The World Bank in Serbia

# Country Snapshot

*An overview of the World Bank's work in Serbia*

**October 2019**

| SERBIA | 2018 |
|---|---|
| Population, million | 7.0 |
| GDP, current US$ billion | 50.5 |
| GDP per capita, current US$ | 7,220 |
| School Enrollment, primary (% gross) (2016) | 100.6 |
| Life Expectancy at birth, years (2016) | 75.7 |

## At a Glance

- After a fiscal surplus in 2018, Serbia will have a small deficit in 2019 of about 0.5% of GDP. The government decided to increase salaries in the public sector, as well as some discretionary expenditures, which means that expenditures will be higher than otherwise well-performing revenues.

- Labor market outcomes improved. Average activity rate continued to increase from 54.5 percent in 2018 to 54.8 in Q2 2019. Employment reached a record 49.1 percent in Q2 2019.

- The World Bank program supports the Government's implementation of complex structural reforms, with a focus on changing the role and size of the state and on stimulating the private sector and attracting more investment. Some of the most difficult companies (e.g., RTB Bor and PKB) were resolved in 2018.

## Country Context

The global financial crisis exposed the structural weaknesses in Serbia's economic growth model and prompted the need for fiscal consolidation and an acceleration of the unfinished transition to a market economy.

Serbia's rapid growth in 2001–08 was driven mainly by domestic consumption and led to significant internal and external imbalances that proved to be unsustainable.

The Government formed after the April 2016 elections stepped up the implementation of structural reforms, broadening the focus to include social sector transformation.

Although the results of the spring 2017 presidential election led to a change in prime minister (as the incumbent became Serbia's new president), the Government experienced only minor changes, enabling it to maintain an emphasis on reforming state administration, public finances, and the economy, along with pursuing the European Union (EU) accession process.

The Government's economic reform program focuses on ensuring economic and financial stability, reducing debt, and creating an environment for economic recovery and growth to foster employment and raise living standards. There have been signs lately that the government is wavering on reforms.

## The World Bank and Serbia

The overarching goal of the World Bank Group's (WBG) Country Partnership Framework for 2016–20 is to support the creation of a competitive and inclusive economy in Serbia and through this, achieve the country's integration into the EU.

The strategy is based on available evidence and expertise and focused on reducing poverty and increasing prosperity across Serbian society in a sustainable manner. Key areas of WBG support in Serbia include:

- restoring fiscal and macroeconomic stability;
- creating conditions for accelerated private sector growth and job creation;
- improving infrastructure;
- strengthening public sector management and improving public service delivery to citizens.

These focus areas emerged from six fundamental priorities identified by a comprehensive Systematic Country Diagnostic that examined the key challenges constraining growth and greater shared prosperity.

The active portfolio reflects these priorities through 13 projects in the areas of transport, real estate management/business environment, competitiveness and jobs, health, flood recovery and flood protection, disaster risk management, financial sector reform, public sector modernization, including digitalization of selected public services and modernization of tax administration, and early childhood education.

## Key Engagement

The WBG has engaged in a multi-faceted effort to address Serbia's complex legacy reforms, including commercial SOE reform, financial consolidation in public utilities and public transport companies, and more efficient and competent core public administration.

### WORLD BANK PORTFOLIO

No. of Projects: 13
IBRD Lending: $1.09 Billion
EU Trust Funds: 3 (€7.9 Million)

More than four years of intensive dialogue and technical advice, combined with policy-based and results-based lending, have started to yield important and increasingly impressive results.

Key operations included the **Public Enterprise and Public Utilities Development Policy Lending (DPL)** series, the **Competitiveness and Jobs Project**, the Program for Results in support of Public Administration Modernization and Optimization, the State-Owned Financial Institutions Reform Project as well as the Program for Results in support of Enhancing Infrastructure Efficiency and Sustainability.

In FY 2019, two new operations were added: the **Tax Administration Modernization Project**, and the **Enabling Digital Governance Project**.

As a result of these efforts, for example, public utilities are returning to financial health with gradually improving services, and the local scientists are linking with enterprises to commercialize their innovations, thus contributing to growth and jobs.

Next generation reforms are focusing on a new growth agenda and deepening public sector reforms to promote economic initiative, entrepreneurship, innovation, and the digital economy.

## Recent Economic Developments

Based on the latest estimates, y-o-y growth in the first and second quarter of 2019 reached 2.7 and 2.9 percent, respectively. Given this performance, the growth projection for 2019 has been revised downwards from 3.5 percent to 3.3 percent.

