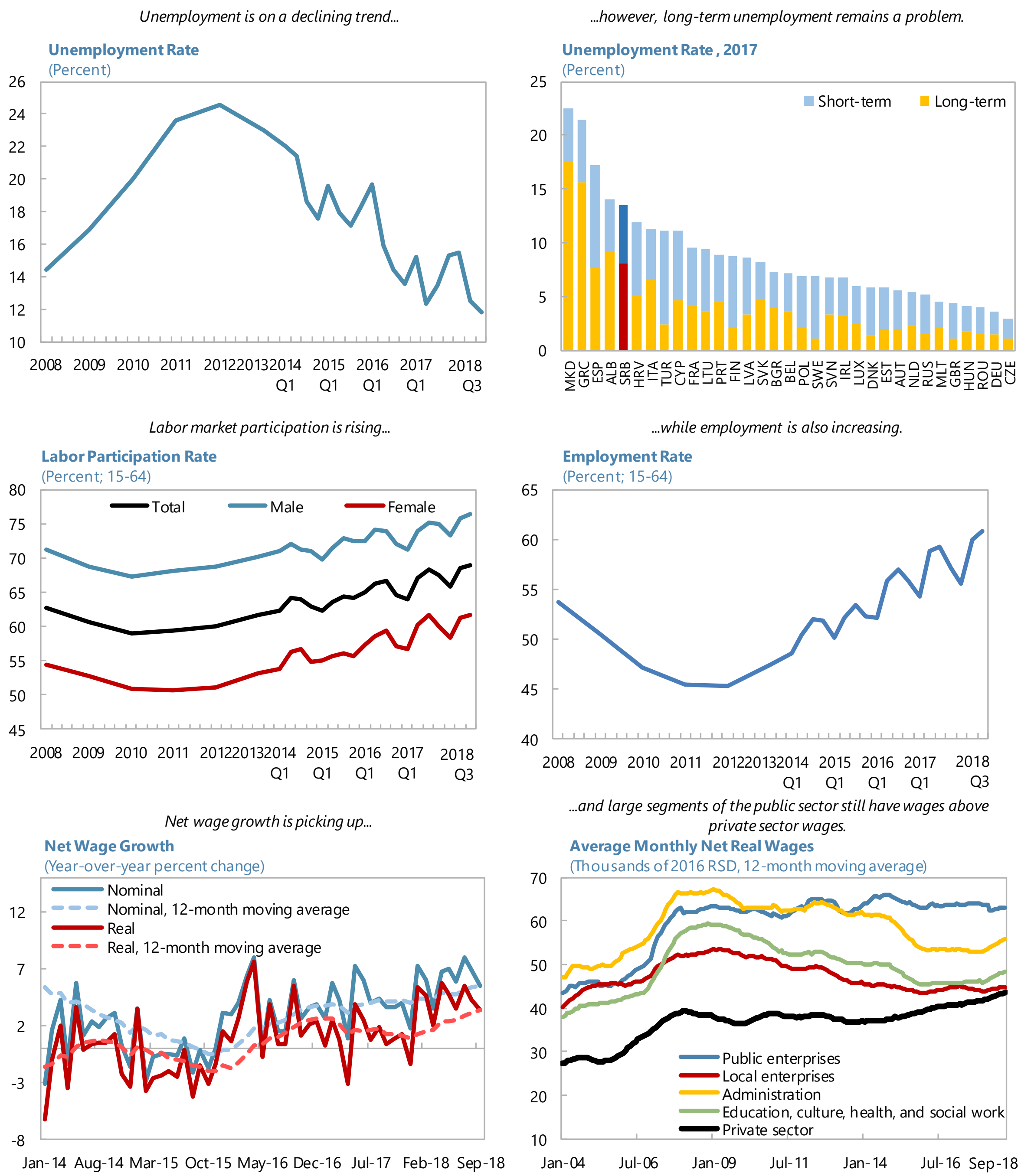


Sources: Ministry of Finance; and IMF staff calculations.

1/ Staff estimates of monthly GDP consistent with the revised annual national accounts for 2015-17.

2/ State aid includes direct subsidies, net lending through the budget, assumption of SOE's debt, and the service of guaranteed debt called by creditors.

Figure 7. Serbia: Labor Market Developments, 2008–18



Sources: International Labour Organization; OECD database; Republic of Serbia National Employment Service; Statistical Office of the Republic Serbia; and IMF staff calculations.

Table 1. Serbia: Selected Economic and Social Indicators, 2016–19

	2016	2017	2018		2019	
			CR 18/237	Proj.	CR 18/237	Proj.
	(Percent change, unless otherwise indicated)					
Real sector 1/						
Real GDP	3.3	2.0	**3.5**	4.2	**3.5**	3.5
Real domestic demand (absorption)	1.4	3.9	**3.9**	4.8	**3.7**	3.6
Consumer prices (average)	1.1	3.1	**1.6**	2.1	**2.6**	2.4
GDP deflator	1.5	3.0	**2.6**	2.4	**3.1**	3.3
Unemployment rate (in percent) 2/	15.9	14.1	**...**	...	**...**	...
Nominal GDP (in billions of dinars)	4,521	4,754	**4,740**	5,074	**5,058**	5,424
	(Percent of GDP)					
General government finances						
Revenue 3/	40.8	41.5	**43.3**	41.1	**42.2**	39.9
Expenditure 3/	41.9	40.4	**42.7**	40.6	**42.7**	40.4
Current 3/	37.9	36.7	**38.8**	36.4	**38.6**	36.0
Capital and net lending	3.2	3.1	**3.5**	3.8	**3.8**	4.1
Amortization of called guarantees	0.9	0.6	**0.4**	0.4	**0.4**	0.2
Fiscal balance 4/	-1.2	1.1	**0.6**	0.5	**-0.5**	-0.5
Primary fiscal balance (cash basis)	1.7	3.6	**2.8**	2.6	**1.8**	1.4
Structural primary fiscal balance 5/	1.8	3.5	**3.0**	2.7	**1.9**	1.8
Gross debt	68.9	58.7	**58.4**	54.0	**55.8**	51.9
	(End of period 12-month change, percent)					
Monetary sector						
Money (M1)	20.3	9.7	**8.4**	8.1	**7.7**	9.4
Broad money (M2)	9.8	3.3	**5.3**	6.9	**5.4**	6.6
Domestic credit to non-government 6/	1.8	4.4	**4.3**	7.1	**4.5**	5.9
	(Period average, percent)					
Interest rates (dinar)						
NBS key policy rate	4.0	3.9	...	...	...	...
Interest rate on new FX and FX-indexed loans	3.3	3.2	...	...	...	...
	(Percent of GDP, unless otherwise indicated)					
Balance of payments						
Current account balance	-2.9	-5.2	**-5.7**	-5.3	**-5.5**	-5.1
Exports of goods	34.9	35.9	**39.6**	37.1	**41.1**	38.4
Imports of goods	-43.4	-46.1	**-50.7**	-48.6	**-51.7**	-49.4
Trade of goods balance	-8.5	-10.2	**-11.1**	-11.5	**-10.6**	-11.1
Capital and financial account balance	0.6	4.8	**5.8**	5.7	**5.6**	5.7
External debt (percent of GDP)	75.9	67.6	**65.2**	61.3	**61.0**	57.4
of which: Private external debt	29.7	30.2	**29.3**	28.1	**27.1**	26.3
Gross official reserves (in billions of euro)	10.2	10.4	**10.5**	10.6	**10.5**	10.8
(in months of prospective imports)	5.5	4.9	**4.6**	4.5	**4.2**	4.3
(percent of short-term debt)	409.4	202.9	**286.0**	250.8	**206.0**	208.4
(percent of broad money, M2)	58.7	55.7	**52.9**	52.7	**49.8**	50.7
(percent of risk-weighted metric)	168.2	163.7	**165.7**	165.4	**156.6**	161.1
Exchange rate (dinar/euro, period average)	123.1	121.4	...	...	...	...
REER (annual average change, in percent; + indicates appreciation)	-1.1	2.9	...	...	...	...
Social indicators						
Per capita GDP (in US$)	5,756	6,284	**7,095**	7,266	**7,686**	7,688
Population (in million)	7.1	7.0	**7.0**	7.0	**7.0**	7.0

Sources: Serbian authorities; and IMF staff estimates and projections.

1/ SORS released revised 2015-17 national accounts in October 2018.
2/ Unemployment rate for working age population (15-64).
3/ Includes employer contributions.
4/ Includes amortization of called guarantees.
5/ Primary fiscal balance adjusted for the automatic effects of the output gap both on revenue and spending as well as one-offs.
6/ At constant exchange rates.

Table 2. Serbia: Medium-Term Framework, 2016–23

	2016	2017	2018		2019		2020		2021	2022	2023
			CR 18/237	Proj.	CR 18/237	Proj.	CR 18/237	Proj.	Proj.	Proj.	Proj.
					(percent change)						
Real sector											
GDP growth 1/	3.3	2.0	**3.5**	4.2	**3.5**	3.5	**4.0**	4.0	4.0	4.0	4.0
Domestic demand (contribution)	1.4	4.0	**4.5**	5.1	**4.3**	3.8	**4.9**	4.2	4.2	4.1	4.2
Net exports (contribution)	1.9	-2.0	**-1.0**	-0.9	**-0.8**	-0.3	**-0.9**	-0.2	-0.2	-0.1	-0.2
Consumer price inflation (average)	1.1	3.1	**1.6**	2.1	**2.6**	2.4	**3.0**	3.0	3.0	3.0	3.0
Consumer price inflation (end of period)	1.5	3.0	**1.9**	2.6	**2.7**	2.4	**3.0**	3.0	3.0	3.0	3.0
Output gap (in percent of potential)	-0.3	-0.9	**-0.4**	0.0	**-0.3**	0.0	**0.0**	0.0	0.0	0.0	0.0
Potential GDP growth	2.6	2.6	**3.0**	3.3	**3.4**	3.5	**3.7**	4.0	4.0	4.0	4.0
Domestic credit to non-gov. (constant exchange rate) 2/	1.8	4.4	**4.3**	7.1	**4.5**	5.9	**6.4**	5.7	6.4	4.2	4.7
					(percent of GDP, unless otherwise indicated)						
General government											
Revenue 3/	40.8	41.5	**43.3**	41.1	**42.2**	39.9	**42.0**	39.7	39.6	39.4	39.3
Expenditure 3/	41.9	40.4	**42.7**	40.6	**42.7**	40.4	**42.5**	40.2	40.1	39.9	39.7
Current 3/	37.9	36.7	**38.8**	36.4	**38.6**	36.0	**38.4**	35.9	35.8	35.5	35.5
of which: Wages and salaries 3/	9.2	9.0	**9.8**	9.2	**9.7**	9.2	**9.6**	9.2	9.2	9.2	9.2
of which: Pensions	11.1	10.7	**11.1**	10.5	**11.1**	10.4	**11.0**	10.3	10.3	10.3	10.3
of which: Goods and services	7.5	7.7	**8.6**	8.1	**8.5**	8.0	**8.5**	8.0	7.9	7.8	7.8
Capital and net lending	3.2	3.1	**3.5**	3.8	**3.8**	4.1	**3.8**	4.1	4.1	4.1	4.1
Amortization of called guarantees	0.9	0.6	**0.4**	0.4	**0.4**	0.2	**0.3**	0.2	0.2	0.2	0.1
Fiscal balance 4/	-1.2	1.1	**0.6**	0.5	**-0.5**	-0.5	**-0.5**	-0.5	-0.5	-0.5	-0.5
change (+ = consolidation)	*2.3*	*2.3*	***-0.6***	*-0.6*	***-1.1***	*-1.0*	***0.0***	*0.1*	*0.0*	*0.0*	*0.0*
Primary fiscal balance	1.7	3.6	**2.8**	2.6	**1.8**	1.4	**1.9**	1.6	1.6	1.6	1.6
change (+ = consolidation)	*2.1*	*1.9*	***-1.1***	*-1.0*	***-1.0***	*-1.2*	***0.1***	*0.1*	*0.1*	*0.0*	*0.0*
One-off fiscal items, net 5/	0.1	0.5	**0.0**	-0.1	**0.0**	-0.4	**0.0**	-0.1	0.0	0.0	0.0
Structural primary balance	1.8	3.5	**3.0**	2.7	**1.9**	1.8	**1.9**	1.6	1.6	1.6	1.6
change (+ = consolidation)	*1.8*	*1.7*	***-1.0***	*-0.8*	***-1.1***	*-0.9*	***0.0***	*-0.1*	*0.0*	*0.0*	*0.0*
Structural primary balance net of capital expenditures	4.8	6.3	**6.3**	6.3	**5.5**	5.8	**5.6**	5.6	5.6	5.5	5.5
Gross debt	68.9	58.7	**58.4**	54.0	**55.8**	51.9	**53.0**	48.9	46.0	43.4	41.0
Effective interest rate on government borrowing (percent)	4.3	4.1	**3.8**	3.8	**4.2**	3.9	**4.6**	4.2	4.6	4.7	4.8
Domestic borrowing (including FX)	5.2	4.8	**4.6**	4.9	**5.1**	4.7	**5.2**	4.8	4.8	4.8	4.8
External borrowing	3.3	3.2	**3.3**	3.1	**3.6**	3.3	**3.7**	3.4	3.4	3.4	3.4
					(percent of GDP, unless otherwise indicated)						
Balance of payments											
Current account	-2.9	-5.2	**-5.7**	-5.3	**-5.5**	-5.1	**-5.3**	-4.8	-4.6	-4.4	-4.2
of which: Trade balance	-8.5	-10.2	**-11.1**	-11.5	**-10.6**	-11.1	**-10.4**	-10.7	-10.5	-10.2	-10.1
of which: Current transfers, net (excl. grants)	8.4	8.6	**9.1**	9.2	**8.5**	8.6	**8.3**	8.2	8.1	8.0	8.0
Capital and financial account	0.6	4.8	**5.8**	5.7	**5.6**	5.7	**5.5**	5.2	4.9	4.7	4.5
of which: Foreign direct investment	5.2	6.2	**6.6**	6.2	**5.8**	5.7	**5.8**	5.4	5.6	5.6	5.6
External debt (end of period)	75.9	67.6	**65.2**	61.3	**61.0**	57.4	**56.7**	53.2	48.8	44.6	40.5
of which: Private external debt	29.7	30.2	**29.3**	28.1	**27.1**	26.3	**24.9**	24.5	22.7	20.8	19.0
Gross official reserves											
(in billions of euros)	10.2	10.4	**10.5**	10.6	**10.5**	10.8	**10.6**	11.0	11.2	11.4	11.6
(in percent of short-term external debt)	409.4	202.9	**286.0**	250.8	**206.0**	208.4	**207.2**	212.2	215.2	219.5	223.5
REER (ann. av. change; + = appreciation)	-1.1	2.9	**...**	...	**...**	...	**...**	...	...	...	...

