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Original paper

THE TRANSITION IN SERBIA 2000-2018: THE COMPARATIVE ANALYSIS[1]

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Abstract: By low participation of investments in GDP, which amounts to about 18%, Serbia is among the negative record holders in analyzed 15 countries of Central and Eastern Europe. To achieve long-term sustainable GDP growth rates, Serbia would have to increase the share of investments in GDP to around 22.2%, which is the average of observed 15 countries of Central and Eastern Europe.

To increase the share of investments in GDP, Serbia needs to improve economic environment, increase the share of the public investments in GDP, and improve the business of public companies along with solving problems of social-owned companies in privatization. The largest shortfall of investments, of around 3% of GDP, relates to the private sector, especially when the small and medium domestic companies are concerned.

A strong increase of investments, especially those in the production of tradable goods, would not only lead to the acceleration of economic growth but also would improve the overall structure of GDP. This was the case in many of analyzed 15 countries of Central and Eastern Europe, especially in those who are today

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members of the EU. The growth of investments would remarkably speed up the rise of export, so that the Serbian economy, like the Hungarian or Slovakian ones, would achieve high and sustainable economic growth. Solving accumulated problems in the Serbian economy and creating conditions for long-term sustainable growth requires a strong shift in economic policy, as well as acceleration of reforms. First of all, the reforms related to the rule of law.

Key words: investments, GDP, Serbia, 15 countries of Central and Eastern Europe, the period 2000-2018.

INTRODUCTION

Since 2000, Serbia and Croatia came to a process of transition to the market economy and democratic society. In the case of remaining countries of the Western Balkans: B&H, Macedonia, Montenegro, and Albania, this process came somewhat earlier, as well as when the territory of Kosovo is concerned. Former so-called socialist countries of Central Europe and Baltic undertake the transition from 1990 and in the second half of the last decade of the 20th century achieved rapid progress, which can be seen through significant GDP growth. For Russia, the critical point is the 1998 crisis, after which the strong recovery, connected with the growth of prices of energy, started. Regarding Bulgaria and Romania, a somewhat slower process of transition occurred compared to the Central European countries, but generally speaking in the second part of the 1990s some progress was attained. Ukraine and Moldova are specific cases due to reform fatigue and wars, while in the case of Belarus elements of the transition process are the smallest of all 'socialist' European countries.

In an attempt to figure out the reason for Serbia's lagging behind the majority of other CIE countries, which also had some kind of real-socialism and relatively successfully reformed in the last three decades, we analyzed the tendencies of the main economic indicator: GDP and its main generator (fixed) investments. First, on the basis of IMF data, we calculated average growth rate in the second half of the last decade of the previous century for 15 selected countries (CIE 15[4]). After that, we made the calculation of the (discrete) average growth rate for the period 2000-2017, the pre-crisis (sub)period 2000-2008, and the period after the breakout of the crisis (late 2008), until today (also, separating the period from 2015 until today). We calculated the average participation of the investments in GDP for the entire period beginning with 2000, as well as for the (sub) period beginning with 2009 and ending with 2017. We chose almost all European countries in transition excluding relatively small and remote ones (Baltic countries, Moldova) or those which did not exercise significant reforms like Belarus.

[4] CIE 15 includes: Poland, Czech Republic, Slovakia, Hungary, Slovenia, Romania, Bulgaria, Ukraine, Russia, Serbia, Croatia, B&H, Macedonia, Albania, and Montenegro.

COMPARATIVE INSIGHTS IN THE SERBIAN TRANSITION PROGRESS

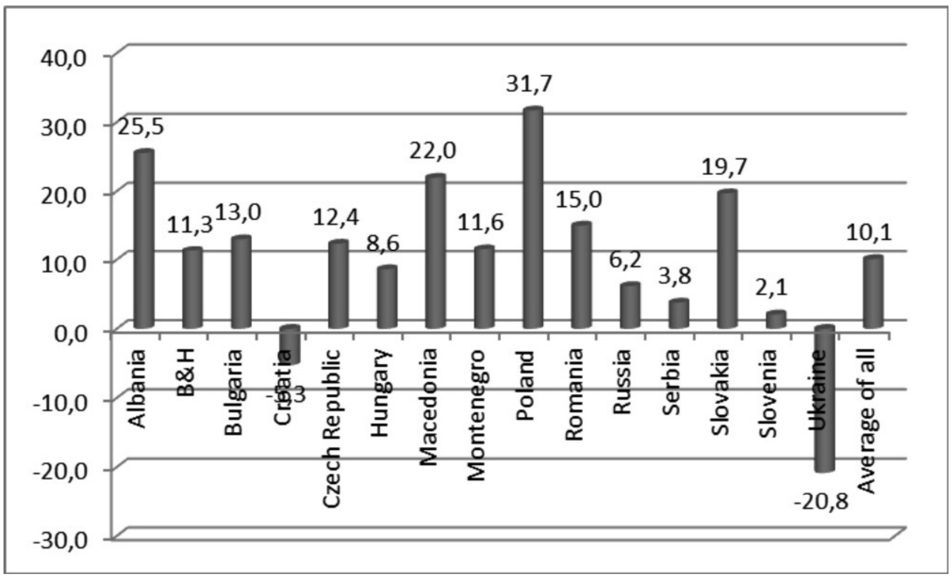
Our findings are discouraging for Serbia. While the Serbian economy faced drastic fall during the first half of the 1990s (GDP was halved), the transition economies of Eastern and Central Europe after not so dramatic recession in the first half of the 1990s, reported solid growth in the period 1995-2000 of 3.2%, comparing to the modest Serbian average GDP growth of 1.5%. True, the Serbian economy achieved an average growth in the period 2000-2017 of 3%, which is practically identical to the average growth for all 15 observed countries, but the low base inherited from the 1990s was of the fundamental significance to understand the low level of today's GDP per capita of Serbia. Additionally, a low level of fixed investments in GDP during the whole period (21.1% of GDP is not an impressive level of participation compared to those of observed 14 countries, excluding Macedonia, which the average share of investments amounted to 23.9%), and especially in the second sub-period beginning in 2009 (18.8%, against 22.2%), also contributed to relatively slow economic growth. Considering the insufficient level of development of Serbia, and by that, the potential for higher growth, what has been achieved until today is certainly discouraging. In all likelihood, it points to the structural problem of the Serbian economic as well as the political milieu.

