INTERNATIONAL MONETARY FUND

IMF Country Report No. 23/243

REPUBLIC OF SERBIA

July 2023

2023 ARTICLE IV CONSULTATION, FIRST REVIEW UNDER THE STAND-BY ARRANGEMENT, AND REQUEST FOR MODIFICATION OF PERFORMANCE CRITERIA—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR REPUBLIC OF SERBIA

In the context of the Serbia—2023 Article IV Consultation, First Review Under the Stand-By Arrangement, and Request for Modification of Performance Criteria, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board and summarizing the views of the Executive Board as expressed during its June 28, 2023, consideration of the staff report on issues related to the Article IV Consultation and the IMF arrangement
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on June 28, 2023, following discussions that ended on June 9, 2023, with the officials of Republic of Serbia on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on June 15, 2023.
- An **Informational Annex** prepared by the IMF staff.
- A **Debt Sustainability Analysis** prepared by the staff of the IMF.
- A **Statement by the Executive Director** for Republic of Serbia.

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.

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International Monetary Fund
Washington, D.C.

IMF Executive Board Concludes 2023 Article IV Consultation and First Review Under the Stand-By Arrangement with the Republic of Serbia

FOR IMMEDIATE RELEASE

Washington, DC—June 28, 2023: The Executive Board of the International Monetary Fund (IMF) concluded the 2023 Article IV consultation[1] and first review of the Stand-By Arrangement with the Republic of Serbia. An additional SDR164 million (over €200 million) is available to purchase, which would bring cumulative drawing to SDR949 million (around €1.2 billion).

Over the last decade, Serbia has, despite external shocks, achieved impressive economic results reflecting its strong economic policies. Such policies supported strong growth, low inflation, and declining public debt. As a result, incomes rose, employment increased, and poverty declined. Large and diversified FDI inflows more than covered the current account deficit. The Covid-19 pandemic affected growth, but the economy quickly recovered in 2021 with the support of a strong package of policy measures.

Nevertheless, spillovers from Russia's invasion of Ukraine and domestic problems, primarily in the energy sector, hit the economy hard. A sharp increase in international energy prices, domestic electricity production problems, and tightening global financial conditions led to an increase in fiscal and external financing needs in 2022. Under a Fund-supported Stand-By Arrangement (SBA), macroeconomic imbalances have already started to decline, and foreign exchange reserves are at an all-time high.

Headline inflation, however, at 15 percent in May, remains well above target and core inflation remains in double digits. Conditional on tighter monetary policy, which likely requires further policy rate increases, inflation should decline to around 8 percent by the end of the year and is projected to return to within the National Bank of Serbia's target band in 2024. The projected fiscal deficit, which is not expected to exceed 3 percent of GDP in 2023, will support disinflation and further public debt reduction.

Growth is expected to decline to 2 percent in 2023, as tighter monetary and fiscal policies, still-high inflation, and weak external demand and tightening global financial conditions all weigh on activity. Over the medium term, growth should return to potential of around 4 percent. The current account deficit is expected to narrow to around 4½ percent of GDP as energy import prices fall and export volumes continue to grow.

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

Following the Executive Board's discussion, Mr. Bo Li, Deputy Managing Director and Acting Chair of the Board, issued the following statement:

Tighter monetary policy is appropriate to address the challenging high inflation environment, support dinarization, and further strengthen reserves. While banks remain resilient, continued close monitoring is needed, given rising interest rates and risks from global financial turbulence. Steps to close remaining regulatory and supervisory gaps with the EU and support deeper capital markets are important.

The tight fiscal stance is supporting disinflation and helping to reduce public debt. The authorities have made strong progress on fiscal-structural reforms, including related to investment and risk management. Going forward, it will be important to adhere to the new fiscal rule, avoid ad hoc spending measures, and ensure that future fiscal overperformance is saved or used for priority investments.

Energy sector reform remains essential. Ongoing electricity and gas tariff hikes have helped to reduce fiscal subsidies and will be critical for financing essential energy investments over coming years. The new State-Owned Enterprise (SOE) law, which is aligned with OECD best practices, provides a strong foundation for governance reform in the energy sector and beyond. In parallel, considerable progress is being made in improving the structure and management of energy SOEs.

The authorities' structural reform measures to improve the business environment are important, including strengthening the rule of law, improving the efficiency of the judicial system, and strengthening governance and anti-corruption.

Table 1. Serbia: Selected Economic Indicators

Population: 6.87 million (2021)

Quota: SDR654.8 million

Main products and exports: manufactured goods, food, machinery and transport equipment.

Key export markets: the EU (Germany, Italy) and ex-Yugoslavian states.

	2021	2022		2023	
		SBA Approval	Est.	**SBA Approval**	Proj.
Output					
Real GDP growth (%)	7.5	**2.5**	2.3	**2.3**	2.0
Employment					
Unemployment rate (labor force survey) (%)	11.0	**10.5**	9.4	**11.1**	9.1
Prices					
Inflation (%), end of period	7.9	**15.8**	15.1	**8.2**	8.2
General Government Finances					
Revenue (% GDP)	43.3	**43.0**	43.4	**41.6**	42.1
Expenditure (% GDP)	47.4	**46.8**	46.4	**44.9**	44.9
Fiscal balance (% GDP)	-4.1	**-3.8**	-3.0	**-3.3**	-2.8
Public debt (% GDP)	57.2	**56.9**	55.6	**56.5**	55.3
Money and Credit					
Broad money, eop (% change)	13.0	**3.3**	6.9	**7.9**	11.3
Credit to the private sector, eop (% change) 1/	9.9	**10.3**	7.3	**7.7**	5.9
Balance of Payments					
Current account (% GDP)	-4.3	**-9.0**	-6.9	**-8.4**	-4.7
FDI (% GDP)	6.9	**6.1**	7.1	**5.2**	6.1
Reserves (months of prospective imports)	6.0	**4.1**	5.2	**4.1**	5.6
External debt (% GDP)	74.4	**68.0**	72.1	**65.4**	66.8
Exchange Rate					
REER (% change)	1.4	**…**	3.2	**…**	…

Sources: Serbian authorities and IMF staff estimates.

1/ Calculated at a constant exchange rate to exclude the valuation effect.

REPUBLIC OF SERBIA

June 15, 2023

STAFF REPORT FOR THE 2023 ARTICLE IV CONSULTATION, FIRST REVIEW UNDER THE STAND-BY ARRANGEMENT, AND REQUEST FOR MODIFICATION OF PERFORMANCE CRITERIA

EXECUTIVE SUMMARY

Context: Serbia has made impressive economic gains over much of the past decade: living standards improved, inflation fell, public finances were strengthened, and reserves increased, helped by ample foreign direct investment (FDI) inflows. But spillovers from the war in Ukraine—especially the sharp increase in international energy prices—and deep-rooted problems in Serbia's energy sector that came to a head last year, led to large external and fiscal financing needs, prompting the authorities to request a Fund-supported Stand-By Arrangement (SBA). Fiscal and external outturns for 2022 were both better than expected, and unemployment remains low. Record FDI inflows continue to drive reserves higher. But inflation remains a pressing challenge. Led by high food and energy prices, headline inflation is now well above the National Bank of Serbia's (NBS's) target band and core inflation has also increased sharply. Fiscal policy is expected to remain relatively tight in 2023, despite additional mid-year spending measures. Deep structural problems persist in the energy sector and are a key focus of the SBA. Long-standing geopolitical challenges remain.

Policies: Tighter monetary policy is needed to reduce inflation. The NBS should ensure that real ex-ante policy rates become positive and that such rates stay positive until the path of inflation is clearly converging to target. Fiscal policy should work alongside monetary policy as fiscal consolidation helps disinflation and lowers public debt. And any fiscal over-performance should be saved or used for priority investments. Energy sector reforms are a program priority and cover ongoing tariff hikes and broader structural reforms, including important new state-owned enterprise (SOE) legislation, reforms of large energy SOEs, and a new prioritized energy investment plan. The financial sector appears sound, although continued vigilance, especially on bank deposit outflows and liquidity, is required. Continued structural reforms that improve the business climate and strengthen governance, rule of law and anti-corruption are essential to sustain Serbia's impressive growth record. Staff supports the authorities' request to modify performance criteria.

Approved By
Laura Papi (EUR)
Pritha Mitra (SPR)

Discussions were held in Belgrade during March 23 to April 4, 2023 and virtually during June 8-9, 2023. The staff team comprised Donal McGettigan (head), Alex Pienkowski, Christiane Roehler, Mengxue Wang (all EUR), John Hooley (FAD), Lukas Kohler (SPR), Tongli Zhang (MCM), Yulia Ustyugova (resident representative), Desanka Obradović and Marko Paunović (local economists). Vuk Djoković (OED) attended some discussions. HQ support was provided by Amelia Oliveira and Zeju Zhu (EUR).

CONTENTS

TABLES

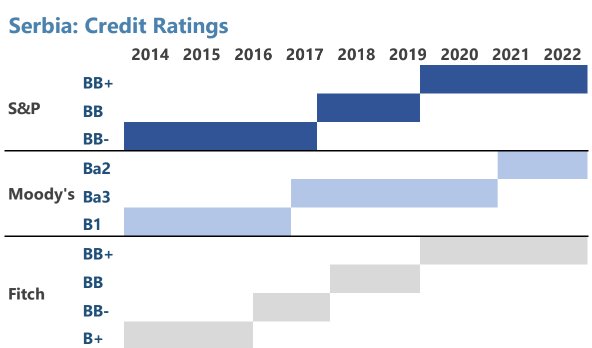
ANNEXES

APPENDICES

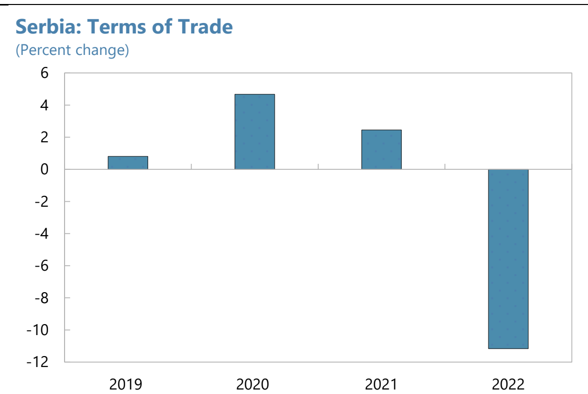
CONTEXT

1. **Serbia has delivered impressive economic results over much of the past decade** (Text Figure 1, Figure 1, and Annex I). Before the pandemic, and helped by successful IMF-supported programs, including the recent Policy Coordination Instrument (PCI) programs, GDP and employment both grew strongly while inflation remained low. Poverty fell. The fiscal deficit was eliminated, and public debt declined. Robust and diversified FDI more than financed the current account deficit and reserves increased (Annex II). Although the Covid-19 pandemic hurt growth, the downturn was brief and shallow, and was followed by a rapid growth rebound, supported by comprehensive fiscal, monetary, and financial sector measures. Fiscal consolidation resumed in 2021 and public debt started falling once more. Serbia's sovereign ratings were, as a result, upgraded and now stand only one notch below investment grade.

2. **But Serbia's terms of trade deteriorated and its financing needs increased after Russia's invasion of Ukraine.** Higher international energy prices led to a sharp deterioration in Serbia's terms of trade. This, along with energy supply problems (in large part because of years of underinvestment in the energy sector and poor management), increased external financing needs. Following short-lived FX deposit outflows in early 2022, the National Bank of Serbia (NBS) sold FX to maintain the de-facto stabilized exchange rate regime but subsequently more than rebuilt its reserves. Fiscal financing needs also increased, exacerbated by capped domestic energy prices, which meant the budget had to make up for large losses at the two major state-owned enterprises (SOEs), the gas utility Srbijagas and the electricity company Elektroprivreda Srbije (EPS). Broader fiscal support was also needed to help those most affected by higher energy prices.



Sources: S&P, Moody's, and Fitch Rating.



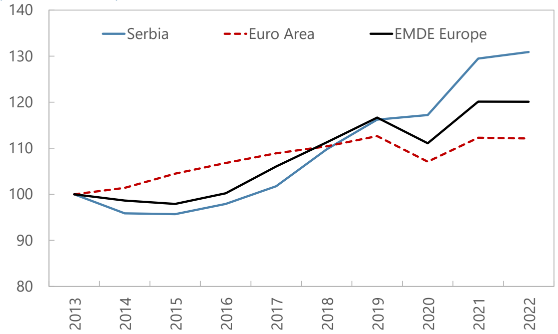
Sources: SORS and IMF staff calculations.

Figure 1. Key Macroeconomic Variables Over the Past Decade

GDP grew rapidly over the past decade …

Serbia: Real Euro GDP Per Capita

(Index, 2013=100)

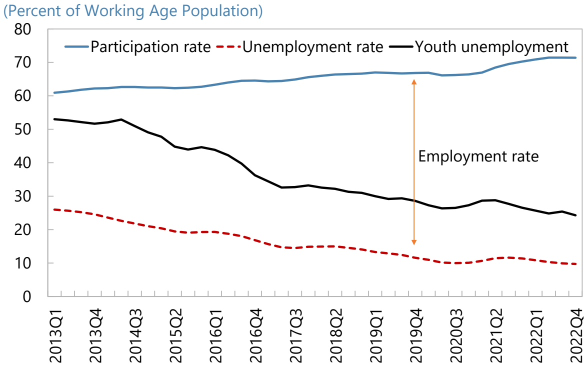


Sources: Haver Analytics and IMF staff calculations

… and the labor market showed impressive strength.

Serbia: Labor Market Indicators

(Percent of Working Age Population)

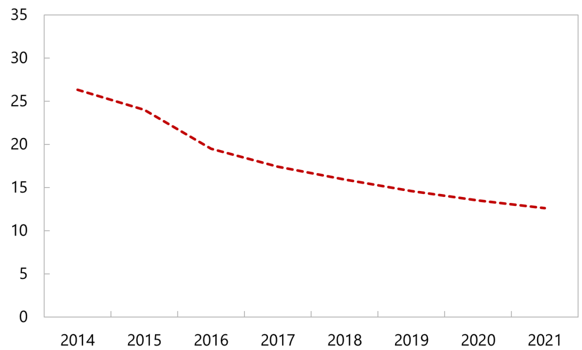


Sources: Haver Analytics and IMF staff calculations.

As a result, poverty fell.

Serbia: Severe Material Deprivation

(in percent of population)

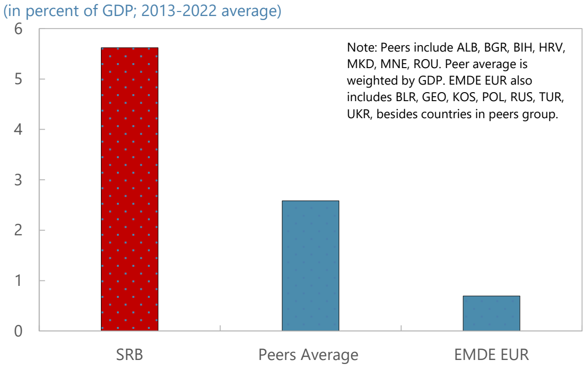


Source: SORS, World Bank World Development Indicators

Serbia has attracted impressively large FDI inflows.

Serbia: Foreign Direct Investment Inflows

(in percent of GDP; 2013-2022 average)

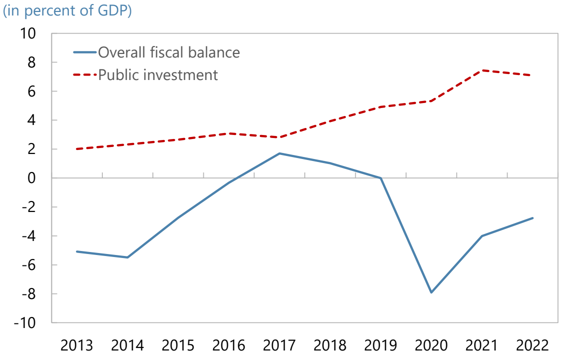


Sources: IMF WEO and IMF staff calculations

The fiscal deficit was eliminated pre-pandemic, even as public investment increased …

Serbia: Fiscal Balance and Public Investment

(in percent of GDP)

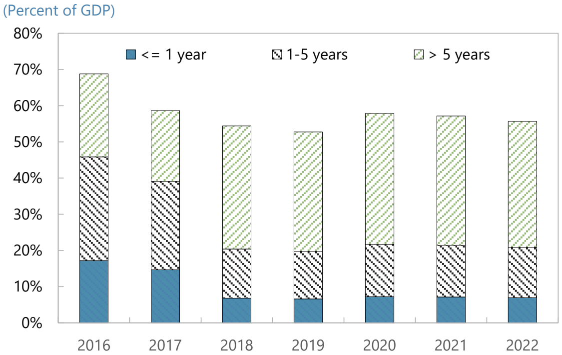


Sources: IMF WEO and IMF staff calculations.

… and both the level and composition of public debt improved.

Serbia: Public Debt by Residual Maturity

(Percent of GDP)



Sources: PDA and IMF staff calculations

3. With higher balance of payment needs, and greater uncertainty in the global economy, the authorities requested a 2-year Stand-By Arrangement (SBA) in late 2022. Access available under the SBA is equivalent to almost €2½ billion (or 290 percent of Fund quota) and was frontloaded at approval. The SBA aims to address Serbia's balance of payment needs in a catalytic manner and to lower inflation and strengthen buffers through tight macroeconomic policies, and by building on reforms under the earlier Policy Coordination Instrument (PCI) and addressing Serbia's deep-rooted energy sector problems. The program also aims to improve further fiscal transparency and management, including to support the implementation of the new fiscal rule, and foster broader SOE reforms.

4. Russia's war in Ukraine highlighted long-standing regional geopolitical challenges. A recent EU proposal aims at normalizing Serbia-Kosovo relations and at reducing regional tensions. While a new cluster on "Green Agenda and Sustainable Connectivity" in the EU accession negotiation was opened in December 2021, progress on EU accession remains slow, lately because of Serbia's limited alignment with the EU foreign policy as Serbia has not formally joined sanctions against Russia.

RECENT DEVELOPMENTS

5. Economic growth has softened although the labor market remains resilient (Text Figure 2, Figure 2). Real GDP grew by 4 percent year on year in H1:22 but by only ¾ percent in the second half of the year, partly because of fading "carryover" from 2021. Private consumption growth slowed through the year as high inflation eroded real wages and credit growth fell; and real public consumption hardly grew reflecting tight expenditure control. After a large increase in 2021, gross fixed capital formation fell slightly in 2022 because of uncertainty over the war in Ukraine and higher interest rates. Both import and export volumes grew considerably in 2022 reflecting strong FDI and continued integration into global supply chains. While the net export growth impact was negative last year, this was partly because of a large import-led inventory buildup (including higher gas and oil storage), which has started to reverse. The 2023Q1 growth outturn (0.7 percent, year on year) suggests continued weakness in activity. Despite the growth slowdown, unemployment fell from 11 percent in 2021 to below 9½ percent in 2022.

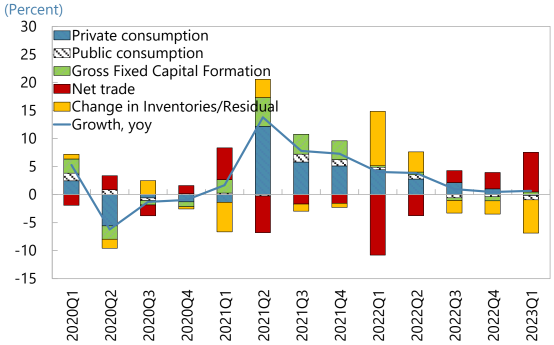
6. Inflation remains well above the NBS's target band (Figure 3). Annual headline and core CPI inflation were 15 and 10 percent in May. Around two-thirds of the increase in headline inflation reflects higher food and energy prices (Box 1). While monthly inflation is below its peak, the annualized inflation rate in May remains high (10.5 percent). Wage growth has only been broadly in line with inflation despite unemployment close to historic lows. And, while inflation expectations have risen, they have stabilized of late and remain contained at medium-term horizons.

Text Figure 1. Recent Macroeconomic Developments

GDP growth fell as private consumption growth slowed ...

Serbia: Real GDP and Contributions

(Percent)

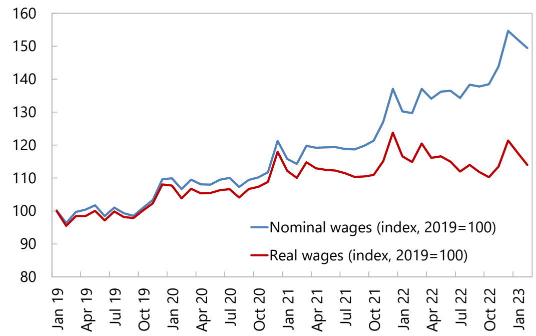


Sources: Haver Analytics and IMF staff calculations

... driven by weak real wage growth ...

Serbia: Net Wages

(Index, Jan 2019 = 100)

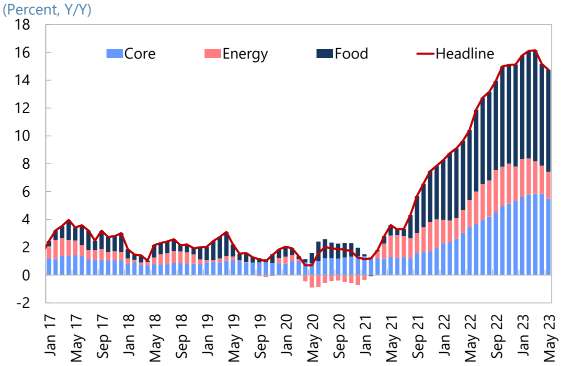


Sources: Haver Analytics; SORS; and IMF staff calculations

... as a result of high inflation, mainly from energy and food prices.

Serbia: Contribution to Annual Inflation

(Percent, Y/Y)

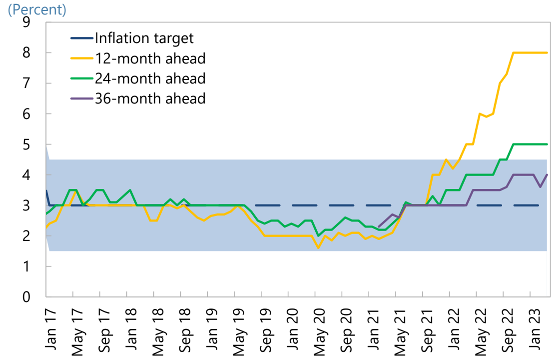


Source: SORS

Nearer-term inflation expectations rose well above the target band but have stabilized.

Serbia: Inflation Expectations of Financial Sector

(Percent)

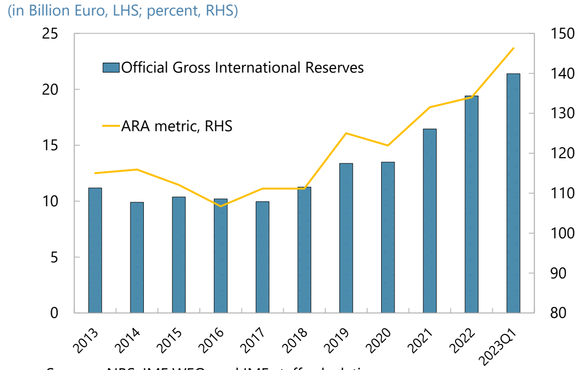


Sources: Bloomberg, SORS, and IMF staff projections

7. Despite a large current account deficit in 2022, reserves have reached new highs (Figure 4). Although high international energy prices that resulted from war-related spillovers led to a pickup in the current account deficit, Serbia secured record FDI inflows that continued to fully finance its current account deficit, while other sources of financing (including a USD 1 billion loan from UAE) allowed the NBS to increase reserves to almost €19½ billion by end-2022. Reserves have increased further since, to new record highs. The external sector assessment indicates that the external position in 2022 was weaker than the level implied by fundamentals and desirable policies, although this assessment is subject to model uncertainty especially since 2022 was a year of exceptionally large external shocks (see Annex III).

Serbia: Gross International Reserves

(in Billion Euro, LHS; percent, RHS)



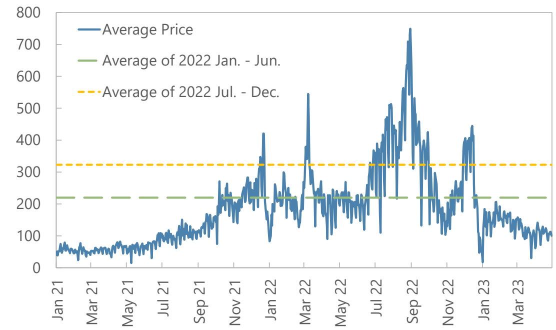
Sources: NBS, IMF WEO, and IMF staff calculations

Text Figure 2. Regional Energy Import Prices, 2021–23[1]

Regional electricity prices …

Hungarian Power Exchange Electricity Average Price

(in EUR/MWh)

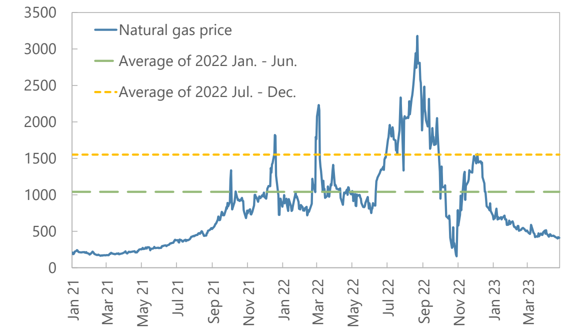


Source: HUPX

… the reference price for natural gas prices …

Dutch TTF Natural Gas Price

(in EUR/1000 Cubic Meters)

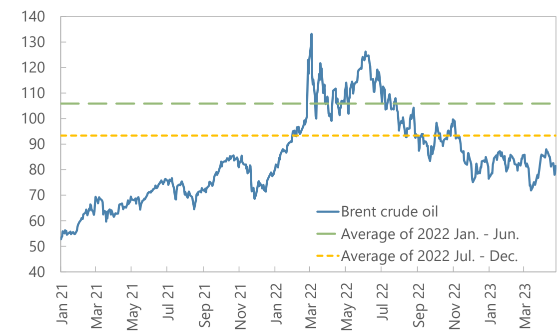


Source: Bloomberg

… the oil price…

Brent Crude Oil Price

(in USD/Barrel)

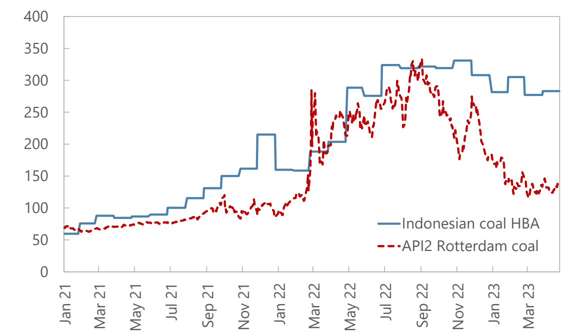


Source: Bloomberg

… and coal prices, have all declined significantly since their summer 2022 peak.

Indonesian and Rotterdam Coal Prices

(in USD/metric tonne)



Source: Bloomberg

1/ Serbia's energy imports mainly follow European prices. It also imports coals from Indonesia.

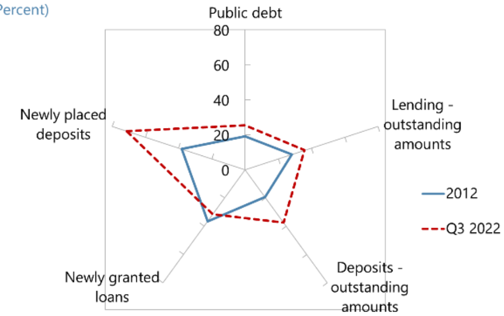
8. **Fiscal outcomes have been strong** (Figure 5). The 2022 fiscal deficit fell to 3.0 percent of GDP despite large unplanned energy SOE fiscal support. Tight administrative controls on spending and strong revenues, helped by high inflation, contributed to this positive outcome. The 2023 budget was approved in December 2022 in line with the understandings under the SBA. New measures were subsequently introduced in May and June, including expanded agricultural subsidies, an ad hoc mid-year pension increase, and additional public sector pay rises. These measures amount to about 0.9 percent of GDP in 2023, but can be accommodated within program targets, with around half offset by revenue overperformance and half from savings elsewhere, including lower subsidies to energy SOEs.