Sources: NBS, MoF, SORS and IMF staff estimates and projections.

1/ SORS released revised 2015-17 national accounts in October 2018.

2/ Using constant dinar/euro and dinar/swiss franc exchange rates for converting FX and FX-indexed loans to dinars.

3/ Includes employer contributions.

4/ Includes amortization of called guarantees.

5/ Calculated as one-off revenue items minus one-off expenditure items. Negative sign indicates net expenditure.

Table 3. Serbia: Growth Composition, 2016–23 1/

	2016	2017	2018		2019		2020		2021	2022	2023
			CR 18/237	Proj.	CR 18/237	Proj.	CR 18/237	Proj.	Proj.	Proj.	Proj.
			(Percent change, unless otherwise noted)								
Real											
Gross Domestic Product (GDP)	3.3	2.0	**3.5**	4.2	**3.5**	3.5	**4.0**	4.0	4.0	4.0	4.0
Domestic demand	1.4	3.9	**3.9**	4.8	**3.7**	3.6	**4.3**	3.9	3.9	3.9	3.9
Consumption	1.2	2.2	**3.0**	3.4	**2.9**	2.8	**4.0**	3.4	3.5	3.5	3.5
Non-government	1.3	1.9	**2.7**	3.1	**3.2**	3.0	**4.2**	3.8	3.8	3.9	3.9
Government	1.2	3.3	**4.1**	4.6	**1.7**	2.1	**3.0**	1.5	2.3	1.7	1.6
Investment	1.8	11.7	**7.5**	11.0	**6.6**	6.6	**5.4**	5.9	5.4	5.2	5.3
Gross fixed capital formation	5.4	7.3	**8.8**	12.4	**7.6**	7.5	**6.2**	6.2	5.8	5.7	5.7
Non-government	3.0	9.8	**7.7**	9.0	**6.5**	6.0	**6.6**	6.5	6.0	5.9	5.9
Government	20.8	-6.2	**15.3**	34.0	**13.3**	15.3	**4.2**	4.9	4.9	5.0	4.7
Exports of goods and services	11.9	8.2	**10.3**	10.5	**9.1**	9.0	**8.7**	8.7	8.7	8.8	8.7
Imports of goods and services	6.7	11.1	**9.5**	10.8	**8.3**	8.4	**8.2**	8.0	8.0	8.1	8.1
			(contributions to GDP, percent)								
Gross Domestic Product (GDP)	3.3	2.0	**3.5**	4.2	**3.5**	3.5	**4.0**	4.0	4.0	4.0	4.0
Domestic demand (absorption)	1.4	4.0	**4.5**	5.1	**4.3**	3.8	**4.9**	4.2	4.2	4.1	4.2
Net exports of goods and services	1.9	-2.0	**-1.0**	-0.9	**-0.8**	-0.3	**-0.9**	-0.2	-0.2	-0.1	-0.2
Consumption	1.1	1.9	**2.7**	2.9	**2.6**	2.4	**3.6**	2.9	3.0	3.0	2.9
Non-government	0.9	1.4	**2.0**	2.2	**2.3**	2.1	**3.0**	2.7	2.6	2.7	2.7
Government	0.2	0.5	**0.7**	0.8	**0.3**	0.3	**0.5**	0.2	0.4	0.3	0.2
Investment	0.3	2.1	**1.8**	2.2	**1.6**	1.4	**1.4**	1.3	1.2	1.2	1.2
Gross fixed capital formation	0.9	1.3	**1.8**	2.2	**1.6**	1.5	**1.4**	1.3	1.2	1.2	1.2
Non-government	0.4	1.4	**1.4**	1.4	**1.2**	1.0	**1.2**	1.1	1.0	1.0	1.0
Government	0.5	-0.2	**0.5**	0.8	**0.4**	0.5	**0.2**	0.2	0.2	0.2	0.2
Change in inventories	-0.6	0.9	**0.0**	0.0	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0
Exports of goods and services	5.4	4.0	**5.8**	5.4	**5.5**	4.9	**5.5**	5.0	5.2	5.6	5.8
Imports of goods and services	3.5	6.0	**6.8**	6.4	**6.3**	5.3	**6.5**	5.2	5.5	5.7	5.9
			(Percent change, unless otherwise noted)								
Nominal											
Gross Domestic Product (GDP)	4.9	5.2	**6.2**	6.7	**6.7**	6.9	**7.2**	7.5	7.5	7.6	7.5
Domestic demand (absorption), contribution to GDP growth	2.9	7.3	**6.2**	9.6	**6.7**	6.9	**7.6**	7.5	7.7	7.9	7.8
Net exports of goods and services, contribution to GDP growth	1.9	-2.1	**0.0**	-2.9	**0.0**	0.0	**-0.4**	0.0	-0.2	-0.2	-0.3
Non-government	3.3	5.0	**4.7**	5.3	**5.6**	5.2	**7.2**	6.8	6.9	7.0	6.9
Government	2.0	6.5	**10.5**	11.2	**5.8**	7.3	**6.2**	6.5	6.8	7.3	7.2
Investment	1.1	15.0	**5.7**	20.7	**8.3**	9.5	**7.2**	7.7	8.3	8.3	8.5
Gross fixed capital formation	6.0	10.1	**11.2**	15.7	**10.5**	10.3	**9.2**	7.7	8.4	8.4	8.4
Non-government	3.0	13.2	**9.9**	11.6	**9.3**	8.5	**9.7**	8.0	8.6	8.6	8.7
Government	21.7	-3.9	**17.7**	37.2	**16.3**	18.0	**7.2**	6.4	7.5	7.6	7.5
Exports of goods and services	12.6	9.3	**9.1**	7.0	**10.9**	10.9	**10.6**	10.7	10.4	10.4	10.3
Imports of goods and services	7.2	12.5	**7.9**	11.2	**9.4**	9.3	**10.0**	9.2	9.5	9.6	9.7
Memorandum items:											
GDP deflator (percent)	1.5	3.0	**2.6**	2.4	**3.1**	3.3	**3.1**	3.4	3.4	3.5	3.3
Nominal GDP (billions of dinars)	4521	4754	**4740**	5074	**5058**	5424	**5421**	5832	6269	6746	7250

Sources: Serbian Statistical Office; and IMF staff estimates and projections.

1/ SORS released revised 2015-17 national accounts in October 2018.

Table 4a. Serbia: Balance of Payments, 2016–23 1/

(Billions of Euros)

	2016	2017	2018		2019		2020		2021	2022	2023
			CR 18/237	Proj.	CR 18/237	Proj.	CR 18/237	Proj.	Proj.	Proj.	Proj.
					(Billions of euros)						
Current account balance	-1.1	-2.1	**-2.3**	-2.3	**-2.4**	-2.4	**-2.4**	-2.4	-2.4	-2.5	-2.5
Trade of goods balance	-3.1	-4.0	**-4.4**	-4.9	**-4.5**	-5.1	**-4.8**	-5.2	-5.5	-5.8	-6.1
Exports of goods	12.8	14.1	**15.9**	15.9	**17.6**	17.6	**19.4**	19.4	21.4	23.6	25.9
Imports of goods	-15.9	-18.1	**-20.3**	-20.8	**-22.1**	-22.6	**-24.2**	-24.6	-26.9	-29.4	-32.1
Services balance	0.9	1.0	**1.1**	1.2	**1.2**	1.3	**1.3**	1.4	1.6	1.8	1.9
Exports of nonfactor services	4.6	5.2	**5.7**	5.8	**6.4**	6.5	**7.0**	7.2	8.0	8.8	9.7
Imports of nonfactor services	-3.7	-4.3	**-4.6**	-4.7	**-5.2**	-5.3	**-5.8**	-5.8	-6.4	-7.0	-7.8
Income balance	-2.0	-2.5	**-2.6**	-2.4	**-2.7**	-2.5	**-2.7**	-2.6	-2.8	-3.0	-3.2
Net interest	-1.0	-0.9	**-0.7**	-0.6	**-0.8**	-0.6	**-0.8**	-0.6	-0.7	-0.7	-0.8
Current transfer balance	3.2	3.5	**3.7**	3.9	**3.6**	3.9	**3.8**	4.0	4.3	4.5	4.9
Others, including private remittances	3.1	3.4	**3.6**	3.9	**3.6**	3.9	**3.8**	4.0	4.3	4.5	4.9
Capital and financial account balance 2/	0.2	1.9	**2.3**	2.4	**2.4**	2.6	**2.5**	2.6	2.6	2.7	2.8
Foreign direct investment balance	1.9	2.4	**2.6**	2.6	**2.5**	2.6	**2.6**	2.7	3.0	3.2	3.4
Portfolio investment balance	-0.9	-0.8	**-0.4**	-0.7	**0.3**	0.2	**0.4**	0.2	-0.1	-0.2	-0.3
of which: debt liabilities	-0.9	-0.8	**-0.4**	-0.7	**0.3**	0.2	**0.4**	0.2	-0.1	-0.2	-0.3
Other investment balance	-0.7	0.3	**0.1**	0.5	**-0.4**	-0.2	**-0.5**	-0.3	-0.3	-0.3	-0.4
Public sector 2/ 3/	0.3	-0.5	**0.2**	0.3	**-0.3**	-0.2	**-0.3**	-0.3	-0.2	-0.1	-0.1
Domestic banks	-0.5	0.0	**0.1**	0.1	**0.1**	0.1	**0.1**	0.1	0.1	-0.1	-0.1
Other private sector 4/	-0.5	0.8	**-0.1**	0.1	**-0.2**	-0.1	**-0.3**	-0.1	-0.2	-0.1	-0.1
Errors and omissions	0.5	0.4	**0.0**	0.0	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0
Overall balance	-0.3	0.2	**0.0**	0.1	**0.0**	0.3	**0.1**	0.2	0.2	0.2	0.2
Financing	0.3	-0.2	**0.0**	-0.1	**0.0**	-0.3	**-0.1**	-0.2	-0.2	-0.2	-0.2
Gross international reserves (increase, -)	0.3	-0.2	**0.0**	-0.1	**0.0**	-0.3	**-0.1**	-0.2	-0.2	-0.2	-0.2
Financing Gap	0.0	0.0	**0.0**	0.0	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0
Use of Fund credit, net	0.0	0.0	**0.0**	0.0	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0
Purchases	0.0	0.0	**0.0**	0.0	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0
Repurchases	0.0	0.0	**0.0**	0.0	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0

Sources: NBS; and IMF staff estimates and projections.

1/ SORS released revised 2016 BOP in October 2017.

2/ Excluding net use of IMF resources.

3/ Includes SDR allocations in 2009.

4/ Includes trade credits (net).