In the period 2000-2008, industrial production in Serbia has risen only 1.9% annually on average. It is hard to estimate over-industrialization of Serbia in the 1980s. However, using comparative indicators for other countries, it could be concluded that the natural level of the share of industry in GDP should be 33-36%, while in 2017 it is estimated to about 18% of GDP. This dramatic fall of the share of industry in GDP led to others disbalances, which can be seen from the facts relating to the growth of the foreign and public debt - in the first phase the debt of mainly private companies, and after the crisis the public debt. Namely, the dramatic fall of the inflow of foreign funds was to be covered with external loans because required adjustments could not have been done in short-term. As the strong growth of export was not real, hence the growing indebtedness of the WB countries, including Serbia, was unavoidable (Cerović, 2015, pp. 59-74).

THE PHASES OF SERBIAN TRANSITION

After 2000 sanctions were lifted and economic reforms started. The period between 2000 and 2008 represents the only phase of significant growth of the Serbian economy for almost three decades, which was ended by the Great Recession. In this period the cumulative growth of the Serbian GDP was 58.2%. The next phase began in the last quarter of 2008 and lasted until the end of 2014, that is precisely the first half of 2015, and it was the period when the Serbian economy practically stagnated (the average growth rate was -0.2%, the cumulative fall of GDP amounted to 1,4%). Whether 2015 marks the beginning of the new phase of growth is the question, but recent results are encouraging (cumulative GDP increase in the period beginning in 2015 and ending with the projected growth of 2018 was 10%; while compared with 2000 the cumulative growth was 70%).

Graph 1:
The cumulative GDP growth of selected countries 2008-2017



Source: The calculation of authors on the basis of IMF data (IMF, 2017)

After decades of transition, Serbia is the one of a small number of countries in transition whose GDP is smaller compared to the pre-transition period. The Serbian GDP in 2017 was by 20% lower than in 1989, while other transition countries in the same period increased its GDP by about 67% on average. As a result of this divergence, the GDP pc of the 15 CIE countries in 2017 compared to Serbia was higher by 89%, while in 1989 GDP pc for all mentioned countries (in average) and Serbia was approximately equal.

REFLECTIONS ON THE CRASH IN THE 1990S

According to Arsić (2016, pp.25-41), the basic reason for the low development level of the Serbian economy was the crash in the 1990s when the GDP decreased by more than half (in 2000 the Serbian GDP was by 53% lower than in 1989), while in the same period the GDP of European transition countries was on average decreased by about 20% (transition recession usually lasted three to four years). At the same time, the potential GDP decreased by around 40%, which implied a strong fall in the production capability of the Serbian economy. The potential GDP during the 1990s decreased primarily due to the amortization of capital as a result of very low investment in the same period (12-14% of GDP, while the adequate level of investment to sustain capital on the constant level was estimated to 17%-18% of GDP). It is a dominant consequence of the sanction which lasted for one decade, while certainly smaller effects were caused both by NATO bombardment in 1999 and mistakes in the economic policy.

Table 1:

Average GDP growth of selected countries in the period 1996-2000, 2000-17, and 2008-17

	1996-2000	2000-17	2008-17
Albania	5.4	4.2	2.6
B&H	12.9	2.9	1.2
Bulgaria	-0.1	3.6	1.4
Croatia	3.4	1.7	-0.6
Czech Republic	1.9	2.7	1.3
Hungary	3	2	0.9
Macedonia	3	2.8	2.2
Montenegro	/	3	1.2
Poland	5.4	3.5	3.1
Romania	-1	3.9	1.6
Russia	1.8	3.4	0.7
Serbia	1.5	3	0.4
Slovakia	3.3	4	2
Slovenia	/	2.1	0.2
Ukraine	-1.8	1.9	-2.6
Average of all	3.2	3.0	1.0

Source: The calculation of authors on the basis of IMF data (IMF, 2017)

The results of the analysis (Arsić, 2016, pp. 39-41) showed that the economic crash during the 1990s was the main contributor to today's low level of the Serbian development comparing to advanced transition countries (while effects of reforms and the economic policy after 2000 are insignificant). Approximate equality of the potential and actual GDP after 2007 implies that growth can be generated by high investment which would increase the potential GDP, while expansive fiscal and monetary policies are not effective.