9. **Fiscal financing pressures have eased** (Figure 6 and 7). Serbia made a successful return to international capital markets in January, selling USD 1.75 bn of Eurobonds in two heavily oversubscribed issuances. After hedging into euros, the final interest rates were on par with, or better than, neighboring peers. Domestic RSD and Euro-denominated debt was issued at

progressively declining yields this year. Public debt stood at just above 55 percent of GDP at end-2022 and is on a declining path (Annex IV).

10. The financial sector remains resilient and dinarization has increased to an all-time high. Contagion from the recent global financial market instability has been minimal. NPLs have fallen to a record low of 3 percent, while capital and liquidity remain strong, as does bank profitability. Reflecting strong policies, deposit dinarization increased to an all-time high of 42 percent at end-2022, following a temporary fall earlier in the year at the outbreak of the war in Ukraine.

Serbia: Dinarization Indicators
(Percent)



Source: NBS

OUTLOOK AND RISKS

11. Policy settings are tightening and external headwinds are expected to continue this year before easing. Under the baseline, the NBS is expected to target a tight monetary stance and to maintain the de facto stabilized exchange rate. The ECB is expected to continue to tighten policy and reach its terminal interest rate around mid-2023, which will help with Serbia's disinflation given the high degree of euroization in the economy. Fiscal policy is expected to remain tight, with a deficit of less than 3 percent of GDP in 2023 (which implies a negative fiscal impulse of almost ½ percent of GDP) followed by further reductions in later years in line with the new fiscal rule. Activity in Serbia's main trading partners is expected to remain weak in 2023 before recovering, in line with IMF April WEO projections.

12. Activity is expected to slow temporarily but inflation and external imbalances look set to improve (Text table and Tables 1–5). Key macro-economic variable projections include:

- Real GDP growth is expected to weaken on the back of tighter monetary and fiscal policy, weaker trading partner activity, anemic credit growth, and stagnant real wages. Growth is expected to recover from 2 percent in 2023 to 3 percent in 2024, and to return to potential of about 4 percent from 2025 onwards (Annex V).

- Inflation peaked in 2023Q1, has begun to moderate in Q2, and is expected to fall more rapidly in the second half of the year as monetary policy and global financial conditions tighten further, the new agricultural season begins (no repeat drought is assumed), negative supply shocks diminish, and global commodity prices fall. Higher energy tariffs, other administered price increases and possible excise tax rises will temper modestly the extent of the decline in the short term.

- **The current account deficit** is projected to narrow to less than 5 percent of GDP in 2023, falling further to around 4¼ percent over the medium term. The deficit is expected to continue to be fully financed by FDI inflows. The external debt outlook remains stable (see Annex VI).

Serbia: Key Macroeconomic Variables, 2022–28

		2022	2023	2024	2025	2026	2027	2028
Real GDP growth (percent)	*Current*	2.3	2.0	3.0	4.5	4.0	4.0	4.0
	Program request	2.5	2.3	3.0	4.5	4.0	4.0	
CPI, average (percent)	*Current*	12.0	12.4	5.3	3.5	3.2	3.0	3.0
	Program request	12.1	12.2	5.3	3.5	3.2	3.0	
CPI, eop (percent)	*Current*	15.1	8.2	4.0	3.5	3.2	3.0	3.0
	Program request	15.8	8.2	4.0	3.5	3.2	3.0	
Current account (percent of GDP)	*Current*	-6.9	-4.7	-4.6	-4.5	-4.4	-4.3	-4.2
	Program request	-9.0	-8.4	-6.0	-5.3	-5.3	-5.3	

Sources: IMF WEO and IMF staff calculations

13. Uncertainty remains high, and downside risks predominate (Annex VII). Uncertainties continue over potential negative spillovers from geopolitical tensions and energy sector developments, trading-partner growth, the still-challenging inflation environment, domestic political uncertainty, and global financial market conditions. FDI inflows, a core element of Serbia's growth model, are sensitive to geopolitical developments. On the upside, Serbia's open economy has significant potential, including from the further relocation of skilled migrants and businesses, and continued nearshoring.

14. Authorities' Views. While agreeing that the outlook remains uncertain, the authorities expect growth of 2–3 percent for the year, driven by continued employment growth, higher export volumes and slowing inflation. The authorities' inflation trajectory is broadly aligned with the staff forecast, although the authorities expected inflation to fall to within the NBS's target band by mid-2024 or earlier, somewhat earlier than staff. They agreed that the current account deficit looks set to remain fully financed by continued FDI inflows, attracted by Serbia's competitiveness and strong investment climate.

PROGRAM PERFORMANCE

15. The program is on track. All end-December 2022 quantitative performance criteria (QPCs) and end-March 2023 indicative targets were met (Appendix 1, Tables 1a–1b).

- Supported by sizable open market purchases, net international reserves (NIR) stood at about €14 billion at end-2022, well exceeding the program's NIR floor.

- The 2022 fiscal deficit QPC was met by a wide margin (0.8 percent of GDP) because of across-the-board spending restraint and strong revenues, helped by high inflation. The 2022 QPC ceiling on primary current expenditure was also observed, albeit narrowly, as direct budget support was provided to Srbijagas, instead of the previously-planned issuance of a government guaranteed loan (which would not have counted as primary spending).

- End-December 2022 inflation of 15.1 percent was also lower than projected and ended up well below the upper limit of the inflation consultation band.

16. Structural reforms are progressing, albeit with some warranted delays (Appendix 1, Table 2).

- Encouraged by staff, the authorities postponed the approval of a new SOE governance law (end-December 2022 SB) to allow time for a full-fledged review against international best practice. The SOE governance law was adopted by cabinet in May 2023 and is expected to be submitted to parliament shortly after the ongoing public communication campaign to explain the goals of the SOE governance reform.
- EPS's legal status was changed to a joint stock company in early April (end-February 2023 SB), after the EPS statute was changed to be consistent with the anticipated provisions in the new SOE governance law.
- The end-March 2023 SB on expanding the central electronic public wage and employment registry for the education sector was met.
- The authorities raised electricity and natural gas tariffs further by 8 and 10 percent, respectively, effective May 1, 2023 (meeting end-April 2023 SBs).
- In mid-June, the authorities adopted a new energy investment plan to enhance energy security, stabilize electricity generation, and conserve energy (end-May 2023 SB). The plan will be published as a part of the forthcoming Energy Sector Development Strategy.

POLICY DISCUSSIONS

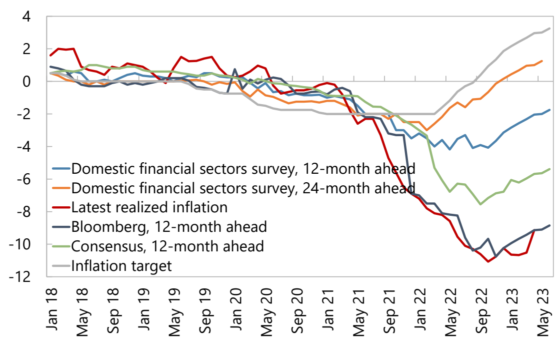
Despite weaker growth, a tight macroeconomic policy setting is needed to lower inflation, rebuild buffers, and support the de facto stabilized exchange rate. Monetary policy should continue to be tightened and kept tight until inflation is dealt with, and fiscal policy should work alongside monetary policy to help with disinflation and to lower public debt further to rebuild fiscal space. It is important to minimize the use of ad hoc fiscal measures and to follow all aspects of the new fiscal rule to ensure its credibility. Forcefully tackling domestic energy sector challenges—which played such a large role in increasing Serbia's financing needs—remains at the core of the program's structural reforms, although broader reforms, especially on fiscal, remain important.

A. Monetary Policy—Need to Stay the Course

17. Still-high inflation remains a critical challenge. Despite recent monetary tightening, negative ex-ante real policy rates, tight labor markets, and Serbia's troubled inflation history all risk prolonging high inflation, de-anchoring inflation expectations, and undermining policy credibility. That said, favorable base effects should help reduce inflation going forward, as should slowing credit growth (Figure 8, Tables 8 and 9). ECB policy rate hikes should also help disinflation efforts given the still-high degree of euroization in the economy, but also may put pressure on the NBS to raise its policy rates further.

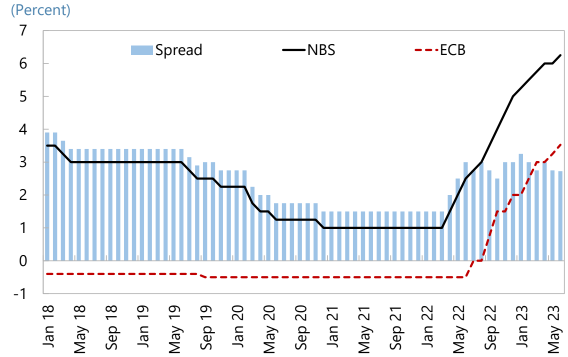
18. Against this backdrop, the NBS should continue to tighten monetary policy to lower inflation, strengthen dinarization, and underpin Serbia's de facto stabilized exchange rate. As a guide, the NBS should aim for positive ex ante real policy interest rates (at the 12–18 month horizon), which likely calls for further policy rates increases (Box 3). Inflation developments need to be monitored closely, especially for stronger wage growth and second round inflation effects. Once tightened, such a monetary policy stance needs to be maintained until the projected path of inflation is comfortably back within the NBS's target range.

Serbia: Real Policy Rate Based on Different Inflation Expectations
(Percent)



Sources: Haver Analytics and IMF staff calculations

Central Bank Policy Interest Rates
(Percent)



Sources: Bloomberg, Haver Analytics and IMF staff calculations

19. The de-facto stabilized exchange rate regime remains appropriate, although a move to greater flexibility over time should be considered. The dinar's stability against the euro remains an important policy for the NBS, helping to support confidence and Serbia's attractiveness as an investment location. Maintaining the de-facto stabilized exchange rate regime does, however, require continued strong, supportive, macroeconomic policies, which the authorities are delivering. Over the medium term, a gradual return to a more flexible exchange rate should be considered, particularly under supportive conditions, as this would be more consistent with the official inflation targeting regime, would reduce the incentive for the private sector to take on FX risk, and would provide an important shock absorbing role.

20. Authorities' Views. The authorities recognize the pressing inflation challenge in Serbia and are committed to bringing inflation back to target by next year, adjusting policy rates as needed to secure such an outcome. They underscored that any further policy rate hikes should consider the effects of past monetary tightening and they expected inflation to fall substantially from the second half of the year. Higher global interest rates (especially from the ECB), falling commodity prices, and an expected recovery in agriculture will put downward pressure on inflation. The authorities underscored the flexibility of their monetary policy framework that allows tightening through a higher weighted-average repo rate, without necessarily raising the policy rate. In addition, the authorities emphasize that exchange rate stability is essential for macroeconomic stability and for broader confidence.

B. Fiscal Policy—Supporting Disinflation and Rebuilding Buffers

21. Fiscal policy should remain tight, working with monetary policy to deal with inflation and reduce debt. A deficit of no more than 3 percent of GDP in 2023 would be consistent with a relatively tight policy stance but would leave sufficient room for priority investments. The authorities have, therefore, agreed to tighten the program's QPC to an equivalent of a 3 percent of GDP deficit. Staff projects a slightly lower deficit of 2.8 percent GDP based on budget overperformance, despite the recent announcement of new ad hoc spending measures. Gradual fiscal consolidation should also continue beyond 2023 with the aim of securing a deficit of no more than 1.5 percent of GDP in 2025, in compliance with the authorities' new fiscal rule.[1]

Serbia: Overall Fiscal Balance
(Percent of GDP)

	2022	2023	2024	2025
Staff projection	-3.0	-2.8	-2.0	-1.5
Cyclically adjusted	-3.2	-2.8	-2.1	-1.6
Fiscal impulse[1]	-1.3	-0.4	-0.8	-0.5
QPC ceiling[2]		-3.0	-2.2	

[1]The fiscal impulse is defined as the negative of the change in the general government cyclically-adjusted balance as a percent of GDP
[2]Quantitative Performance Criteria: Ceiling on the general government fiscal deficit, expressed as a percentage of projected GDP

22. While the authorities have agreed to offset the recent expenditure hikes, future ad hoc spending should be kept to a minimum, and deviations from the fiscal rule avoided. The authorities have tapped into buffers arising from fiscal overperformance to date (including lower subsidies to energy SOEs) and have committed to new measures, mainly in the form of excise revenue increases, to offset their higher spending commitments in 2023-24 (MEFP ¶13). The recent ad hoc increase in pension payments went well beyond the increase called for under the new pension indexation mechanism, which is a core part of the fiscal rule. Such actions undermine the rule's credibility, and future deviations should be avoided. In addition, any future fiscal overperformance relative to program targets should be saved or used for priority investments, rather than being spent in an ad hoc manner.

23. The authorities should continue to build on their strong public debt management record. The recent, heavily oversubscribed, Eurobond issuance, and SBA disbursements, policy loans and grants from development partners, and external project financing will be more than sufficient to cover overall fiscal financing needs in 2023. Such funding will also allow for a further buildup of domestic Treasury deposits this year even as net issuance of domestic securities is expected to be negative. Should domestic borrowing costs continue to fall, the authorities should gradually increase the share of dinar-denominated debt to help contain foreign currency risk and to develop the domestic debt market. Borrowing at longer maturities to limit gross financing needs should also continue as is planned.

[1] The fiscal rule was incorporated into the Budget System Law along with the approval of the 2023 budget in December 2022. While the deficit rule is not binding until 2025, the expenditure rules on pensions and public sector wages are already in force. For details on the rule see IMF Country Report No. 22/384, Annex III.

24. The authorities continue to make good progress on a wide range of fiscal structural reforms.

- Fiscal Rule (MEFP ¶18–19). The authorities are increasing coverage of their fiscal accounts to include all materially relevant general government bodies. Once complete, the reform will inform a review of the parameters of the fiscal rule (end-November 2024 SB). The authorities are also developing an action plan, with IMF technical assistance, to make medium-term budgeting more effective and binding (end-July 2023 SB). A strong Fiscal Council should continue to play its crucial role in monitoring fiscal performance, including under the new fiscal rule.

- Public Investment Management (PIM, MEFP ¶21). It is important to closely manage public investment projects to ensure value for money and to contain fiscal risks. A general agreement on the "strategic relevance evaluation" of all investment projects has been reached with the Ministry of European Integration (MOEI). The new PIM Information System (PIMIS) should be rolled out as planned to all relevant entities at the national level and expanded to cover all investment projects from the project idea stage.

- Fiscal Risk Management (MEFP ¶20). The role of the Fiscal Risks Monitoring department at the Ministry of Finance is being strengthened, including through additional staff. Further work is needed on using fully new methodologies to monitor fiscal risks from SOEs, local governments, litigation, and natural disasters. The commitment to start enhanced fiscal risk reporting in the updated Fiscal Strategy 2024–26 (to be published in 2023Q4) is welcome.

- Public Wage Registry (MEFP ¶23–24). The phased implementation of the public wage and employment register (ISKRA) for about 450 thousand employees by end-2024 is on track. The education sector (excluding higher education institutions) was included as planned (end-March 2023 SB), and the health sector will follow (new end-January 2024 SB).

- Procurement (MEFP ¶21). To enhance transparency and competitive pricing, the authorities should cut the share of procurement conducted under exceptional procedures, e.g., by tightening the qualification criteria for such treatment. They should also aim to increase the number of bidders, e.g., by structuring tenders so smaller companies can meet the requirements. They should also maintain continued alignment of procurement rules with the EU acquis.

- Tax Administration (MEFP ¶22). Tax administration reforms continue. The roll-out of a new e-fiscalization system for VAT aims to support revenue collection and "big data" analysis is being expanded. Procurement of a new off-the-shelf IT system, organizational procedural reforms, change management, and HR strategy development are supported by IMF and World Bank technical assistance.

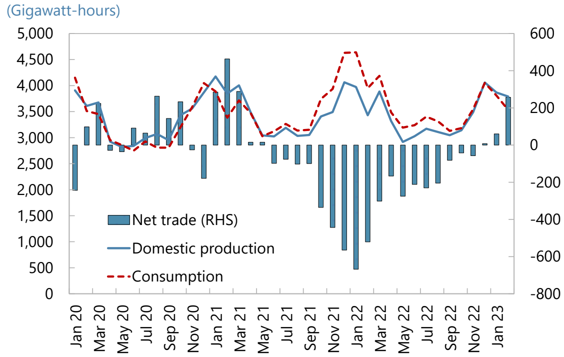
- Social Benefit Administration (MEFP ¶**37).** The new IT systems for the administration of social benefits should help targeting and enforcement. The new Social Card Registry, which covers the nearly 800 thousand benefit recipients with active benefit rights, is welcome. The authorities are also developing a comprehensive information system on social protection (IS SOZIS) to support benefit administration.

25. Authorities' Views. The authorities agreed with the need to keep fiscal policy tight to support disinflation, to reduce debt, and re-build buffers, and to prepare for the deficit target under the fiscal rule, which takes full effect in 2025. At the same time, the additional fiscal space resulting from higher revenues and lower subsidies to energy SOEs has allowed for further support to several priority groups: teachers and nurses to bring their wages closer to the public sector averages, families with children ahead of the new school year, and pensioners who were particularly affected by high inflation. The authorities do not think that the extraordinary mid-year pension increase goes against the fiscal rule and argue that with high inflation an ad-hoc adjustment was warranted as pensioners are hit particularly hard by the recent high inflation, dominated as it has been by food and energy price increases. The authorities were confident that the 2023 budget is fully financed and are turning their attention to 2024 financing plans, including the development of offsetting measures to be adopted in the context of the 2024 budget discussions. The authorities reasserted their commitment to continued comprehensive structural fiscal reforms.

C. Energy Sector Policies—The Core of the Program

26. Energy tariff increases have helped limit the fiscal subsidies provided to energy sector SOEs and reduce arrears. The January and May energy tariff hikes have helped strengthen EPS and Srbijagas balance sheets, as have falling regional energy prices and a pickup in domestic electricity generation (Box 2). Fiscal transfers to state-owned energy companies are budgeted to fall by about 1½ percent of GDP in 2023. And energy SOEs have been reducing their previously accumulated arrears.

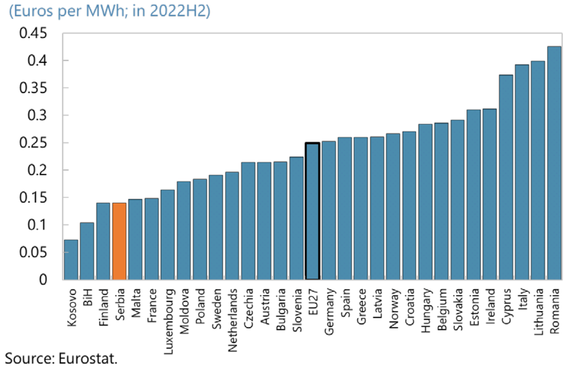
Serbia: Electricity Balance
(Gigawatt-hours)



Sources: Eurostat and IMF staff calculations

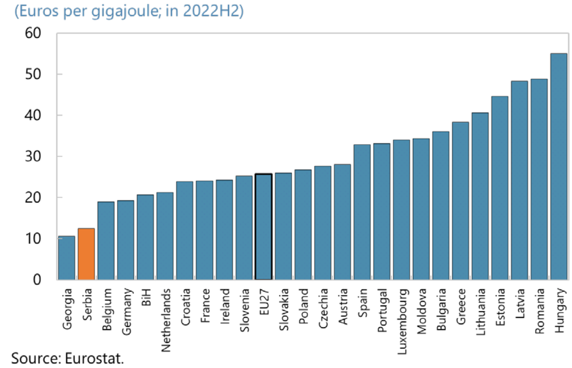
27. But further electricity and gas tariff increases are needed. Tariff increases in November (**new end-October 2023 SB)** and in 2024 are needed to eliminate all fiscal subsidies to energy SOEs by the end of the program and to finance much-needed investment spending over coming years. Non-household gas and electricity prices remain low compared to peers, so further price increases should not materially affect firm competitiveness (text charts). At the same time, it is important to soften the impact of the ongoing tariff adjustments on the most vulnerable. Existing block tariffs, with a lower electricity price for households up to a given electricity consumption threshold, provide helpful support. The authorities also broadened eligibility criteria for its budget-financed consumer protection program for the energy vulnerable to raise the share of households benefitting from the reduced energy bill from 3 to about 10 percent. The uptake has, however, been limited. The authorities have therefore launched an information campaign to raise awareness of the new program. New uptake should be closely monitored, with further outreach or changes to eligibility implemented as needed.

Electricity Prices: Non-Household Medium-Size Consumers
(Euros per MWh; in 2022H2)



Source: Eurostat.
Note: Band IC : 500 MWh < Consumption < 2 000 MWh

Gas Prices: Non-Household Medium-Size Consumers
(Euros per gigajoule; in 2022H2)



Source: Eurostat.
Note: Band I3 : 10 000 GJ < Consumption < 100 000 GJ

28. Major energy investments are needed in the electricity sector and to enhance energy security. The authorities have developed a prioritized and fully costed energy investment plan for the next 2–5 years (**end-May 2023 SB**). The plan includes projects in the electricity, gas and oil sectors that aim to enhance energy security, stabilize electricity generation, and conserve energy. These range from projects to ensure reliable coal-based electricity production to new natural gas interconnectors to diversify supply, new oil pipelines, energy savings projects, and green infrastructure developments. The plan is aligned with projected energy consumption needs over the medium-to-long term and will be published as part of the forthcoming Energy Sector Development Strategy. Total estimated energy investment needs are significant, and are allocated across the energy SOEs, public capital investment and private sector involvement drawing on prioritization and bottom-up costing exercises.

29. Other energy sector reforms are also critical. The recent conversion of EPS into a joint stock company and the appointment of a new supervisory board with qualified members will help strengthen EPS governance and underpin its future transformation, to be elaborated in the upcoming EPS strategic restructuring plan (**end-December 2023 SB)**.[2] The "unbundling" of the state-owned Srbijagas is also a priority for EU accession. More broadly, the restructuring of the energy sector should be guided by high-level strategic objectives. Both the National Energy and Climate Plan (NECP) and Energy Development Strategy are expected to be adopted by end-2023. The NECP will define Serbia's goals and strategies for reducing greenhouse gas emissions, increasing the share of renewable energy sources, and setting goals for greater energy efficiency. The Energy Development Strategy will include projections through 2050 consistent with the NECP and will include the strategic development and business plans for the energy SOEs, as well as guidance for the private sector including on green energy.

[2] This plan will focus on the companies' stabilization and transformation, including reforming EPS's governance and organizational structure, as well as the managerial and sectorial layout, audit processes, internal controls, and compliance procedures.

30. Authorities' Views. The authorities are keenly aware of the challenges facing the energy sector and are committed to comprehensive reforms to ensure stable and reliable energy supply, to improve energy efficiency and, over the medium to long run, to reduce carbon emissions substantially. The authorities agreed that, to achieve these goals, further increases in electricity and gas tariffs are needed. At the same time, they emphasized the need to protect the most vulnerable members of society from the effects of these increases and the need to preserve Serbia's competitiveness as the leading regional FDI destination. The authorities plan to make large investments in the energy sector and recognize this will require significant financial resources, from the energy SOEs, the budget, and the private sector. They believe the benefits of a more sustainable and secure energy system will outweigh the long-run costs, and, if carefully planned and prioritized, can be implemented in a fiscally sustainable manner. The authorities' priorities also include further reforming large energy SOEs to improve their governance, efficiency, accountability, and transparency. They are aware that implementing energy sector reforms requires navigating complex political and social dynamics, balancing competing interests, and building consensus among stakeholders, and are confident they will succeed.

D. Financial Sector Policies—Strong Results, but Close Monitoring Needed in the Face of Elevated Risks

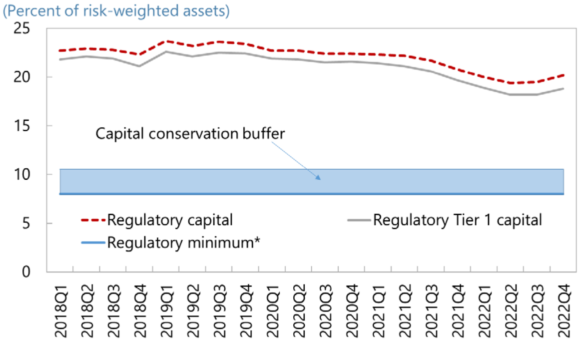
31. While bank prudential indicators remain strong, continued close monitoring of risks remains critical given elevated risks (Text Figure 3). Aggregate capital and liquidity ratios remain high, NPLs are low, and bank profitability has recovered. As domestic and external interest rates rise, however, and with risks to global financial stability remaining, continued vigilance is required. Staff supports the authorities' plan to conduct a gap analysis with the EU of the legal framework for banks.

Text Figure 3. Key Banking Sector Indicators

While well above regulatory minimums, bank capital has declined of late.

Serbia: Regulatory Capital

(Percent of risk-weighted assets)



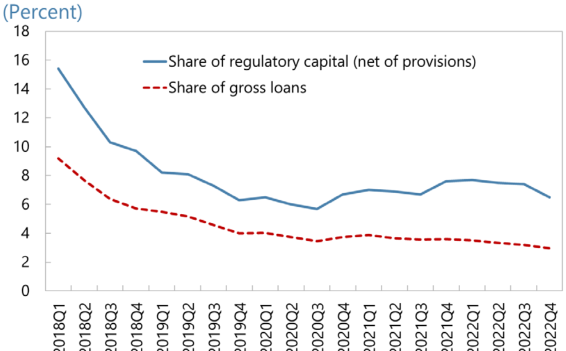
Source: Haver Analytics

*The NBS also has a countercyclical capital buffer (currently 0%), a capital buffer for systemically important banks and a systemic risk buffer.

But NPLs remain low compared to recent history.

Serbia: Non-Performing Loans

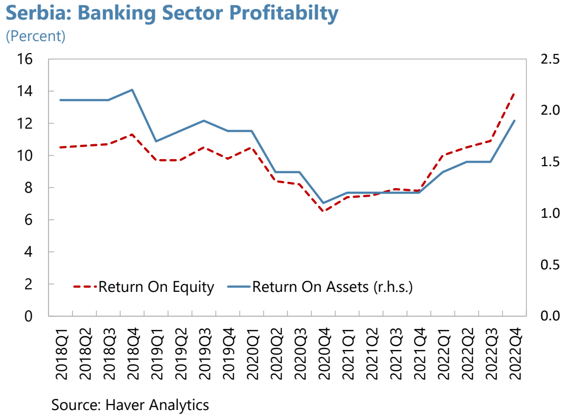
(Percent)



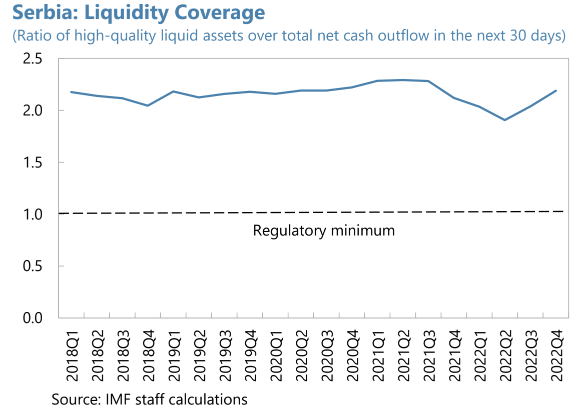
Source: Haver Analytics

Text Figure 3. Key Banking Sector Indicators (concluded)

A recovery in profitability should support capital accumulation and lending.