Table 4b. Serbia: Balance of Payments, 2016–23 1/

(Percent of GDP)

	2016	2017	2018		2019		2020		2021	2022	2023
			CR 18/237	Proj.	CR 18/237	Proj.	CR 18/237	Proj.	Proj.	Proj.	Proj.
						(Percent of GDP)					
Current account balance	-2.9	-5.2	**-5.7**	-5.3	**-5.5**	-5.1	**-5.3**	-4.8	-4.6	-4.4	-4.2
Trade of goods balance	-8.5	-10.2	**-11.1**	-11.5	**-10.6**	-11.1	**-10.4**	-10.7	-10.5	-10.2	-10.1
Exports of goods	34.9	35.9	**39.6**	37.1	**41.1**	38.4	**42.5**	39.4	40.5	41.6	42.6
Imports of goods	-43.4	-46.1	**-50.7**	-48.6	**-51.7**	-49.4	**-52.9**	-50.1	-51.0	-51.7	-52.7
Services balance	2.5	2.5	**2.8**	2.7	**2.8**	2.7	**2.8**	2.9	3.1	3.1	3.2
Income balance	-5.5	-6.5	**-6.5**	-5.7	**-6.2**	-5.4	**-6.0**	-5.3	-5.3	-5.2	-5.2
Current transfer balance	8.6	9.0	**9.1**	9.2	**8.5**	8.6	**8.3**	8.2	8.1	8.0	8.0
Official grants	0.2	0.4	**0.1**	0.1	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0
Others, including private remittances	8.4	8.6	**9.1**	9.2	**8.5**	8.6	**8.3**	8.2	8.1	8.0	8.0
Capital and financial account balance 2/	0.6	4.8	**5.8**	5.7	**5.6**	5.7	**5.5**	5.2	4.9	4.7	4.5
Capital transfers balance	0.0	0.0	**0.0**	0.0	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0
Foreign direct investment balance	5.2	6.2	**6.6**	6.2	**5.8**	5.7	**5.8**	5.4	5.6	5.6	5.6
Portfolio investment balance	-2.5	-2.1	**-1.1**	-1.6	**0.8**	0.4	**0.9**	0.4	-0.1	-0.3	-0.5
Other investment balance	-2.0	0.8	**0.2**	1.1	**-0.9**	-0.4	**-1.2**	-0.6	-0.6	-0.5	-0.6
Public sector 2/ 3/	0.8	-1.2	**0.4**	0.6	**-0.6**	-0.4	**-0.7**	-0.6	-0.5	-0.2	-0.2
Domestic banks	-1.4	0.0	**0.1**	0.2	**0.2**	0.2	**0.2**	0.2	0.2	-0.2	-0.2
Other private sector 4/	-1.5	1.9	**-0.3**	0.2	**-0.6**	-0.2	**-0.7**	-0.2	-0.3	-0.2	-0.2
Errors and omissions	1.5	1.0	**0.0**	0.0	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0
Overall balance	-0.8	0.6	**0.1**	0.3	**0.1**	0.6	**0.1**	0.4	0.3	0.4	0.3
Memorandum items:											
Export growth	11.9	9.8	**12.5**	13.0	**10.9**	10.5	**10.4**	10.3	10.3	10.3	10.0
Import growth	5.5	13.4	**12.3**	15.4	**8.8**	8.5	**9.4**	8.8	9.3	9.2	9.2
Export volume growth	12.7	8.5	**11.0**	11.0	**9.1**	8.6	**8.7**	8.5	8.7	8.8	9.0
Import volume growth	11.0	10.0	**10.3**	12.0	**7.7**	7.7	**7.8**	7.8	7.9	7.8	7.8
Trading partner import growth	5.4	8.1	**6.7**	6.6	**4.6**	5.2	**4.6**	5.2	5.2	5.2	5.2
Export prices growth	-0.7	1.2	**1.4**	1.8	**1.6**	1.7	**1.6**	1.7	1.6	1.4	1.3
Import prices growth	-4.9	3.1	**1.9**	3.0	**1.1**	0.8	**1.5**	1.0	1.3	1.3	1.3
Change in terms of trade	4.4	-1.8	**-0.5**	-1.2	**0.6**	1.0	**0.1**	0.7	0.3	0.1	0.0
Gross official reserves (in billions of euro)	10.2	10.4	**10.5**	10.6	**10.5**	10.8	**10.6**	11.0	11.2	11.4	11.6
(In months of prospective imports of GNFS)	5.5	4.9	**4.6**	4.5	**4.2**	4.3	**3.9**	4.0	3.7	3.4	3.1
(in percent of short-term debt)	409.4	202.9	**286.0**	250.8	**206.0**	208.4	**207.2**	212.2	215.2	219.5	223.5
(in percent of broad money, M2)	58.7	55.7	**52.9**	52.7	**49.8**	50.7	**46.8**	48.0	45.3	43.0	40.8
(in percent of risk-weighted metric, float) 5/	168.2	163.7	**165.7**	165.4	**156.6**	161.1	**152.7**	156.8	160.4	160.9	160.2
(in percent of risk-weighted metric, other) 5/	113.4	112.7	**…**	111.4	**…**	108.8	**…**	105.8	105.0	103.7	102.0
GDP (billions of euros)	36.7	39.2	**40.1**	42.8	**42.7**	45.8	**45.7**	49.1	52.8	56.7	60.9

Sources: NBS; and IMF staff estimates and projections.
1/ SORS released revised 2016 BOP in October 2017.
2/ Excluding net use of IMF resources.
3/ Includes SDR allocations in 2009.
4/ Includes trade credits (net).
5/ Although Serbia was reclassified as crawl-like exchange rate regime in 2018, Serbia does not target any specific exchange rate.

Table 5. Serbia: External Financing Requirements, 2016–23

	2016	2017	2018	2019	2020	2021	2022	2023
			Proj.					
	(Billions of euros)							
1. Total financing requirement	**3.9**	**4.8**	**7.6**	**6.8**	**7.7**	**8.6**	**7.2**	**6.9**
Current account deficit	1.1	2.1	2.3	2.4	2.4	2.4	2.5	2.5
Debt amortization	3.1	2.5	5.1	4.2	5.2	6.0	4.5	4.1
Medium and long-term debt	2.8	1.8	4.2	3.3	4.3	5.1	3.6	3.2
Public sector	1.0	0.6	2.7	1.6	2.2	3.0	1.5	1.5
Of which: Eurobonds	0.2	0.7	0.9	0.0	1.3	1.7	0.0	0.0
Of which: Domestic bonds (non-residents)	0.0	0.0	1.0	0.8	0.2	0.6	0.7	0.7
Commercial banks	1.0	1.2	0.6	0.7	0.9	1.0	1.0	1.1
Corporate sector	0.8	0.0	1.0	1.0	1.2	1.1	1.1	0.7
Short-term debt	0.3	0.7	0.9	0.9	0.9	0.9	0.9	0.9
Public sector	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Commercial banks	0.2	0.6	0.8	0.8	0.8	0.8	0.8	0.8
Corporate sector	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Change in gross reserves (increase=+)	-0.3	0.2	0.1	0.3	0.2	0.2	0.2	0.2
2. Total financing sources	**3.9**	**4.8**	**7.6**	**6.8**	**7.7**	**8.6**	**7.2**	**6.9**
Capital transfers	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign direct investment (net)	1.9	2.4	2.6	2.6	2.7	3.0	3.2	3.4
Portfolio investment (net) 1/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt financing	2.7	2.9	4.9	4.2	5.1	5.6	4.0	3.5
Medium and long-term debt	2.0	2.0	4.0	3.3	4.2	4.8	3.1	2.6
Public sector 2/	1.1	0.0	2.2	1.6	2.1	2.7	1.3	1.0
Of which: Eurobonds	0.0	0.0	0.0	0.0	1.0	1.8	0.0	0.0
Of which: Domestic bonds (non-residents)	0.0	0.0	1.2	1.0	0.6	0.5	0.6	0.4
Commercial banks	0.3	1.1	0.7	0.8	1.0	1.1	0.9	0.9
Corporate sector	0.6	0.8	1.1	0.9	1.1	0.9	1.0	0.6
Short-term debt	0.7	0.9	0.9	0.9	0.9	0.9	0.9	0.9
Public sector	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Commercial banks	0.6	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Corporate sector	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other net capital inflows 3/	-0.7	-0.5	0.0	0.0	0.0	0.0	0.0	0.0
o/w trade credit and currency and deposits	0.3	0.1	0.0	0.0	0.0	0.0	0.0	0.0
3. Total financing needs	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Memorandum items:								
Debt service	4.1	3.3	5.7	4.8	5.8	6.7	5.2	4.9
Interest	0.9	0.8	0.6	0.6	0.6	0.7	0.7	0.8
Amortization	3.1	2.5	5.1	4.2	5.2	6.0	4.5	4.1

Sources: NBS; and Fund staff estimates and projections.

1/ Only includes equity securities and financial derivatives.

2/ Excluding IMF.

3/ Includes all other net financial flows and errors and omissions.

Table 6a. Serbia: General Government Fiscal Operations, 2016–23 1/

(Billions of RSD)

	2016	2017	2018		2019		2020		2021	2022	2023
			CR 18/237	Proj.	CR 18/237	Proj.	CR 18/237	Proj.	Proj.	Proj.	Proj.
Revenue	1,843	1,973	**2,051**	2,086	**2,134**	2,162	**2,279**	2,317	2,484	2,658	2,847
Taxes	1,586	1,718	**1,800**	1,817	**1,877**	1,916	**2,013**	2,072	2,223	2,381	2,552
Personal income tax	155	168	**177**	176	**167**	188	**176**	201	212	224	238
Social security contributions 2/	527	567	**609**	618	**628**	653	**675**	702	755	812	871
Taxes on profits	80	112	**104**	115	**111**	120	**118**	128	140	149	160
Value-added taxes	454	479	**504**	505	**538**	539	**580**	586	629	672	724
Excises	266	280	**288**	285	**306**	291	**328**	318	340	366	390
Taxes on international trade	36	40	**43**	43	**47**	47	**50**	51	55	58	63
Other taxes	67	72	**75**	75	**80**	77	**86**	86	92	99	106
Non-tax revenue	239	241	**235**	257	**241**	231	**248**	232	247	263	280
Capital revenue	8	6	**0**	0	**0**	0	**0**	0	0	0	0
Grants	9	9	**16**	11	**17**	15	**18**	13	13	14	15
Expenditure	1,897	1,921	**2,024**	2,060	**2,160**	2,191	**2,306**	2,344	2,513	2,689	2,880
Current expenditure	1,715	1,745	**1,838**	1,847	**1,950**	1,954	**2,084**	2,093	2,244	2,398	2,573
Wages and salaries 3/	418	426	**467**	469	**493**	502	**523**	538	577	620	666
Goods and services	339	365	**406**	413	**431**	434	**459**	466	494	526	563
Interest	132	121	**106**	107	**117**	106	**130**	118	131	137	146
Subsidies	113	113	**113**	110	**121**	125	**129**	133	141	152	164
Transfers	714	720	**746**	748	**789**	786	**842**	839	901	962	1,035
Pensions 4/	503	506	**527**	531	**560**	563	**597**	602	647	693	748
Other transfers 5/	211	214	**219**	217	**229**	223	**245**	237	253	269	287
Capital expenditure	139	134	**158**	184	**183**	217	**196**	230	248	267	287
Net lending	3	13	**8**	9	**8**	7	**9**	8	9	10	10
Amortization of activated guarantees	39	29	**21**	20	**19**	13	**17**	12	13	15	11
Fiscal balance	-54	52	**27**	26	**-26**	-29	**-27**	-27	-29	-31	-33
Financing	54	-52	**-27**	-26	**26**	29	**27**	27	29	31	33
Privatization proceeds	5	2	**20**	20	**0**	0	**0**	0	0	0	0
Equity investment	0	0	**0**	0	**0**	0	**0**	0	0	0	0
Domestic	20	-38	**49**	38	**46**	49	**99**	43	35	37	50
Banks	148	27	**52**	-42	**25**	11	**18**	13	4	25	36
Government deposits ((-) means accumulation)	35	5	**-12**	-1	**-5**	-7	**-10**	-8	-4	-20	-15
Securities held by banks (net)	99	90	**76**	-30	**54**	23	**53**	45	31	69	74
Other domestic bank financing	14	-68	**-12**	-11	**-24**	-5	**-25**	-24	-23	-24	-22
Non-banks (incl. non-residents)	-128	-65	**-3**	80	**21**	38	**80**	30	31	12	13
Securities held by non-banks (non-residents, net)	-37	-50	**8**	93	**23**	45	**80**	30	31	12	13
Others (incl. amortization)	-91	-15	**-11**	-13	**-2**	-7	**0**	0	0	0	0
External	29	-16	**-97**	-84	**-21**	-20	**-72**	-17	-6	-6	-16
Program	0	61	**0**	0	**0**	0	**0**	0	0	0	0
Project	73	60	**57**	66	**45**	45	**48**	67	57	56	48
Bonds and loans	23	0	**59**	48	**20**	32	**119**	131	221	27	22
Amortization	-67	-137	**-213**	-198	**-85**	-97	**-239**	-214	-284	-89	-86
Memorandum items:											
Wages and salaries excluding severance payments	418	426	**467**	469	**493**	502	**523**	538	577	620	666
Gross 1 wages and salaries	354	361	**394**	396	**421**	428	**446**	459	492	529	569
Arrears accumulation (domestic)	-1	-1	**-1**	-1	**-1**	-1	**0**	0	0	0	0
Quasi-fiscal support to SOEs (gross new issuance of guarantees)	86	54	**8**	8	**30**	30	**15**	15	10	7	0
Government deposits (stock)	107	102	**113**	103	**118**	110	**128**	118	123	143	158
Gross public debt	3114	2792	**2770**	2741	**2821**	2817	**2873**	2854	2886	2930	2972
Gross public debt (including restitution)	3357	3035	**3013**	2984	**3044**	3060	**3077**	3077	3090	3113	3136
Nominal GDP (billions of dinars)	4521	4754	**4740**	5074	**5058**	5424	**5421**	5832	6269	6746	7250

Sources: Ministry of Finance; and IMF staff estimates and projections.