The main problem is depreciation of the capital, which mainly becomes unproductive in the conditions of the open market economy. The capital capacity was saved but its economic value was depreciated. This is not so obvious, hence the opponents of reforms and privatization were assured that sales of some of the companies to foreigners for the relatively small price were great mistake or corruption.

To dismiss the hypothesis about the negative impact of the reforms since 2000 on the poor performance of the Serbian economy we can use one indirect proof. Namely, similar reforms (privatization, liberalization) and by that policies were used by all other transition countries, which today have a significantly higher level of development.

The actual and potential GDP of Serbia is roughly uniform since the middle of the previous decade. It implies that the growth of the Serbian economy was impossible to generate by the increase in private and government consumption, which means by the expansive fiscal and monetary policies. In the situation when the actual and potential GDP are equated, the growth can only be generated by increasing the rate of investment by which the production potential of a country can be increased.

EIGHTEEN YEARS OF ECONOMIC TRANSITION IN THE WESTERN BALKANS

Over the past 18 years, the WB countries have undergone a major economic transformation, so many of them are unrecognizable compared to where they were at the turn of the century. Since the 1990s the majority of these countries have started a comprehensive rebuilding and reforms of their economies. They have opened towards the global trade and have focused more on export, expanded the rule of the private sector, enforced regulations that stifle the development of the corporate sector, and started with building the institutions required to support the market economy. Banking systems were built with the help of foreign capital and expertise. The results of these efforts have been reflected in stable economic growth, a remarkable rise in incomes and living standards, as well as greater macroeconomic stability.

However, the process of structural transformation stalled in mid-2000, faced with interest groups and beginning of reform fatigue, and remained incomplete.

Until the beginning of the global financial crisis, growth in the WB was more driven by massive global liquidity and unsustainable capital inflows rather than the real progress of economic reforms (the average annual economic growth across the region was over 5% in the period 2000-2008), which was also reflected in the remarkably high unemployment rate. In the period after the crisis, the growth in the WB countries lost its impetus.

The WB countries should generate workplaces if they want to reverse the trend of poor outcomes in the labor market, which is the reason for lagging behind the advanced countries. It is necessary to preserve the achievements so far, for example, the low inflation. The countries facing high fiscal deficits and public debt should urgently solve these issues. All across the region, the investments in the sectors exposed to import competition are needed in order to strengthen export and reduce the large trade deficit, as well as the current account deficit.

According to the IMF study (2015), the countries of the WB have experienced significant transformation over the period 2000-2015. They have gone through the system of market economy, privatized many inefficient state and socially owned companies, quickly adopted modern banking system, and strengthened the external orientation of their economies (a large range of state-owned or socially-owned enterprises has been privatized which tripled the share of private sector in GDP). As companies from the WB have discovered new markets, the inflows of the FDI in the region have also begun. The banking sector is one who was entirely transformed by the FDI which facilitated more efficient capital allocation.

However, the pace of structural reforms was disappointing due to the combination of reforms fatigue, the resistance of interest groups, and the influence of politics that limited the reforms efforts and caused delays with the EU membership. Looking back, part of the process of compensation for the backlogs was driven by the unsustainable capital inflows in the years before the global financial crisis. The result of this, a large number of NPLs (non-performing loans) represented priority if the intention was to support the economic recovery with credit. The tendency of most countries of the WB towards a fixed or almost fixed exchange rate has additionally complicated the need to adapt to the competitiveness challenge. Perhaps the largest mistake of the WB economic model is the chronic problem of the insufficient use of human resources. In 2008, at the very end of the growth wave, the unemployment rate in the region still amounted to more than 20% on average. Indicators of employment are equally disappointing, and from 2000 they range between 40% and 45% on average, which was 10% lower than in the new member states of the EU.

Part of the explanation for the slower progress of the WB comparing to the Central European countries in transition lies in a lesser geographical distance between the new member states and the heart of Europe, which has contributed to integrating some of them into the German supply chain. The other part of the explanation is that the convergence of income in the WB was slower because the structural reforms process went slower and did not go as far as in the new member states, especially in the area of state property reduction and improved governance.

The WB countries are still lagging behind new members of the EU in the sense of economic transformation and the level of incomes, accounting for about one-third of the level of advanced EU economies. The key challenge for the region is the completion of the process of structural transformation that started two decades ago. According to the recently projected growth rate, the economies of the WB will close only a small part of the gap with respect to the level of income per capita of the advanced economies of the EU by 2030.