Banking sector liquidity also remains high, despite a temporary dip in early 2022.



32. The NBS's recent relaxation of regulatory measures to deal with adverse shocks should be phased out. While recognizing the need to protect affected sectors, the recent relaxation of regulatory standards risks undermining transparency and market discipline. While the macro-economic impact of the regulatory measures appears limited, they should be phased out.

Text Box 1. 2022–23 Relaxation of Regulatory Measures

In 2022–23, the NBS introduced several regulations on banks aimed at addressing the adverse impacts of last year's shocks. Details of the main measures are outlined below.

- In June 2022, the NBS adopted a regulation enabling banks to exclude 70 percent of net unrealized losses from falling bond prices from the calculation of CET 1 capital until the end of 2022. The measure was subsequently extended through end-2023. The authorities report that this measure increases system-wide CET 1 capital by 0.6 percentage points.

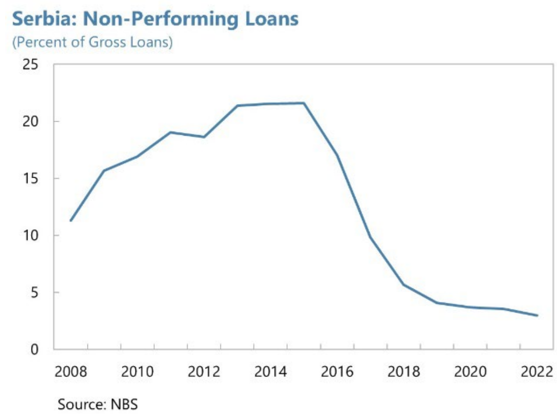
- In August 2022, the NBS encouraged a "gentlemen's agreement" with banks to limit the fees for a basic bank account in dinar and required banks to report any fee changes.

- In October 2022, the NBS allowed the rescheduling of principal payments on agricultural loans by six to twelve months, as the sector was severely hit by last year's drought. In January 2023, this measure was extended to borrowers engaged in the purchase and storage of fruit, with an application deadline of end-April 2023. The extended loans are not required to move from stage 1 to stage 2 treatment under IFRS9.

- In December 2022, the NBS extended pandemic measures enabling banks to lengthen the repayment period for housing loans by up to five years without any impact on the regulatory treatment of those loans through end-2023. Uptake of this measure is reportedly low.

- In December 2022, amendments to the Decision on Capital Adequacy of Banks adopted a permanent measure enabling banks to extend the maturity of consumer and cash loans of financially distressed individuals by three years although requiring such loans move from stage 1 to stage 2 treatment under IFRS9.

33. The Deposit Insurance Agency (DIA) made good progress in selling its legacy assets. In 2015, NPLs were over 20 percent of gross loans. A strategy to help debt write-offs, improve the collection of receivables, and support secondary market NPL sales helped lower NPLs to 3 percent in 2022. The DIA is tasked with recovering the assets of bankrupt banks including through asset sales and the settlement of creditors' claims. Such sales are expected to be completed by the first half of 2023.



34. Capital market deepening would help foster domestic savings and investment, spurring growth. Serbia's financial system remains largely bank based. While this is not unusual for a country at Serbia's stage of development, developing non-bank financial institutions would help boost domestic private savings and investment. The recent new Law on Capital Markets aligns Serbia's regulatory framework with the EU acquis and with MiFID II requirements. The authorities are building on these efforts by creating a One Stop Shop internet platform for market participants and creating a new unit in the Ministry of Finance to support capital market participants.

35. Authorities' Views. The authorities agreed that maintaining financial stability is a priority while they were confident that the sector is stable. They will continue to closely monitor risks in the banking sector, strengthen financial sector regulatory and supervisory frameworks to be fully aligned with international standards, and promote financial inclusion. The authorities will also continue working on enhancing Serbia's capital markets and diversifying sources of long-term financing in line with their Capital Market Development Strategy.

E. Governance and Other Structural Policies—An Ambitious Agenda

36. The new SOE governance law, adopted by Government in May 2023, will, if fully implemented, help transform the way SOEs are run in Serbia. The new law will help minimize political interference in daily SOE activities and will help professionalize the sector. In line with the OECD Guidelines for corporate governance of SOEs, the new law: (i) mandates supervisory boards to appoint general managers at arm's length from the government; (ii) defines mechanisms for setting and monitoring SOE mandates and objectives; (iii) defines the main principles for covering costs of public policy objectives; and (iv) prescribes strong disclosure and transparency requirements. The law will also help reduce the current excessive reliance on acting directors in SOEs and will lead to their replacement by permanent, professional, management. Adoption of this landmark legislation by the National Assembly is expected to take place shortly, followed by a transition period of up to 2 years for its full implementation.

37. Further improving the investment climate will strengthen Serbia's medium-term growth prospects. Serbia's strong macroeconomic performance, its location and good infrastructure links with Europe, and its well-trained workforce, all make it an attractive FDI destination (Figure 4). Further improving the investment climate would help increase positive spillovers to local firms (Annex II). Priority areas include increasing judicial efficiency and predictability, streamlining business regulations, and further aligning tertiary education and vocational training to skills needed in the workplace.

38. Serbia also needs to prepare now for the introduction of the EU's Carbon Border Adjustment Mechanism (CBAM). Recent staff analysis suggests that while the CBAM may have a small impact at the macroeconomic level, its effects on some carbon-intensive sectors may not be trivial, and there would be need for targeted support to ensure that resources and employment are redirected toward greener activities.[3]

39. The informal economy remains large despite recent welcome declines. Supported by tax administration and "e-fiscalization" reforms, the informal economy has been shrunk in recent years, but it still accounts for about 20 percent of GDP as of 2021.[4] Building on earlier reforms, the authorities adopted a new program for 2023–25 with 23 measures aimed at: (i) strengthening the capacity of inspections and misdemeanor courts; (ii) improving tax oversight and reporting procedures; and (iii) facilitating fiscal and administrative relief for legal businesses. While increased monitoring and enforcement play an important role, the authorities should also focus on streamlining business regulation and simplifying tax administration.

40. The authorities continue to make progress on governance and anti-corruption reforms. Beyond SOE reforms, other measures to strengthen governance and anti-corruption are in the works. To improve asset declaration, progress has been made on coordination and data exchange across relevant agencies. The authorities are also working on addressing outstanding GRECO[5] recommendations including broadening the definition of Persons with Top Executive Functions (PTEFs) to include Ministerial Chief of Cabinets and Advisors and ensuring systematic examinations of the declarations outside of the annual verification plan by September 2023, when the next GRECO evaluation is due. At the same time, human resource constraints continue to hamper anti-corruption agencies, particularly on verification. The new judiciary law, which takes effect in June, reduces Parliament's role in judicial appointments. It would be important to complement this by introducing the planned new IT system for judicial decisions to improve decision transparency and consistency.

41. AML/CFT reforms continue apace. The authorities plan to continue implement the requirements of all AML/CFT-related EU Directives and Regulations, in line with the FATF Standards and with EU implementation deadlines. They have re-assessed and modified the National AML/CFT Strategy and Action Plan (2022–24) which focuses, among other areas, on retention and further

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[3] See Cevik and others (2023), *Climate Change Mitigation and Policy Spillovers in the EU's Immediate Neighborhood*, IMF Departmental Paper, forthcoming.

[4] Atanasijevic and others, Shadow Economy Estimation Using Cash Demand Approach: The Case of Serbia, Sustainability 2022, 14(20), 13179; https://doi.org/10.3390/su142013179.

[5] EU Group of States against Corruption. https://www.coe.int/en/web/greco/home

improvement of human, financial, and technical resources. The transparency of beneficial ownership of legal entities operating in Serbia will also be further strengthened by enacting a new law that will enhance Serbia's capacities to ensure adequate, accurate and up-to-date information on beneficial owners. In addition, the authorities plan to review the Law on Centralized Records of Beneficial Owners to improve record content and relevant software applications. The authorities should also continue strengthening the AML/CFT risk-based supervision of banks (including issuance of sufficiently dissuasive sanctions for failure to implement the AML/CFT preventive measures and managing the regulatory and reputational risks arising from Serbia's exposure to EU sanctions) and gatekeepers (lawyers, accountants, and trust and company service providers) to mitigate the regulatory and reputational risk of sanction evasion.

42. **Distortive restrictions on international trade and direct market interventions should be minimized.** The removal of the excise discount on fuel is welcome. But the temporary imposition of new import duties on milk and cheese to protect local farmers needs to be phased out by June 2023, as currently envisaged. Special easing of banking regulations by the NBS like the recent loan rescheduling provision for fruit producers are also inappropriate. The authorities should also phase out remaining price regulations on gasoline and diesel as soon as possible.

43. **Data are broadly adequate for surveillance.** The authorities continue to work on improving coverage in government finance statistics (Informational Annex).

44. **Authorities' Views.** The authorities are fully committed to implementing further structural reforms to improve the business environment and support higher private sector led growth. E-fiscalization has been effective at reducing the size of the informal economy, but there is potential for further progress, especially when complemented with measures to modernize the tax administration and to promote digitalization in other administrative areas. The authorities recognize the need to further improve social assistance outreach while leveraging active labor market measures. Strengthening governance and AML-CFT enforcement are key priorities, not least given their importance for EU accession. In this regard, the new IT system for judicial decisions will be fully operational by end-2024. Finally, the authorities are committed to strengthening SOE governance, with the new SOE law setting the foundation for improved practices.

PROGRAM MODALITIES

45. **The program remains fully financed.** The Fund-supported program is fully financed, with firm commitments for the first 12 months of the arrangement and good prospects for the remaining program period. The authorities plan to purchase SDR163.7 million after completion of the first review of the SBA to fill a balance of payment financing need (Table 12). Good progress has been made in agreeing budget support (World Bank/ADF/KfW) and energy-sector support (EBRD) loans. In the baseline, which assumes the same path of planned remaining purchases from the IMF as at SBA approval, reserves are now expected to peak above 140 percent of the Assessing Reserve Adequacy (ARA) metric and to remain above 130 percent of the ARA metric throughout the projection horizon, better than at program approval.

46. Staff recommends that the end-December 2023 QPC on the fiscal deficit be tightened, the NIR floors updated, and new program targets be set through June 2024. The authorities have requested modification of (i) the end-June and end-December 2023 QPC on NIR and (ii) the end-December 2023 fiscal deficit QPC. Specifically, it is proposed that the end-2023 QPC on the fiscal deficit be set equivalent to a deficit of no more than 3 percent of GDP (0.3 percent of GDP tighter than at SBA approval). With continued elevated inflation and uncertainty over needed energy sector support, it is proposed that the ceiling on current primary expenditure of the Republican budget be left unchanged. The 2023 path of program floors on NIR is updated to reflect the latest ARA metric projection. ITs for March 2024 and QPCs for June 2024 are consistent with the program design at SBA approval: no more than a 2.2 percent of GDP fiscal deficit for 2024 and a NIR floor consistent with GIR at 80 percent of the ARA metric.

47. New proposed structural benchmarks reflect earlier policy commitments. Two new structural benchmarks, both effective November 1, 2023, envisage further increases in: (i) average natural gas tariffs by 10 percent, and (ii) electricity tariffs for households and the cap for the electricity prices for the corporate sector by 8 percent (**new end-October 2023 SB**). The authorities and staff also propose a new SB to further expand the ISKRA system to cover the health sector and make it fully operational (**new end-January 2024 SB**). This would be an important measure to support the long-planned public wage grid reform.

48. Serbia's capacity to repay the Fund is assessed to be adequate, including under the adverse scenario (Tables 5a and 5b and Annex VIII). Under the baseline, with purchases of total authorized access, including precautionary tranches, of 290 percent of quota, Fund credit outstanding would reach a maximum of 3.2 percent of GDP, and 10.0 percent of gross reserves in 2024, while debt service to the Fund would peak at 1.8 percent of exports of goods and nonfactor services in 2027 before declining.

49. Serbia has small sovereign arrears outstanding. The authorities have been in contact with their Libyan counterparts to resolve Serbia's arrears to Libya, which arose in 1981 due to unsettled government obligations related to a loan for importing crude oil.

50. Risks to the program remain moderate while uncertainty remains high. Key risks continue to be the uncertain duration of Russia's invasion of Ukraine and its economic repercussions across Europe, global recession risks and renewed commodity price shocks (see Annex VIII for an illustrative scenario). The authorities' actions to retain and expand natural gas storage, and the increases in energy tariffs mitigate fiscal risks. The authorities also have a strong long track record of maintaining macroeconomic stability and of program implementation.

51. An updated safeguards assessment of the National Bank of Serbia is underway. The IMF safeguards assessment mission in April 2023 found a sound legal framework, strong operational controls, with financial reporting and internal and external audit processes that are aligned with international standards. Governance arrangements at the NBS have strengthened with the establishment of an Audit Committee since the 2015 assessment. Recommendations include further solidifying the Council's oversight by providing for recourse to external expertise (when needed) and efforts to strengthen the risk management function.

STAFF APPRAISAL

52. Serbia has made impressive economic gains over much of the past decade. Living standards improved, inflation fell, public finances were strengthened, and reserves were increased to an all-time high, helped by ample FDI inflows. The pandemic only temporarily interrupted this strong performance. At the same time, weak banks and NPLs were dealt with—NPLs are now at an all-time low and banks have strong balance sheets. Reflecting these positive developments, Serbia's sovereign credit ratings were upgraded steadily over the past decade and now stand one notch below investment grade.

53. But spillovers from the war in Ukraine and deep-rooted energy sector problems generated large external and fiscal financing needs, prompting the authorities to request a two-year SBA. High energy import prices, a regional drought, shortfalls in domestic electricity production (after years of energy sector underinvestment), and tightening global financial conditions all acted as major headwinds to the Serbian economy. Growth slowed in the second half of 2022 and, in response to elevated financing needs, the authorities requested a disbursing Fund-supported program.

54. Macroeconomic imbalances have started to moderate under the program and further improvements are expected over the medium term. The 2022 fiscal and current account deficits have turned out far lower than expected at the time of program approval, and foreign exchange reserves are now well above program projections. Unemployment is at a historic low. And record FDI inflows continue to support investment, exports, and productivity growth, as well as helping reserves. Growth is expected to recover to potential and the current account deficit to narrow further by the end of the program. Continued fiscal consolidation will put public debt on a firm downward trajectory.

55. But inflation remains a pressing challenge. Driven by high food and energy prices, headline inflation is now well above the NBS's target band. Core inflation has also increased sharply, as high input prices were passed through the value chain. Inflation expectations are also elevated, although they have stabilized in recent months, and appear to remain anchored.

56. Risks have fallen since SBA approval but remain high. Uncertainty stems from domestic political and geopolitical and energy sector developments, concerns over trading-partner growth, a still-challenging global inflation environment, and adverse global financial market developments. The energy sector remains an acute source of vulnerability to the economy. On the upside, Serbia could benefit from the relocation of skilled migrants and businesses and continued nearshoring.

57. Tighter monetary policy is needed to lead the disinflation drive. The NBS should ensure that real ex-ante policy rates become positive, including by raising rates further as needed. This will help bring about the expected disinflation under the program and restore inflation to target by the program's end. But the NBS will need to persist with tight policies until the path of inflation is clearly converging to target, especially given Serbia's troubled inflation history. A tight monetary stance will also support dinarization and help to further build foreign exchange reserves.

58. Continued fiscal consolidation is essential to help lower inflation and public debt. A fiscal deficit of no more than 3 percent of GDP in 2023 is appropriate. Any fiscal overperformance should be saved or used for well-targeted capital and social spending, but untargeted and one-off fiscal measures should be avoided. All aspects of the fiscal rule should be followed. Further consolidation in 2024 would provide for a smooth transition to the full implementation of the new fiscal rule, which comes into effect in 2025, just after the end of the program.

59. Energy sector reform remains a program priority. The costly energy sector fiscal subsidies in 2022 were caused in part by high international prices, but deep-rooted sectoral weaknesses from years of underinvestment and poor management added to the problem. Reform of this sector has started and remains a core component of the SBA.

60. Further energy reforms should comprise ongoing tariff hikes and structural reforms that address Serbia's deep-rooted energy sector problems. Higher end-user tariffs on gas and electricity are critically important to improve the financial viability of the energy SOEs and to help finance much-needed investment. On the structural side, the new SOE governance law, which is aligned with OECD best practice, provides a strong foundation for governance reform in the energy sector and beyond. Building on this, the conversion of EPS to a joint-stock company is an important first step towards a deeper strategic restructuring by end-2023. Staff also welcomes the adoption of a prioritized and fully-costed energy sector investment plan, which will help to enhance energy security, stabilize electricity generation, and start the green transition by reducing emissions and conserving energy.

61. The financial sector appears sound, although continued vigilance is required as interest rates rise and as global financial sector risks remain elevated. Bank capital and liquidity ratios remain well above minimum regulatory levels, and non-performing loans are at a historic low. Although contagion from the recent global financial sector turmoil has been limited, the riskier global environment calls for continued scrutiny of the sector, including ongoing careful monitoring of deposits and liquidity. Further closing regulatory and supervisory gaps with the EU should remain the priority.

62. Private sector led growth should be supported by further improving the business climate. Reforms to strengthen the rule of law, improve the efficiency of the judicial system, and curb corruption are critical for the investment climate. Efforts to tackle informality should continue. Deepening domestic capital markets would help diversify sources of long-term financing, ease access to financing for small and medium enterprises, and support medium-term growth.

63. Staff supports the authorities' request for completion of the first review under the SBA. In addition, staff support the authorities' request to modify the three SBA QPCs on the NIR (end-June and end-December 2023) and fiscal deficit (end-December 2023). Finally, staff also recommends that the next Article IV consultation with Serbia be held on the 24-month cycle.

Box 1. Inflation Dynamics

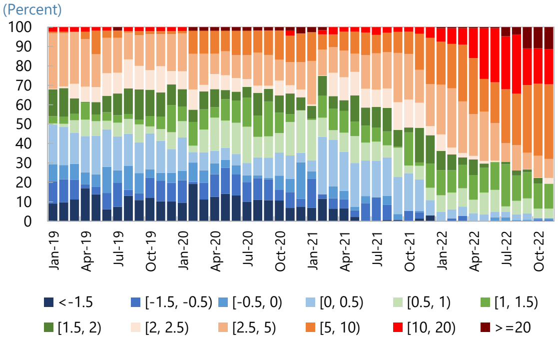
External factors, including international food and energy prices, were significant drivers of inflation in 2022 for West Balkan countries, including Serbia. Serbia-specific domestic factors also play important roles in explaining its inflation.

Inflation surged in Serbia in 2022 because of international commodity price increases, supply shortages from drought, and a strong recovery of domestic demand after the pandemic. Inflation became increasingly broad-based, manifested in the increasing share of CPI components showing large price increases and different measures of "core" inflation picking up in varying degrees (box figures), making it a priority for policymakers to accurately diagnose the drivers of the current surge in inflation.

International food prices are an important driver of headline and core inflation in Serbia. A panel Phillips curve regression employing data from West Balkan countries identifies external factors, in particular international food prices, as a major driver of regional inflation. The significance of international food prices partly reflects the large share of food items in the consumption basket (more than 30 percent). Notably, international food prices also appear to affect core inflation. This may be because of the large share of food prices in Western Balkan countries' CPIs, which means they may play a role in determining wages that in turn affect core inflation. Average wage growth has been broadly in line with headline inflation in recent months.

Serbia: Inflation Dispersion of Core Items 1/

(Percent)

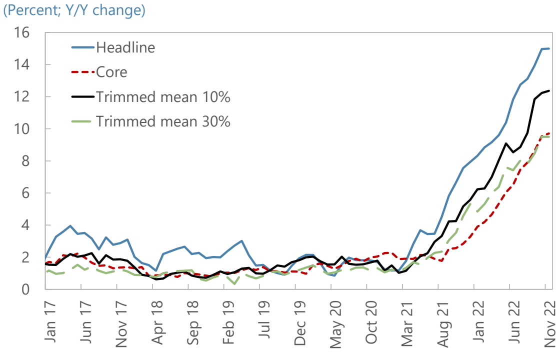


1/ Share of consumption basket within each inflation band. Exclude food and energy items.

Sources: NBS, Haver Analytics, and IMF staff calculations

Serbia: Different Measures of Underlying Inflation

(Percent; Y/Y change)



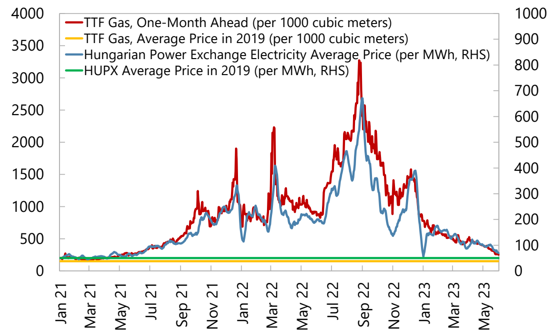
Sources: NBS, Haver Analytics, and IMF staff calculations

Box 2. Energy Sector Developments

International energy prices have fallen to levels prevailing prior to the war in Ukraine but remain above historical averages. Domestic electricity production has also recovered. These factors will ease balance of payment pressures and, alongside higher domestic tariffs, will reduce required fiscal subsidies. Energy SOE balance sheets need to be strengthened further, however, and large operations and investment needs remain.

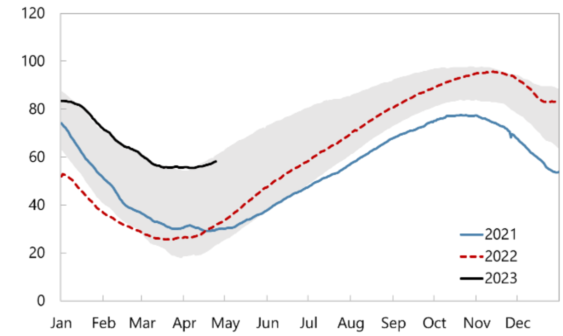
International energy prices have fallen to levels prevailing before the war in Ukraine. Warmer-than-normal weather in Europe and historically high EU natural gas storage levels pushed gas prices to below those at the time of SBA approval, and significantly below the summer 2022 peak. As gas-powered generation is the marginal producer of electricity in European wholesale markets, electricity prices also fell as gas prices declined. Oil—which also acts as a reference price for some gas contracts—and coal prices have also fallen significantly.

Wholesale Energy Prices
(in Euro)



Sources: Bloomberg and HUPX

EU: Gas Storage
(Percent of Capacity)



Source: Gas Infrastructure Europe, Storage Database

Serbia's domestic electricity production has recovered, and domestic energy consumption and imports have fallen.[1] The restoration of hydropower generation as drought conditions ended and continued imports of coal underpinned the recovery of electricity production at EPS. Electricity supply was also supported by the first gas-powered plant in Serbia, which started operating in November 2022. Warm winter weather and tariff-related incentives to promote household energy conservation limited domestic energy demand and allowed Serbia to export electricity during the winter, supporting EPS's finances.

The favorable long-term gas contract with Russia's Gazprom has been temporarily expanded. The new annexes to the contract allow for imports of 8 million cubic meters (CM) per day on top of 6 million CM agreed under the original contract. These combined amounts meet daily peak winter consumption demand. However, the gas price for these additional imports is higher than the prices agreed under the original contract, currently at about US$380 per thousand CM.[2] Taking advantage of these temporary agreements, the authorities have preserved gas reserves in their storage facilities in Serbia and Hungary, even during winter months. As of early May 2023, total gas reserves at the domestic Banatski Dvor and the Hungarian storage were sufficient to cover about 68 days of annual average daily consumption.

[1]For an overview of the structure of Serbia's energy market, see Annex VI of the December 2022 Request for a SBA.

[2]The price is calculated as 70 percent market price and 30 percent of price under the long-term contract with Gazprom (indexed to crude oil prices).

Box 2. Energy Sector Developments (concluded)

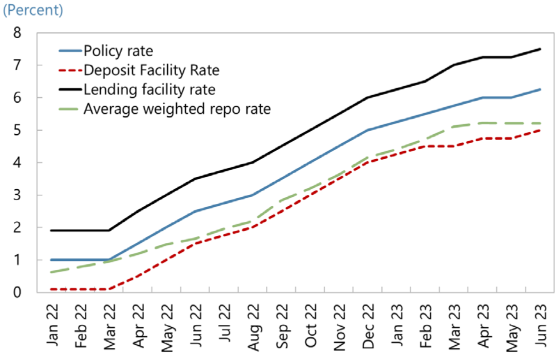
These developments will ease balance of payments pressures, but with a lag, as energy imports are contracted several months ahead of delivery. Lower demand—driven by warmer weather and higher end-user prices—have also reduced import volumes. It is estimated that the value of energy imports in 2023 will be over 30 percent lower than 2022, reducing the current account deficit by around €2.2 billion (about 3 percent of GDP), driven largely by 20 percent lower average energy import prices and no electricity imports as domestic production returns to normal. Fiscal support to EPS and Srbijagas is expected to fall from 2.5 percent of GDP in 2022 to below 1.0 percent in 2023.

Box 3. Monetary Policy Operations in Serbia

As with many central banks, the NBS has two key interest rates that influence reserve renumeration: (i) the deposit rate on "excess reserves" above the minimum reserve requirement, and (ii) the policy rate that applies to open market operations (OMOs).[1] Since the beginning of 2022, both interest rates have increased in parallel, apart from March 2023, when the deposit rate was kept unchanged while the policy rate was raised by 25 basis points.

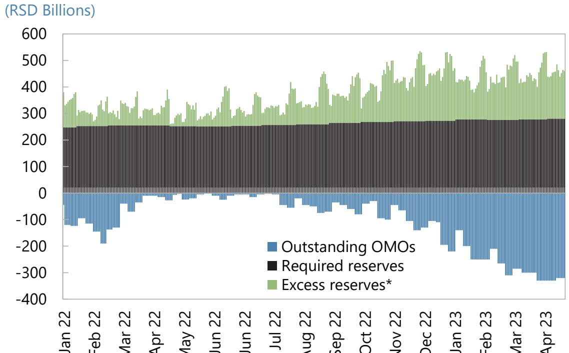
As the pace of foreign exchange intervention increased since November 2022, Dinar liquidity rose significantly. To sterilize these purchases, OMOs—1-week repo operations—also increased. In Serbia, the NBS determines the amount of liquidity that is sterilized each week and an auction determines the average interest rate of these repos.[2] This market-determined interest rate is below the policy rate[3,] and only just above the deposit rate (which acts as a lower bound). In recent months, 'excess reserves' in the system—renumerated at the deposit rate—have increased significantly. It is likely that banks would prefer to hold fewer excess reserves but are limited by the scale of the repo auctions held by the NBS.