1/ Includes the republican budget, local governments, social security funds, and the Road Company, but excludes indirect budget beneficiaries (IBBs) that are reporting only on an annual basis.

2/ Includes employer contributions.

3/ Including severence payments. Includes employer contributions.

4/ Includes RSD10 billion military pension payment in 2015 following a Constitution Court ruling.

5/ Excluding foreign currency deposit payments to households, reclassified below the line.

Table 6b. Serbia: General Government Fiscal Operations, 2016–23 1/
(Percent of GDP)

	2016	2017	2018		2019		2020		2021	2022	2023
			CR 18/237	Proj.	CR 18/237	Proj.	CR 18/237	Proj.	Proj.	Proj.	Proj.
Revenue	40.8	41.5	**43.3**	41.1	**42.2**	39.9	**42.0**	39.7	39.6	39.4	39.3
Taxes	35.1	36.1	**38.0**	35.8	**37.1**	35.3	**37.1**	35.5	35.5	35.3	35.2
Personal income tax	3.4	3.5	**3.7**	3.5	**3.3**	3.5	**3.3**	3.4	3.4	3.3	3.3
Social security contributions 2/	11.7	11.9	**12.8**	12.2	**12.4**	12.0	**12.4**	12.0	12.0	12.0	12.0
Taxes on profits	1.8	2.4	**2.2**	2.3	**2.2**	2.2	**2.2**	2.2	2.2	2.2	2.2
Value-added taxes	10.0	10.1	**10.6**	10.0	**10.6**	9.9	**10.7**	10.0	10.0	10.0	10.0
Excises	5.9	5.9	**6.1**	5.6	**6.0**	5.4	**6.1**	5.4	5.4	5.4	5.4
Taxes on international trade	0.8	0.8	**0.9**	0.8	**0.9**	0.9	**0.9**	0.9	0.9	0.9	0.9
Other taxes	1.5	1.5	**1.6**	1.5	**1.6**	1.4	**1.6**	1.5	1.5	1.5	1.5
Non-tax revenue	5.3	5.1	**5.0**	5.1	**4.8**	4.3	**4.6**	4.0	3.9	3.9	3.9
Capital revenue	0.2	0.1	**0.0**	0.0	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0
Grants	0.2	0.2	**0.3**	0.2	**0.3**	0.3	**0.3**	0.2	0.2	0.2	0.2
Expenditure	41.9	40.4	**42.7**	40.6	**42.7**	40.4	**42.5**	40.2	40.1	39.9	39.7
Current expenditure	37.9	36.7	**38.8**	36.4	**38.6**	36.0	**38.4**	35.9	35.8	35.5	35.5
Wages and salaries 3/	9.2	9.0	**9.8**	9.2	**9.7**	9.2	**9.6**	9.2	9.2	9.2	9.2
Goods and services	7.5	7.7	**8.6**	8.1	**8.5**	8.0	**8.5**	8.0	7.9	7.8	7.8
Interest	2.9	2.5	**2.2**	2.1	**2.3**	2.0	**2.4**	2.0	2.1	2.0	2.0
Subsidies	2.5	2.4	**2.4**	2.2	**2.4**	2.3	**2.4**	2.3	2.3	2.3	2.3
Transfers	15.8	15.1	**15.7**	14.7	**15.6**	14.5	**15.5**	14.4	14.4	14.3	14.3
Pensions 4/	11.1	10.7	**11.1**	10.5	**11.1**	10.4	**11.0**	10.3	10.3	10.3	10.3
Other transfers 5/	4.7	4.5	**4.6**	4.3	**4.5**	4.1	**4.5**	4.1	4.0	4.0	4.0
Capital expenditure	3.1	2.8	**3.3**	3.6	**3.6**	4.0	**3.6**	4.0	4.0	4.0	4.0
Net lending	0.1	0.3	**0.2**	0.2	**0.2**	0.1	**0.2**	0.1	0.1	0.1	0.1
Amortization of activated guarantees	0.9	0.6	**0.4**	0.4	**0.4**	0.2	**0.3**	0.2	0.2	0.2	0.1
Fiscal balance	-1.2	1.1	**0.6**	0.5	**-0.5**	-0.5	**-0.5**	-0.5	-0.5	-0.5	-0.5
Financing	1.2	-1.1	**-0.6**	-0.5	**0.5**	0.5	**0.5**	0.5	0.5	0.5	0.5
Privatization proceeds	0.1	0.0	**0.4**	0.4	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0
Equity investment	0.0	0.0	**0.0**	0.0	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0
Domestic	0.4	-0.8	**1.0**	0.8	**0.9**	0.9	**1.8**	0.7	0.6	0.6	0.7
Banks	3.3	0.6	**1.1**	-0.8	**0.5**	0.2	**0.3**	0.2	0.1	0.4	0.5
Government deposits ((-) means accumulation)	0.8	0.1	**-0.2**	0.0	**-0.1**	-0.1	**-0.2**	-0.1	-0.1	-0.3	-0.2
Securities held by banks (net)	2.2	1.9	**1.6**	-0.6	**1.1**	0.4	**1.0**	0.8	0.5	1.0	1.0
Other domestic bank financing	0.3	-1.4	**-0.2**	-0.2	**-0.5**	-0.1	**-0.5**	-0.4	-0.4	-0.4	-0.3
Non-banks (incl. non-residents)	-2.8	-1.4	**-0.1**	1.6	**0.4**	0.7	**1.5**	0.5	0.5	0.2	0.2
Securities held by non-banks (non-residents, net)	-0.8	-1.0	**0.2**	1.8	**0.5**	0.8	**1.5**	0.5	0.5	0.2	0.2
Others (incl. amortization)	-2.0	-0.3	**-0.2**	-0.3	**0.0**	-0.1	**0.0**	0.0	0.0	0.0	0.0
External	0.6	-0.3	**-2.0**	-1.7	**-0.4**	-0.4	**-1.3**	-0.3	-0.1	-0.1	-0.2
Program	0.0	1.3	**0.0**	0.0	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0
Project	1.6	1.3	**1.2**	1.3	**0.9**	0.8	**0.9**	1.1	0.9	0.8	0.7
Bonds and loans	0.5	0.0	**1.2**	0.9	**0.4**	0.6	**2.2**	2.2	3.5	0.4	0.3
Amortization	-1.5	-2.9	**-4.5**	-3.9	**-1.7**	-1.8	**-4.4**	-3.7	-4.5	-1.3	-1.2
Memorandum items:											
Wages and salaries excluding severance payments	9.2	9.0	**9.8**	9.2	**9.7**	9.2	**9.6**	9.2	9.2	9.2	9.2
Gross 1 wages and salaries	7.8	7.6	**8.3**	7.8	**8.3**	7.9	**8.2**	7.9	7.9	7.8	7.8
Arrears accumulation (domestic)	0.0	0.0	**0.0**	0.0	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0
Government deposits (stock)	2.4	2.1	**2.4**	2.0	**2.3**	2.0	**2.4**	2.0	2.0	2.1	2.2
Gross financing need	12.3	9.0	**8.7**	8.4	**8.0**	7.8	**9.4**	7.6	6.5	4.2	4.1
Gross public debt	68.9	58.7	**58.4**	54.0	**55.8**	51.9	**53.0**	48.9	46.0	43.4	41.0
Gross public debt (including restitution)	74.3	63.8	**63.6**	58.8	**60.2**	56.4	**56.8**	52.8	49.3	46.1	43.2
Nominal GDP (billions of dinars)	4,521	4,754	**4,740**	5,074	**5,058**	5,424	**5,421**	5,832	6,269	6,746	7,250

Sources: Ministry of Finance; and IMF staff estimates and projections.

1/ Includes the republican budget, local governments, social security funds, and the Road Company, but excludes indirect budget beneficiaries (IBBs) that are reporting only on an annual basis.

2/ Includes employer contributions.

3/ Including severence payments. Includes employer contributions.

4/ Includes RSD10 billion military pension payment in 2015 following a Constitution Court ruling.

5/ Excluding foreign currency deposit payments to households, reclassified below the line.

Table 7a. Serbia: Monetary Survey, 2016–23

	2016	2017	2018		2019		2020		2021	2022	2023
			CR 18/237	Proj.	CR 18/237	Proj.	CR 18/237	Proj.	Proj.	Proj.	Proj.
			(Billions of dinars, unless otherwise indicated; end of period) 1/								
Net foreign assets 2/	1156	986	**975**	985	**970**	1006	**967**	1019	1025	1066	1106
in billions of euro	9.4	8.3	**8.3**	8.3	**8.2**	8.5	**8.1**	8.6	8.6	8.9	9.3
Foreign assets	1512	1391	**1383**	1399	**1390**	1433	**1399**	1458	1477	1506	1534
NBS	1271	1191	**1184**	1200	**1191**	1233	**1200**	1259	1277	1306	1333
Commercial banks	241	200	**198**	199	**199**	199	**199**	200	200	200	200
Foreign liabilities (-)	-356	-405	**-407**	-414	**-420**	-427	**-433**	-440	-452	-440	-428
NBS	-6	-4	**-4**	-4	**-4**	-4	**-4**	-4	-4	-4	-4
Commercial banks	-350	-401	**-403**	-410	**-416**	-423	**-429**	-436	-448	-436	-424
Net domestic assets	989	1,231	**1,359**	1,386	**1,491**	1,522	**1,660**	1,679	1,846	1,990	2,163
Domestic credit	2,321	2,362	**2,491**	2,499	**2,615**	2,650	**2,778**	2,798	2,960	3,100	3,269
Government, net	341	353	**404**	352	**430**	372	**448**	387	393	422	461
NBS	-210	-215	**-226**	-216	**-231**	-223	**-241**	-232	-236	-257	-272
Claims on government	4	4	**4**	4	**4**	4	**4**	4	4	4	4
Liabilities (deposits)	214	219	**230**	220	**235**	227	**245**	235	240	261	276
Banks	551	568	**630**	568	**661**	595	**689**	619	629	679	733
Claims on government	638	630	**692**	630	**723**	658	**752**	681	692	741	795
Liabilities (deposits)	87	63	**62**	62	**62**	62	**62**	62	62	63	63
Local governments, net	-20	-31	**-31**	-31	**-31**	-31	**-31**	-31	-31	-31	-31
Non-government sector	2,000	2,040	**2,117**	2,177	**2,216**	2,308	**2,360**	2,441	2,597	2,708	2,839
Households	840	905	**962**	1,004	**1,016**	1,095	**1,083**	1,158	1,232	1,285	1,347
Enterprises	1,127	1,103	**1,122**	1,138	**1,165**	1,177	**1,240**	1,245	1,324	1,381	1,447
Other	34	32	**33**	34	**35**	36	**37**	39	41	43	45
Other assets, net	-1,332	-1,131	**-1,131**	-1,112	**-1,124**	-1,128	**-1,118**	-1,118	-1,113	-1,109	-1,106
Capital accounts (-)	-1,016	-963	**-956**	-959	**-941**	-945	**-928**	-932	-919	-907	-895
NBS	-391	-298	**-283**	-283	**-269**	-269	**-256**	-256	-243	-231	-219
Banks	-625	-664	**-672**	-676	**-672**	-676	**-672**	-676	-676	-676	-676
Provisions (-)	-281	-161	**-168**	-145	**-174**	-174	**-181**	-178	-185	-192	-200
Other assets	-34	-7	**-8**	-8	**-8**	-8	**-9**	-9	-10	-10	-11
Broad money (M2)	2146	2217	**2335**	2371	**2461**	2528	**2626**	2698	2872	3056	3269
M1	566	621	**673**	671	**725**	734	**777**	789	849	914	983
Currency in circulation	159	164	**178**	177	**191**	194	**205**	208	224	241	259
Demand deposits	407	457	**495**	494	**533**	540	**572**	581	625	673	723
Time and saving deposits	195	196	**213**	212	**229**	232	**245**	249	268	289	310
Foreign currency deposits	1385	1400	**1449**	1488	**1507**	1562	**1604**	1659	1755	1853	1976
in billions of euro	11.2	11.8	**12.3**	12.6	**12.7**	13.2	**13.5**	14.0	14.8	15.6	16.6
Memorandum items:			(year-on-year change unless indicated otherwise)								
M1	20.3	9.7	**8.4**	8.1	**7.7**	9.4	**7.2**	7.5	7.5	7.7	7.5
M2	9.8	3.3	**5.3**	6.9	**5.4**	6.6	**6.7**	6.7	6.4	6.4	6.9
Velocity (Dinar part of money supply)	5.9	5.8	**5.4**	5.7	**5.3**	5.6	**5.3**	5.6	5.6	5.6	5.6
Velocity (M2)	2.1	2.1	**2.0**	2.1	**2.1**	2.1	**2.1**	2.2	2.2	2.2	2.2
Deposits at constant exchange rate	8.5	5.9	**5.6**	7.2	**5.0**	6.3	**6.6**	6.6	6.3	6.2	6.8
Credit to non-gov. (current exchange rate)	2.6	2.0	**1.7**	4.7	**2.3**	3.8	**3.4**	3.7	4.0	2.8	3.3
Credit to non-gov. (constant exchange rates) 3/	1.5	4.9	**2.3**	5.1	**2.1**	3.6	**3.3**	3.6	4.0	2.7	3.2
Domestic	1.8	4.4	**4.3**	7.1	**4.5**	5.9	**6.4**	5.7	6.4	4.2	4.7
Households	9.8	9.8	**6.7**	11.3	**5.6**	8.9	**6.4**	5.7	6.4	4.2	4.7
Enterprises and other sectors	-3.3	0.5	**2.4**	3.8	**3.7**	3.3	**6.4**	5.6	6.4	4.1	4.7
External	0.9	5.7	**-1.6**	1.1	**-2.9**	-1.3	**-3.7**	-1.2	-1.8	-1.2	-1.2
Credit to non-gov. (real terms) 4/	1.0	-1.0	**-0.2**	2.0	**-0.4**	1.3	**0.4**	0.7	1.0	-0.2	0.3
Domestic credit to non-gov. (real terms)	1.1	-1.0	**1.8**	4.0	**1.9**	3.5	**3.4**	2.7	3.3	1.2	1.8
Households	8.8	4.6	**4.3**	8.2	**2.9**	6.5	**3.4**	2.7	3.3	1.2	1.8
Enterprises and other sectors	-3.8	-5.1	**-0.2**	0.6	**1.1**	1.0	**3.4**	2.7	3.3	1.2	1.8
External	0.8	-0.9	**-4.2**	-2.0	**-5.3**	-3.4	**-6.3**	-3.9	-4.6	-3.9	-4.0
12-m change in NBS's NFA, billions of euros	0.1	-0.2	**0.1**	0.0	**0.0**	0.2	**0.0**	0.2	0.1	0.3	0.2
Deposit euroization (percent of total) 5/	69.7	68.2	**67.2**	67.8	**66.4**	66.9	**66.3**	66.6	66.3	65.8	65.7
Credit euroization (percent of total) 5/	68.3	67.1	**66.1**	66.6	**65.1**	65.8	**64.1**	64.8	63.8	62.8	61.8