Cerović (2015, pp. 72-73) points out that it is hard to say that the process of transition appear as successful when the achieved performances of the WB economies are concerned. First, countries from the WB have lagged behind in the context of the achievement of transition indicators (low indexes of EBRD). The WB countries have not been attractive enough for foreign investors, which can in large scope explain relatively low inflow of the FDI that has negatively impacted economic growth. Second, the reason for backwardness is the model of growth, very connected with the transition. Namely, in transition economies, the main instigator for growth was formed on the basis of import oriented growing demand, whose constant increase was based on the inflow of the foreign funds. Additionally, although these inflows were relatively small, they have primarily targeted the internal market. Thus, the FDI were often directed towards the services, especially finance, retail trade, telecommunication, sometimes houses. As a consequence, this has changed the sector structure of these economies in favor of untradeable goods and services. Third, only when the Great Depression began these distortions were detected as well as the fact that they have meaning and negative effect on the development of all transition countries. The main problem lied in the absence of precisely defined elements of the industrial policy. Namely, after the first wave of reforms (that, according to standard, cover the macroeconomic stabilization, the market liberalization of prices and exchange rate at a certain level, as well as privatization of smaller companies), in the second phase of implementation of reforms it has been necessary to conceive and implement some frame of industrial policy. It turned out that with the progress of reforms the change of development model was indispensable, and it can be even stated that very progress of reforms in certain levels requires a new growth model.

THE FIRST PHASE OF THE TRANSITION (2000-2008)

The Serbian economy achieved high growth in the period since 2000 to 2008 of almost 6% on average (precisely 5.9%), but with the emergence of substantial internal and external unbalances. The sector structure of the growth was extremely unbalanced - three non-tradable sectors (trade, transport and telecommunication, and financial intermediation) generated around 75% of total economic growth. The main generator of growth was the high domestic demand that was financed by the abundant inflow of cheap capital from abroad. A significant portion of capital inflows was realized on the basis of privatization, which means it was one-off. The capital inflows encouraged the real appreciation of the dinar exchange rate, while appreciation encouraged the increase of demand for import goods and the growth of the non-tradable sector. Investment from the EU came primarily to the financial sector, which indicates that Serbia's financial integration with the EU has been achieved, while on the other side,a low level of investment in industry indicates that Serbia's production integration with the EU has not been realized.

Non-dynamic economic growth – especially taking in the account the crash during the 1990s and by that the loss of the potential GDP in the same period - is one of the reasons why Serbia hasn't created new comparative advantages in international trade. Another reason is the structure of that growth –a noticeable over-proportional the growth rate of the gross added value has had the next sectors: transport and telecommunication, trade, and financial activities. Starting with the combined share of 18% of GDP in 2001, these three sectors contributed with 29% when we came to the generators of GDP in 2008. On the other hand, the combined share of agriculture, industry, and construction sector in forming total GDP was declined to 31% in 2008 from 39% in 2001 (Stamenković, Kovačević, Vučković, Nikolić&Bušatlija, 2009. pp. 15-27).

Declining share of tradable goods (agriculture and industry) has declined export supply, and demand for importing goods was increased. Additionally, internal demand and, by that, consumption has declined faster than the GDP – which has required the widening of the deficit of the current account of the balance of payments. The direct consequence of this structural deformation has been the constant growth of foreign trade deficit which has covered growing domestic demand. This kind of the model is sustainable one only if there is adequate foreign capital inflow, which will cover constantly growing current account deficit by a surplus in the capital-financial balance. One additional limitation is the structure of domestic demand where multi-year lack of investments was responsible for the inability to expand the export and by that to service external debt.

Generally, the structure of achieved economic growth has not also secured preconditions for future stable development. The economic policies - especially fiscal and monetary policies – are not by themselves sufficient to help alleviate or solve the fundamental unbalances.

In 2007 and 2008 the value of domestic demand overcame the value of GDP by over one-fifth. It meant that around one-fifth of total domestic demand was covered by the foreign trade deficit. Simultaneously, an explosion of current account deficit has occurred; in several years it is doubled achieving over 20% of GDP (in large part owing to cross-border loans for companies). It was clear that the equilibrium model on the basis of faster growth of internal demand compared to the GDP growth, causing the constant increase of net import, was not sustainable.

THE 2008-09 CRISIS AND STAGNATION UNTIL 2015

In late 2008, the global economic crisis, the so-called Great Recession, started with the bankruptcy of the Lehman Brothers, which automatically hit Serbia. In the first year of the crisis, Serbia achieved relatively favorable results. It's GDP in 2009 dropped by 3.1%, which is lower than in most of the countries in the region (true, industrial production has declined strongly by 12.6%). Domestic demand was significantly reduced primarily as a consequence of the freezing of pensions and wages in the public sector. In addition, the decline in domestic demand, especially investment, was significantly influenced by a decrease in the inflow of funds from abroad. The current account deficit, as a percent of GDP, is more than halved, while inflation particularly instigated by the dinar's depreciation, albeit still high, exhibited a marked downward trend in 2009. With regard to the achieved fiscal deficit of around 4% of GDP, it can be concluded that the fiscal policy in Serbia during 2009 was anti-cyclical, i.e. that the growth of government spending partially alleviated the fall of private spending. The main instrument for state incentives was subsidizing interest, which is a better solution than direct subsidizing of the economy (Petrović&Arsić, 2009; pp: 69-80).