Serbia: Policy Rates
(Percent)



Sources: NBS and IMF staff calculations

Serbia: Central Bank Deposits and OMOs
(RSD Billions)



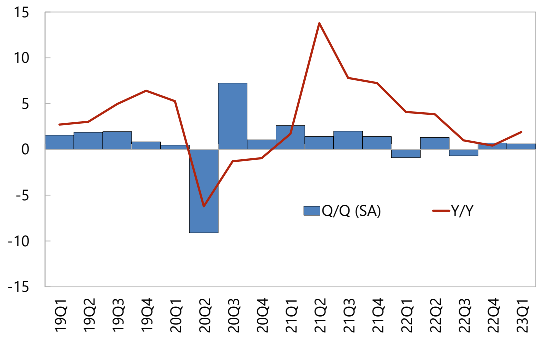
Note: *Includes 'current account of banks' and 'account of deposited liquid resources
Sources: NBS and IMF staff calculations

1/ Required reserves are remunerated at 0.75 percent, and a lending facility is available to banks to meet the reserve requirement at a penal rate.
2/ Alternatively, the OMOs could proceed on a 'full-allotment basis' whereby the central bank determines the interest rate and the market decides on the *quantity* of liquidity that it provides for these repos.
3/ The policy rate is the maximum repo rate accepted at any OMO auction

Figure 2. Real Sector Developments

After a strong post-pandemic rebound, GDP has dipped …

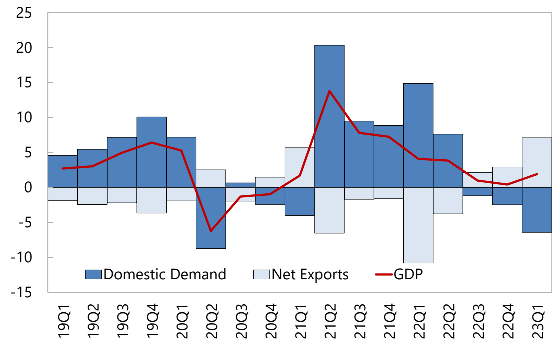
Serbia: Gross Domestic Product
(Percent)



Sources: Haver Analytics, SORS, and IMF staff calculations

… with high inflation and fiscal tightening weighing on domestic demand.

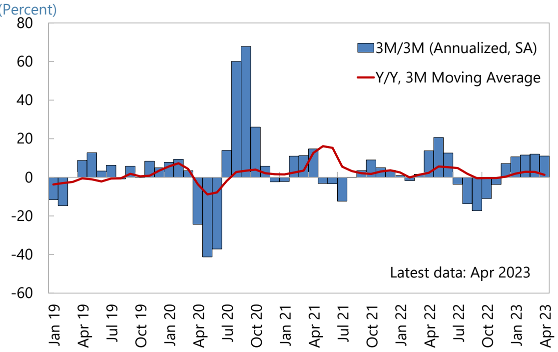
Serbia: Contribution to Growth
(Percent, Y/Y)



Sources: Haver Analytics, SORS, and IMF staff calculations

Industrial production has been hit by high energy prices …

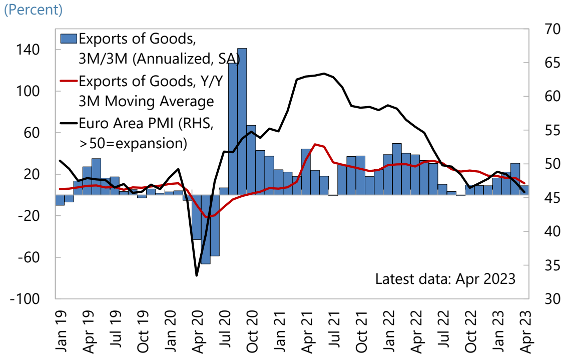
Serbia: Industrial Production
(Percent)



Sources: Haver Analytics, SORS, and IMF staff calculations

… and weak trading partner growth, which reduced export growth until recently

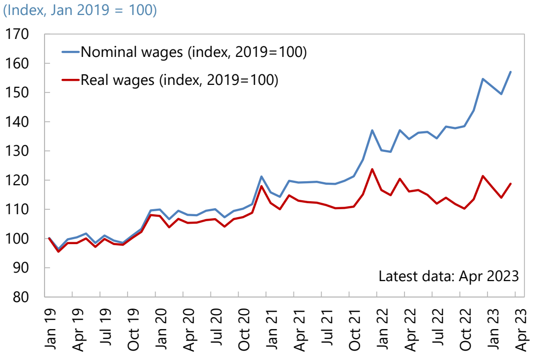
Exports of Goods and Euro Area PMI
(Percent)



Sources: Haver Analytics, SORS, and IMF staff calculations

Real incomes are flat …

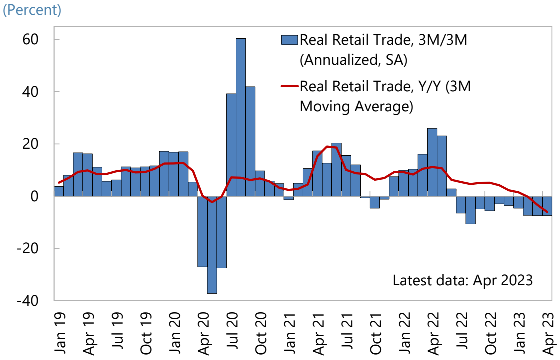
Serbia: Net Wages
(Index, Jan 2019 = 100)



Sources: Haver Analytics, SORS, and IMF staff calculations

… constraining real retail spending growth.

Serbia: Retail Turnover
(Percent)



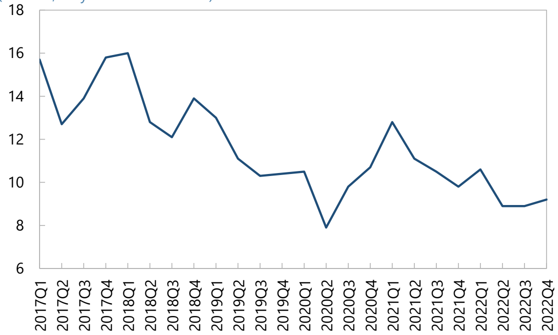
Sources: Haver Analytics, SORS, and IMF staff calculations

Figure 3. Labor Market Developments

Unemployment has fallen …

Serbia: Unemployment Rate

(Percent, 15 years old and more)

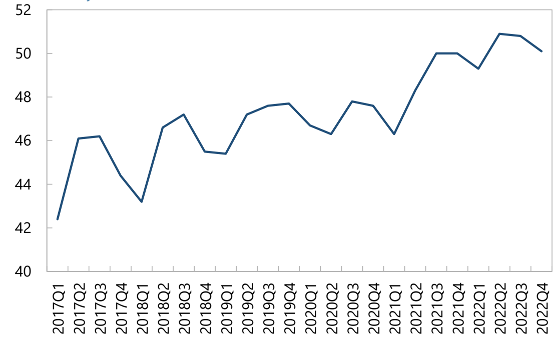


Source: SORS

… and employment has grown.

Serbia: Employment Rate

(Percent, 15 years old and more)

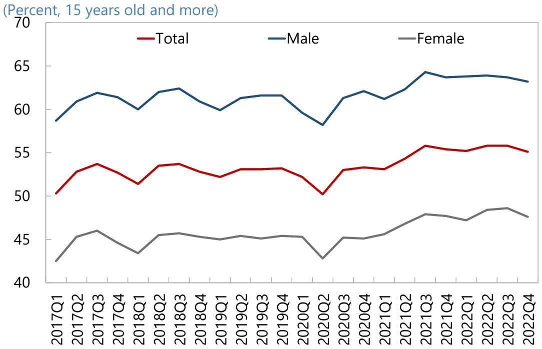


Sources: SORS

Labor force participation has increased …

Serbia: Labor Participation Rate

(Percent, 15 years old and more)

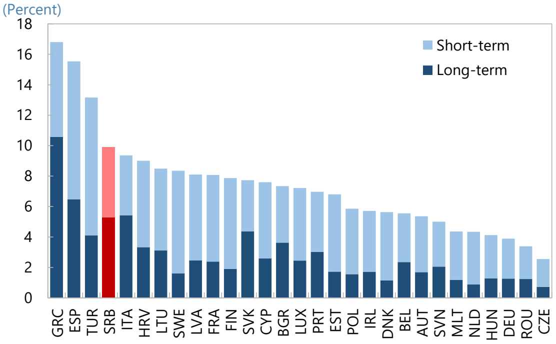


Sources: SORS

… although unemployment, which has fallen, remains high compared to peers.

Unemployment Rate, 2021 or latest available

(Percent)

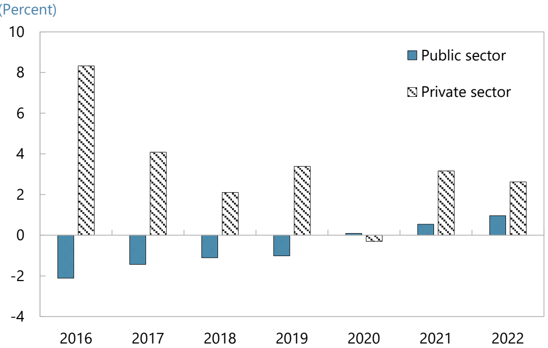


Sources: International Labour Organization; OECD database; Republic of Serbia National Employment Service; and IMF Staff calculations

Employment growth has been driven by the private sector.

Serbia: Employment Growth

(Percent)

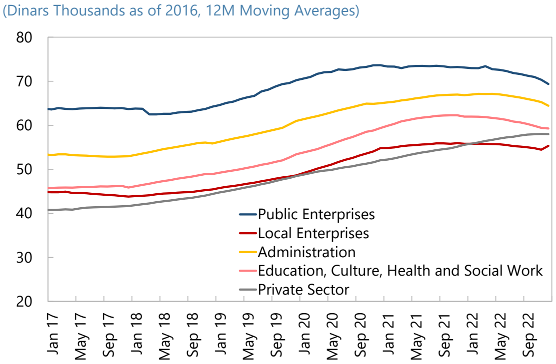


Sources: SORS and IMF staff calculations

And private sector wages have increased faster than in the public sector.

Serbia: Average Monthly Net Real Wages

(Dinars Thousands as of 2016, 12M Moving Averages)



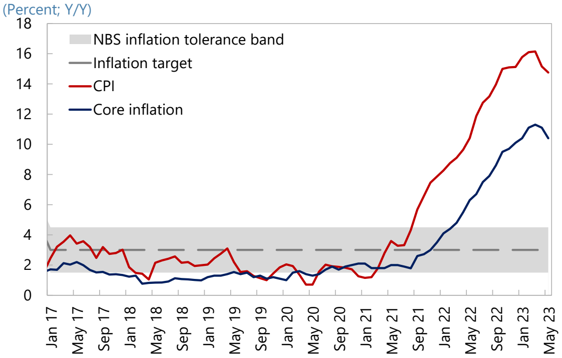
Sources: SORS; and IMF Staff calculations

Figure 4. Inflation and Monetary Policy

Inflation is high but may be levelling off …

Serbia: Inflation

(Percent; Y/Y)

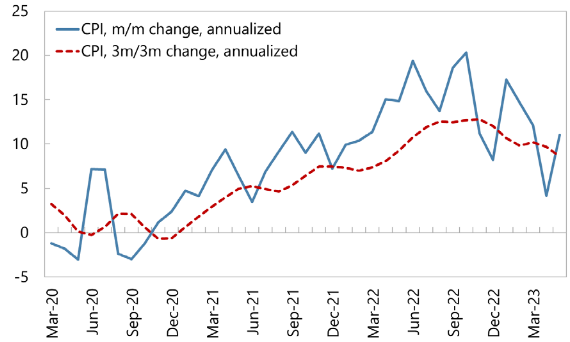


Sources: NBS and IMF staff calculations

… as momentum appears to be starting to slow.

Serbia: Inflation Momentum

(Percentage point change; seasonally adjusted)

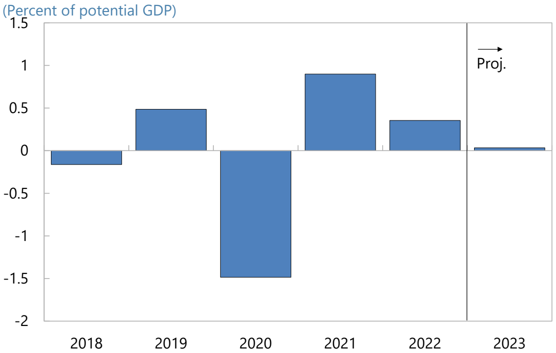


Sources: Haver Analytics and IMF staff calculations

The output gap remains close to zero.

Serbia: Output Gap

(Percent of potential GDP)

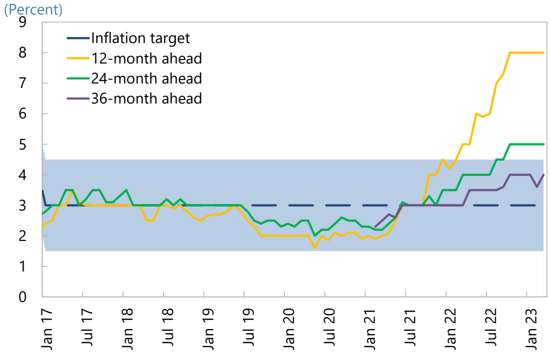


Sources: NBS and IMF staff projections

1-year ahead inflation expectations are high but in line with NBS and staff inflation forecasts.

Serbia: Inflation Expectations of Financial Sector

(Percent)

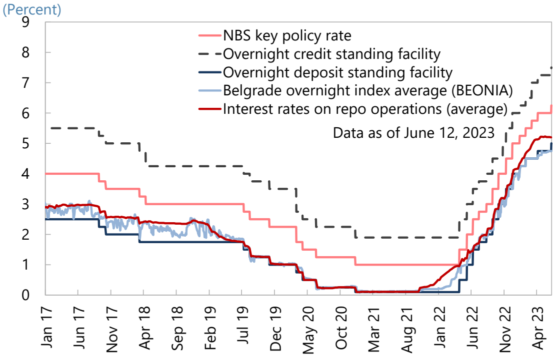


Sources: Bloomberg, SORS, and IMF staff projections

Since April 2022, the NBS increased the policy rate at each meeting until May 2023 when it paused at 6 percent …

Serbia: Interest Rates

(Percent)

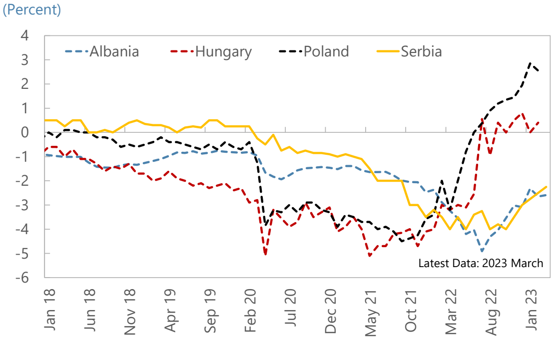


Sources: NBS and Haver Analytics

… despite this being negative in real terms and low compared to peer countries.

Policy Rate in Real Terms in Selected Countries

(Percent)



Sources: Haver Analytics and IMF staff calculations

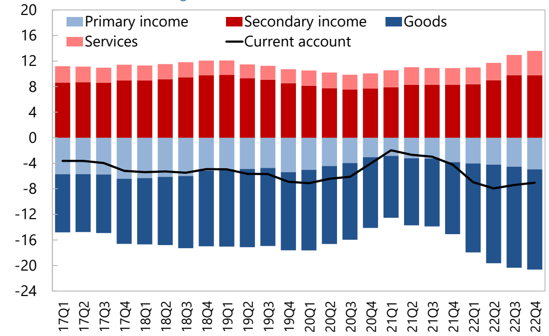
Note: Nominal policy rates adjusted by 1- year ahead inflation expectations.

Figure 5. Balance of Payments and NIR

The current account deficit has begun to narrow …

Serbia: Current Account Balance

(Percent of GDP; 4Q moving sum)

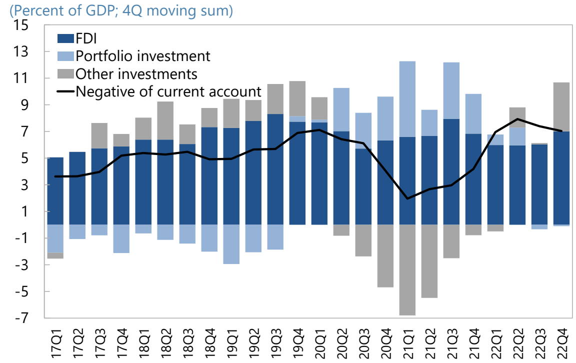


Sources: Haver Analytics and IMF staff calculations

… FDI remains robust, covering the current account deficit.

Serbia: Financial Account Composition

(Percent of GDP; 4Q moving sum)

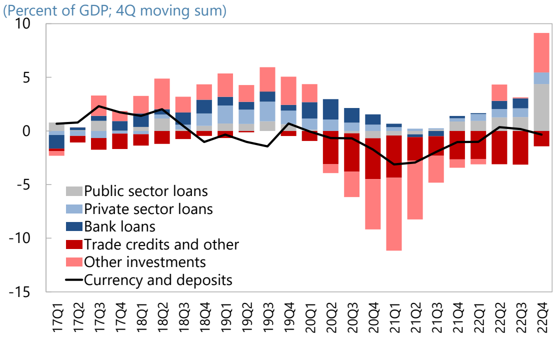


Sources: Haver Analytics and IMF staff calculations

Other investments are dominated by trade credits.

Serbia: Other Investments

(Percent of GDP; 4Q moving sum)

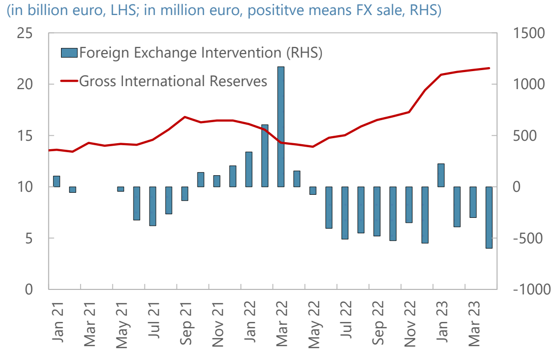


Sources: Haver Analytics and IMF staff calculations

International reserves have continued to increase.

Serbia: Reserves and Interventions

(in billion euro, LHS; in million euro, posititve means FX sale, RHS)



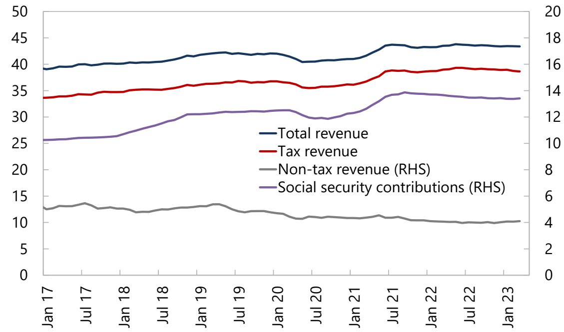
Source: NBS

Figure 6. Fiscal Developments

Revenues collection has performed well …

Serbia: Total Revenue Composition

(Percent of GDP, 12M sum)

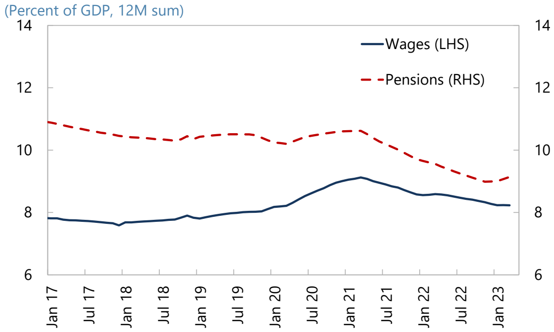


Sources: Ministry of Finance and IMF staff calculations

… while public sector wage and pension bills have declined as a share of GDP due to unexpected inflation.

Serbia: Wages and Pensions 1/

(Percent of GDP, 12M sum)



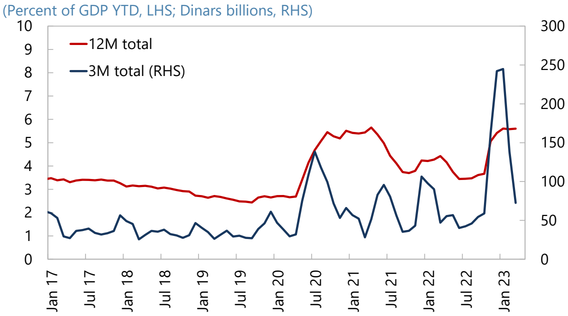
Sources: Ministry of Finance and IMF staff calculations

1/ Excludes employers' contributions

Support to companies was boosted during the pandemic, and more recently because of the energy crisis …

Serbia: State Aid 2/

(Percent of GDP YTD, LHS; Dinars billions, RHS)



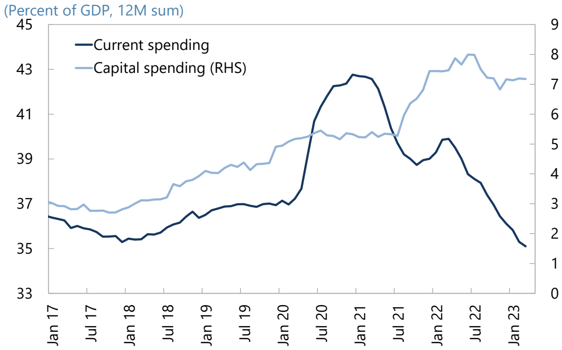
Sources: Ministry of Finance and IMF staff calculations

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.

… but public capital spending remains high.

Serbia: Current and Capital Spending

(Percent of GDP, 12M sum)

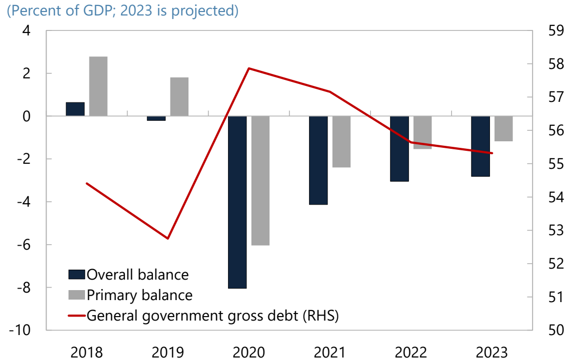


Sources: Ministry of Finance and IMF staff calculations

The fiscal deficit and public debt have declined since the pandemic spike.

Serbia: Fiscal Balance and Debt

(Percent of GDP; 2023 is projected)

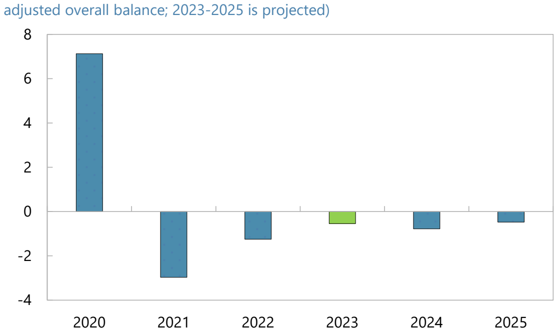


Sources: Ministry of Finance and IMF staff calculations

Fiscal adjustment is proceeding at a measured pace.

Serbia: Fiscal Impulse

(Percent of GDP; negative of the change in the general government cyclically-adjusted overall balance; 2023-2025 is projected)



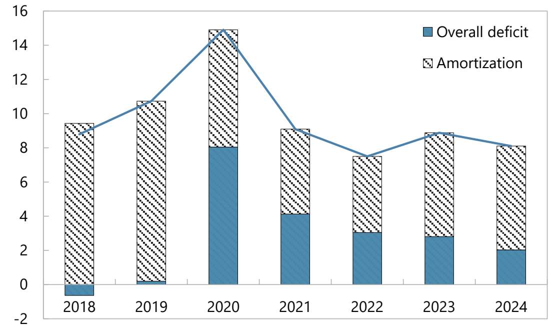
Source: IMF staff calculations

Figure 7. Fiscal Financing

Gross financing needs are expected to fall as the deficit declines and amortization needs ease.

Serbia: Gross Financing Needs

(Percent of GDP)

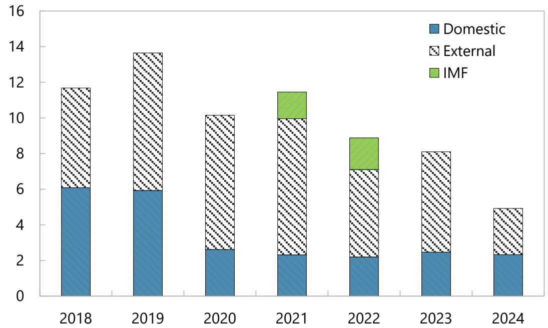


Sources: Ministry of Finance and IMF staff calculations

Financing has come of late mainly from external sources.

Serbia: Sources of Financing

(Percent of GDP)

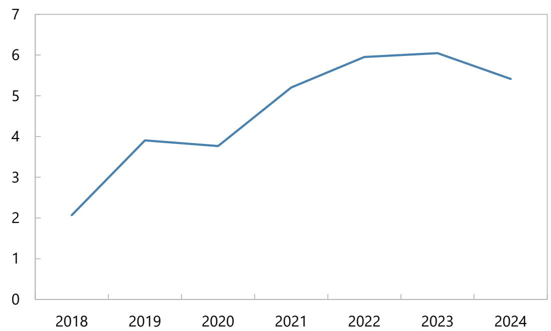


Sources: Ministry of Finance and IMF staff calculations

A large accumulation of deposits has taken place.

Serbia: Stock of Government Liquid Deposits

(Percent of GDP)

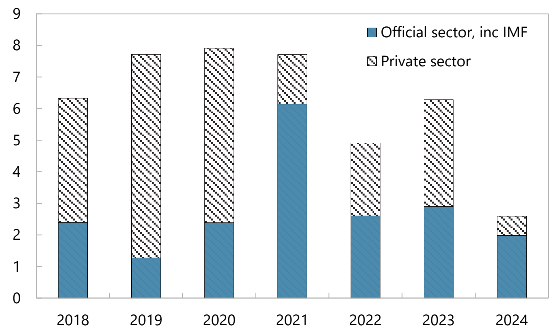


Sources: Ministry of Finance and IMF staff calculations

A significant share of external financing is expected to come from the official sector.

Serbia: External Financing

(Percent of GDP)

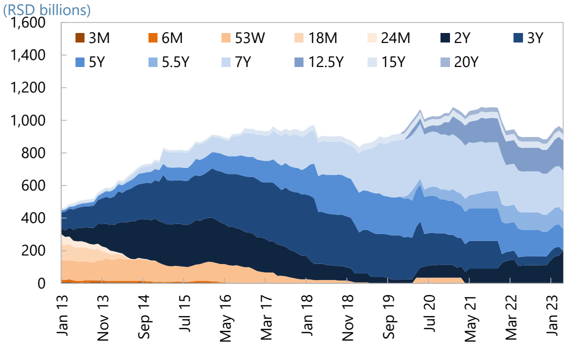


Sources: Ministry of Finance and IMF staff calculations

Most domestic debt is issued as securities, with the average maturity increasing.

Serbia: Domestic Debt Stock 1/

(RSD billions)



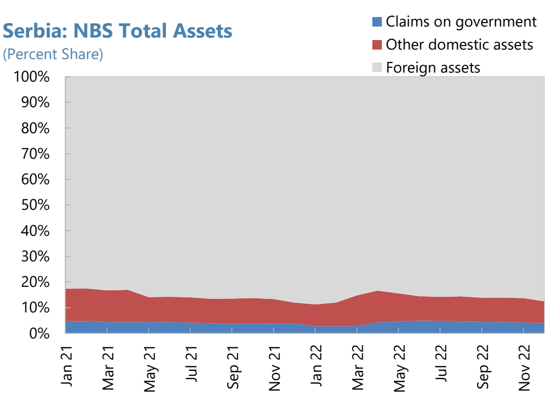
Source: National Bank of Serbia

1/ Sum of dinar and FX-denominated securities at current exchange rate

Only a small share of government debt is held by the NBS.