Sources: National Bank of Serbia; and IMF staff estimates and projections.

1/ Foreign exchange denominated items are converted at current exchange rates.

2/ Excluding undivided assets and liabilities of the FSRY and liabilities to banks in liquidation.

3/ Using constant program dinar/euro and dinar/swiss franc exchange rates for converting FX and FX-indexed loans to dinars agreed under 2015-17 SBA.

4/ Calculated as nominal credit at current exchange rates deflated by the change in the 12-month CPI index.

5/ Using current exchange rates.

Table 7b. Serbia: NBS Balance Sheet, 2016–23

	2016	2017	2018		2019		2020		2021	2022	2023
			CR 18/237	Proj.	CR 18/237	Proj.	CR 18/237	Proj.	Proj.	Proj.	Proj.
	(Billions of dinars, unless otherwise indicated; end of period) 1/										
Net foreign assets	1265	1187	**1180**	1196	**1187**	1230	**1196**	1255	1273	1302	1329
(In billions of euro)	10.3	10.0	**10.0**	10.1	**10.0**	10.4	**10.1**	10.6	10.7	10.9	11.1
Gross foreign reserves	1271	1191	**1184**	1200	**1191**	1233	**1200**	1259	1277	1306	1333
Gross reserve liabilities (-)	-6	-4	**-4**	-4	**-4**	-4	**-4**	-4	-4	-4	-4
Net domestic assets	-663	-596	**-638**	-605	**-610**	-625	**-594**	-639	-615	-607	-584
Net domestic credit	-272	-298	**-355**	-321	**-341**	-356	**-338**	-383	-372	-376	-365
Net credit to government	-210	-215	**-226**	-216	**-231**	-223	**-241**	-232	-236	-257	-272
Claims on government	4	4	**4**	4	**4**	4	**4**	4	4	4	4
Liabilities to government (-)	-214	-219	**-230**	-220	**-235**	-227	**-245**	-235	-240	-261	-276
Liabilities to government (-): local currency	-95	-118	**-118**	-118	**-118**	-118	**-118**	-118	-118	-118	-118
Liabilities to government (-): foreign currency	-119	-101	**-112**	-102	**-117**	-109	**-127**	-118	-122	-143	-158
Net credit to local governments	-43	-48	**-50**	-50	**-50**	-50	**-50**	-50	-50	-50	-50
Net claims on banks	-33	-45	**-88**	-65	**-70**	-93	**-57**	-111	-96	-79	-52
Capital accounts (-)	-391	-298	**-283**	-283	**-269**	-269	**-256**	-256	-243	-231	-219
Reserve money	602	591	**542**	591	**577**	604	**602**	616	658	696	745
Currency in circulation	159	164	**178**	177	**191**	194	**205**	208	224	241	259
Commercial bank reserves	221	232	**163**	207	**175**	193	**173**	176	190	196	211
Required reserves	147	156	**161**	165	**168**	174	**178**	185	195	206	220
Excess reserves	73	76	**2**	41	**8**	19	**-5**	-8	-6	-10	-9
FX deposits by banks, billions of euros	1.8	1.6	**1.7**	1.7	**1.8**	1.8	**1.9**	1.9	2.1	2.2	2.3

Sources: National Bank of Serbia; and IMF staff estimates and projections.

1/ Foreign exchange denominated items are converted at current exchange rates.

Table 8. Serbia: Banking Sector Financial Soundness Indicators, 2012–18

	2012	2013	2014	2015	2016	2017	2018	
							Mar	Jun
Capital adequacy								
Regulatory capital to risk-weighted assets	19.9	20.9	20.0	20.9	21.8	22.6	22.7	22.9
Regulatory Tier 1 capital to risk-weighted assets	19.0	19.3	17.6	18.8	20.0	21.6	21.8	22.1
Nonperforming loans net of provisions to capital	52.3	55.9	56.0	44.0	27.1	17.7	15.4	12.7
Regulatory Tier 1 capital to assets	11.6	11.2	10.1	10.7	11.6	13.7	13.9	14.3
Large exposures to capital	104.5	90.4	130.5	115.7	86.0	69.3	73.3	68.6
Regulatory capital to total assets	12.2	12.2	11.4	11.9	12.7	14.4	14.5	14.8
Asset quality								
Nonperforming loans to total gross loans	18.6	21.4	21.5	21.6	17.0	9.8	9.2	7.8
Sectoral distribution of loans (percent of total loans)								
Deposit takers	0.3	0.3	0.8	0.1	0.5	0.3	0.2	0.3
Central bank	2.1	5.8	0.4	1.6	1.7	2.1	1.9	3.0
General government	3.0	2.3	2.3	1.7	1.5	1.3	1.2	1.2
Other financial corporations	1.6	1.6	0.5	0.7	0.9	0.9	0.7	0.8
Nonfinancial corporations	58.2	54.1	56.3	55.9	52.6	50.5	50.6	49.1
Agriculture	3.0	2.7	3.5	3.7	3.6	3.5	3.4	3.5
Industry	17.9	18.4	19.2	18.4	16.5	16.2	16.3	16.2
Construction	5.8	4.6	4.2	3.8	4.1	4.0	4.1	4.1
Trade	15.0	13.5	13.9	13.9	14.3	14.6	14.9	14.2
Other loans to nonfinancial corporations	16.5	14.9	15.6	16.2	14.1	12.2	11.9	11.0
Households and NPISH	33.0	34.8	38.3	39.1	41.5	42.9	43.8	43.7
Households and NPISH of which: mortgage loans to total l	16.1	16.8	18.0	18.1	17.9	16.9	17.2	16.8
Foreign sector	1.9	1.1	1.4	0.9	1.4	2.0	1.6	1.9
IFRS provision for NPLs to gross NPLs	50.0	50.9	54.9	62.3	67.8	58.1	60.8	60.9
Specific and general provisions for NPLs to gross NPLs	111.1	105.5	107.6	106.4	108.5	112.1	0.0	0.0
Specific and general provisions for balance sheet losses to N	120.7	113.8	114.5	114.2	118.9	133.2	0.0	0.0
Specific and general provisions to NPLs	126.5	117.9	118.4	118.2	123.2	140.9	0.0	0.0
IFRS provision of total loans to total gross loans	10.2	11.9	12.7	14.4	12.4	6.6	6.7	5.8
Earnings and Profitability								
Return on assets	0.4	-0.1	0.1	0.3	0.7	2.1	2.1	2.1
Return on equity	2.0	-0.4	0.6	1.5	3.3	10.5	10.5	10.6
Liquidity								
Customer deposits to total (noninterbank) loans	84.9	92.3	95.7	99.7	108.1	106.9	105.4	106.8
Foreign-currency-denominated loans to total loans	74.1	71.6	70.1	72.3	69.4	67.5	67.3	67.0
Average monthy liquidity ratio	2.1	2.4	2.2	2.1	2.1	2.0	2.2	2.1
Average monthy narrow liquidity ratio	1.6	1.8	1.7	1.7	1.7	1.7	1.8	1.8
Sensitivity to Market Risk								
Foreign-currency-denominated liabilities to total liabilities	80.1	76.7	74.7	72.7	71.1	69.7	70.2	69.8
Total off-balance sheet items to total assets	103.5	111.0	207.3	234.1	219.9	209.4	0.0	0.0
Classified off-balance sheet items to classified balance sheet a	26.1	28.7	27.6	30.6	32.4	36.4	36.0	37.1

Source: National Bank of Serbia.

Table 9. Serbia: Schedule of Reviews Under the Policy Coordination Instrument, 2018–20

Program Review	Proposed Date
Board discussion of a PCI request	July 18, 2018
First Review	December 1, 2018
Second Review	June 1, 2019
Third Review	December 1, 2019
Fourth Review	June 1, 2020
Fifth Review	December 1, 2020

Source: IMF staff.

Appendix I. Program Statement

Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C., 20431
U.S.A.

Belgrade, December 7, 2018

Dear Ms. Lagarde:

Our economic program, supported by a Policy Coordination Instrument (PCI) approved by the IMF Executive Board on July 18, 2018, builds on the precautionary Stand-By Arrangement successfully completed in February 2018 and aims at maintaining macroeconomic and financial stability and advancing an ambitious structural and institutional reform agenda to foster rapid and inclusive growth, job creation and improved living standards. This Program Statement (PS) describes progress made so far and sets out the economic policies that the Government and the National Bank of Serbia (NBS) intend to implement under the PCI.

Quantitative program targets (QTs) have been met, apart from a minor deviation on the QT for domestic arrears, and good progress has been made on reform targets. The end-September QTs on the fiscal balance and current primary spending have been met. Inflation has remained within the NBS target band and within the inner limit of the program inflation consultation clause. As a prior action for the review, parliament has approved the 2019 budget consistent with program objectives.

The implementation of our program will continue to be monitored through quantitative, indicative, and reform targets, and an inflation consultation clause, as described in the PS and the attached Technical Memorandum of Understanding (TMU). Reviews by the Fund will be completed on a semi-annual basis to assess progress in implementing the program and reach understandings on any additional measures that may be needed to achieve its objectives.

We believe that the policies set forth in this PS are adequate to achieve the objectives of the PCI-supported program, and we will promptly take any additional measures that may become appropriate for this purpose. We will consult with the Fund on the adoption of these measures and in advance of revisions to the policies contained in this PS. Moreover, we will provide all information requested by the Fund to assess implementation of the program.

In line with our commitment to transparency, we wish to make this letter available to the public, along with the PS and TMU, as well as the IMF staff report on the request for a PCI. We therefore authorize their publication and posting on the IMF website, subject to Executive Board approval. These documents will also be posted on the official website of the Serbian government.

Sincerely,

/s/
Ana Brnabić
Prime Minister

/s/
Jorgovanka Tabaković
Governor of the National Bank of Serbia

/s/
Siniša Mali
Minister of Finance

Attachment: Technical Memorandum of Understanding

Program Statement

1. **This program statement sets out our economic program for the rest of this year and 2019.** The program aims to strengthen the foundation for healthy economic growth by addressing Serbia's short-term and medium-term economic challenges. To this end, the program focuses on policies to ensure macroeconomic stability, most notably by maintaining fiscal sustainability, bolster financial sector resilience, and improve competitiveness.

2. **Macroeconomic policies have remained sound.** The fiscal balance is expected to remain in surplus in 2018. Public debt is on a firm downward path, and the external position is broadly in line with fundamentals. Monetary policy has kept inflation under firm control, while supporting economic activity and maintaining broad exchange rate stability. The stronger confidence associated with the improved macroeconomic situation has been reflected in higher private investment and supported employment and growth.

3. **We are making progress on structural reforms, but further efforts are needed to ensure Serbia is put on a faster convergence path.** We have made progress in implementing our structural reform agenda—in particular reform of tax administration and resolution of SOEs. Our plans envisage measures to foster private sector-led growth, reduce the size of the shadow economy, and complete reforms in public administration and restructuring of state-owned utilities, enterprises, and financial institutions. We will continue to advance reforms in public finance and tax administration, while strengthening public investment management frameworks.