Twelve months since the beginning of the 2008 crisis the share of NPLs in total loans have risen by more than 5 pp. yearly ending in 3Q 2009 (achieving 10.4%). The main cause for the growth of NPL is a decrease of activity in companies' sector that is fall of GDP, and especially industrial production. The rate of NPLs in Serbia was raised from 2008 to 2014 almost four times, achieving the level of 22%, whereby the level of NPLs considering companies was much larger compared to those of citizens. The so-called "Wien Initiative" was an agreement which stipulated that banks with foreign ownership would not decrease exposure towards Serbia, which reduced financial risks.

If we analyze the whole period since the outbreak of the crisis, we can see that Serbian economic growth lagged behind the average growth of not only the countries in the region but also the whole CIE 15. The reason for this lag one can see in the internal structural problems of the Serbian economy that reflects on the low participation of investments in the GDP. Low share of investments in Serbia is affected by the bad investment environment, as indicated by the poor ranking of Serbia in relevant competitiveness and corruption surveys (WB, WEF, Transparency International). Because of the bad environment, the private sector, particularly small and medium enterprises, as well as entrepreneurs, invest less in Serbia than in other comparable countries. In addition, the state directly affects the low level of total investments in the country due to the insufficient spending of funds intended for public investments and due to the poor management of public and state enterprises.

Since the beginning of the Great Recession (the fourth quarter of 2008) until 2015 there was not real cumulative growth, owing to the negative rates of GDP growth in 2009, 2012, and 2014. Namely, the average growth of the Serbian GDP in the period 2008-2015 was -0.1%, while at the same time, the average economic growth in countries CIE 15 amounted to 0.5%. First, two recession cycles (2008 and 2011) were much more connected with negative economic trends in the EU, because in the countries of the EU - which reported negative growth in these years – dominant part of the Serbian exports had been shipped. Because during 2014 in the EU was detected moderate economic growth, one could conclude that the third recession in Serbia was caused by internal factors.

Regarding production activities, it can be detected that since 2008 the highest drop was recorded in the construction sector, which was caused by the decrease of incomes, employment, credits as well as the limitation on the supply side, such is building licenses (Ranđelović, Brčerević&Arsić, 2015. pp. 9-27).

In the period after 2009 it came to considerable imports slowdown, which was caused by the fall of real incomes and a deceleration in lending activity, while exports – after significant fall in 2009 – have strongly raised from 2010 so that in 2014 it was about 51% bigger than in 2008, causing the rise of imports-exports coverage ratio from 46% in 2008, to 76% in 2014.

As we say, the main structural reason for the low economic growth in Serbia and lagging behind other CIE 15 countries is seen in the multi-years insufficient participation of investments in GDP. To attain high and sustainable economic growth in Serbia, it is needed that the share of investments in GDP is at least 22.2%, which is the average level of CIE 15. Insufficient participation of investments in GDP not only inhibits economic growth but also contributes to macroeconomic unbalances. The Serbian economy, in addition to the low share of investments, deviates from the average of the CEE countries by the low share of exports and by the high share of private consumption.

Serbia has entered the crisis with relatively low fiscal deficits and public debt. The measures of fiscal policy have led the fiscal deficit to grow constantly (from the beginning of the crisis), while in other European countries it has begun to fall from 2011. In 2014, with fiscal deficit of 6.6% of GDP, Serbia was among the highest in Europe, while the public debt was almost tripled from 28.3% of GDP at the end of 2008 to 70.4% of GDP in 2014, and 74.7% of GDP in 2015 (The Ministry of Finance of the Republic of Serbia 2018).

The high current account deficit from 2008, with a significant fall of GDP in 2009, has contributed to the strong rise of foreign debt of the country, from 64.6% of GDP in 2008 to 80% of GDP in 2014, which is considered the upper limit of the sustainable external debt in a long run. The current account deficit is significantly reduced (from 21.1% of GDP in 2008), but in 2014 it was still very high (6% of GDP).

High long-run unemployment, a relatively high current account deficit and external debt, an noticeable high fiscal deficit and unsustainable tendencies in the movement of public debt, poor business conditions, the decline in credit activity, high rate of the NPLs and relatively low investments, all these factors indicate that the unfavorable economic situation in Serbia is a result of accumulation of a large number of structural problems, some of which were inherited from previous years, and some were newly emerging. In order to significantly improve the outlook for higher economic growth in mid-terms, the government proposed, in accordance with the IMF, a necessary set of the structural reforms towards the end of the transition process- the so-called fiscal consolidation.

