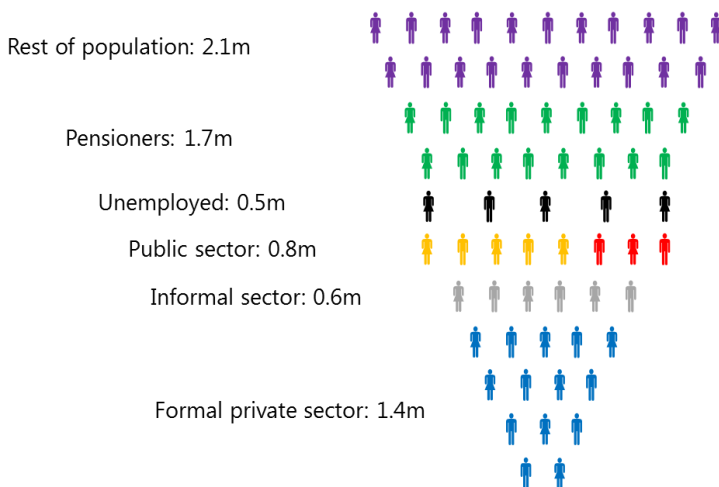


Serbia needs a stronger private sector

The strong trends upward in employment and downward in unemployment are important signs that Serbia's economic program is working. But the structure of the labor market shows how far Serbia still has to go to fulfill its potential as a dynamic market economy. Put simply, the private sector - which is the source of economic growth, and of tax revenue to pay for pensions, public wages and public services - is still too small to provide for a high standard of living for all Serbians.



This chart from my talk at the Kopaonik Business Forum last week explores the problem. Starting at the bottom of the triangle, the formal private sector – the part paying taxes and social contributions - makes up only 20 percent of Serbia's total population of 7.1 million. Employment in the shadow economy could be as much as half that of the formal private sector – cheating workers of benefits and the government of taxes, and competing unfairly with legitimate firms. Next

up is public employment, split into government (the orange figures) and public or state-owned enterprises (the red ones). Relative to population, Serbia's public sector is probably only a bit larger than the EU average. But relative to the private sector that has to pay for it, it is hugely out of line. This is why it is so hard to afford higher public sector wages without cutting back public employment.

So far we have covered total employment of 2.8 million. But we still have 4.3 million people to go! – most of whom require support from the state in one form or another. First, nearly half a million unemployed. Second, Serbia's high and rising band of pensioners – outnumbering the formal private sector workers paying into the pension system, which helps explain why there is such a big hole in pension fund finances. And finally the "other" category, including school children and students, stay-at-home parents, and discouraged workers who have given up looking for a job, among others.

Looking at the above chart, it's easy to see why Serbians are perennially dissatisfied with the State. The blue people think taxes are too high. The grey ones complain they can't get benefits. The orange and red ones want higher wages. The black ones want a job. The green ones believe their pensions are lower than they deserve. And the purple ones complain of low social benefits and share overall frustration with the quality of education, healthcare and other public services.

There is only one way to resolve this dynamic, and it is to expand the formal private sector, so it can better carry the weight of the whole society. This means helping people move from the grey, orange, red, black and purple sectors into the blue sector (and even from green to blue, as many pensioners still have valuable skills to offer).

To see how much Serbia needs to change in the long term, we can compare with countries like Germany or the UK. These countries have large pensioner populations too, but a much healthier labor

market structure overall. Formal private sector employment is roughly twice as high as in Serbia, relative to total population – making a solid base for the economy.

The shift from an inefficient, intrusive and protected public sector to a productive, competitive private sector is exactly what Serbia's program supported by the IMF aims to achieve. It is happening. But it needs to happen faster to meet the aspirations of Serbians as they compare their living standards with other European countries. This is why we always encourage more and faster progress in "structural reforms" such as improving the business environment, combatting the grey economy, restructuring state enterprises and reforming public administration. As these reforms increasingly come to fruition Serbia will surely see stronger income growth for all sectors of society - and hopefully some less dissatisfaction too.