4. **The goals of the economic program are compatible with our aspirations to join the EU, having started the accession process in January 2014.** Implementing this program will allow Serbia to realize the sizable potential for convergence towards EU income levels.

Recent Economic Developments and Outlook

5. **Strong macroeconomic performance continues.** Growth accelerated in the first half of 2018 (4.9 percent year-on-year) supported by private consumption and strong investment and exports. Labor market indicators continue to improve, with robust employment growth in the formal sector and declining unemployment. Private sector wages are rising steadily and the minimum wage will increase by 8.6 percent from January 1, 2019. Headline inflation has remained in the lower half of the inflation target range (at 2.2 percent yoy in October), while core inflation remains low and stable at around 1 percent.

6. **We expect the consistent implementation of the policy actions and reforms envisaged under our economic program to maintain the virtuous cycle of boosting confidence, improving private sector dynamism, and fostering jobs and growth**.

- **Real GDP growth** is projected at 4.2 percent in 2018 and 3½ percent in 2019, rising to 4 percent over the medium term. Full implementation of our structural reform agenda will further boost growth potential.

- **Inflation** is projected to remain in the lower half of the inflation target band over 2018 and 2019, and at around 3 percent over the medium term.

- **The current account deficit** is projected at about 5¼ percent of GDP in 2018, driven by investment-related imports, and to decline to around 4 percent of GDP over the medium term. The projected deficit will continue to be fully financed by net FDI. External financing will continue to rely mostly on FDI, and bilateral and infrastructure project loans.

ECONOMIC POLICIES

A. Fiscal Policies

7. Strong fiscal performance continued in the first nine months of 2018. The general government recorded a surplus of RSD 54.3 billion in the period January-September, compared to the adjusted program target of RSD 48.9 billion. Capital spending execution has been strong, while current spending, including mandatory spending on wages and pensions, grew in line with expectations. Public debt fell below 57 percent of GDP at end-September, while yields on government securities have stabilized near record-low levels.

8. We are committed to preserve the hard-won fiscal gains to keep the public debt-to-GDP ratio firmly on a downward path, while supporting growth. For 2018, we project a general government surplus of 0.6 percent of GDP, unchanged from the program request. Receipts from the airport concession will be used to reduce debt and to boost liquidity buffers. Public debt is projected to decline further, while the debt profile will continue to improve, with increased maturity and higher share of dinar-denominated debt.

9. For 2019, we will aim at an overall deficit of ½ percent of GDP, in line with program objectives. This stance will imply a reduction of public debt to about 52 percent of GDP by end-2019. As a **prior action**, the National Assembly approved the 2019 budget consistent with program fiscal parameters.

- We will increase capital spending by RSD 32 billion to address Serbia's sizeable infrastructure needs.

- We will moderately reduce the tax burden on labor by abolishing the employer part of the unemployment contribution.

- We will reduce or abolish some fees and charges related to non-tax revenue of the central government, through the amendment of the Law on Charges.

- We have unwound the crisis-era temporary pension cuts and introduced a supplement to lower pensions of up to 5 percent, effective in November 2018, while ensuring that the pension bill does not increase in percent of GDP.

- We will begin to unwind the crisis-era wage cuts for public enterprises and SOEs over the next two years, while ensuring that the general government wage bill does not increase in percent of GDP compared to 2018. The law on temporary wage cuts will remain in force for all other public entities until the implementation of the new public wage system.

10. We will aim to further reduce fiscal risks and will prepare contingency measures as needed. We will maintain an adequate level of fiscal buffers and will not accumulate public sector external debt payment arrears (continuous target). We will also refrain from accumulating domestic payment arrears. Our efforts to contain public spending will be monitored through a ceiling on current primary expenditure of the Serbian Republican budget, excluding capital spending and interest payments (quantitative target).

B. Structural Fiscal Policies

11. We are committed to complete the general government employment and wage system reforms, which are critical for improving the efficiency of public services and containing current expenditure.

- **General government employment framework.** The current framework is governed by (i) the annual Law on the Maximum Number of Employees, which sets the employment ceiling on permanent staff at the institution level; and (ii) an employment freeze, with exceptions managed through the government Employment Commission, considering individual institutions' employment ceilings, budgetary envelopes, and specialist staffing needs. This system, which includes local public enterprises, has helped to reduce public employment, but also resulted in reliance on fixed-term and contractual positions and staffing shortages in some units. We will examine options to replace the existing framework with a more flexible system while containing fiscal pressures from public sector wages, ensure adequate allocation of staffing across the public administration, and restrain hiring by public enterprises. We will adopt a decision on a revised public employment framework for 2020 (**new end-September 2019 RT**).

- **Public wage system reform.** The Law on Public Sector Employees Wage System approved in 2016 sets the stage for a new system where employees are granted equal pay for equal work across the government, in a more transparent and systematic manner. Secondary legislation for local governments and public services (health, education, culture, and social protection) was approved in December 2017. We have mapped employees to the new wage matrix and will adopt secondary legislation for all other sectors (including police and armed forces) in 2019. The decree specifying the coefficients under the new wage system has not yet been adopted (**end-September reform target**), and we intend to pass it in time for the preparation of the 2020 budget.

We will set the base under the new wage system to prevent an increase of the general government wage bill as a share of GDP.

12. To improve execution and reduce gaps in the quantity and quality of public infrastructure, we are strengthening the public investment management framework. We will continue to include all project loans in the budget. In April, we adopted the Planning System Law, which established a national planning framework and will lead to preparation of a National Development Plan and a corresponding Investment Plan by 2020. We are committed to improve the public investment management framework in line with recommendations of IMF technical assistance. We will:

- Issue a detailed guideline as a Rule Book to the 2017 decree on capital expenditure projects covering project appraisal and selection (**end-January 2019 reform target**) and publish summaries of feasibility studies of large and mega projects, as defined in the guideline.

- Establish the Capital Investment Commission (CIC) and update the 2017 decree on public investment project appraisal to (i) clarify the roles of the MOF, CIC, and Expert Commission; and (ii) remove the exclusion of IPA-funded projects as well as those financed through government-to-government agreements (**end-April 2019 reform target**).

13. To raise the efficiency of revenue collection and improve the business environment, we are committed to improve tax administration. This work is based on recommendations of IMF technical assistance and the Tax Administration Diagnostic Assessment Tool review.

- The Transformation Action Plan (TAP, 2018-23) approved by the government in December 2017 provides strategic guidance and timelines on actions needed to create a modern tax administration utilizing electronic business processes, improved taxpayer services, and a risk-based approach to compliance.

- The first phase of reforms envisages (i) the separation of core and non-core activities administered by the STA to be supported by separate organizational structures with their own program budget allocation, headquarters design, business plans, management structures, and reporting lines; and (ii) a consolidation of core tax administration functions into fewer sites (**end-June 2019 reform target**). The STA has identified 38 branch offices to be retained in the first round of consolidation of core activities. External consultants have been engaged to analyze the workflows and resource needs for each business stream, develop appropriate organization and management structures, and provide a road map for implementation of the new arrangements, which will be completed by mid-January 2019. To ensure prompt implementation of the TAP, we will also engage consultants with expertise in project management, workforce planning and change management to strengthen the STA reform project management and governance arrangements.

- The second phase of reforms aims at the modernization of IT and records management systems and business process re-engineering. A decision on the preferred approach to redeveloping the IT system will be adopted, with the assistance of an external consultant, by April 2019.

- We have started to introduce measures to reduce the average processing time for VAT refunds. Refunds are processed according to the legally prescribed timelines and the STA takes a cautious approach to minimize fraud. We are monitoring the stock of pending refunds with an aim to substantially reduce the processing time, with a specific target to be determined following the modification of the VAT-management software in October.

14. We will use existing fiscal space on measures to support growth and improve the business climate. To reduce the labor tax wedge, we have abolished—effective January 2019—the employers' part of the unemployment contribution. We are introducing a set of measures to promote innovation and R&D, including revised depreciation allowances, full recognition of marketing costs, relief of tax burden on earnings in the form of stock options, tax relief on recreational benefits for employees, increased tax deduction of R&D costs, and IP box tax incentives. We have submitted the draft Law on Charges to parliament (end-October reform target) with a view to adopt it by parliament by end-December. This law aims at consolidating all parafiscal charges faced by businesses in one law to reduce uncertainty and increase transparency, while also eliminating or merging some charges.

15. Over the program period, we will strengthen fiscal frameworks, including tax policy, intergovernmental fiscal relationships and fiscal rules. Tax policy reform will focus on strengthening competitiveness and rationalizing revenue sharing and transfers to local government. We will revise fiscal rules to achieve the following principles: (i) stronger institutional significance of the debt limit as the primary medium-term anchor for fiscal policy; (ii) a more transparent and credible operational rule to help achieve the objective, while also helping to improve accountability and facilitate transition towards the EU fiscal framework; and (iii) a retain a strong role of the Fiscal Council. To ensure a more rules-based pension system, we will reintroduce indexation of pensions for 2020.

16. We will continue implementing public financial management measures.

- To prevent arrears, we will continue the publication of monthly reporting of overdue receivables to Srbijagas and EPS of their top 20 debtors on the companies' websites.

- We have been strictly limiting issuance of state guarantees since 2015. We will not issue any new state guarantees for liquidity support, or state guarantees for any company in the portfolio of the former Privatization Agency. The Government will continue to refrain from issuing any implicit state guarantees.

- We have developed a new software for the Public Debt Administration aiming at establishing a custom-made debt management system to enable efficient and precise debt recording and reporting. This system will serve as the foundation for risk management and future tool for strategic analysis.

17. To safeguard fiscal consolidation, limit risks, and strengthen institutions:

- We will continue to submit financial plans of social security funds with estimates for their indirect beneficiaries to the National Assembly, in parallel with the Republican budget. We will include all indirect budget beneficiaries of the central government (except for indirect budget beneficiaries of the Ministry of Education, Science and Technological Development) in the Information System for Budget Execution (ISIB) gradually by end-2019. We have upgraded the budget execution system to be able to support the integration of new users. We have included institutions for the enforcement of penal sanctions and cultural institutions in ISIB since January 1, 2018. In 2019, social protection institutions will be integrated.

- We are committed to ensure that a full assessment of all proposed Public-Private Partnerships (PPPs) is reviewed by the Ministry of Finance (MOF), including PPPs' key financing features, cost-benefit analysis, and risk sharing arrangements with the government. To improve control of fiscal implications and risks, we amended the existing Law on Public-Private Partnership and Concessions mandating that PPPs larger than EUR 50 million are submitted to the government for consideration only after receiving the MOF's consent. By end-2018, we will adopt additional amendments to the Law aimed at limiting overall fiscal exposure, ensuring a competitive tender process.

- The fiscal risks management unit at the MOF will be fully staffed by end-2018.

C. Monetary and Exchange Rate Policies

18. The current inflation targeting framework remains appropriate for maintaining stable inflation and protecting the economy against external shocks. We remain committed to the objective of keeping inflation within the tolerance band (3±1½ percent). Inflation developments will continue to be monitored via a consultation clause with consultation bands set around the central projection (Table 1). In this context, we have kept the key policy rate unchanged since April, reflecting internal and external conditions.

19. We will maintain the current managed float exchange rate regime in line with the inflation targeting framework. We believe that well-managed exchange rate flexibility provides a needed buffer against external shocks. Therefore, foreign exchange interventions will continue to be used to smooth excessive short-term exchange rate volatility without targeting a specific level or path for the exchange rate, while considering the implications for financial sector and price stability. The current level of gross international reserves is comfortable for precautionary purposes.

20. We have made progress in advancing our dinarization objective. The dinarization strategy adopted in 2012 is based on three pillars: (i) maintaining overall macroeconomic stability; (ii) creating favorable conditions for developing the dinar bond market; and (iii) promoting hedging instruments. Macroeconomic imbalances have been reduced significantly and inflation has remained low and stable, which should all support dinarization. We have introduced several measures to increase dinarization, such as higher reserve requirements on FX deposits and mandatory down-payment ratios for FX loans. We have also enhanced our communication to the public on the risks of unhedged FX borrowing, need of prudent management of FX risks, availability of hedging instruments, and promoting dinar savings. Meanwhile, we have increased the share of public debt in local currency, issuing dinar securities at longer maturities (up to 10 years). The Law on Financial Collateral adopted earlier this year will improve legal certainty with regard to the development of the repo and financial derivatives markets. In October, we introduced a new instant payment system, which will encourage broader use of dinar mobile payments and help reduce informality. Currently, banks are obliged to provide at least one channel for instant payments, but starting from April 2019, banks will have to enable instant payments on all available channels that they provide (at the counter, through m-banking/e-banking applications, at the point of sale, etc.). By September 2018, deposit dinarization has increased to 31 percent, while household lending dinarization has also increased, exceeding 53 percent.

21. We are updating our dinarization strategy (end-December reform target) to facilitate dinarization, further strengthen liquidity management, and develop local currency debt and hedging markets. Specifically, we plan to:

- Continue efforts to (i) further instill awareness of two-way exchange rate movements (ii) further develop local and foreign currency derivative markets, and (iii) encourage prudent pricing of credit risks of unhedged foreign currency borrowing.