THE FINAL RECOVERY (2015-2018)

Since the Great Recession that began in Serbia at the end of 2008, and especially after several years of high net borrowing by state, which in the period from the end of 2009 to the end of 2014 amounted on average to 2.5 billion euros annually, leading to a strong accrual in public debt by over 40% of GDP, it found itself in a difficult economic and social situation. The country found itself at the brink of the public debt crisis, with all the accompanying severe economic consequences for the population (a strong real fall in incomes and a drastic growth in unemployment). As a necessity, the radical reform was imposed, and in particular (especially) a quick fiscal adjustment ('belt tightening'). Already during 2013, the Serbian Government made efforts towards economic reforms. However, more serious steps were made only in the mid-2014, when a package of reform laws was adopted, and in November of the same year, when pensions and salaries in public sector were reduced, and the VAT rate was raised for the second time. The draft of Fiscal strategy from late 2014, which was formalized in February 2015, and the reduction of salaries in public sectors and pensions since the beginning of November 2014, actually marked the beginning of fiscal consolidation in Serbia (The Ministry of Finance of the Republic of Serbia 2018). Then an agreement with the IMF followed, which besides measures of Fiscal Consolidation, contained a number of measures aimed at creating favorable conditions for economic growth (privatization of former social-owned companies, restructuring of public companies, the creation of conditions for growth of credit activity). The commencement of the three-year arrangement with the IMF at the beginning of 2015 gave credibility to the program and increased confidence of creditors, first of all, in terms of stopping the growth of public debt. The measures of fiscal consolidation that would permanently reduce the annual state expenditures (by net of EUR 1.7 billion) were planned by adopted fiscal strategies of the Government of Serbia.

The recovery of economic activity since 2015 indicated that fiscal consolidation did not have any major negative impact on it. Namely, the GDP growth in the second half of 2015 stood at a solid 1.8%, after the same year-on-year decline in the first quarter of the same year and slow growth in the second quarter (by 0.9%). It can be said the recovery of the Serbian economy was at the beginning in the second half of 2015, although it overstepped the pre-crisis level of GDP (2008) only in the next year – 2016 (The Ministry of Finance of the Republic of Serbia 2018).

The fiscal deficit has been strongly and permanently reduced, while economic activity, instead of the expected continuation of the recession, started to recover. In any case, it was evident that the economic situation in the country improved since 2015 (Minić, Petrović, Brčerević, 2016. pp.3-25).

In addition, in the period since 2014, the reduction in internal and external imbalances has continued, while the growth of the economy was increasingly strong. An important factor of the solid growth was a global fall in raw material prices (oil, gas, food), which substantially stimulated economic growth in the whole region in 2015 and 2016, by about 1% annually.

The growth of the public debt was stopped already in 2016. However, what casts a shadow on these undeniable fiscal improvements is the fact that more than modest progress has been realized in the implementation of the reform part of fiscal consolidation (primarily in the reform of public and state-owned enterprises).

The Fiscal consolidation 2015-2017 would almost certainly fail if it had relied on the austerity measures from the initial plan, which were directed to the reduction of excessive public expenditures. Namely, only slightly more than half of the originally planned savings have been achieved, which is why public expenditure in 2017, the last year of implementation of the program, was higher for 650 million euros than in the initial plan. The rationalization of the number of employees in the public sector has declined, as only a third of the expected savings will be realized – even though a reduction of 75,000 employees is anticipated. Neither saving from planned frozen salaries and pensions in the period 2015-2017 has been realized. Due to the incomplete implementation of the planned savings measures, the structure of public expenditure in 2017 remarkably deviates from the one originally planned and optimal. For example, subsidies are higher by 1% of GDP than (those) in comparable countries, while public investments are insufficient and need to be increased by at least 1% of GDP.

However, a surprisingly good collection of public revenues, which in 2017 were by about 1.4 billion euros higher than initially planned, has saved the fiscal consolidation. The most significant contribution to such strong growth in public revenues had a more efficient tax collection (by 700-800 million EUR), due to well-targeted ad hoc measures to combat the gray economy that the Tax Administration conducted on the field. A better trend in the labor market led to an increase in revenues from social (and pension) contributions in relation to the initial plan for 400-500 million euros. In the end, non-tax revenues increased in 2017 by about 200 million euros in relation to the initial plan due to the increased payment of public and state companies to the budget on the basis of attained profit – whose economic justification is still questionable.

The big problem is the delay in the reforms of public enterprises and the end of the privatization of state-owned enterprises - one of the basic objectives of the started fiscal consolidation. The poor performance of public and state-owned enterprises is too heavy for public finances (their old debts cost a budget 0.9% of GDP), and as the hot spots of the problem are not eliminated, new expenses to cover their losses are almost inevitable.

According to the Fiscal Council of RS (Fiskalni savet RS, 2017b), the growth of GDP in 2018 will likely be higher (4%) than projected by the Government of RS (3.5%). Namely, the FS added to the current growth trend the expected recovery of agriculture after the drought with the establishment of the usual level of electricity production after a deep fall in the first half of 2017.

The monetary policy in 2017 marked a continuation of gradual relaxation, but with a too slow reduction in the reference interest rate (to 3.5%), especially because in the second half of 2017 deflation was recorded, with an excessive strengthening of the dinar. Additional slowing of inflation at the beginning of 2018 (January) to 1.9% y-o-y is indicative.

In 2017, the banking sector entered the final stage of consolidation with the gradual revival of credit activity. The share of NPL in 2017 was reduced from about 20% to around 12%, and there were some ownership changes in several major banks. All these changes announced a stronger growth of credit activity in 2018, and this trend will also be tackled by the extremely low-interest rates in Europe that are expected in 2018.