Serbia: NBS Total Assets

(Percent Share)

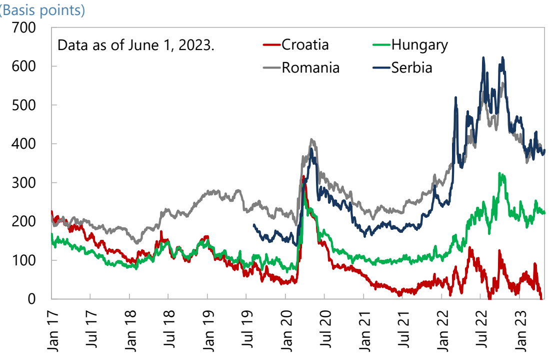


Sources: NBS and IMF staff calculations

Figure 8. Financial and Exchange Rate Developments

EMBIG spreads are narrowing somewhat …

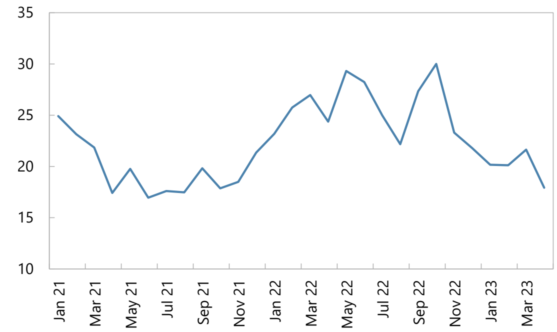
Sovereign Risk - Euro EMBIG Spreads
(Basis points)



Source: Bloomberg

… as global risk aversion has fallen back to pre-war levels.

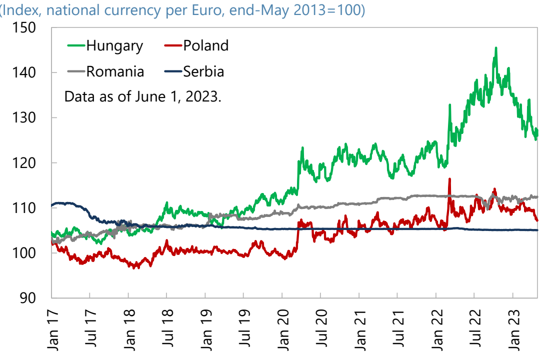
CBOE Volatility Index (VIX)
(Index)



Source: Federal Reserve Economic Data

The NBS maintains a de-facto stabilized exchange rate regime …

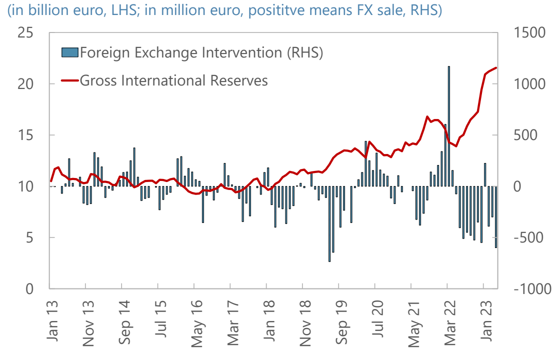
Exchange Rates in the Region
(Index, national currency per Euro, end-May 2013=100)



Sources: Bloomberg

… with ongoing FX intervention to address two-sided pressures.

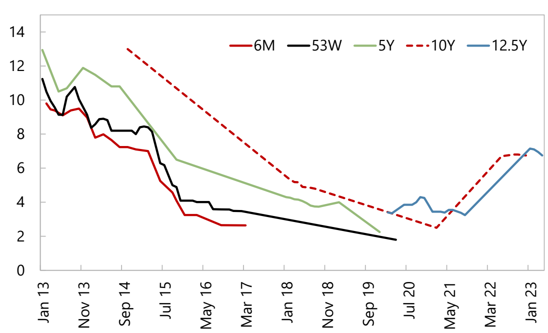
Serbia: Reserves and Interventions
(in billion euro, LHS; in million euro, posititve means FX sale, RHS)



Source: NBS

Yields have picked up since mid-2021, but remain negative in real terms for dinar-denominated securities.

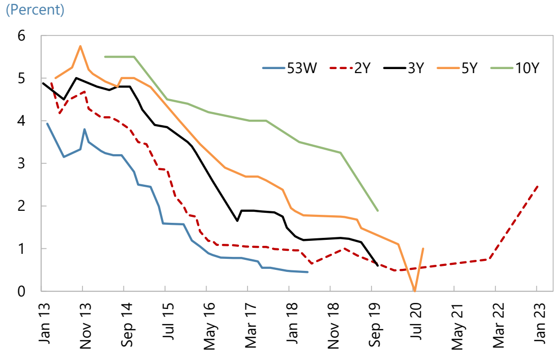
Serbia: Yields on Dinar-Denominated Domestic Securities
(Percent)



Source: NBS

Yields on euro-denominated securities also increased as ECB policy rates increased.

Serbia: Yields on Euro-Denominated Domestic Securities
(Percent)

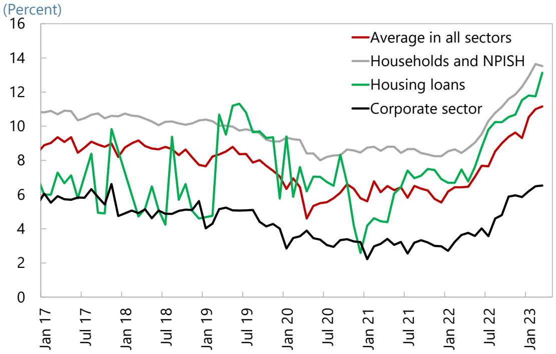


Source: NBS

Figure 9. Selected Interest Rates and Credit Development

Lending rates have increased for RSD-denominated debt …

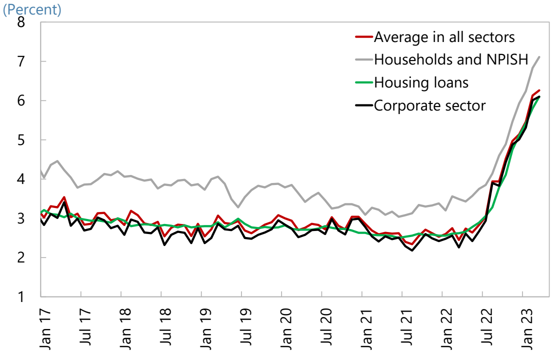
Serbia: Bank Lending Interest Rates (RSD)
(Percent)



Source: NBS

… and for FX and FX linked loans.

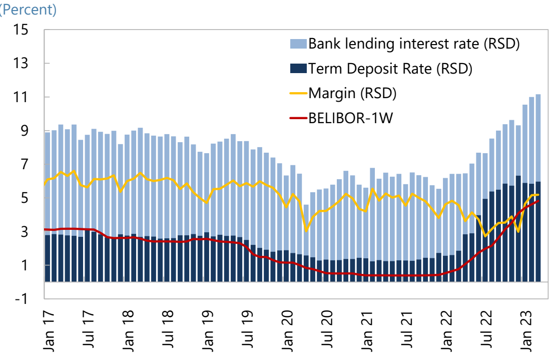
Serbia: Bank Lending Interest Rates (FX and FX-linked)
(Percent)



Source: NBS

But RSD lending margins appear broadly stable …

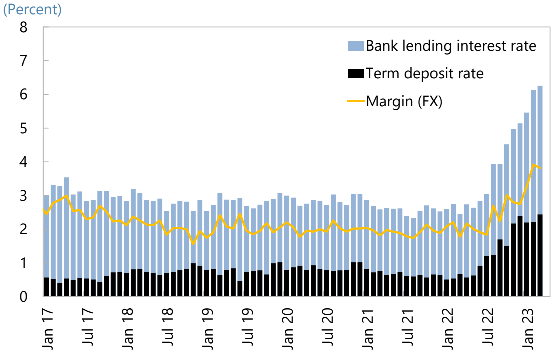
Serbia: Selected Interest Rates (RSD)
(Percent)



Source: NBS

… while FX lending spreads have ticked up.

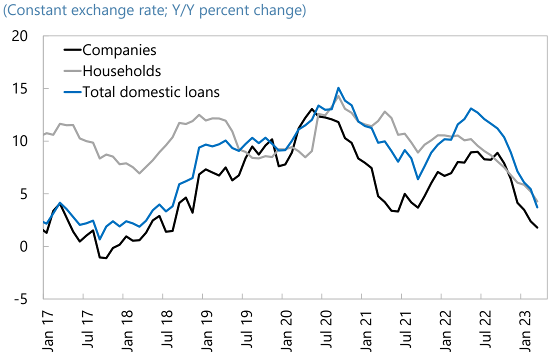
Serbia: Selected Interest Rates (FX and FX-linked)
(Percent)



Source: NBS

Credit growth is weakening …

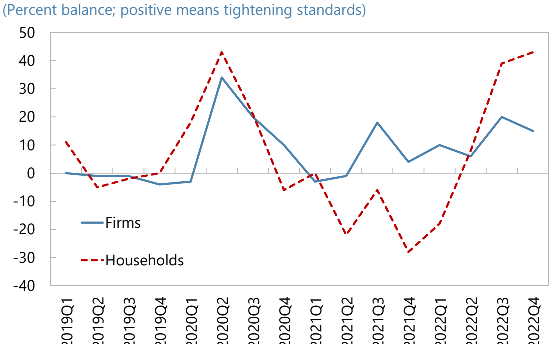
Serbia: Credit Growth to Non-Government
(Constant exchange rate; Y/Y percent change)



Source: NBS

… and credit standards have tightened.

Serbia: Credit Standards
(Percent balance; positive means tightening standards)



Note: share of banks that have tightened/loosened loan standards over past 3 months
Source: Haver Analytics

Table 1. Serbia: Selected Economic and Social Indicators, 2021–28

	2021	2022		2023		2024		2025	2026	2027	2028
		CR 22/384	Est.	CR 22/384	Proj.	CR 22/384	Proj.	Proj.	Proj.	Proj.	Proj.
				(Percent change, unless otherwise indicated)							
Real sector											
Real GDP	7.5	**2.5**	2.3	**2.3**	2.0	**3.0**	3.0	4.5	4.0	4.0	4.0
Real domestic demand (absorption)	7.7	**2.9**	3.9	**2.3**	1.7	**1.3**	2.8	4.3	3.9	3.8	3.7
Consumer prices (average)	4.1	**12.1**	12.0	**12.2**	12.4	**5.3**	5.3	3.5	3.2	3.0	3.0
Consumer prices (end of period)	7.9	**15.8**	15.1	**8.2**	8.2	**4.0**	4.0	3.5	3.2	3.0	3.0
GDP deflator	5.9	**10.3**	10.6	**10.7**	12.1	**6.7**	5.1	3.9	3.4	3.1	3.0
Unemployment rate (in percent) 1/	11.0	**10.5**	9.4	**11.1**	9.1	**10.6**	9.0	8.8	8.7	8.6	8.5
Nominal GDP (in billions of dinars)	6,270	**7,088**	7,091	**8,026**	8,109	**8,821**	8,784	9,537	10,256	11,001	11,787
				(Percent of GDP)							
General government finances											
Revenue 2/	43.3	**43.0**	43.4	**41.6**	42.1	**41.6**	42.1	42.4	42.4	42.4	42.4
Expenditure 2/	47.4	**46.8**	46.4	**44.9**	44.9	**43.8**	44.2	43.9	44.0	44.0	43.9
Current 2/	39.0	**37.1**	36.1	**36.1**	36.5	**36.0**	36.8	36.4	36.5	36.5	36.6
Capital and net lending	8.3	**9.4**	10.1	**8.4**	8.1	**7.5**	7.0	7.0	7.2	7.3	7.2
Amortization of called guarantees	0.1	**0.3**	0.3	**0.3**	0.3	**0.3**	0.3	0.5	0.2	0.2	0.1
Fiscal balance 3/	-4.1	**-3.8**	-3.0	**-3.3**	-2.8	**-2.2**	-2.0	-1.5	-1.5	-1.5	-1.5
Primary fiscal balance (cash basis)	-2.4	**-2.2**	-1.5	**-1.5**	-1.0	**-0.4**	0.0	0.3	0.3	0.3	0.4
Gross debt 4/	57.2	**56.9**	55.6	**56.5**	55.3	**53.2**	53.3	50.7	47.6	45.2	43.8
				(End of period 12-month change, percent)							
Monetary sector											
Broad money (M2)	13.0	**3.3**	6.9	**7.9**	11.3	**10.9**	8.7	8.8	3.4	3.6	3.9
Domestic credit to non-government 5/	9.9	**10.3**	7.3	**7.7**	5.9	**10.5**	11.6	11.0	9.3	8.0	8.4
				(End of period, percent)							
Interest rates (dinar)											
NBS key policy rate	1.0	**...**	4.5	**...**	...		...	...	...	...	...
Interest rate on new FX and FX-indexed loans	2.5	**...**	5.0	**...**	...		...	...	...	...	...
				(Percent of GDP, unless otherwise indicated)							
Balance of payments											
Current account balance	-4.3	**-9.0**	-6.9	**-8.4**	-4.7	**-6.0**	-4.6	-4.5	-4.4	-4.3	-4.2
Trade of goods balance	-11.1	**-14.8**	-15.5	**-13.1**	-11.9	**-10.3**	-10.8	-9.8	-9.0	-8.3	-7.6
Exports of goods	39.0	**42.8**	44.6	**43.2**	42.9	**42.5**	43.7	44.1	44.9	45.6	46.5
Imports of goods	-50.1	**-57.6**	-60.1	**-56.3**	-54.8	**-52.8**	-54.5	-53.9	-53.9	-53.9	-54.1
Capital and financial account balance	8.9	**7.0**	9.4	**7.3**	6.7	**6.7**	7.0	6.6	6.9	6.2	6.6
External debt (percent of GDP)	74.4	**68.0**	72.1	**65.4**	66.8	**61.5**	63.8	60.3	57.4	54.0	51.3
of which: Private external debt	32.6	**29.4**	32.8	**26.8**	28.9	**25.1**	26.9	25.0	23.6	22.3	21.2
Gross official reserves (in billions of euro)	16.5	**16.3**	19.4	**16.6**	22.0	**17.6**	24.0	25.7	27.3	28.3	30.4
(in months of prospective imports)	6.0	**4.1**	5.2	**4.1**	5.6	**4.1**	5.7	5.6	5.6	5.4	5.4
(percent of short-term debt)	338.2	**335.1**	399.0	**341.9**	451.6	**361.2**	493.2	527.2	561.4	581.1	625.1
(percent of risk-weighted metric) 6/	131.5	**118.9**	134.0	**111.8**	143.1	**110.4**	145.3	138.9	138.6	135.0	139.6
Exchange rate (dinar/euro, period average)	117.6	**...**	117.6	**...**	...	**...**	...	...	...	...	...
REER (annual average change, in percent; + indicates appreciation)	1.4	**...**	3.2	**...**	...	**...**	...	...	...	...	...
Social indicators											
Per capita GDP (in US$)	9,230	**9,309**	10,417	**10,203**	10,802	**11,222**	11,683	12,738	13,706	14,662	15,500
Population (in million)	6.8	**6.8**	6.8	**6.8**	6.8	**6.8**	6.8	6.7	6.7	6.7	6.7

Sources: NBS, Ministry of Finance, SORS and IMF staff estimates and projections.

1/ Unemployment rate of the 15-64 year old labor force.
2/ Includes employer contributions.
3/ Includes amortization of called guarantees.
4/ Excludes state guarantees on bank loans under the credit guarantee scheme introduced in response to the COVID-19 crisis. Includes restitution bonds.
5/ At constant exchange rates.
6/ The risk-weighted metric is the IMF's ARA metric under fixed exchange rate. Serbia was reclassified as a de facto stabilized exchange rate regime in 2018.

Table 2. Serbia: Medium-Term Framework, 2021–28

	2021	2022		2023		2024		2025	2026	2027	2028
		CR 22/384	Est.	CR 22/384	Proj.	CR 22/384	Proj.	Proj.	Proj.	Proj.	Proj.
					(Percent change)						
Real sector											
GDP growth	7.5	2.5	2.3	2.3	2.0	3.0	3.0	4.5	4.0	4.0	4.0
Domestic demand (contribution)	8.5	3.3	4.3	2.6	1.9	1.5	3.2	4.8	4.4	4.2	4.1
Net exports (contribution)	-1.0	-0.8	-2.1	-0.3	0.1	1.5	-0.2	-0.3	-0.4	-0.2	-0.1
Consumer price inflation (average)	4.1	12.1	12.0	12.2	12.4	5.3	5.3	3.5	3.2	3.0	3.0
Consumer price inflation (end of period)	7.9	15.8	15.1	8.2	8.2	4.0	4.0	3.5	3.2	3.0	3.0
Output gap (in percent of potential)	1.2	-0.6	0.7	-1.1	-0.1	-1.1	0.0	0.0	0.0	0.0	0.0
Potential GDP growth	4.9	3.2	2.7	2.8	2.9	3.0	2.9	4.5	4.0	4.0	4.0
Domestic credit to non-government 1/	9.9	10.3	7.3	7.7	5.9	10.5	11.6	11.0	9.3	8.0	8.4
					(Percent of GDP, unless otherwise indicated)						
General government											
Revenue 2/	43.3	43.0	43.4	41.6	42.1	41.6	42.1	42.4	42.4	42.4	42.4
Expenditure 2/	47.4	46.8	46.4	44.9	44.9	43.8	44.2	43.9	44.0	44.0	43.9
Current 2/	39.0	37.1	36.1	36.1	36.5	36.0	36.8	36.4	36.5	36.5	36.6
of which: Wages and salaries 2/	10.0	9.7	9.6	9.6	9.7	9.8	9.9	10.0	10.1	10.1	10.1
of which: Pensions	9.9	9.0	9.0	9.6	9.6	9.9	10.5	10.1	10.1	10.1	10.0
of which: Goods and services	10.4	10.1	9.6	8.8	8.9	8.8	8.3	8.4	8.4	8.4	8.4
Capital and net lending	8.3	9.4	10.1	8.4	8.1	7.5	7.0	7.0	7.2	7.3	7.2
Amortization of called guarantees	0.1	0.3	0.3	0.3	0.3	0.3	0.3	0.5	0.2	0.2	0.1
Unidentified measures	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Fiscal balance 3/	-4.1	-3.8	-3.0	-3.3	-2.8	-2.2	-2.0	-1.5	-1.5	-1.5	-1.5
Gross debt 4/	57.2	56.9	55.6	56.5	55.3	53.2	53.3	50.7	47.6	45.2	43.8
Effective interest rate on government borrowing (percent)	3.4	3.2	2.9	3.6	3.7	3.5	4.0	3.7	3.9	4.2	4.8
Domestic borrowing (including FX)	4.5	5.0	5.0	5.4	5.4	6.1	6.1	6.2	6.7	7.0	6.9
External borrowing	2.4	2.1	2.1	2.0	2.0	2.9	2.9	3.0	3.3	3.8	3.9
					(Percent of GDP, unless otherwise indicated)						
Balance of payments											
Current account	-4.3	-9.0	-6.9	-8.4	-4.7	-6.0	-4.6	-4.5	-4.4	-4.3	-4.2
of which: Trade balance	-11.1	-14.8	-15.5	-13.1	-11.9	-10.3	-10.8	-9.8	-9.0	-8.3	-7.6
of which: Current transfers, net (excl. grants)	7.5	7.6	8.9	6.7	8.2	6.6	7.6	7.0	6.7	6.4	6.2
Capital and financial account	8.9	7.0	9.4	7.3	6.7	6.7	7.0	6.6	6.9	6.2	6.6
of which: Foreign direct investment	6.9	6.1	7.1	5.2	6.1	5.5	5.7	5.4	5.5	5.4	5.4
External debt (end of period)	74.4	68.0	72.1	65.4	66.8	61.5	63.8	60.3	57.4	54.0	51.3
of which: Private external debt	32.6	29.4	32.8	26.8	28.9	25.1	26.9	25.0	23.6	22.3	21.2
Gross official reserves											
(in billions of euros)	16.5	16.3	19.4	16.6	22.0	17.6	24.0	25.7	27.3	28.3	30.4
(in percent of short-term external debt)	338.2	335.1	399.0	341.9	451.6	361.2	493.2	527.2	561.4	581.1	625.1
REER (ann. av. change; + = appreciation)	1.4	…	3.2	…	…	…	…	…	…	…	…

Sources: NBS, Ministry of Finance, SORS and IMF staff estimates and projections.

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

2/ Includes employer contributions.

3/ Includes amortization of called guarantees.

4/ Excludes state guarantees on bank loans under the credit guarantee scheme introduced in response to the COVID-19 crisis. Includes restitution bonds.

Table 3. Serbia: Growth Composition, 2021–28

	2021	2022		2023		2024		2025	2026	2027	2028
		CR 22/384	Est.	CR 22/384	Proj.	CR 22/384	Proj.	Proj.	Proj.	Proj.	Proj.
	(Percent change, unless otherwise indicated)										
Real											
Gross Domestic Product (GDP)	7.5	**2.5**	2.3	**2.3**	2.0	**3.0**	3.0	4.5	4.0	4.0	4.0
Domestic demand	7.7	**2.9**	3.9	**2.3**	1.7	**1.3**	2.8	4.3	3.9	3.8	3.7
Consumption	7.1	**1.9**	3.0	**2.1**	1.7	**2.6**	2.6	4.0	3.7	3.8	3.8
Non-government	7.7	**2.5**	3.7	**2.5**	1.5	**2.5**	2.5	4.0	3.8	3.8	3.8
Government	4.1	**-0.8**	0.2	**0.0**	2.6	**3.0**	3.2	4.2	3.5	3.6	3.9
Investment	9.7	**6.3**	6.7	**3.1**	1.6	**-2.4**	3.5	5.0	4.4	3.8	3.3
Gross fixed capital formation	15.9	**0.3**	-0.6	**2.1**	7.9	**1.9**	2.9	2.3	4.2	4.1	3.5
Non-government	17.8	**2.5**	-0.7	**1.0**	4.0	**2.0**	3.0	3.0	4.0	4.0	4.0
Government	8.6	**-8.6**	0.0	**6.9**	23.6	**1.7**	2.5	0.0	4.9	4.3	1.6
Exports of goods and services	19.5	**5.2**	17.6	**3.1**	5.5	**4.5**	5.3	5.9	5.4	5.3	5.2
Imports of goods and services	17.7	**5.5**	17.8	**3.0**	4.5	**1.7**	4.7	5.3	5.1	4.8	4.6
	(Contributions to GDP, percent)										
Gross Domestic Product (GDP)	7.5	**2.5**	2.3	**2.3**	2.0	**3.0**	3.0	4.5	4.0	4.0	4.0
Domestic demand (absorption)	8.5	**3.3**	4.3	**2.6**	1.9	**1.5**	3.2	4.8	4.4	4.2	4.1
Net exports of goods and services	-1.0	**-0.8**	-2.1	**-0.3**	0.1	**1.5**	-0.2	-0.3	-0.4	-0.2	-0.1
Consumption	6.0	**1.6**	2.6	**1.7**	1.4	**2.2**	2.2	3.4	3.2	3.2	3.2
Non-government	5.3	**1.7**	2.5	**1.7**	1.1	**1.7**	1.7	2.8	2.6	2.6	2.6
Government	0.7	**-0.1**	0.0	**0.0**	0.4	**0.4**	0.5	0.6	0.5	0.6	0.6
Investment	2.5	**1.7**	1.8	**0.9**	0.5	**-0.7**	1.0	1.4	1.2	1.1	0.9
Gross fixed capital formation	3.6	**0.1**	-0.1	**0.5**	1.9	**0.5**	0.7	0.6	1.0	1.0	0.9
Non-government	3.2	**0.5**	-0.1	**0.2**	0.8	**0.4**	0.6	0.6	0.8	0.8	0.8
Government	0.4	**-0.4**	0.0	**0.3**	1.1	**0.1**	0.1	0.0	0.3	0.2	0.1
Change in inventories	-1.1	**1.6**	1.9	**0.4**	-1.4	**-1.1**	0.2	0.8	0.2	0.1	0.1
Exports of goods and services	10.4	**3.1**	10.4	**1.9**	3.8	**2.8**	3.7	4.2	3.9	4.0	3.9
Imports of goods and services	11.4	**3.9**	12.5	**2.2**	3.7	**1.3**	3.9	4.5	4.3	4.2	4.0
	(Percent change, unless otherwise indicated)										
Nominal											
Gross Domestic Product (GDP)	13.9	**13.0**	13.1	**13.2**	14.4	**9.9**	8.3	8.6	7.5	7.3	7.1
Domestic demand (absorption), contribution to GDP growth	14.5	**18.5**	17.4	**13.0**	12.3	**7.5**	8.4	8.5	7.6	7.4	7.2
Net exports of goods and services, contribution to GDP growth	-0.6	**-5.4**	-4.3	**0.2**	2.0	**2.4**	-0.1	0.0	-0.1	-0.1	-0.1
Non-government	12.8	**14.9**	16.0	**15.1**	13.2	**8.0**	8.0	7.7	7.1	6.9	6.9
Government	9.8	**10.9**	9.2	**10.8**	13.9	**10.7**	9.4	9.4	7.6	7.3	7.5
Investment	17.8	**27.4**	21.1	**4.1**	4.3	**1.3**	6.4	7.8	6.8	6.7	6.1
Gross fixed capital formation	22.7	**19.7**	11.8	**3.7**	14.1	**6.5**	5.9	4.8	6.9	7.0	6.3
Non-government	10.7	**24.0**	13.2	**2.0**	7.7	**6.6**	6.1	5.9	6.6	6.9	7.1
Government	59.2	**10.6**	9.0	**7.9**	28.1	**6.3**	5.6	2.8	7.5	7.3	4.7
Exports of goods and services	28.7	**24.4**	31.7	**12.4**	8.6	**7.6**	8.8	8.8	8.3	7.6	7.5
Imports of goods and services	25.6	**30.1**	34.7	**10.1**	4.6	**3.0**	8.0	7.8	7.6	7.1	6.9
Memorandum items:											
GDP deflator (percent)	5.9	**10.3**	10.6	**10.7**	12.1	**6.7**	5.1	3.9	3.4	3.1	3.0
Nominal GDP (billions of dinars)	6,270	**7,088**	7,091	**8,026**	8,109	**8,821**	8,784	9,537	10,256	11,001	11,787

Sources: SORS; and IMF staff estimates and projections.