- Strengthen public debt management by (i) updating by the Ministry of Finance the legal foundation of debt management (**end-December reform target**), (ii) establishing the primary dealer system and developing adequate supervisory framework, and (iii) improving the PDA's operational framework, and setting up a Debt Market Committee comprising of representatives of the PDA and the MOF. We will set up a working group comprising of representatives of the PDA, MOF, primary dealers, and other relevant institutions to implement the primary dealership system.

- Further strengthen the liquidity management framework. With this aim, we are (i) formalizing the communication between the NBS and the Ministry of Finance (through a Service Level Agreement) concerning exchange of information; and (ii) establishing a Consultative Committee on Liquidity Management aimed at strengthening the management and oversight of the Consolidated Treasury Account balance and improving the quality of liquidity forecasting.

22. During the period of the PCI we will not, without IMF approval, impose or intensify restrictions on the making of payments and transfers for current international transactions, nor introduce or modify any multiple currency practices or conclude any bilateral payment agreements that are inconsistent with Article VIII of the IMF's Articles of Agreement. Moreover, we will not impose or intensify import restrictions for balance of payments reasons.

D. Financial Sector Policies

23. We will continue to strengthen financial sector regulatory and supervisory frameworks, to fully align them with international standards. Basel III compliant regulatory standards on capital and liquidity were implemented in June 2017 and IFRS 9 has been implemented since January 2018. We will continue to enhance the prudential framework for banks and insurance companies to ensure full compliance with international standards and EU requirements. We will also work on further harmonizing our financial legal framework with EU Acquis taking into account the specificities of the Serbian financial market.

24. We will further enhance financial safety nets. Significant progress has been achieved in strengthening the bank resolution, deposit insurance, and crisis management frameworks. We will further align the deposit insurance scheme with international standards. A review of the appropriate parameters of the deposit insurance fund, including the target level, premium, deposit base for calculation, and investment policy, and a IADI core principles assessment will be completed by December. We will submit to parliament amendments to the Law on Deposit Insurance Agency and the Law on Deposit Insurance to reflect the findings of the review and assessment and introduce risk-based premia (**end-June 2019 reform target**).

25. Results of the implementation of the NPL resolution strategy have been impressive, but SOBs still lag. As of September, the NPL ratio reached 6.4 percent, but progress has been uneven. In private banks, sizeable NPL sales helped lower NPLs to below pre-crisis levels (about 6 percent in September). Although NPLs remain relatively high for some SOBs (10.5 percent in September, on average), they are fully covered by regulatory reserves for estimated losses and significant improvements have been made driven primarily by write-offs. By end-December, we will update, with support of IFIs, our NPL resolution strategy, focusing on measures to accelerate NPL resolution in SOBs, while also broadening the scope to include the export credit agency (AOFI), the Development Fund (DF), and the bad assets managed by the Deposit Insurance Agency (DIA) on behalf of the State and the bankruptcy estates of banks in liquidation. In line with the updated strategy, the government and the DIA, as an end-December reform target, will: (i) approve a time-bound action plan to resolve the DIA portfolio of bad assets by end-2020 through a tendering process implemented in two phases (portfolios of about EUR 230 million and EUR 830 million consisting of both bad assets managed on behalf of the state and on behalf of bankrupt banks, as agreed with the World Bank); and (ii) complete the first phase of the sale by end-December (**end-December reform target**). The action plan will also propose options to resolve the residual portfolio of low-value assets. The DIA has engaged consultants to prepare the first phase of the tender process based on the portfolio of bad assets agreed with the World Bank, and the tender process was initiated in October. We will launch the tender for the second phase, in line with the time-bound action plan **(new end-September 2019 reform target)**.

26. We will continue to implement our state-owned financial institutions reform agenda. We are strengthening our oversight over financial institutions with state-ownership.

- We are implementing the new strategy for Banka Postanska Stedionica (BPS). The focus of the strategy is on (i) the bank's commercial reorientation towards retail banking, entrepreneurs, micro-enterprises and small enterprises, (ii) improvements of the bank's internal organization, corporate governance and risk management, (iii) enhancement of its IT infrastructure, and (iv) a business plan for the period 2018-20. BPS will sign contracts with external consultants for the procurement and implementation support of a new core banking system by end-2018.

- We have launched a tender for a privatization advisor for Komercijalna Bank. We will adopt a decision to initiate privatization by end-February 2019, with a view to launch a privatization tender (**end-June 2019 reform target**) and complete the sale by end-December 2019. Meanwhile, the bank is implementing necessary measures to address corporate governance weaknesses, in line with NBS recommendations.

- We are working on the implementation of strategic options for the smaller banks, based on the updated government strategy for state-owned banks. In April, we (i) withdrew the banking license of Jugobanka Jugbanka and approved a takeover of part of the bank's assets and liabilities to BPS, after protracted efforts to find a strategic investor to recapitalize the bank failed; and (ii) initiated procedures concerning the sale of the State's shares in Jubmes Bank and expect to complete this transaction by end-2018.

- The DF and AOFI have continued to implement (i) the supervisory boards' decisions recognizing losses on their credit portfolios and (ii) the government conclusion to restrict the institutions' exposures to SOEs, enhance risk management frameworks and prevent further deterioration in asset quality, and establish a timeline to resolve impaired assets.

27. We are strengthening the AML/CFT framework in line with the FATF action plan. We have advanced in addressing shortcomings identified in the 2016 MONEYVAL AML/CFT mutual evaluation report through an inter-agency working group, with the aim to complete the work ahead of the January 2019 deadlines agreed with the FATF. The Law on Anti-Money Laundering came into effect on April 1 defining notaries as a new obliged entity and providing a clear legal base for the STA to start inspection in two casinos. A targeted National Risk Assessment (NRA) was completed in June, with support from the World Bank. We have also passed numerous other laws, regulations, and guidelines addressing specific recommendations in the MONEYVAL report, including on politically exposed persons, public notaries, correspondent banking, beneficial ownership, supervision of groups and foreign branches, and sanctioning regimes. We are committed to implement all measures listed in the action plan to address the AML/CFT weaknesses identified by the FATF (**end-February 2019 reform target**).

28. We will work on strategies for capital market deepening and development finance. Serbia's capital markets remain underdeveloped with limited stock-market activity, nascent domestic bond market volumes, and a virtually nonexistent corporate bond market. Alternative sources of financing such as private equity or venture capital, are negligible. We have established a working group to draft, with the World Bank support, a strategy for development finance by end-December 2019. We are currently undertaking a diagnostic assessment focused on developing capital markets and diversifying sources of long-term financing. This diagnostic report will be prepared with the support of the World Bank, with a view to inform the government's strategy to enhance capital markets.

E. Structural Policies

29. We will implement a comprehensive set of structural reforms to improve the business environment to support higher private sector-led growth. Our focus is on policies that improve the business environment and private investment climate, promote job creation, and complete the resolution of public and state-owned enterprises.

30. We are implementing measures to fight the grey economy. In December 2015, we adopted a National Program for Countering the Grey Economy and an Action Plan for the Implementation of the National Program for 2016-2017, which was updated in 2017 to cover 2018-19. Our priorities include improvements in the inspection system (better coordination and increased usage of IT systems), modernization of Tax Administration (risk-based audits, trainings, reorganization, and better control of trading in excise goods), strengthening of incentives for voluntary compliance, and improving the business environment to encourage entrepreneurship and innovation. In this regard, we have amended the Law on Inspection Supervision (**end-September reform target**) and aligned all sectoral laws and introduced new inspection tools to permit supervision of unregistered activities. We will also improve coordination across inspections by developing e-inspection software, which provides a horizontal e-platform facilitating full implementation of a risk-based approach to inspection oversight.

31. We are implementing measures to further increase labor force participation:

- In June, we adopted the Law on Simplified Seasonal Employment in Specific Industries defining rights and obligations in the context of seasonal work and allowing simplified registration of seasonal workers.
- By end-2018, we will adopt the Law on Work Through Temporary Employment Agencies, which will contribute to improving labor conditions for agency employees working in beneficiary companies, eliminate unfair competition in this area, and increase employment.

- We have amended the Law on Financial Support for Families with Children to increase the bonuses for child birth aimed at raising fertility rates, completing the replacement of the previous entitlement to VAT reimbursement for baby food and equipment.

32. We are committed to continue restructuring large public utilities companies to enhance efficiency and contain fiscal costs. We are planning to fully implement the required corporate and financial restructuring in these companies over the medium term.

- **Elektroprivreda Srbije (EPS).** We have continued implementing the 2016–19 labor optimization plan. We have engaged the World Bank and the EBRD to support our plan to enhance corporate governance, management, and procurement and planning frameworks. A time-bound action plan prepared by the EBRD to improve management will be adopted in December. In 2020, we will change the legal status of EPS to a joint stock company, in line with the ongoing corporate restructuring process and financial consolidation, aiming to improve the viability of the company and ensure its professional management. As an interim step, in 2019 we will adopt a government decision to establish ownership rights of all property and assets.

- **Srbijagas.** Payment discipline has improved and an investment appraisal methodology proposed by the World Bank based on an economic and financial cost-benefit framework and including other relevant appraisal criteria, has been adopted in November 2017. We will adopt a capital expenditure plan in line with the new methodology by end-2018. These measures will help improve Srbijagas' financial position and put the company on a sustainable path. We will ensure phasing out Srbijagas' reliance on government support for servicing debt by the end of the program period.

33. We will make progress on the few strategic companies in the portfolio of the former Privatization Agency for which resolution is still pending:

- After the unsuccessful second tender to privatize MSK, we intend to launch a third one after exploring options with potential strategic investors.

- After failed attempts to find a strategic investor for Azotara, the Ministry of Economy requested the State Attorney Office to initiate bankruptcy procedures, and these were initiated by the court in September.

- We have selected a Chinese mining company as a strategic investor for RTB Bor, and the transaction will be completed by end-2018.

- We intend to launch the privatization tender for Petrohemija by end-February 2019 following ongoing discussions with potential investors (**end-September reform target, reset to end-February 2019**).

- A privatization tender for PKB was closed on September 10. A UAE-based company was selected and the transaction will be completed by end-2018.

- We are developing, with the assistance of the World Bank, an action plan for Resavica mines. By end-2018, we will (i) begin the closure procedures of two unviable mines; and (ii) update the closure timetables for at least two additional unviable mines, and (iii) develop a voluntary social program and labor optimization plans and ensure that sufficient resources are allocated in the 2019 budget.

34. We continue to resolve enterprises in the portfolio of the former Privatization Agency through either privatization or bankruptcy, in accordance with the revised Privatization Law. By September 2018, more than 310 companies entered bankruptcy, and 54 were privatized since end-2014. About 34,800 employees from 336 companies have received severance payments. 92 companies with nearly 39,000 employees remain.

35. We intend to develop a strategy for SOEs during 2019. The strategy will provide an integrated approach to oversight and monitoring of SOE operations, financial consolidation, restructuring or divestment plans, and measures to improve governance and institutional frameworks.

36. We are working to improve the quality and transparency of our national statistics:

- We commit to comprehensive, timely, and automatic data sharing across relevant compiling agencies (including SORS and NBS) for statistical purposes (updating existing or signing new memorandum of understandings where necessary).

- In April 2018, we published the list of institutional units that are defined as part of the general government as well as other main sectors of the economy, in line with European System of Accounts (ESA) 2010 and GFSM 2014. By the end of the program, the Serbian Statistical Agency (SORS) will submit monthly GFSM 2014 fiscal accounts to the Enhanced General Data Dissemination System (eGDDS), covering the budgetary government and road funds.

- In June 2018, we subscribed to the IMF's eGDDS. We will continue to improve our data standards by publishing a 12-month ahead data release calendar for the Ministry of Finance by end-December 2018, to support our goal of achieving the top threshold of eGDDS by the end of the program period. In December 2018, we will also subscribe to the World Bank/IMF Public Sector Debt Statistics Database covering core debt of the budgetary central government. Public sector debt data will be transmitted quarterly for loans and debt securities covering budgetary central government units valued at face value.

- In conjunction with Eurostat and the IMF, we are working to upgrade our national accounts. In October, we released revised annual GDP time series for the period 2015–17, and in November we also released revised quarterly series for the same period. We continue to develop and improve metadata to support compilation processes, in particular the informal economy, and will make new metadata available on the SORS website by end-December 2018. We are also developing supply and use tables (SUT) for 2015-17, to be disseminated by September 2019.

PROGRAM MONITORING

37. Progress in the implementation of the policies under this program will be monitored through quantitative targets (QTs) and indicative targets (ITs)—including an inflation consultation clause, continuous targets (CTs) and reform targets (RTs). These are detailed in Tables 1 and 2, with definitions provided in the attached Technical Memorandum of Understanding.