The budget is again, after more than ten years, in surplus - of about 0.5% of GDP. Public debt in 2017 was strongly reduced, to 61.5% of GDP at the end of the year.

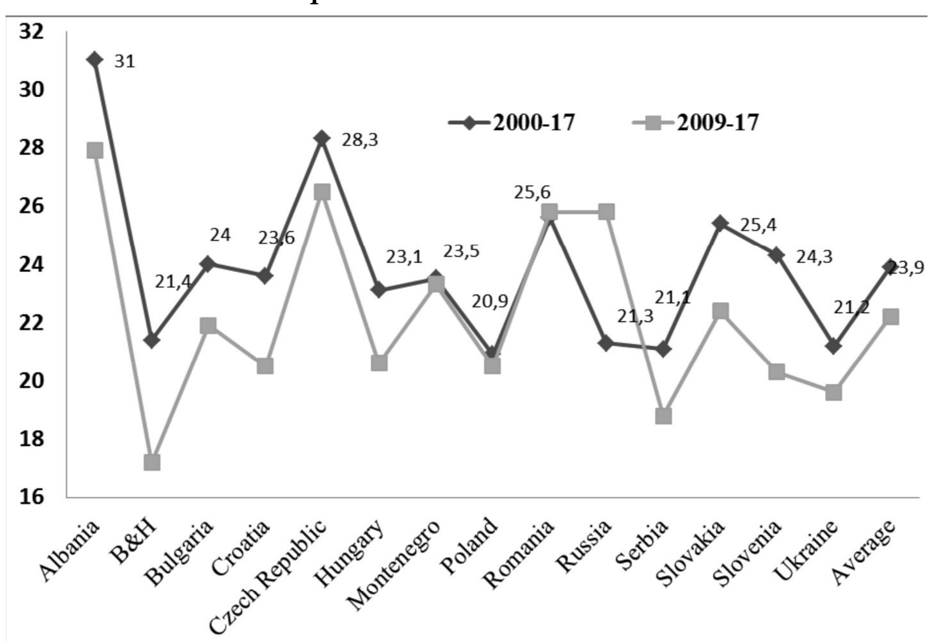
The EU economy – which is crucial for Serbia – will probably be in recovery in the coming years, so high demand growth cannot be expected, or the strong inflow of the FDI to Serbia. In such circumstances, Serbia only retains the ability to attract as much as possible of scarce capital through the exchange rate policy and the promotion of the economic environment.

CONCLUDING REMARKS

The projection of the Serbian Central Bank: NBS (2018) is that the GDP growth, after a temporary slowdown in 2017 (1.8%), owing to effects of shocks on the supply side, will accelerate in 2018 to around 3.5%. GDP growth at a similar pace (around 3.5%) is also projected for 2019. It will be supported, as in 2018 also, by the growth of investment and export, which will be positively impacted by the effects of structural reforms, FDI inflows and high external demand. Growth in investment and external demand, as the recovery in household spending, will continue to support the growth of manufacturing and service sectors, which, in 2019 also, should be the drivers of GDP growth, seen from the production side. According to the analysis of experts of MAT (2018) economic activity (industry, foreign trade, real turnover in the retail trade), at the beginning of 2018 (January) is recovered after the reduction of its dynamics in December. They optimistically estimate growth of manufacturing industry by over 8% in 2018, which indicate to good economic results in this year.

Graph 2:

Average share of investments in GDP in selected countries in the period 2000-2017 and 2009-2017



The calculation of authors on the basis of IMF data (IMF, 2017)

Also, high export growth would have to be preceded by a huge growth in investments over the years ahead, but this is not the case at the present, and it is unlikely that dramatic changes will occur in 2018 or 2019. The eventual arrival of some particularly large private investment directed towards the export (such as FIAT) in coming years is not still certain, but even if it occurs, the effect on the growth of export in this and the next year will not be meaningful.

A study by Simon (2017) is indicative of this. He shows that, because of a protracted transition exacerbated by crises and wars, Serbia's economic catch-up with Austria will require a long time, but a more efficient economic policy, in addition to the attraction of foreign assets, may result in a more rapid catch-up. This process can be accelerated by increasingly investing in human capital (education and R&D).

When cooperation with abroad is concerned, the paper by CHEN Xin& Yang Chengyu (2017) is important.Namely, they evaluate the development and level of the cooperation between China and 16 CEE countries based on 18 set of index data. They show that bilateral cooperation between China and Serbia is at a higher level. Most of the cooperation fields are doing well, including politics, investment, people-to-people exchange and finance, while the trade cooperation should be improved.

Serbia could expect a fast economic growth since 2018, but only if it implements a number of reforms which would significantly improve the business conditions in Serbia. Improving Serbia's position in the competitiveness lists has attracted the attention of investors around the world, which in future could also lead to the growth of investments and even without the state's subsidies.

The structural problem why the economic growth in Serbia is lower than in comparable countries is lack of investments. By low participation of investments in GDP, which amounts to about 18%, Serbia is among the negative record holders in CIE countries. To achieve long-term sustainable GDP growth rates, Serbia would have to increase the share of investments in GDP to around 22.2% (which is the average of comparable countries). To achieve even faster growth and reach other CIE countries (making so-called catch-up effect), Serbia would have to invest about 25% of GDP.