Table 4a. Serbia: Balance of Payments (Billions of Euros), 2021–28[1]

	2021	2022		2023		2024		2025	2026	2027	2028
		CR 22/384	Est.	CR 22/384	Proj.	CR 22/384	Proj.	Proj.	Proj.	Proj.	Proj.
Current account balance	-2.3	**-5.4**	-4.1	**-5.7**	-3.3	**-4.4**	-3.5	-3.7	-3.8	-4.0	-4.2
Trade of goods balance	-5.9	**-8.9**	-9.4	**-8.9**	-8.2	**-7.6**	-8.1	-8.0	-7.9	-7.8	-7.6
Exports of goods	20.8	**25.8**	26.9	**29.3**	29.6	**31.5**	32.7	36.0	39.4	42.9	46.6
Imports of goods	-26.7	**-34.7**	-36.3	**-38.2**	-37.8	**-39.2**	-40.8	-43.9	-47.3	-50.6	-54.1
Services balance	1.4	**1.4**	2.3	**1.4**	2.4	**1.8**	2.1	2.0	1.8	1.5	1.2
Exports of nonfactor services	7.8	**9.7**	11.1	**10.7**	11.7	**11.5**	12.2	12.9	13.5	14.0	14.6
Imports of nonfactor services	-6.4	**-8.3**	-8.8	**-9.2**	-9.3	**-9.7**	-10.1	-10.9	-11.7	-12.5	-13.4
Income balance	-2.1	**-2.7**	-3.0	**-3.2**	-3.4	**-3.7**	-3.4	-3.6	-3.8	-4.0	-4.2
Net interest	-0.7	**-0.9**	-0.8	**-1.0**	-0.8	**-1.1**	-0.8	-1.0	-1.1	-1.2	-1.3
Current transfer balance	4.3	**4.8**	5.9	**5.0**	6.0	**5.2**	5.9	5.9	6.1	6.2	6.4
Others, including private remittances	4.0	**4.6**	5.4	**4.5**	5.6	**4.9**	5.7	5.7	5.9	6.0	6.2
Capital and financial account balance 1/	4.7	**4.2**	5.7	**4.9**	4.6	**5.0**	5.2	5.4	6.1	5.8	6.6
Foreign direct investment balance	3.7	**3.7**	4.3	**3.5**	4.2	**4.1**	4.2	4.4	4.8	5.1	5.4
Portfolio investment balance	1.6	**-0.3**	-0.1	**-0.3**	1.0	**0.7**	2.7	0.4	1.1	0.4	1.1
of which: debt liabilities	1.6	**-0.3**	-0.1	**-0.3**	1.0	**0.7**	2.7	0.4	1.1	0.4	1.1
Other investment balance	-0.4	**0.9**	1.4	**1.7**	-0.6	**0.2**	-1.7	0.5	0.1	0.3	0.2
Public sector 1/ 2/	0.5	**1.9**	1.6	**2.4**	0.6	**-0.1**	-1.4	0.9	0.4	0.7	0.6
Domestic banks	-0.6	**-0.1**	0.6	**-0.1**	-0.6	**0.0**	0.0	0.0	0.0	0.1	0.1
Other private sector 3/	-0.4	**-0.9**	-0.8	**-0.5**	-0.6	**0.3**	-0.3	-0.4	-0.3	-0.5	-0.6
Errors and omissions	0.2	**0.0**	0.4	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0	0.0
Overall balance	2.6	**-1.2**	1.9	**-0.8**	1.4	**0.5**	1.8	1.7	2.2	1.8	2.4
Financing	-2.6	**1.2**	-1.9	**0.8**	-1.4	**-0.5**	-1.8	-1.7	-2.2	-1.8	-2.4
Gross international reserves (increase, -)	-2.6	**0.2**	-2.9	**-0.3**	-2.6	**-0.9**	-2.0	-1.7	-1.7	-1.0	-2.1
Financing Gap		**1.0**	1.0	**1.1**	1.2	**0.4**	0.2	0.0	-0.6	-0.8	-0.3
Use of Fund credit, net		**1.0**	1.0	**0.6**	0.6	**0.0**	0.0	0.0	-0.6	-0.8	-0.3
Purchases		**1.0**	1.0	**0.6**	0.6	**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	-0.6	-0.8	-0.3
Development partners		**0.0**	0.0	**0.5**	0.5	**0.4**	0.2	0.0	0.0	0.0	0.0
GDP (billions of euros)	53.3	**58.9**	60.3	**65.6**	68.9	**72.0**	74.8	81.5	87.7	93.9	100.1

Sources: NBS; and IMF staff estimates and projections.

1/ Excluding net use of IMF resources.
2/ Includes SDR allocations in 2021.
3/ Includes trade credits (net).

Table 4b. Serbia: Balance of Payments (Percent of GDP), 2021–28

	2021	2022		2023		2024		2025	2026	2027	2028
		CR 22/384	Est.	CR 22/384	Proj.	CR 22/384	Proj.	Proj.	Proj.	Proj.	Proj.
Current account balance	-4.3	**-9.0**	-6.9	**-8.4**	-4.7	**-6.0**	-4.6	-4.5	-4.4	-4.3	-4.2
Trade of goods balance	-11.1	**-14.8**	-15.5	**-13.1**	-11.9	**-10.3**	-10.8	-9.8	-9.0	-8.3	-7.6
Exports of goods	39.0	**42.8**	44.6	**43.2**	42.9	**42.5**	43.7	44.1	44.9	45.6	46.5
Imports of goods	-50.1	**-57.6**	-60.1	**-56.3**	-54.8	**-52.8**	-54.5	-53.9	-53.9	-53.9	-54.1
Services balance	2.6	**2.3**	3.8	**2.1**	3.4	**2.4**	2.8	2.4	2.0	1.6	1.2
Income balance	-3.9	**-4.4**	-5.0	**-4.8**	-5.0	**-5.1**	-4.5	-4.4	-4.3	-4.2	-4.2
Current transfer balance	8.0	**7.9**	9.8	**7.3**	8.7	**7.0**	7.9	7.2	6.9	6.6	6.4
Official grants	0.6	**0.3**	0.9	**0.7**	0.6	**0.3**	0.2	0.2	0.2	0.2	0.2
Others, including private remittances	7.5	**7.6**	8.9	**6.7**	8.2	**6.6**	7.6	7.0	6.7	6.4	6.2
Capital and financial account balance 1/	8.9	**7.0**	9.4	**7.3**	6.7	**6.7**	7.0	6.6	6.9	6.2	6.6
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	6.9	**6.1**	7.1	**5.2**	6.1	**5.5**	5.7	5.4	5.5	5.4	5.4
Portfolio investment balance	2.9	**-0.6**	-0.1	**-0.5**	1.5	**0.9**	3.6	0.5	1.3	0.4	1.1
Other investment balance	-0.8	**1.5**	2.4	**2.6**	-0.8	**0.3**	-2.3	0.6	0.2	0.3	0.2
Public sector 1/ 2/	0.9	**3.2**	2.7	**3.5**	0.9	**-0.1**	-1.9	1.1	0.5	0.7	0.6
Domestic banks	-1.0	**-0.1**	1.1	**-0.2**	-0.9	**0.0**	0.1	0.0	0.0	0.1	0.1
Other private sector 3/	-0.7	**-1.6**	-1.3	**-0.7**	-0.8	**0.4**	-0.5	-0.5	-0.4	-0.5	-0.6
Errors and omissions	0.3	**0.0**	0.6	**0.0**	0.0	**0.0**	0.0	0.0	0.0	0.0	0.0
Overall balance	4.9	**-1.9**	3.2	**-1.2**	2.0	**0.7**	2.4	2.0	2.5	1.9	2.4
Financing	-4.9	**1.9**	-3.2	**1.2**	-2.0	**-0.7**	-2.4	-2.0	-2.5	-1.9	-2.4
Gross international reserves (increase, -)	-4.9	**0.3**	-4.8	**-0.5**	-3.7	**-1.3**	-2.7	-2.0	-1.9	-1.0	-2.1
Financing Gap		**1.7**	1.7	**1.7**	1.7	**0.5**	0.3	0.0	-0.6	-0.9	-0.3
Use of Fund credit, net		**1.7**	1.7	**0.9**	0.9	**0.0**	0.0	0.0	-0.6	-0.9	-0.3
Purchases		**1.7**	1.7	**0.9**	0.9	**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	-0.6	-0.9	-0.3
Development partners		**0.0**	0.0	**0.7**	0.8	**0.5**	0.3	0.0	0.0	0.0	0.0
Memorandum items:											
Nominal growth of exports of goods	29.3	**24.2**	29.5	**13.5**	9.9	**7.6**	10.5	10.0	9.6	8.8	8.6
Nominal growth of import of goods	25.5	**30.1**	35.8	**9.9**	4.2	**2.6**	7.9	7.8	7.6	7.1	6.9
Volume growth of exports of goods	14.7	**5.1**	4.2	**4.1**	6.8	**4.6**	6.9	7.1	6.6	6.5	6.3
Volume growth of import of goods	14.1	**5.5**	5.5	**2.9**	4.1	**1.4**	4.6	5.3	5.1	4.8	4.6
Trading partner import growth	12.5	**4.7**	7.5	**3.0**	2.9	**4.5**	3.7	3.6	3.4	3.1	3.1
Export prices growth	12.7	**18.2**	9.8	**9.0**	2.9	**2.9**	3.3	2.8	2.8	2.1	2.2
Import prices growth	10.0	**23.3**	23.6	**6.8**	0.1	**1.2**	3.1	2.3	2.4	2.1	2.2
Change in terms of trade	2.5	**-4.1**	-11.2	**2.0**	2.8	**1.7**	0.2	0.4	0.3	0.0	0.0
Gross official reserves (in billions of euro)	16.5	**16.3**	19.4	**16.6**	22.0	**17.6**	24.0	25.7	27.3	28.3	30.4
(In months of prospective imports of GNFS)	6.0	**4.1**	5.2	**4.1**	5.6	**4.1**	5.7	5.6	5.6	5.4	5.4
(in percent of short-term debt)	338.2	**335.1**	399.0	**341.9**	451.6	**361.2**	493.2	527.2	561.4	581.1	625.1
(in percent of broad money, M2)	52.1	**45.7**	54.4	**41.6**	53.9	**40.0**	54.0	53.1	52.6	50.9	51.5
(in percent of risk-weighted metric) 4/	131.5	**118.9**	134.0	**111.8**	143.1	**110.4**	145.3	138.9	138.6	135.0	139.6
GDP (billions of euros)	53.3	**60.3**	60.3	**67.9**	68.9	**74.1**	74.8	81.5	87.7	93.9	100.1

Sources: NBS; and IMF staff estimates and projections.
1/ Excluding net use of IMF resources.
2/ Includes SDR allocations in 2021.
3/ Includes trade credits (net).
4/ The risk-weighted metric is the IMF's ARA metric for the fixed exchange rate. Serbia was reclassified as a de facto stabilized exchange rate regime in 2018.

Table 5a. Serbia: External Financing Requirements and Sources (Baseline), 2021–28

(In billions of euros)

	2021	2022	2023	2024	2025	2026	2027	2028
		Est.	Proj.					
Total financing requirement	**10.2**	**11.6**	**10.5**	**11.0**	**9.3**	**10.5**	**12.0**	**10.3**
Current account deficit	2.3	4.1	3.3	3.5	3.7	3.8	4.0	4.2
Debt amortization	5.2	4.5	4.6	5.5	4.0	5.0	7.0	3.9
Medium and long-term debt	3.7	3.8	3.0	3.8	2.3	3.3	5.3	2.2
Public sector	2.5	2.1	1.8	2.8	1.5	2.4	4.6	1.9
Of which: IMF	0.0	0.0	0.0	0.0	0.0	0.6	0.8	0.3
Of which: Eurobonds	0.6	0.0	0.0	0.1	0.2	0.0	2.1	0.1
Of which: Domestic bonds (non-residents)	1.1	1.1	0.8	-0.4	0.3	0.3	0.3	0.3
Commercial banks	0.4	0.7	0.6	0.6	0.3	0.2	0.2	0.1
Corporate sector	0.8	1.0	0.6	0.5	0.5	0.6	0.4	0.2
Short-term debt	1.6	0.7	1.7	1.7	1.7	1.7	1.7	1.7
Commercial banks	1.5	0.6	1.5	1.5	1.5	1.5	1.5	1.5
Corporate sector	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Change in gross reserves (increase=+)	2.6	2.9	2.6	2.0	1.7	1.7	1.0	2.1
Total financing sources	**10.2**	**10.6**	**9.3**	**10.8**	**9.3**	**11.0**	**12.8**	**10.5**
Capital transfers	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign direct investment (net)	3.7	4.3	4.2	4.2	4.4	4.8	5.1	5.4
Portfolio investment (net) 1/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt financing (excl. except. financing)	7.7	5.9	6.0	7.0	5.4	6.1	7.4	4.5
Medium and long-term debt	6.1	5.2	4.3	5.3	3.7	4.4	5.7	2.9
Public sector 2/	4.6	3.2	3.4	4.0	2.7	3.3	4.7	2.2
Of which: Eurobonds	2.7	0.0	1.6	2.1	0.5	1.0	2.2	1.0
Of which: Domestic bonds (non-residents)	0.5	0.5	0.3	0.3	0.3	0.3	0.4	0.4
Commercial banks	0.6	0.7	0.2	0.7	0.4	0.3	0.3	0.2
Corporate sector	0.9	1.3	0.7	0.6	0.7	0.8	0.7	0.4
Short-term debt	1.6	0.7	1.7	1.7	1.7	1.7	1.7	1.7
Other net capital inflows 3/	-1.1	0.4	-0.9	-0.5	-0.5	0.1	0.3	0.6
o/w trade credit and currency and deposits	-2.0	-1.0	-0.9	-0.6	-0.6	-0.6	-0.7	-0.7
Total financing needs	**0.0**	**1.0**	**1.2**	**0.2**	**0.0**	**-0.6**	**-0.8**	**-0.3**
Exceptional financing (net)		**1.0**	**1.2**	**0.2**	**0.0**	**-0.6**	**-0.8**	**-0.3**
IMF		1.0	0.6	0.0	0.0	-0.6	-0.8	-0.3
Development partners, *by debtor:* 4/		0.0	0.5	0.2	0.0	0.0	0.0	0.0
General government		0.0	0.1	0.2	0.0	0.0	0.0	0.0
SOEs (from IFIs)		0.0	0.4	0.0	0.0	0.0	0.0	0.0
Memorandum items:								
Gross international reserves (**without** except. financing)		18.4	19.8	21.6	23.2	25.5	27.2	29.6
as % of ARA Metric		127.0	128.9	130.7	125.8	129.1	130.0	135.9
Gross international reserves (**with** except. financing)	16.5	19.4	22.0	24.0	25.7	27.3	28.3	30.4
as % of ARA Metric	131.5	134.0	143.1	145.3	138.9	138.6	135.0	139.6
Debt service	6.0	5.3	5.5	6.3	4.8	5.6	7.8	4.7
Interest	0.7	0.8	0.8	0.7	0.8	0.7	0.8	0.7
Amortization	5.2	4.5	4.6	5.5	4.0	5.0	7.0	3.9

Sources: NBS; and IMF 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.
4/ Exceptional financing is provided by the World Bank, AFD, KfW and EBRD (see MEFP). Some loans are disbursed to the budget and are public debt, others are disbursed to SOEs in the energy sector and are publicly guaranteed debt.

Table 5b. Serbia: Indicators of Capacity to Repay the Fund (Baseline), 2021–28[1]

(In billions of euros, unless otherwise indicated)

	2021	2022 Est.	2023 Proj.	2024 Proj.	2025 Proj.	2026 Proj.	2027 Proj.	2028 Proj.
Fund repurchases and charges 2/								
In millions of SDRs	-	4	36	71	102	530	777	545
In millions of euro	-	5	46	90	130	681	1,007	716
In percent of exports of goods and NFS	-	0.0	0.1	0.2	0.3	1.3	1.8	1.2
In percent of GDP	-	0.0	0.1	0.1	0.2	0.8	1.1	0.7
In percent of quota	-	0.6	5.6	10.9	15.6	81.0	118.7	83.2
In percent of total external debt service	-	0.1	0.8	1.4	2.7	12.1	13.0	15.3
In percent of gross international reserves	-	0.0	0.2	0.4	0.5	2.5	3.6	2.4
Fund credit outstanding (end-period)								
In millions of SDRs	-	786	1,266	1,899	1,899	1,465	753	237
In millions of euro	-	987	1,595	2,407	2,428	1,887	982	314
In percent of exports of goods and NFS	-	2.6	3.9	5.4	5.0	3.6	1.7	0.5
In percent of GDP	-	1.6	2.3	3.2	3.0	2.2	1.0	0.3
In percent of quota	-	120.0	193.3	290.0	290.0	223.8	115.0	36.2
In percent of total external debt	-	2.3	3.5	5.0	4.9	3.7	1.9	0.6
In percent of gross international reserves	-	5.1	7.3	10.0	9.5	6.9	3.5	1.0
Memorandum items:								
Exports of goods and NFS	28,583	38,000	41,259	44,888	48,824	52,883	56,906	61,166
Quota (in millions of SDRs)	654.8	654.8	654.8	654.8	654.8	654.8	654.8	654.8
GDP	53,329	60,309	68,904	74,824	81,528	87,714	93,947	100,076
Total external debt service	5,978	5,306	5,478	6,262	4,759	5,649	7,754	4,666
Public sector external debt	22,293	23,724	26,140	27,582	28,793	29,666	29,770	30,116
Total external debt	39,687	43,489	46,032	47,743	49,192	50,323	50,756	51,379
Total external debt stock excluding IMF	39,687	42,475	44,399	46,111	47,559	49,250	50,499	51,379
Gross international reserves	16,455	19,416	21,972	23,996	25,651	27,315	28,276	30,415

Source: IMF staff estimates.

1/ Assumes purchase of the full authorized access under the SBA arrangement including precautionary tranches.
2/ Includes GRA basic rate of charge, surcharges, service fees, and SDR charges.

Table 6a. Serbia: General Government Fiscal Operations (Billions of RSD), 2021–28[1]

	2021	2022		2023		2024		2025	2026	2027	2028
		CR 22/384	Est.	CR 22/384	Proj.	CR 22/384	Proj.	Proj.	Proj.	Proj.	Proj.
Revenue	2,712	3,048	3,076	3,339	3,412	3,670	3,702	4,046	4,351	4,667	4,999
Taxes	2,420	2,746	2,760	2,974	3,005	3,283	3,311	3,605	3,881	4,165	4,464
Personal income tax	256	298	302	333	338	376	369	403	429	461	497
Social security contributions 2/	862	947	952	1,019	1,053	1,144	1,169	1,268	1,368	1,460	1,560
Taxes on profits	159	209	209	199	219	216	225	243	272	297	323
Value-added taxes	659	777	779	869	855	930	947	1,032	1,107	1,190	1,271
Excises	330	337	338	355	350	399	393	433	464	497	532
Taxes on international trade	62	80	79	88	83	91	95	104	111	118	126
Other taxes	92	98	100	111	107	127	114	122	130	143	156
Non-tax revenue	261	268	285	297	329	341	339	386	413	441	469
Capital revenue	12	13	16	14	17	16	19	21	22	24	25
Grants	19	22	16	53	60	30	33	34	35	37	40
Expenditure	2,971	3,320	3,292	3,603	3,640	3,860	3,881	4,189	4,510	4,836	5,179
Current expenditure	2,445	2,629	2,560	2,899	2,960	3,178	3,236	3,473	3,748	4,013	4,313
Wages and salaries 3/	629	688	684	774	783	861	872	953	1,036	1,116	1,196
Goods and services	651	718	680	708	724	778	731	801	859	922	989
Interest	109	115	107	145	146	157	180	175	190	203	230
Subsidies	206	186	160	216	259	217	238	264	283	299	320
Transfers	850	922	929	1,056	1,047	1,165	1,214	1,281	1,380	1,473	1,577
Pensions	619	639	638	772	777	873	925	966	1,039	1,111	1,184
Other transfers 4/	231	283	291	284	270	292	289	315	341	362	394
Capital expenditure	467	516	508	557	578	592	586	637	715	767	811
Net lending	52	153	206	119	76	65	30	31	26	38	41
Amortization of activated guarantees	8	21	18	28	26	25	28	48	21	19	15
Fiscal balance	-259	-272	-216	-264	-228	-190	-178	-143	-159	-170	-181
Financing	259	272	216	264	228	190	178	143	159	170	181
Privatization proceeds	0	0	0	0	0	0	0	0	0	0	0
Equity investment	0	0	0	0	0	0	0	0	0	0	0
Domestic	-63	-37	-247	-192	-204	52	48	34	85	181	55
External	322	308	463	279	252	56	107	109	132	59	138
Program	0	146	186	183	0	0	0	19	15	15	15
Project	126	154	139	176	175	177	175	170	183	196	210
Bonds and loans	346	9	111	32	187	130	297	58	117	258	118
IMF resources (net)		83	106	0	0	0	0	0	0	0	0
Amortization	-151	-83	-78	-112	-111	-251	-365	-138	-182	-410	-206
Financing gap		0	0	177	180	82	23	0	-58	-71	-12
IMF - SBA		0	0	143	144	48	0	0	-58	-71	-12
Development partners		0	0	35	36	35	23	0	0	0	0
Memorandum items:											
Gross wages and salaries	538	590	587	663	672	739	748	817	888	957	1,026
Arrears accumulation (domestic)	0	-1	0	0	-1	0	0	0	0	0	0
Quasi-fiscal support to SOEs (gross new issuance of guarantees)	23	75	47	9	9	5	5	5	5	5	5
Government deposits (stock)	326	311	422	403	490	351	476	482	406	247	222
Gross public debt 5/	3,584	4,031	3,945	4,534	4,484	4,697	4,682	4,831	4,880	4,973	5,165
Nominal GDP (billions of dinars)	6,270	7,088	7,091	8,026	8,109	8,821	8,784	9,537	10,256	11,001	11,787

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

5/ Excludes state guarantees on bank loans under the credit guarantee scheme introduced in response to the COVID-19 crisis. Includes restitution bonds.

Table 6b. Serbia: General Government Fiscal Operation (Percent of GDP), 2021–28[1]

	2021	2022		2023		2024		2025	2026	2027	2028
		CR 22/384	Est.	CR 22/384	Proj.	CR 22/384	Proj.	Proj.	Proj.	Proj.	Proj.
Revenue	43.3	**43.0**	43.4	**41.6**	42.1	**41.6**	42.1	42.4	42.4	42.4	42.4
Taxes	38.6	**38.7**	38.9	**37.1**	37.1	**37.2**	37.7	37.8	37.8	37.9	37.9
Personal income tax	4.1	**4.2**	4.3	**4.1**	4.2	**4.3**	4.2	4.2	4.2	4.2	4.2
Social security contributions 2/	13.7	**13.4**	13.4	**12.7**	13.0	**13.0**	13.3	13.3	13.3	13.3	13.2
Taxes on profits	2.5	**2.9**	3.0	**2.5**	2.7	**2.5**	2.6	2.6	2.6	2.7	2.7
Value-added taxes	10.5	**11.0**	11.0	**10.8**	10.5	**10.5**	10.8	10.8	10.8	10.8	10.8
Excises	5.3	**4.8**	4.8	**4.4**	4.3	**4.5**	4.5	4.5	4.5	4.5	4.5
Taxes on international trade	1.0	**1.1**	1.1	**1.1**	1.0	**1.0**	1.1	1.1	1.1	1.1	1.1
Other taxes	1.5	**1.4**	1.4	**1.4**	1.3	**1.4**	1.3	1.3	1.3	1.3	1.3
Non-tax revenue	4.2	**3.8**	4.0	**3.7**	4.1	**3.9**	3.9	4.0	4.0	4.0	4.0
Capital revenue	0.2	**0.2**	0.2	**0.2**	0.2	**0.2**	0.2	0.2	0.2	0.2	0.2
Grants	0.3	**0.3**	0.2	**0.7**	0.7	**0.3**	0.4	0.4	0.3	0.3	0.3
Expenditure	47.4	**46.8**	46.4	**44.9**	44.9	**43.8**	44.2	43.9	44.0	44.0	43.9
Current expenditure	39.0	**37.1**	36.1	**36.1**	36.5	**36.0**	36.8	36.4	36.5	36.5	36.6
Wages and salaries 3/	10.0	**9.7**	9.6	**9.6**	9.7	**9.8**	9.9	10.0	10.1	10.1	10.1
Goods and services	10.4	**10.1**	9.6	**8.8**	8.9	**8.8**	8.3	8.4	8.4	8.4	8.4
Interest	1.7	**1.6**	1.5	**1.8**	1.8	**1.8**	2.0	1.8	1.9	1.8	2.0
Subsidies	3.3	**2.6**	2.3	**2.7**	3.2	**2.5**	2.7	2.8	2.8	2.7	2.7
Transfers	13.6	**13.0**	13.1	**13.2**	12.9	**13.2**	13.8	13.4	13.5	13.4	13.4
Pensions	9.9	**9.0**	9.0	**9.6**	9.6	**9.9**	10.5	10.1	10.1	10.1	10.0
Other transfers 4/	3.7	**4.0**	4.1	**3.5**	3.3	**3.3**	3.3	3.3	3.3	3.3	3.3
Capital expenditure	7.4	**7.3**	7.2	**6.9**	7.1	**6.7**	6.7	6.7	7.0	7.0	6.9
Net lending	0.8	**2.2**	2.9	**1.5**	0.9	**0.7**	0.3	0.3	0.3	0.3	0.3
Amortization of activated guarantees	0.1	**0.3**	0.3	**0.3**	0.3	**0.3**	0.3	0.5	0.2	0.2	0.1
Fiscal balance	-4.1	**-3.8**	-3.0	**-3.3**	-2.8	**-2.2**	-2.0	-1.5	-1.5	-1.5	-1.5
Financing	4.1	**3.8**	3.0	**3.3**	2.8	**2.2**	2.0	1.5	1.5	1.5	1.5
Privatization proceeds	0.0	**0.0**	0.0	**0.0**	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	-1.0	**-0.5**	-3.5	**-2.4**	-2.5	**0.6**	0.5	0.4	0.8	1.6	0.5
External	5.1	**4.3**	6.5	**3.5**	3.1	**0.6**	1.2	1.1	1.3	0.5	1.2
Program	0.0	**2.1**	2.6	**2.3**	0.0	**0.0**	0.0	0.2	0.1	0.1	0.1
Project	2.0	**2.2**	2.0	**2.2**	2.2	**2.0**	2.0	1.8	1.8	1.8	1.8
Bonds and loans	5.5	**0.1**	1.6	**0.4**	2.3	**1.5**	3.4	0.6	1.1	2.3	1.0
IMF resources (net)		**1**	1.5	**0**	0.0	**0**	0.0	0.0	0.0	0.0	0.0
Amortization	-2.4	**-1.2**	-1.1	**-1.4**	-1.4	**-2.8**	-4.2	-1.5	-1.8	-3.7	-1.7
Financing gap		**0.0**	0.0	**2.2**	2.2	**0.9**	0.3	0.0	-0.6	-0.6	-0.1
IMF - SBA		**0.0**	0.0	**1.8**	1.8	**0.5**	0.0	0.0	-0.6	-0.6	-0.1
Development partners		**0.0**	0.0	**0.4**	0.4	**0.4**	0.3	0.0	0.0	0.0	0.0
Memorandum items:											
Gross wages and salaries	8.6	**8.3**	8.3	**8.3**	8.3	**8.4**	8.5	8.6	8.7	8.7	8.7
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)	5.2	**4.4**	6.0	**5.0**	6.0	**4.0**	5.4	5.1	4.0	2.2	1.9
Gross financing need	9.1	**8.9**	7.5	**9.0**	8.9	**6.9**	8.1	4.9	5.2	5.5	3.3
Gross public debt 5/	57.2	**56.9**	55.6	**56.5**	55.3	**53.2**	53.3	50.7	47.6	45.2	43.8
Nominal GDP (billions of dinars)	6,270	**7,088**	7,091	**8,026**	8,109	**8,821**	8,784	9,537	10,256	11,001	11,787

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

5/ Excludes state guarantees on bank loans under the credit guarantee scheme introduced in response to the COVID-19 crisis. Includes restitution bonds.

Table 7. Serbia: Decomposition of Public Debt and Debt Service by Creditor, 2020–25[1]

(Central government debt, in billions of euros)

	Debt stock (end of period)			Expected debt service			
	2020	2021	2022	2022	2023	2024	2025
Total	26.7	30.1	33.3	3.2	4.5	4.8	2.9
External	15.2	18.5	21.6	1.1	1.1	3.2	1.3
Multilateral creditors[2]	5.4	5.6	6.5	0.6	0.6	0.7	0.5
IMF	0.5	0.5	1.3				
World Bank	0.0	0.0	0.0				
ADB/AfDB/IADB	0.0	0.0	0.0				
Other Multilaterals	5.0	5.2	5.3				
o/w: IBRD	2.2	2.2	2.2				
EIB	1.8	1.8	1.9				
Others (IDA, EU, CEB, EBRD, EUROFIMA, KfW)	1.0	1.1	1.2				
Bilateral Creditors	4.5	5.1	6.4	0.5	0.5	2.5	0.6
Paris Club	0.9	0.7	0.6	0.1	0.2	0.1	0.1
o/w: PC Germany KfW	0.0	0.0	0.0				
PC United Kingdom	0.0	0.0	0.0				
Non-Paris Club	3.6	4.3	5.8	0.4	0.4	2.4	0.5
o/w: UAE	1.6	1.7	2.5				
China	1.1	1.6	2.2				
Russia	0.7	0.7	0.8				
Others	0.3	0.3	0.2				
Bonds	5.1	7.3	7.3	0.0	0.0	0.0	0.2
Commercial creditors	0.1	0.4	0.8	0.0	0.0	0.0	0.1
Other international creditors	0.1	0.1	0.5				
o/w: JICA	0.1	0.1	0.1				
Domestic	11.4	11.6	11.8	2.1	3.4	1.6	1.6
Held by residents, total	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Held by non-residents, total	n/a	n/a	n/a	n/a	n/a	n/a	n/a
T-Bills	0.0	0.0	0.0	0.0	0.3	0.0	0.0
Bonds	10.7	11.2	10.5	2.0	2.9	1.4	1.5
Loans and other domestic debt	0.7	0.4	1.3	0.1	0.2	0.2	0.1
Memo items:	0.0						
Collateralized debt[3]	0.0	0.0	0.0				
o/w: Related	0.0	0.0	0.0				
o/w: Unrelated	0.0	0.0	0.0				
Contingent liabilities	1.4	1.4	1.5				
o/w: Public guarantees	1.4	1.4	1.5				
o/w: Other explicit contingent liabilities[4]	0.0	0.0	0.0				
Nominal GDP	57.0	56.5	55.1				

1/As reported by country authorities according to their classification of creditors, including by official and commercial. Debt coverage corresponds to central government.