Table 1a. Serbia: Quantitative Program Targets 1/

	2018							2019			
	Mar.	Jun.		Sep.			Dec.	Mar.	Jun.	Sep.	Dec.
	Act.	Proj. CR 18/237	Act.	Prog. QT CR 18/237	Adj. Prog.	Act.	IT 6/	Prog. QT	IT 6/	Prog. QT	IT 6/
I. Quarterly Quantitative Targets (QT)/Indicative Targets (IT)											
1 Ceiling on the general government fiscal deficit 2/ 3/ (in billions of dinars)	-3.7	-22.8	-32.9	-31.3	-48.9	-54.5	-1.6	18.9	2.2	7.5	29.0
2 Ceiling on current primary expenditure of the Serbian Republican Budget excluding capital expenditure and interest payments (in billions of dinars) 2/	198.8	428.1	422.8	648.7	647.9	639.8	921.3	221.9	457.8	686.1	950.3
3 Ceiling on accumulation of domestic payment arrears by the consolidated general government except local governments, the Development Fund, and AOFI (in billions of dinars)	-0.2	0.0	0.1	0.0	...	0.2	0.0	0.5	0.5	0.5	0.5
II. Continuous Targets											
4 Ceiling on accumulation of external debt payment arrears by General Government, Development Fund, and AOFI (in billions of euros)	0.0	0.0	0.0	0.0	...	0.0	0.0	0.0	0.0	0.0	0.0
III. Inflation consultation band (quarterly) 4/											
Upper band limit (1.5 percent above center point)				3.0			4.1	4.4	3.5	4.0	3.9
End of period inflation, center point 5/	*1.4*	*1.6*	*2.3*	*1.5*	...	*2.1*	*2.6*	*2.9*	*2.0*	*2.5*	*2.4*
Lower band limit (1.5 percent below center point)				0.0			1.1	1.4	0.5	1.0	0.9

1/ As defined in the Program Statement and the Technical Memorandum of Understanding.
2/ Cumulative since the beginning of a calendar year.
3/ Refers to the fiscal balance on a cash basis, including the amortization of called guarantees.
4/ Staff level consultation is required upon breach of the band limits.
5/ Defined as the change over 12 months of the end-of-period consumer price index, as measured and published by the Serbian Statistics Office.
6/ Indicative targets are not monitored as part of the program conditionality.

Table 1b. Serbia: Standard Continuous Targets

Not to impose or intensify restrictions on the making of payments and transfers for current international transactions.
Not to introduce or modify multiple currency practices.
Not to conclude bilateral payments agreements which are inconsistent with Article VIII.
Not to impose or intensify import restrictions for balance of payments reasons.

Table 2. Serbia: Prior Actions and Reform Targets

	Actions	Target Date	Status	Objective
	Prior Actions			
1	Adoption by the National Assembly of the 2019 budget consistent with program objectives.		Met.	Increase fiscal transparency.
	Reform Targets			
	Fiscal			
1	Approve a government decree defining wage coefficients under the new Public Sector Employee Wage System for local governments, public services, and public administration.	End-September, 2018	Not met.	Rationalize pay and improve incentives across public sector.
2	Submit to the National Assembly a draft Law on Charges.	End-October, 2018	Not met. Submitted in November.	Improve transparency and predictability, reduce parafiscal tax burden on businesses.
3	Issue a detailed rule book to the 2017 Capital Project Regulation, covering methodology for project appraisal and selection.	End-January, 2019		Unifies methodology for the project and cost-benefit analysis and raise transparency.
4	Establish Capital Investment Commission (CIC) and update Capital Project Regulation to (i) clarify roles of MoF, CIC, and Expert Commission, (ii) remove the exclusion of IPA-funded projects, and (iii) expand the coverage to government-to-government agreements.	End-April, 2019		Improve selection, appraisal, and implementation of public infrastructure projects.
5	Complete consolidation of core STA activities into fewer sites.	End-June, 2019		Advance reforms of the State Tax Administration.
	Financial			
6	Approve a time-bound action plan to resolve part of the DIA portfolio of bad assets by end-2020 through a tendering process implemented in two phases (agreed with the World Bank); and complete the first phase of the sale.	End-December, 2018		Resolve bad assets and address fiscal risks.
7	Approve an updated Dinarization Strategy in line with the IMF recommendations.	End-December, 2018		Strengthen financial stability and increase dinarization.
8	Submit to the National Assembly amendments to the Law on Public Debt with a view to update legal foundation of debt management.	End-December, 2018	Met.	Strengthen public debt management.
9	Implement items listed in Serbia's action plan to address the significant AML/CFT weaknesses identified by the FATF.	End-February, 2019		Remove Serbia from FATF listing and prevent pressures on capital inflows and correspondent banking relationships.
10	(i) Submit to the National Assembly amendments to the Law on Deposit Insurance Agency and the Law on Deposit Insurance to incorporate the findings of IADI assessment and update parametrization; and (ii) introduce risk-based premia.	End-June, 2019		Align deposit insurance scheme with international standards.
11	Launch a privatization tender for Komercijalna Banka.	End-June, 2019		Reduce state involvement in the financial sector and reduce fiscal risks.
	Structural			
12	Adopt a government decision to launch a privatization tender for Petrohemija.	End-September, 2018	Not met. Reset to end-February 2019.	Reduce fiscal risks.
13	Approve amendments to the Law on Inspection Supervision.	End-September, 2018	Not met. Approved in December.	Reduce gray economy.
	Proposed New Reform Targets			
14	Adopt a government decision on a revised public employment framework for 2020.	End-September, 2019		Improve employment flexibility while containing fiscal pressures.
15	Issue tenders for the second phase of DIA asset sales, in line with the time-bound action plan.	End-September, 2019		Resolve bad assets and address fiscal risks.

Attachment I. Technical Memorandum of Understanding

1. This Technical Memorandum of Understanding (TMU) sets out the understandings regarding the definition of indicators used to monitor developments under the program. To that effect, the authorities will provide the necessary data to the European Department of the IMF as soon as they are available. As a general principle, all indicators will be monitored on the basis of the methodologies and classifications of monetary, financial, and fiscal data in place on May 18, 2018, except as noted below.

A. Fiscal Conditionality

2. **The general government fiscal deficit** is defined as the difference between total general government expenditure (irrespective of the source of financing) including expenditure financed from foreign project loans, payments of called guarantees, cost of bank resolution and recapitalization, cost of debt takeover if debt was not previously guaranteed, repayments of debt takeover if debt was previously guaranteed, and payment of arrears (irrespective of the way they are recorded in the budget law) and total general government revenue (including grants). For program purposes, the consolidated general government comprises the Serbian Republican government (without indirect budget beneficiaries), local governments, the Pension Fund, the Health Fund, the Military Health Fund, the National Agency for Employment, the Roads of Serbia Company (JP Putevi Srbije) and any of its subsidiaries, and the company Corridors of Serbia. Any new extra budgetary fund or subsidiary established over the duration of the program would be consolidated into the general government. Privatization receipts are classified as a financial transaction and are recorded "below the line" in the General Government fiscal accounts. Privatization receipts are defined in this context as financial transactions.

3. **Current primary expenditure of the Republican budget (without indirect budget beneficiaries)** includes wages, subsidies, goods and services, transfers to local governments and social security funds, social benefits from the budget, other current expenditure, net lending, payments of called guarantees, cost of bank resolution and recapitalization, cost of debt takeover if debt was not previously guaranteed, repayments of debt takeovers if debt was previously guaranteed, and payment of arrears (irrespective of the way they are recorded in the budget law). It does not include capital spending and interest payments.

Adjustors

- The quarterly ceilings on **the general government fiscal deficit** will be adjusted downward (upward) to the extent that cumulative non-tax revenues of the General Government from dividends exceed (fall short of) programmed levels.
- The quarterly ceilings on **the general government fiscal deficit** will be adjusted downward to the extent that cumulative non-tax revenues of the General Government from debt recovery receipts, debt issuance premiums, and concession and Public Private Partnership (PPP) receipts

recorded above-the-line exceed programmed levels. The IMF Statistics Department will determine the proper statistical treatment of any concession or PPP transaction signed during the IMF program.

Cumulative Programmed Revenues of the General Government from Dividends, Debt Recovery Receipts, and Debt Issuance at a Premium

(In billions of dinars)

	End-Sep. 2018	End-Dec. 2018	End-Mar. 2019	End-Jun. 2019	End-Sep. 2019	End-Dec. 2019
Programmed cumulative dividends	17.1	17.1	17.1	17.1	17.1	17.1
Programmed cumulative debt recovery receipts	0	0	2.5	2.5	2.5	2.5
Programmed cumulative debt issuance at a premium	0	0	0	0	0	0
Programmed concession and PPP receipts recorded above the line	0	0	0	0	0	0

- The quarterly ceilings on the **primary current expenditure of the Republican budget** will be adjusted upward (downward) to the extent that (i) cumulative earmarked grant receipts exceed (fall short of) the programmed levels and (ii) cumulative proceeds from small-scale disposal of assets (the sale of buildings, land, and equipment) recorded as non-tax revenues exceed the programmed levels up to a cumulative annual amount of 2 billion dinars in each year. For the purposes of the adjustor, grants are defined as noncompulsory current or capital transfers received by the Government of Serbia, without any expectation of repayment, from either another government or an international organization, including the EU.

Cumulative Receipts from Earmarked Grants and Small-scale Asset Disposal
(In billions of dinars)

	End-Sep. 2018	End-Dec. 2018	End-Mar. 2019	End-Jun. 2019	End-Sep. 2019	End-Dec. 2019
Programmed cumulative ear-marked grants receipts	7.6	14.2	2.5	5.5	9.3	13.9
Programmed cumulative receipts from small-scale disposal of assets	0	0	0	0	0	0

4. Domestic arrears. For program purposes, domestic arrears are defined as the belated settlement of a debtor's liability which is due under the obligation (contract) for more than 60 days, or the creditor's refusal to receive a settlement duly offered by the debtor. The program will include a quantitative target on the change in total domestic arrears of (i) all consolidated general government entities as defined in ¶2 above, except local governments; (ii) the Development Fund, and (iii) AOFI. Arrears to be covered include outstanding payments on wages and pensions; social security contributions; obligations to banks and other private companies and suppliers; as well as arrears to other government bodies.

5. Debt issued at a premium. For program purposes, debt issued at a premium refers to proceeds accruing to the government that are recorded as revenue when the government issues debt at a premium. It most commonly occurs when a bond with an above-market coupon is reopened ahead of a coupon payment.

B. Ceiling on External Debt Service Arrears

6. Definition. External debt-service arrears are defined as overdue debt service arising in respect of obligations incurred directly or guaranteed by the consolidated general government, the Export Credit and Insurance Agency (AOFI), and the Development Fund, except on debt subject to rescheduling or restructuring.[1] The program requires that no new external arrears be accumulated at any time under the arrangement on public sector or public sector guaranteed debts. The authorities are committed to continuing negotiations with creditors to settle all remaining official external debt-service arrears.

[1] Debt subject to rescheduling or restructuring includes the US$44.7 million in arrears to Libya.

7. Reporting. The accounting of external arrears by creditor (if any), with detailed explanations, will be transmitted on a monthly basis, within four weeks after the end of each month.

C. Inflation Consultation Mechanism

8. Inflation is defined as the change over 12 months of the end-of-period consumer price index (CPI), base index (2006=100), as measured and published by the Serbian Statistics Office (SORS). Where the official press release differs from the index calculation, the index calculation will be used.

9. Breaching the inflation consultation band limits (specified in Program Statement, Table 1) at the end of a quarter would trigger discussions with IMF staff on the reasons for the deviation and the proposed policy response.

D. Reporting

10. Net international reserves of the NBS will be submitted within one week of the end of the month.

11. General government revenue data and the Treasury cash position table will be submitted weekly; and the stock of spending arrears as defined in ¶6 45 days after the end of each quarter. General government comprehensive fiscal data (including social security funds) will be submitted within 35 days of the end of each month.

12. The stock of spending arrears (> 60 days past due) as reported in the MOF e-invoice system will be submitted within 14 calendar days after the end of each month.

13. Gross issuance of new guarantees by the Republican budget for project and corporate restructuring loans will be submitted within 35 days of the end of each month.

14. Cumulative below-the-line lending by the Republican budget will be submitted within 35 days of the end of each month.

15. Borrowing by the Development Fund and AOFI will be submitted within four weeks of the end of each month.

16. New short-term external debt (maturities less than one year) contracted or guaranteed by the general government, the Development Fund, and AOFI will be submitted within four weeks of the end of each month.

17. Monthly average VAT refund time, stock of pending VAT refunds, and the value of the VAT refunds provided each month will be submitted by the Serbian Tax Administration within 14 calendar days after the end of each month.

18. Receivables of the top 20 debtors to Srbijagas and EPS will be submitted in the agreed-upon templates within 30 calendar days after the end of each month as well as published on the company websites.

Data Reporting for Quantitative Targets		
Reporting Agency	Type of Data	Timing
Statistical Office and NBS	CPI inflation	Within four weeks of the end of the month
Ministry of Finance	Fiscal deficit of the consolidated general government	Within 35 days of the end of the month
Ministry of Finance	Current primary expenditure of the Republican budget excluding capital expenditure and interest payments	Within 35 days of the end of the month
Ministry of Finance	External debt payment arrears by general government, Development Fund and AOFI	Within four weeks of the end of the month
Ministry of Finance	Gross accumulation of domestic payment arrears by the general government (without local government, the Development Fund, and AOFI)	Within 45 days of the end of the quarter
Ministry of Finance	Earmarked grants and receipts from small-scale disposal of assets	Within four weeks of the end of the quarter