To increase the share of investments in GDP, Serbia needs to improve economic environment, rise the share of the public investments in GDP, and improve the business of public companies, along with solving problems of social-owned companies in privatization.

The largest shortfall of investments, of around 3% of GDP, relates to the private sector, especially when the small and medium domestic companies are concerned, which are the most affected by bad economic environment. These companies account for two-thirds of the employment and in turnover of the non-financial sector of the economy, but their investments are significantly less than that, that is, over half of the investments in the non-financial sector are concentrated in large companies. The indicator which indirectly points out that foreign companies easier invest in Serbia than domestic ones is net inflows of the FDI that is about 5-6% of GDP, which is slightly more than average of the region (Fiskalnisavet 2017).

To increase private investments, we need to improve the economic environment. Meaningful progress on the Competitiveness List of the World Economic Forum and on Doing Business report of the World Bank has not yet led to stronger growth in investments. A possible reason for this is that the progress on these lists is achieved due to a strong improvement in only a few indicators, such as issuing building permits and macroeconomic stability. However, according to the indicators related to the rule of low, Serbia remained extremely poorly rated.

The analysis shows that state inefficiently implements public investments, which should rise by 1% of GDP, at least. Poor management of public and state companies led to the fact that their investments are less than needed by 1% of GDP at least.

Another part of investments, which are under direct control of the government and not implemented at a satisfactory level, relates to the investments of public and state companies. Many years of poor managing these companies led to the fact that they generated losses and debts instead of stimulating economic growth with its profit and investments. Only EPS should invest by around 0.5% of GDP more than it currently makes in order to make investments higher than amortization.

A strong increase of investments, especially those in the production of tradable goods, would not only lead to the acceleration of economic growth but also would improve the overall structure of GDP. The growth of investments would remarkably speed up the rise of export, so that the Serbian economy would achieve high and sustainable economic growth, based on investment and export, gradually increase investment share in GDP – which would also mean a reduction in the excessive private consumption in GDP. In addition to investment, according to the IMF (2017b), there is an urgent need to improve the court system, strengthen the quality and independence of the judiciary process, and facilitate the use of effective out-of-court arbitration.

In the empirical analysis of Ivanović, Begović, Kufenko, Stanišić, &Gelosod (2018), the determinants of liquidation, merger and bankruptcy of privatized firms from 2002 to 2015 were analyzed. In Serbia privatization was partly a result of exogenous pressures and the process has been deemed a failure. Namely, a sizeable number of privatized firms were bought by bureaucrats and politicians and all firms were subjected to a period of supervision. The design of this process allowed rent-seekers to conserve their privileges through asset-stripping, which explains the failure. Firms owned by politicians faced significantly higher risks of bankruptcy, especially after the end of supervision.

The reforms implemented in Serbia since 2000 were slow, insufficient, and partial to establish a functioning market economy as it exists in continental European countries. Therefore, it is necessary to speed up reforms in the market economy in Serbia and make the state more efficient. Solving accumulated problems in the Serbian economy, as well as creating conditions for long-term sustainable growth, requires a strong shift in economic policy, as well as acceleration of reforms, before all those related to the rule of law.

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Predrag PETROVIĆ

TRANZICIJA U SRBIJI 2000-2018: KOMPARATIVNA ANALIZA

Apstrakt: Sa niskim učešćem investicija u BDP, koji iznosi oko 18%, Srbija je među negativnim rekorderima od analiziranih 15 zemalja Centralne i Istočne Evrope. Da bi postigla dugoročne stope održivog rasta BDP-a, Srbija mora povećati udeo investicija u BDP naoko 22,2%, što je prosek posmatranih 15 zemalja Centralne i Istočne Evrope.

Radi podizanja udela investicija u BDP, Srbija mora poboljšati ekonomsko okruženje, povećati učešće javnih investicija u BDP i poboljšati poslovanje javnih preduzeća, zajedno sa rešavanjem problema društvenih preduzeća u privatizaciji. Najveći deo 'manjka' investicija, od oko 3% BDP, odnosi se na privatni sektor, posebno na mala i srednja domaća preduzeća.

Snažan porast investicija, posebno onih u proizvodnji 'razmenjivih dobara', ne samo da bi doveo do ubrzanja ekonomskog rasta, već bi poboljšao i ukupnu strukturu BDP, kao što je to bio slučaj u mnogim od analiziranih 15 zemalja, posebno onih koje sudanasčlanovi EU. Rastinvesticija bi posebno uticao na ubrzavanje rasta izvoza, što bi omogućilo srpskoj privredi, kao i mađarskoj ili slovačkoj, da ostvari visok i održiv ekonomski rast. Rešavanje akumuliranih problema u srpskoj ekonomiji, kao i stvaranje uslova za dugoročno održiv rast, zahteva snažne pomake u ekonomskoj politici, kao i ubrzanje reformi, pre svih onih koji se odnose na vladavinu prava.

Ključne reči: investicije, BDP, Srbija, 15 zemalja centralne i istočne Evrope, period 2000-2018.

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