As in the past, strong consumption and investment is not sufficient to compensate for an increasing negative contribution of net-exports to growth, with increasing consumption (both public and private) to a large extent matched by increased imports.

Looking at sectors, industrial output fell by 2 percent in the first half of the year, including a 2.8 percent decrease in manufacturing. Agriculture output is projected to decline or stagnate.

Growth has contributed to labor market improvements. The Q2 activity rate and employment rate among population aged 15 and above continued to increase in 2019, reaching 54.8 and 49.1 percent, respectively.

The employment rate remains lower among female workers and youth. Unemployment declined to an estimated 10.3 percent in the second quarter of 2019 (the unemployment rate for population aged 15-64 stood at 10.8 percent).

In the first half of 2019, average wages increased by 9.9 percent in nominal terms (in real terms 7.2 percent). The private/public sector wage gap has narrowed, with private sector wages growing by 10.7 percent compared to 9.5 percent in the public sector.

Thanks to these trends, combined with higher pensions, poverty (living on income under $5.5/day in 2011PPP terms, the standardized middle-income-country poverty line) is estimated to have declined from 23.8 percent in 2014 to 19.8 percent in 2019.

The consolidated general government budget showed a surplus of 0.3 percent of GDP in the first half of 2019. Revenues increased by 7.6 percent in nominal terms, compared to the same period of 2018. Budgetary spending rose by 9.6 percent in nominal terms, corresponding to 1.7 percent of annual GDP.

Inflation is on a declining path, after reaching a peak in April of 3.1 percent (y/y). External imbalances widened as evidenced by an increase in the CAD by 51 percent in the first half of the year, now projected at 6.7 percent of GDP for 2019. FDI inflows remain strong – up 28 percent in the first half of the year. Total external debt continued to decline as a share of GDP, to 62.5 percent at end-March 2019. Public debt declined to 54 percent of GDP by end-June 2019.

## Economic Outlook

The economy is expected to continue to grow at around 3-4 percent over the medium-term. Investment and consumption will be the main drivers of growth. Consumption will increase as wages and employment are expected to continue to grow. The rising consumption will continue to push up imports, widening the CAD.

The medium-term growth projections crucially depend on the pace of structural reforms and political developments.

Acceleration of the EU accession process is important not only from the point of view of strengthening institutions but also as a signaling device to attract investment. Short- to medium-term growth prospects may be affected by lead times for the election campaign and formation of the government.

With economic growth and improvements in the labor market, poverty is expected to continue its gradual decline. Poverty, measured as income below the standardized $5.5/day 2011PPP line, is estimated to fall to around 18.7 percent by 2020.

## Project Spotlight

### Corridor 10 Highway

Building of the missing links on Corridor 10 highway on both E-75 and E-80 sections improves regional connectivity and unleashes Serbia's economic potential.

Serbia is located at the crossroads between East and West, and represents the shortest link between Western Europe and Southeastern Europe, Greece and Turkey. Corridor 10 Highway is a major infrastructure project in Serbia, both because it connects the country with its neighbors and the wider region, but also because this highway is part of the pan-European transport network.

By building the missing links on the Corridor 10 through its territory – with funding from the World Bank and other IFIs - Serbia gets an uninterrupted highway from its northern and western borders to its eastern and southern borders.

The completed construction of the Corridor 10 in line with modern standards will shorten travel time and provide safer connectivity along this international artery benefiting all users. It will also benefit local communities by providing better linkages to markets and services.

Expected positive impacts of this project on people's lives are manifold, especially in the areas of regional connectivity, local economic development, tourism, environment, cultural heritage.

Completion of this modern highway through Serbia will improve road safety and reduce road traffic accidents. A first fully automated tunnel control center opened under this project will contribute to overall road safety in Serbia.

In building the highway for the generations to come, beside good infrastructure, it is equally important to preserve the nature and protect the environment. This has been ensured through carefully designed environmental management plans and monitoring, and by applying international best practices in environmental protection and biodiversity preservation.

The new highway will have a positive impact on commercial and trade activities in Serbia and in the region, and will contribute to the regional development in the Western Balkans. Completion of Corridor 10 encourages sustainable development and enables Serbia to capitalize on its geographical position as the main transit country in the Trans-European road network.

The "Country Snapshot" is a bi-annual update, highlighting the country's recent developments, economic outlook and major overview of the World Bank's partnership with the country. You can find the latest updates at http://www.worldbank.org/serbia

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