2/ Multilateral creditors are simply institutions with more than one official shareholder and may not necessarily align with creditor classification under other IMF policies (e.g. Lending

3/Debt is collateralized when the creditor has rights over an asset or revenue stream that would allow it, if the borrower defaults on its payment obligations, to rely on the asset or revenue stream to secure repayment of the debt. Collateralization entails a borrower granting liens over specific existing assets or future receivables to a lender as security against repayment of the loan. Collateral is "unrelated" when it has no relationship to a project financed by the loan. An example would be borrowing to finance the budget deficit, collateralized by oil revenue receipts. See the joint IMF-World Bank note for the G20 "Collateralized Transactions: Key Considerations for Public Lenders and Borrowers" for a discussion of issues raised by collateral.

4/Includes other-one off guarantees not included in publicly guaranteed debt (e.g. credit lines) and other explicit contingent liabilities not elsewhere classified (e.g. potential legal claims, payments resulting from PPP arrangements).

Table 8. Serbia: Monetary Survey, 2021–28

	2021	2022		2023		2024		2025	2026	2027	2028
		CR 22/384	Est.	CR 22/384	Proj.	CR 22/384	Proj.	Proj.	Proj.	Proj.	Proj.
	(Billions of dinars, unless otherwise indicated; end of period) 1/										
Net foreign assets 2/	1744	**1738**	1853	**1823**	2346	**1942**	2574	2788	3001	3138	3425
in billions of euro	14.8	**14.8**	15.8	**15.3**	19.9	**16.3**	22.0	23.8	25.7	26.7	29.0
Foreign assets	2378	**2390**	2692	**2496**	3035	**2629**	3272	3496	3720	3866	4166
NBS	1947	**1928**	2291	**1989**	2588	**2102**	2807	3005	3204	3335	3621
Commercial banks	431	**463**	401	**507**	447	**527**	465	491	516	532	545
Foreign liabilities (-)	-633	**-652**	-838	**-673**	-689	**-687**	-698	-708	-719	-729	-741
NBS	0	**-3**	-116	**-3**	-3	**-3**	-3	-3	-3	0	0
Commercial banks	-633	**-649**	-722	**-670**	-686	**-684**	-695	-705	-716	-729	-741
Net domestic assets	1,968	**2,098**	2,117	**2,314**	2,078	**2,647**	2,236	2,443	2,407	2,467	2,398
Domestic credit	3,270	**3,600**	3,348	**3,745**	3,375	**4,169**	3,822	4,218	4,513	4,966	5,425
Government, net	308	**330**	172	**194**	58	**241**	188	193	175	311	418
NBS	-387	**-356**	-476	**-471**	-529	**-434**	-482	-511	-584	-580	-485
Claims on government	84	**101**	101	**80**	80	**56**	56	59	62	65	68
Liabilities (deposits)	471	**456**	577	**551**	609	**490**	539	570	646	645	553
Banks	695	**685**	648	**664**	587	**675**	670	704	759	891	902
Claims on government	787	**778**	729	**757**	668	**770**	765	796	840	973	997
Liabilities (deposits)	92	**92**	81	**93**	81	**95**	95	92	81	81	95
Non-government sector	3,002	**3,310**	3,218	**3,591**	3,358	**3,968**	3,676	4,067	4,380	4,696	5,049
Households	1,375	**1,512**	1,458	**1,637**	1,518	**1,807**	1,660	1,834	1,972	2,112	2,267
Enterprises	1,594	**1,762**	1,715	**1,915**	1,793	**2,119**	1,965	2,176	2,346	2,519	2,711
Other assets, net	-1,302	**-1,503**	-1,231	**-1,430**	-1,297	**-1,522**	-1,586	-1,775	-2,106	-2,499	-3,027
Capital accounts (-)	-1,073	**-1,252**	-1,094	**-1,162**	-1,146	**-1,227**	-1,379	-1,528	-1,834	-2,201	-2,685
Broad money (M2)	3713	**3836**	3971	**4138**	4424	**4589**	4810	5231	5408	5605	5823
Currency in circulation	295	**319**	311	**340**	347	**382**	376	408	438	470	504
Demand deposits	1057	**1002**	1080	**1069**	1204	**1200**	1304	1416	1523	1634	1750
Time and saving deposits	353	**295**	423	**315**	471	**354**	510	554	596	639	685
Foreign currency deposits	2007	**2220**	2158	**2414**	2402	**2653**	2620	2853	2851	2862	2884
in billions of euro	17.1	**18.9**	18.4	**20.3**	20.4	**22.3**	22.4	24.4	24.4	24.4	24.4
Memorandum items:	(Year-on-year change, unless otherwise indicated)										
M2	13.0	**3.3**	6.9	**7.9**	11.3	**10.9**	8.7	8.8	3.4	3.6	3.9
Velocity (M2)	1.7	**1.8**	1.8	**1.9**	1.8	**1.9**	1.8	1.8	1.9	2.0	2.0
Deposits at constant exchange rate	13.2	**2.9**	7.2	**7.2**	11.1	**10.8**	9.2	8.8	3.1	3.1	3.1
Credit to non-gov. (current exchange rate)	10.8	**7.6**	10.1	**7.0**	3.8	**8.0**	6.3	7.5	6.1	6.0	6.3
Credit to non-gov. (constant exchange rates) 3/	10.8	**7.6**	6.6	**6.1**	4.9	**7.9**	8.2	8.1	7.5	6.7	6.9
Domestic	9.9	**10.3**	7.3	**7.7**	5.9	**10.5**	11.6	11.0	9.3	8.0	8.4
Households	10.6	**9.9**	6.2	**7.7**	4.1	**10.3**	9.7	10.5	7.6	6.9	7.0
Enterprises and other sectors	9.4	**10.5**	8.3	**7.7**	6.1	**10.6**	11.8	11.1	9.4	8.1	8.5
External	16.1	**2.2**	0.0	**2.5**	2.5	**2.2**	1.0	1.0	2.6	2.8	2.5
Credit to non-gov. (real terms) 4/	2.8	**-7.1**	-4.4	**-1.1**	-4.1	**3.8**	2.2	3.9	2.8	2.9	3.2
Domestic credit to non-gov. (real terms)	1.9	**-4.8**	-6.9	**0.3**	-3.6	**6.3**	5.3	6.9	4.4	4.1	4.4
Households	2.5	**-5.0**	-7.9	**0.1**	-3.8	**6.1**	5.1	6.7	4.2	4.0	4.2
Enterprises and other sectors	1.4	**-4.6**	-6.0	**0.4**	-3.4	**6.4**	5.4	7.0	4.5	4.2	4.5
External	4.5	**-11.7**	0.0	**-4.2**	-5.1	**-1.7**	-3.6	-2.4	-0.6	0.2	0.3
Deposit euroization (percent of total) 5/	58.7	**63.1**	59.0	**63.6**	58.9	**63.1**	59.1	59.2	57.4	55.7	54.2
Credit euroization (percent of total) 5/	60.9	**62.9**	64.2	**63.5**	62.2	**62.5**	61.2	59.7	58.7	58.2	58.2

Sources: NBS, 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.
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 9. Serbia: NBS Balance Sheet, 2021–28

	2021	2022		2023		2024		2025	2026	2027	2028
		CR 22/384	Est.	CR 22/384	Proj.	CR 22/384	Proj.	Proj.	Proj.	Proj.	Proj.
	(Billions of dinars, unless otherwise indicated; end of period) 1/										
Net foreign assets	1947	**1924**	2175	**1986**	2584	**2099**	2804	3002	3201	3331	3618
(In billions of euro)	16.6	**16.4**	18.5	**16.7**	21.9	**17.6**	24.0	25.7	27.4	28.4	30.6
Gross foreign reserves	1947	**1928**	2291	**1989**	2588	**2102**	2807	3005	3204	3335	3621
Net domestic assets	-920	**-896**	-964	**-910**	-1391	**-867**	-1471	-1594	-1678	-1730	-1931
Net domestic credit	-530	**-457**	-562	**-516**	-1041	**-492**	-1366	-1594	-1678	-1730	-1931
Net credit to government	-387	**-356**	-476	**-471**	-529	**-434**	-482	-511	-584	-580	-485
Claims on government	84	**101**	101	**80**	80	**56**	56	59	62	65	68
Liabilities to government (-)	-472	**-456**	-577	**-551**	-609	**-490**	-539	-570	-646	-645	-553
Reserve money	1027	**1029**	1211	**1076**	1194	**1232**	1332	1408	1522	1601	1687
Currency in circulation	295	**319**	311	**340**	347	**382**	376	408	438	470	504
Commercial bank reserves	410	**354**	548	**349**	462	**425**	537	544	627	673	721
Required reserves	247	**273**	273	**297**	296	**327**	323	351	351	353	355
Excess reserves	163	**81**	276	**52**	166	**98**	214	192	276	320	365

Sources: NBS; and IMF staff estimates and projections.

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

Table 10. Serbia: Banking Sector Financial Soundness Indicators, 2018–22

	2018	2019	2020	2021				2022			
				Mar	Jun	Sep	Dec	Mar	Jun	Sep	Dec
Capital adequacy											
Regulatory capital to risk-weighted assets	22.3	23.4	22.4	22.3	22.2	21.7	20.8	20.0	19.4	19.5	20.2
Regulatory Tier 1 capital to risk-weighted assets	21.1	22.4	21.6	21.4	21.1	20.6	19.7	18.9	18.2	18.2	18.8
Nonperforming loans net of provisions to regulatory capital	9.7	6.3	6.7	7.0	6.9	6.7	7.6	7.7	7.5	7.4	6.5
Regulatory Tier 1 capital to assets	13.5	14.4	13.1	13.0	12.6	12.3	11.8	11.6	11.4	11.0	11.0
Large exposures to capital	77.4	66.5	73.8	80.0	82.4	80.1	86.0	98.9	104.7	109.3	86.7
Regulatory capital to assets	14.2	15.1	13.6	13.5	13.3	12.9	12.4	12.2	12.2	11.8	11.7
Asset quality											
Nonperforming loans to total gross loans	5.7	4.1	3.7	3.9	3.6	3.6	3.6	3.4	3.3	3.2	3.0
Sectoral distribution of loans (percent of total loans)											
Deposit takers	0.4	0.4	0.3	0.4	0.4	0.1	0.0	0.2	0.8	0.8	0.7
Central bank	0.7	2.8	1.1	1.1	1.1	1.5	1.5	0.4	0.2	1.4	3.3
General government	1.1	1.5	1.6	1.5	1.4	1.5	1.7	1.7	1.9	1.8	2.2
Other financial corporations	0.8	0.8	0.8	0.7	0.7	0.5	0.6	0.6	1.0	0.9	1.1
Nonfinancial corporations	50.0	49.2	49.6	49.1	48.6	49.0	49.3	50.2	49.8	48.8	47.6
Agriculture	3.5	3.5	3.3	3.1	3.0	3.2	3.0	2.8	2.6	2.8	2.8
Industry	16.5	15.0	15.0	14.7	14.5	14.9	15.5	19.5	19.3	19.1	18.4
Construction	4.2	4.8	5.1	5.0	4.9	4.8	4.9	4.9	4.6	4.2	4.1
Trade	14.0	13.7	13.3	13.2	13.1	12.8	12.5	10.9	11.1	11.0	10.7
Other loans to nonfinancial corporations	11.8	12.3	13.0	13.1	13.1	13.2	13.4	12.3	12.1	11.6	11.7
Households and NPISH	44.3	43.8	45.0	45.0	45.6	45.6	45.0	44.7	44.2	43.2	43.2
Households and NPISH of which: mortgage loans to total loans	16.8	15.8	16.4	16.7	17.1	17.4	17.4	17.5	17.3	17.1	17.4
Foreign sector	2.6	1.5	1.6	2.3	2.2	1.8	1.9	2.0	2.1	3.1	2.0
IFRS provision for NPLs to gross NPLs	60.2	61.5	59.0	58.8	58.2	59.3	56.3	56.3	57.0	57.1	58.1
IFRS provision of total loans to total gross loans	4.5	3.4	3.5	3.5	3.3	3.4	3.2	3.1	3.0	3.0	3.1
Earnings and Profitability											
Return on assets	2.2	1.8	1.1	1.2	1.2	1.2	1.2	1.4	1.5	1.5	1.9
Return on equity	11.3	9.8	6.5	7.3	6.9	7.9	7.8	10.0	10.5	10.9	13.9
Liquidity											
Customer deposits to total (noninterbank) loans	110.6	109.2	116.4	117.8	118.1	118.0	119.5	113.1	110.8	114.4	120.5
Foreign-currency-denominated loans to total loans	68.5	67.1	64.7	64.1	63.2	62.8	63.2	64.5	65.7	66.6	65.5
Average monthly liquidity ratio	2.0	2.2	2.2	2.3	2.3	2.3	2.1	2.0	1.9	2.0	2.2
Average monthly narrow liquidity ratio	1.7	1.8	1.9	2.0	1.9	1.9	1.7	1.7	1.6	1.6	1.7
Sensitivity to Market Risk											
Net open position in foreign exchange to regulatory capital	4.3	0.6	0.2	0.5	0.9	1.1	0.4	1.5	1.7	0.4	1.5
Foreign-currency-denominated liabilities to total liabilities	69.3	66.6	62.3	62.8	61.4	60.7	61.4	62.7	64.5	63.7	62.1
Classified off-balance sheet items to classified balance sheet assets	36.8	39.7	36.3	35.2	35.8	37.1	39.1	37.9	37.7	37.7	39.6

Source: NBS.

Table 11. Serbia: Indicators of Monitoring Progress Towards the SDGs

Goals	2010	2015	2020	Latest available year	
Poverty					
Employed population below international poverty line (%)	0.0	0.0	0.1	0.1	2022
Proportion of population living below the national poverty line (%)	...	25.9	...	21.7	2019
Proportion of population covered by social assistance programs (%)	11.3	13.4	...	...	
Proportion of total government spending on essential services, education (%)	10.1	8.9	...	8.6	2019
Prevalence of undernourishment (%)	<2.5	4.1	3.3	...	
Income Inequality					
GINI coefficient	...	40.5	35.0	...	
Health					
Maternal mortality ratio	12.0	13.0	10.2	...	
Under-five mortality rate (deaths per 1,000 live births)	7.6	6.3	5.6	5.5	2021
Number of new HIV infections per 1,000 uninfected population (per 1,000 uninfected	0.02	0.02	0.02	0.02	2021
Proportion of population using safely managed drinking water services (%)	75.0	75.0	75.0	...	
Proportion of population using safely managed sanitation services (%)	20.0	19.0	18.0	...	
Mortality rate attributed to cardiovascular disease, cancer, diabetes or chronic respiratory disease (probability)	24.6	22.2	...	22.0	2019
Education and Innovation					
Completion rate upper secondary, all (%)	69	75	80	...	
Completion rate upper secondary, female (%)	72	80	85	...	
Research and development expenditure as a proportion of GDP (%)	0.70	0.81	0.91	0.99	2021
Inclusion					
Number of seats held by women in national parliaments (number)	54	85	93	87	2023
Proportion of women in managerial positions (%)	32.8	28.6	31.5	33.0	2021
Proportion of population with access to electricity, rural (%)	99.5	99.9	100.0	100.0	2021
Unemployment rate, age 25+ (%) 1/	16.8	15.7	7.8	9.8	2021
Proportion of informal employment in non-agriculture employment (%) 2/	8.3	13.6	12.2	10.1	2021
Proportion of youth not in education, employment or training (%) 1/	21.2	20.4	16.2	16.1	2021
Climate					
Carbon dioxide emissions per unit of manufacturing value added (kilogrammes of CO2 per constant 2015 US dollars)	0.8	0.5	0.4	...	
Global Parnership					
Total official development assistance (gross disbursement) for technical cooperation (millions of 2016 US dollars)	178.7	179.9	323.9	...	

Sources: UN SDG Indicators Global Database; National Authorities; World Bank

1/ Labor Force Survey, ILO Statistics - Micro data processing, 19th ICLS

2/ Labor Force Survey, ILO Statistics - Micro data processing, 13th ICLS

Table 12. Serbia: Schedule of Reviews and Available Access Under the 2-year SBA Arrangement (at SBA Approval), 2022–24

			Access (Additional)			Credit Available (Cumulative)		
Availability Date	Condition	Purchase Intention	SDRs (Mill)	Quota 1/ (Percent)	EURs 2/ (Mill)	SDRs (Mill)	Quota 1/ (Percent)	EURs 2/ (Mill)
December 19, 2022	Approval of the SBA Arrangement	Purchased	785.76	120.00	992.6	785.76	120.00	992.6
June 1, 2023	Observance of end-Dec 2022 PCs, continuous PCs, and completion of First Review	Purchase	163.70	25.00	206.8	949.46	145.00	1,199.4
December 19, 2023	Observance of end-June 2023 PCs, continuous PCs, and completion of Second Review	Purchase	316.53	48.34	399.9	1,265.99	193.34	1,599.3
June 3, 2024	Observance of end-Dec 2023 PCs, continuous PCs, and completion of Third Review	Precautionary	316.46	48.33	399.8	1,582.45	241.67	1,999.1
December 2, 2024	Observance of end-June 2024 PCs, continuous PCs, and completion of Fourth Review	Precautionary	316.47	48.33	399.8	1,898.92	290.00	2,398.9

Source: IMF staff

1/ Quota is SDR 654.8 million

2/ Indicative, at SDR/ EUR exchange rate of 11/16/2022: 0.791589

Annex I. Response to Past Policy Advice

2021 Article IV Recommendation	Policy Action
Fiscal Policy	
Pandemic support measures should be well targeted.	Throughout the pandemic, fiscal policy continued to support households and businesses, including one-off payments to pensioners and payments for medical workers. However, some loan programs remained in place for too long, and the provision of a one-off €100 grant to citizens aged 16–29 was poorly targeted.
Ensure that the pandemic response package is calibrated to the pace of the economic recovery.	With strong real growth in 2021, most support measures were phased out that year. Fiscal policy was set on a gradual adjustment path and the structural primary fiscal balance tightened.
Adopt a new fiscal rule once the recovery is secured.	The new fiscal rule was incorporated into the budget system law in December 2022. It includes transition provisions to 2024 because of the new challenges in the energy sector and from high global uncertainty.
Continue to improve fiscal management.	Ongoing reforms seen in tax administration, fiscal risk management, public investment management, and public wage control.
Monetary and Exchange Rate Policies	
Monetary policy should remain accommodative during pandemic.	The economy rebounded in 2021 and inflation started to rise. In response, monetary policy tightened somewhat in October 2021. With higher inflation, and ECB policy rate increases, the NBS shifted to a faster rate of tightening from April 2022.
Closely monitor risks in the banking sector.	The banking system has remained stable, liquid, and well capitalized since the pandemic.
More exchange rate flexibility over the medium term.	The de facto stabilized exchange rate remains.
Financial Sector Policies	
Pursue reforms to strengthen capital markets and development finance.	The Capital Market Development Strategy was adopted in October 2021. A new Law on Capital Markets, which aligns the regulatory framework with the EU acquis and MiFID II requirements, was also adopted and applied from January 2023.
Structural Policies	
Focus on productivity-led growth and measures to strengthen the labor market.	The authorities have adopted an economic migration strategy encouraging the return of professionals, a law on gender equality to improve opportunities for women

2021 Article IV Recommendation	Policy Action
Fiscal Policy	
	in the labor market, and an industrial policy strategy to support investment in R&D.
Advance SOE reforms.	A centralized and updated database with a registry of all SOEs and their assets was published in December 2021.
Further reduce informal economy.	Reform initiatives for fighting the informal economy include the new e-fiscalization model, and draft legislation on extending the law on seasonal workers beyond agriculture to the construction and tourism sectors.
Transition towards a greener economy.	Progress has been limited. A Green Bond Framework was adopted in September 2021 and a first green bond was issued on the international financial markets shortly after.
Further strengthen the anti-corruption framework.	The AML/ CFT framework continues to be strengthened and progress is being made on anti-corruption initiatives. In the MONEYVAL report following the December 2021 Plenary, Serbia was assessed as "compliant" or "largely compliant" for 39 of the 40 FATF recommendations. The March 2022 Second Interim Compliance Report, which deals with corruption prevention in respect of members of parliament, judges and prosecutors, of the Group of States against Corruption (GRECO) notes that Serbia implemented 8 of 13 recommendations satisfactorily and the remaining were partially implemented.

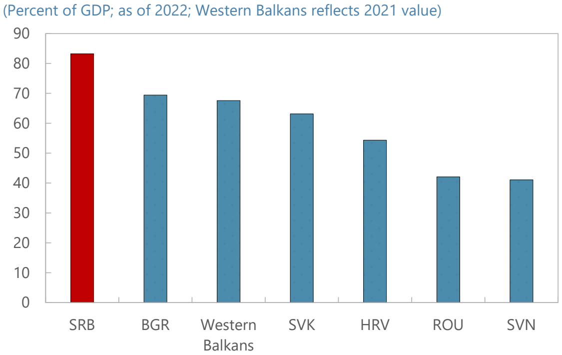
Annex II. Drivers and Outlook for FDI Flows into Serbia

Foreign direct investment (FDI) into Serbia has surged over the last decade. Much of the FDI is in trade-intensive, high-valued-added, manufacturing sectors. FDI inflows from Europe have so far predominated, but China has become increasingly important in recent years. Targeted structural reforms to support human capital development, reduce regulatory costs, increase access to financing, and improve governance would help sustain this strong FDI performance.

Background

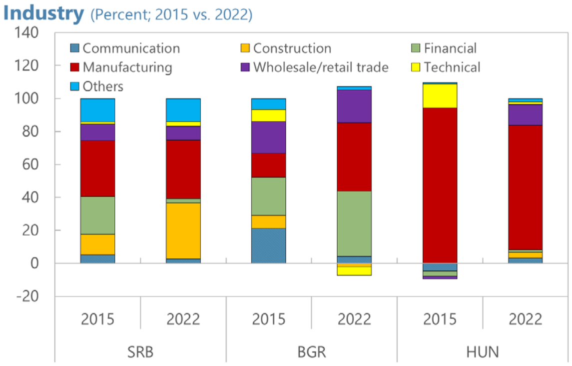
1. FDI inflows to Serbia have been exceptionally strong over the past decade, exceeding regional peers. These large inflows have helped drive investment and economic growth.[1]

Serbia: Foreign Direct Investment, Stocks
(Percent of GDP; as of 2022; Western Balkans reflects 2021 value)



Sources: Haver Analytics and IMF staff calculations

Serbia: Foreign Direct Investment, Inflows by Industry (Percent; 2015 vs. 2022)



Sources: Haver Analytics and IMF staff calculations

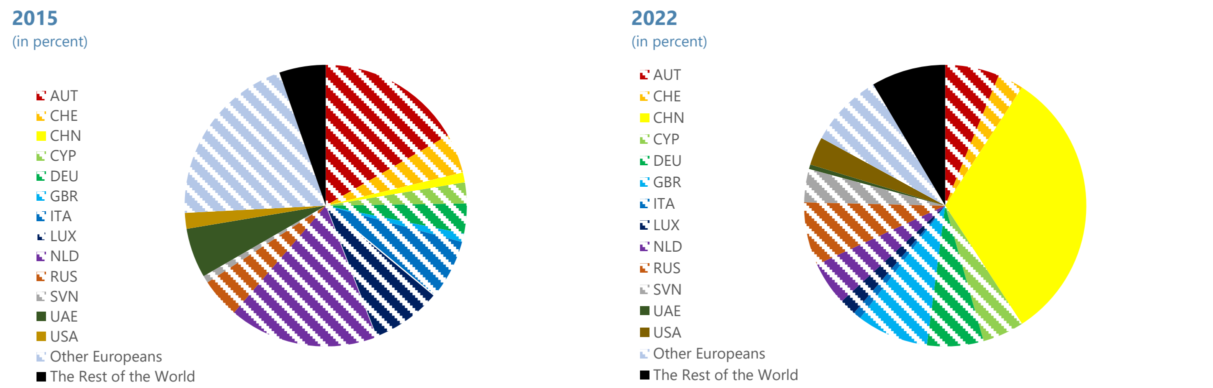
2. FDI source countries, traditionally European, are becoming increasingly diversified. China is now the largest investor (double panel). Larger projects, which mostly come from Asian investors, are also becoming more important.

3. Manufacturing FDI dominates while investment in financial institutions has fallen as most banks are now foreign owned. Manufacturing FDI tends to have greater positive spillovers, while construction, which includes infrastructure, can be more labor intensive. Investment in these sectors is also associated with declining inequality.[2]

[1] According to the EBRD FDI country factsheets, greenfield FDI as a percentage of GDP in Serbia (over 7 percent on average) is significantly higher than the EBRD average (around 4 percent).

[2] Cruz and others. *FDI and the Skill Premium: Evidence from Emerging Economies.* Policy Research Working Paper 8613, World Bank, 2018.

Serbia: Foreign Direct Investment: Inflows by Country of Origin



Sources: Haver Analytics and IMF staff calculations

Drivers of FDI

4. Research has identified macroeconomic and structural factors that generate higher FDI inflows. A recent panel study finds that strong sustainable GDP growth, real exchange rate stability, and low inflation are statistically significant in attracting FDI into emerging market economies.[3] Other studies show that human capital has been an important determinant of FDI inflows, gaining importance over time.[4] Studies also show that institutional qualities also play a determinant role in multinational firm's choice of the destination country.[5] By contrast, FDI in primary (extractive) sector generally demonstrates substantially fewer linkages to economic or institutional factors.[6]

5. Serbia's stable macroeconomic conditions and other endowments are favorable for FDI. Serbia's macroeconomic policies and conditions are described in the body of the staff report. While these are strong, it is also other factors, described below, that set it apart in attracting FDI. Serbia is also helped by its large domestic market, its located and its good transportation links.

6. Serbia's investment climate remains attractive, but targeted reforms would further strengthen Serbia's attractiveness as an investment destination. Serbia's well-educated labor force and relatively low cost of energy are key advantages. Serbia also boasts a successful one-stop shop (the Development Agency of Serbia)[7], which is geared towards large multinational firms and large projects. Top level political support for FDI also plays an important role in generating large FDI inflows. The Serbia authorities also offer numerous incentives to foreign investors, including cash

[3] Haque, Shah, and Arshad. *Sustainable economic Growth and FDI: A Comparative Panel Econometric Analysis of Low- and Middle Income Countries*. Sustainability, 2022, 14.

[4] Farhad Noorbakhsh, Alberto Paloni, Ali Youssef. *Human Capital and FDI Inflows to Developing Countries: New Empirical Evidence*, World Development, Volume 29, Issue 9, 2001,

[5] Bo Bernhard Nielsen, Christian Geisler Asmussen, Cecilie Dohlmann Weatherall, *The location choice of foreign direct investments: Empirical evidence and methodological challenges*, Journal of World Business, Volume 52, Issue 1, 2017,

[6] Paul, Jadhav. *Institutional determinants of foreign investment inflows: evidence from emerging markets*. Journal of Emerging Markets, vol. 15, no. 2, 2020.

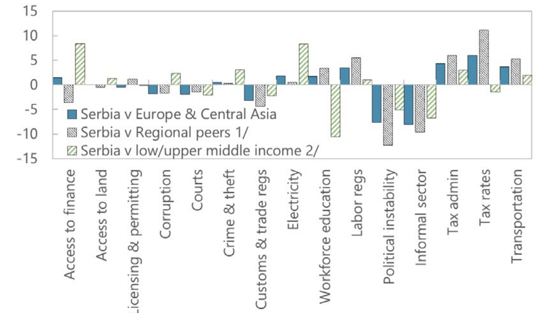
[7] https://ras.gov.rs/en

grants, construction land subsidy, 10-year corporate profit tax holiday, and payroll tax incentives. Serbia's well educated labor force also helps.

7. But challenges remain. For example:

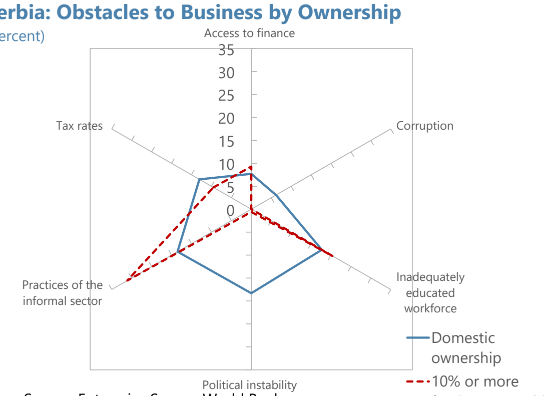
- Tax procedures for local firms are burdensome, and non-tax fees and duties are opaque and numerous, stemming from numerous laws and bylaws.[8] In addition, some commercial land is owned as "right to use" as opposed to "right of ownership," which can inhibit needed investment.
- More than fifty percent of young people (15-24 years old) are unemployed or in temporary jobs, while rate of neither employed nor in training or schooling is near 20 percent. It has also been noted that university degrees and professional training programs were not well aligned to labor needs of FDI and high growth sectors.
- Based on the World Bank Enterprise Surveys, political instability, informality, trade regulations, court processes, and corruption appear to be larger obstacles to the business climate in Serbia than comparators. Serbian firms themselves consider informality, adequately educated workforce, political interference, access to finance, and tax rates as the biggest obstacle to business and investment. These results depend on firm size and ownership, highlighting areas where the playing field is not level. Smaller and domestic firms have a more difficult time related with political institutions. Foreign-owned firms have little problems with politics and corruption but find informality and an inadequately educated workforce to be larger barriers.

Serbia: Investment Obstacles Relative to Comparators
(Differences between aggregate and Serbia; negative means higher share for Serbia)



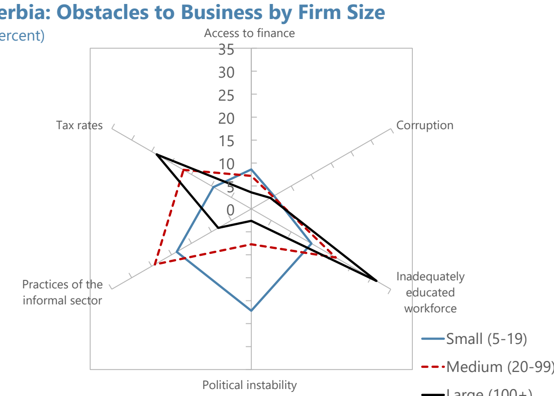
Source: World Bank Enterprise Survey Database
Note: Share of enterprises identifying area as "biggest obstacle" to business and investment environment. Calculated as aggregate share minus Serbian share.
1/ Bulgaria, Croatia, Hungary, Romania, Slovak Rep, and Slovenia. 2/ Lower and upper middle income countries with data in 2018-2022 included in the survey

Serbia: Obstacles to Business by Ownership
(Percent)



Source: Enterprise Survey, World Bank

Serbia: Obstacles to Business by Firm Size
(Percent)



Source: Enterprise Survey, World Bank

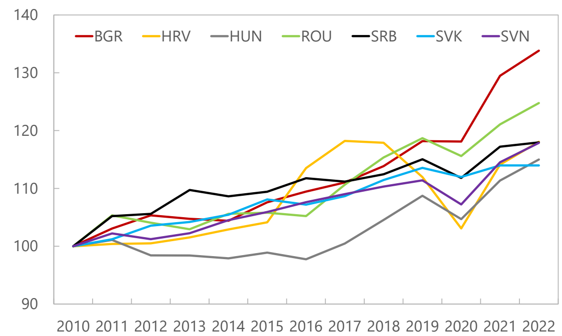
- While subject to measurement uncertainty, Serbia scores poorly on Transparency International's Corruption Perception Index, and the rating has declined since 2016. Anecdotally, the speed and consistency of the judicial processes is an area of concern. Equally, while several of the

[8] Source: European Commission program document; NALED's Grey Book.

Worldwide Governance Indicators have improved over the past 10 years, both the 'control of corruption' and 'voice and accountability' indicators are exceptions and have deteriorated.[9]

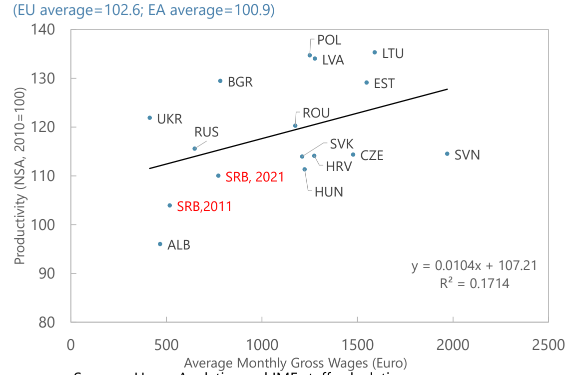
8. Serbia's wage-productivity dynamic is improving but trails key regional peers. Anecdotal evidence and the volumes of FDI inflows suggest that competitiveness is not currently a hurdle, but these dynamics need to be monitored.

Productivity: Output per Employed Person
(Index, NSA, 2010=100)



Sources: Haver Analytics and IMF staff calculations

Wages and Labor Productivity, 2021
(EU average=102.6; EA average=100.9)

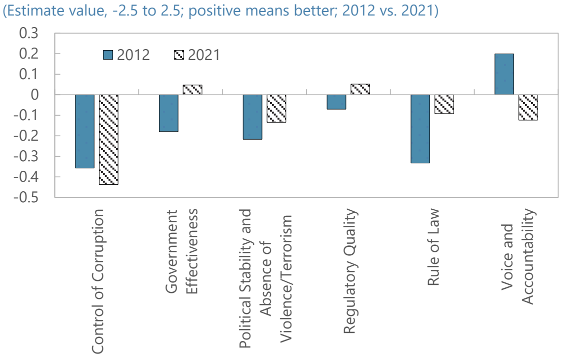


Sources: Haver Analytics and IMF staff calculations

FDI Spillovers

9. FDI often has positive economic spillovers by raising productivity: through (i) domestic competition to supply foreign firms, (ii) worker training and migration, and (iii) new management and operating practices.[10] These channels support total factor productivity growth and also technological spillovers. Importantly, FDI tends to be more labor intensive in countries that combine relatively low labor costs, a good business environment, and good governance.[11]

Serbia: Governance Indicators
(Estimate value, -2.5 to 2.5; positive means better; 2012 vs. 2021)



Source: World Governance Indicators, World Bank

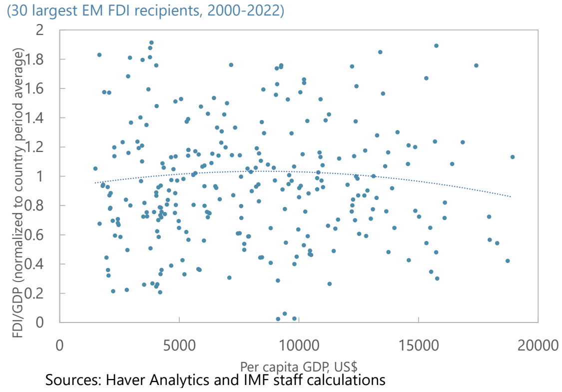
[9] See D. Kaufmann, A. Kraay, and M. Mastruzzi, Worldwide Governance Indicators (WGI), available at http://www.govindicators.org/. The WGI are a research dataset summarizing the views on the quality of governance provided by many enterprise, citizen, and expert survey respondents. The WGI are perception-based indicators and do not reflect the official views of the IMF.

[10] Brussevich & Tan. *New Growth Agenda: Encouraging FDI Spillovers*, Serbia CEM 2019, World Bank Group.

[11] Koczan, Paetzold, Vulic. *These Were the Days? Greenfield FDI, Jobs and Inclusion in Emerging Markets.* EBRD Working Paper N0. 262, 2021.

10. FDI in Serbia tends to be labor intensive, creating job opportunities. As FDI has shifted up the value-added chain, the Serbian authorities have promoted job training for residents, thus increasing spillovers. In Serbia, recent work shows that TFP growth was higher in domestic firms that supplied foreign firms across all firm sizes and in domestic firms in the same market as foreign firms, although smaller firms were the exception.[12]

FDI Inflows and Per Capita Income
(30 largest EM FDI recipients, 2000-2022)



Sources: Haver Analytics and IMF staff calculations

11. As Serbian incomes grow, the authorities need to consistently address structural issues to retain Serbia's FDI attractiveness. A staff analysis of the 30 largest emerging market recipients of FDI in terms of GDP over the past twenty years suggest that there may be a "natural" deceleration of FDI inflows when countries reach US$8,000 to US$10,000 per capita GDP.[13]

Conclusions

12. Serbia remains well positioned to continue attracting FDI, but targeted, structural reforms would support future FDI inflows. Serbia's size, location, and macroeconomic stability are all attractive elements. Targeted reforms should focus on further improving the investment climate and maximizing spillovers to local firms, which also requires leveling the playing field between domestic and multinational firms. These reform areas encompass supporting human capital development, reducing regulatory costs, increasing access to financing, capital investments in infrastructure and climate, and improving governance.

[12] Brussevich & Tan. *New Growth Agenda: Encouraging FDI Spillovers*, Serbia CEM 2019, World Bank Group.

[13] The data is normalized to countries' average level of FDI inflows, so abstracts from endowment or policy differences that affect the magnitude of flows. Hence, the analysis assesses FDI dynamics relative to itself and across peers by income.

Annex III. External Sector Assessment

Overall Assessment: *Serbia's external position in 2022 was weaker than the level implied by fundamentals and desirable policies, although this assessment is subject to model uncertainty and complicated idiosyncratic shocks faced by Serbia in 2022. The current account deficit worsened substantially in 2022 because of higher energy prices, domestic energy supply problems, and weaker trading partner growth. At the same time, FDI and exports remain relatively robust, reflecting Serbia's resilience.*

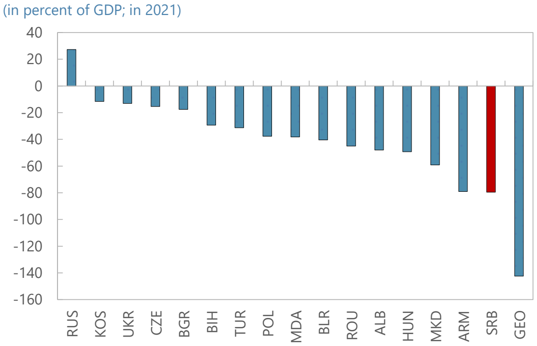
Potential Policy Responses: *Monetary and fiscal policies should remain oriented to fighting inflation and building buffers. Energy reforms will help address energy supply problems. Implementing ambitious structural reforms will help support external competitiveness and high and inclusive growth, which would allow for more exchange rate flexibility as conditions allow. Together, these policies should bring the current account deficit in line with fundamentals.*

Foreign Assets and Liabilities: Position and Trajectory

Background. Serbia's net international investment position (NIIP) is highly negative in absolute and relative terms, mostly because of a large stock of FDI liabilities. After peaking in 2020, the negative NIIP position has moderated, and by 2022 stood at minus 82 percent of GDP. Non-resident holdings of local currency debt has dropped to below 2 percent of GDP, and short-term external debt is less than 3 percent of GDP.

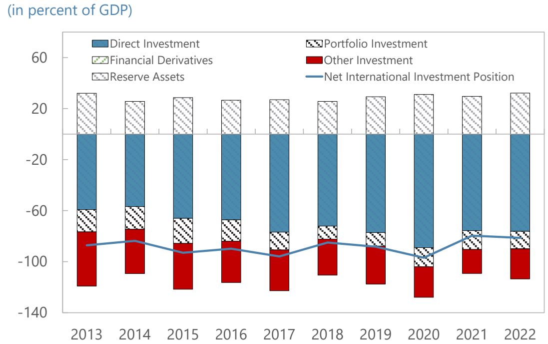
Assessment. Under the baseline scenario, where the current account gradually improves towards its norm, consistent with Serbia's fundamentals, the NIIP broadly stabilizes. To mitigate risks, the authorities should continue to make progress on EU integration and maintain efforts to improve external competitiveness, including reforms to support productivity growth, reduce the cost of doing business and continue to attract foreign investment.

Net International Investment Position
(in percent of GDP; in 2021)



Sources: Haver Analytics, IMF WEO, and IMF staff calculations

Serbia: Net International Investment Position
(in percent of GDP)



Sources: Haver Analytics, IMF WEO, and IMF staff calculations

2022 (% GDP)	NIIP: -82%	Gross Assets: 62%	Debt Assets: 12%	Gross Liab.: 144%	Debt Liab.: 64%

Current Account

Background. Serbia's current account deficit widened to almost 7 percent of GDP in 2022 mainly because of higher energy prices and lower external demand. Continued strong remittances (nearly 9 percent of GDP) and resilient goods and services exports helped contain the deficit. The CA deficit continues to be financed by strong FDI inflows as Serbia becomes increasingly integrated into the global supply chain, especially in manufacturing, and as it continues to expand its IT service sector.

Assessment. With the global terms-of-trade shock for energy importers resulting from Russia's war in Ukraine, the IMF's EBA-lite model estimates that Serbia's external position is weaker than suggested by fundamentals and desirable policies. Uncertainties surrounding this assessment are high. A conservative adjustor is included to account for the cost of higher coal and electricity imports due to one-off technical issues with domestic coal and hydroelectric production, the latter due to a drought.[1] Despite this, Serbia is facing appreciation pressures, because of strong financial inflows. Overall, Serbia's positive policy gap (mostly because of a substantially tighter fiscal stance relative to the world) help offset negative fundamentals (highly negative NIIP and relative capital scarcity).

Serbia: EBA-lite Model Results, 2022

	CA model 1/	**REER model** 1/
	(in percent of GDP)	
CA-Actual	**-6.9**	
Cyclical contributions (from model) (-)	0.1	
Additional temporary/statistical factors (-)	-1.5	
Natural disasters and conflicts (-)	0.1	
Adjusted CA	**-5.6**	
CA Norm (from model) 2/	**-4.1**	
Adjustments to the norm (-)	0.0	
Adjusted CA Norm	**-4.1**	
CA Gap	**-1.5**	**-0.2**
o/w Relative policy gap	4.7	
Elasticity	-0.39	
REER Gap (in percent)	**3.8**	**0.6**

1/ Based on the EBA-lite 3.0 methodology
2/ Cyclically adjusted, including multilateral consistency adjustments.

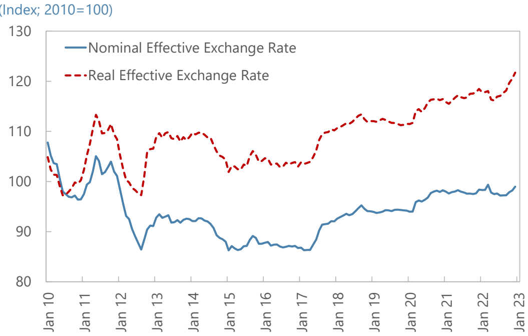
1/ Detailed coal and electricity volume import data is not available. However, based on conservative assumptions, the balance of payments costs of these idiosyncratic shocks resulting from electricity imports only, ranges from1-3 percent of GDP. Staff has taken the mid-point of this range.

Real Exchange Rate

Background. The Serbian dinar has appreciated about 12 percent in real effective terms since 2016, and modestly in 2022, with the dinar remaining relatively stable against the euro while regional peer currencies have seen some depreciation (Figure 4).

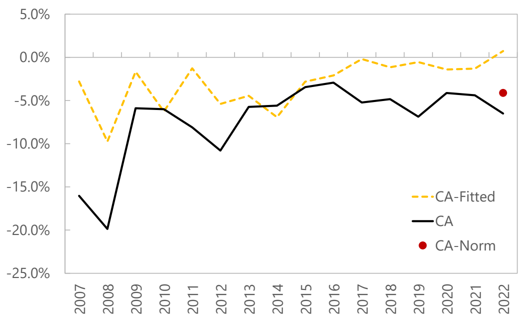
Assessment. The REER model suggests a CA gap of minus 0.2 percent, which, assuming an elasticity of -0.4, translates into a real exchange rate overvaluation of less than 1 percent. The fit of the REER model is poor, however, adding uncertainties to these estimates. Overall, the authorities' de facto stabilized exchange rate regime remains appropriate and, over the medium term, and should conditions allow, the authorities should pursue a policy of gradual exchange rate flexibility supported by ongoing policy reforms.

Serbia: Nominal and Real Effective Exchange Rate
(Index; 2010=100)



Source: IMF INS database

Serbia: Current Account Actual, Fitted, and Norm
(Percent of GDP)



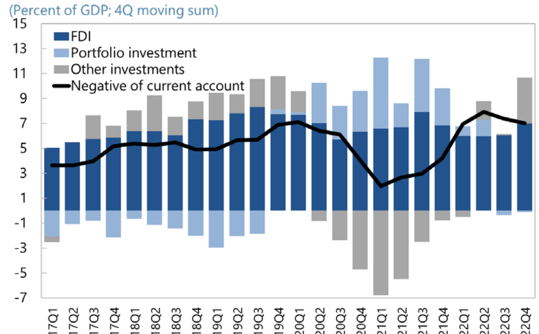
Source: IMF staff calculations

Capital and Financial Accounts: Flows and Policy Measures

Background. Net FDI have dominated Serbia's financial account flows, averaging 6.5 percent of GDP since 2005. The smaller portfolio and other financial flows are dominated by government Eurobond transactions and trade credits respectively. In 2022, net FDI inflows remained strong at more than 7 percent of GDP.

Assessment. While expected to remain strong, FDI dynamics are expected to mature over the medium term with net inflows declining gradually as the marginal return on new investments diminishes. Risks associated with destabilizing changes in capital flows is low in Serbia.

Serbia: Financial Account Composition
(Percent of GDP; 4Q moving sum)



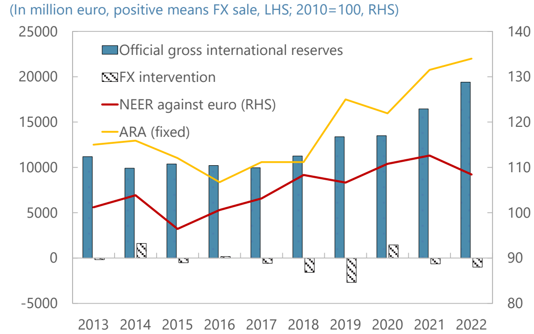
Sources: Haver Analytics and IMF staff calculations

FX Intervention and Reserves Level

Background. Since 2017, Serbia's reserves have increased substantially, from about 106 percent of the ARA metric to 134 percent in 2022. Reserves mainly comprise foreign exchange holdings, mainly in the form of liquid investment grade securities and foreign exchange deposits. Serbia is substantially euroized so pressures on the exchange rate due to depositor confidence shocks could materialize in an adverse scenario. For example, in the first half of 2022, Serbia experienced pressure on the exchange rate, resulting in more than €2.2 billion in sales of reserves through end-April. Confidence was quickly restored, however, and allowed the NBS to purchase about €3 billion in FX through the end of the year in a manner consistent with its de-facto stabilized exchange rate regime.

Assessment. Reserve levels are assessed to be adequate over the five-year projection horizon. Even with Serbia's high level of euroization, reserves at over 50 percent of M2 provide ample buffers to future confidence shocks. In addition, the Serbian financial sector's positions with non-residents are relatively small, as are private capital flows.

Serbia: FX Intervention and Reserves
(In million euro, positive means FX sale, LHS; 2010=100, RHS)



Sources: NBS, IMF WEO, and IMF staff calculations

Annex IV. Sovereign Risk and Debt Sustainability Analysis

Figure 1. Risk of Sovereign Stress

Horizon	Mechanical signal	Final assessment	Comments
Overall	…	Moderate	The overall risk of sovereign stress is moderate. Debt is relatively low compared to peers and is forecast to be on a downward trajectory. Medium term risks are assessed to be low, but demographic trends suggest moderate risks over a longer horizon. These risks can be mitigated by strong implementation of policy actions broadly in line with what were achieved in the recent history.
Near term 1/	n.a.	n.a.	Not applicable
Medium term	Low	Low	Medium-term risks are assessed as low. Gross financing needs are contained by a prudent debt managment strategy, while debt is projected to remain on a declining path. Fanchart analysis indicates a moderate level of risks that require continued improvement of macroeconomic management, particularly medium-term fiscal consolidation.
Fanchart	Moderate	…	
GFN	Moderate	…	
Stress test	…	…	
Long term	…	Moderate	Demographic trends suggest rising pension and health care spending over the long-run, which will put upward pressure on spending and debt if mitigating measures are not adopted.
Sustainability assessment 2/	…	Sustainable	Debt is assessed as sustainable. The projected debt path is expected to fall and GFNs will remain at manageable levels, conditional on the implementation of fiscal adjustment measures that are assessed as feasible
Debt stabilization in the baseline			Yes

DSA Summary Assessment

Commentary: This DSA finds that Serbia's debt is sustainable. The current global and regional environment is increasing Serbia's external financing needs despite solid macroeconomic policies. While the recent exceptional shocks increased the debt level moderately, the strong policy measures to be implemented in the program should help smooth the adjustment while strengthening policies and confidence.

Source: Fund staff.
Note: The risk of sovereign stress is a broader concept than debt sustainability. Unsustainable debt can only be resolved through exceptional measures (such as debt restructuring). In contrast, a sovereign can face stress without its debt necessarily being unsustainable, and there can be various measures—that do not involve a debt restructuring—to remedy such a situation, such as fiscal adjustment and new financing.
1/ The near-term assessment is not applicable in cases where there is a disbursing IMF arrangement. In surveillance-only cases or in cases with precautionary IMF arrangements, the near-term assessment is performed but not published.
2/ A debt sustainability assessment is optional for surveillance-only cases and mandatory in cases where there is a Fund arrangement. The mechanical signal of the debt sustainability assessment is deleted before publication. In surveillance-only cases or cases with IMF arrangements with normal access, the qualifier indicating probability of sustainable debt ("with high probability" or "but not with high probability") is deleted before publication.

Figure 2. Debt Coverage and Disclosures

Comments

1. Debt coverage in the DSA: 1/

CG	GG	NFPS	CPS	Other
	chosen			

1a. If central government, are non-central government entities insignificant? n.a.

2. Subsectors included in the chosen coverage in (1) above:

					Subsectors captured in the baseline	Inclusion
CPS	NFPS	GG: expected	CG	1	Budgetary central government	Yes
				2	Extra budgetary funds (EBFs)	Yes
				3	Social security funds (SSFs)	Yes
				4	State governments	n.a.
				5	Local governments	Yes
				6	Public nonfinancial corporations	No
				7	Central bank	No
				8	Other public financial corporations	No

3. Instrument coverage:

Currency & deposits	Loans	Debt securities	Oth acct. payable 2/	IPSGSs 3/
chosen	chosen	chosen	chosen	chosen

4. Accounting principles:

Basis of recording		Valuation of debt stock		
Non-cash basis 4/	Cash basis	Nominal value 5/	Face value 6/	Market value 7/
	chosen	chosen		

5. Debt consolidation across sectors:

Consolidated	Non-consolidated
chosen	

Color code: chosen coverage | Missing from recommended coverage | Not applicable

Reporting on Intra-government Debt Holdings

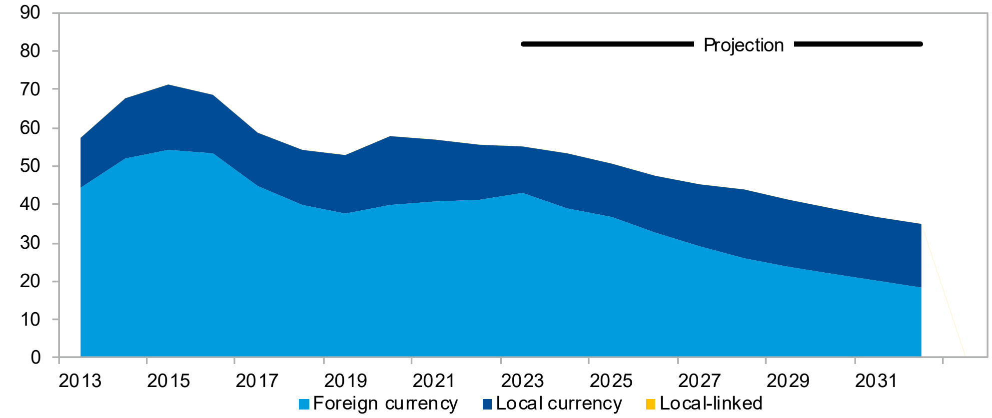
					Issuer \ Holder	Budget. central govt	Extra-budget. funds	Social security funds	State govt.	Local govt.	Nonfin. pub. corp.	Central bank	Oth. pub. fin corp	Total
CPS	NFPS	GG: expected	CG	1	Budget. central gov									0
				2	Extra-budget. funds									0
				3	Social security funds									0
				6	Nonfin pub. corp.									0
				7	Central bank									0
				8	Oth. pub. fin. corp									0
					Total	0	0	0	0	0	0	0	0	0

1/ CG=Central government; GG=General government; NFPS=Nonfinancial public sector; PS=Public sector.
2/ Stock of arrears could be used as a proxy in the absence of accrual data on other accounts payable.
3/ Insurance, Pension, and Standardized Guarantee Schemes, typically including government employee pension liabilities.
4/ Includes accrual recording, commitment basis, due for payment, etc.
5/ Nominal value at any moment in time is the amount the debtor owes to the creditor. It reflects the value of the instrument at creation and subsequent economic flows (such as transactions, exchange rate, and other valuation changes other than market price changes, and other volume changes).
6/ The face value of a debt instrument is the undiscounted amount of principal to be paid at (or before) maturity.
7/ Market value of debt instruments is the value as if they were acquired in market transactions on the balance sheet reporting date (reference date). Only traded debt securities have observed market values.

Commentary:Serbia's debt coverage and disclosure is consistent with the standard recommendations and compare favorably to peer countries. In particular, both public and publically guaranteed debt are included in the total.

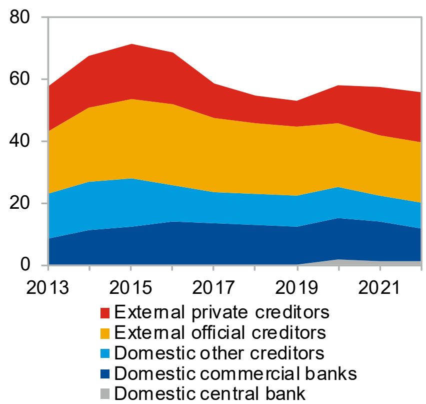
Figure 3. Public Debt Structure Indicators

Debt by Currency (Percent of GDP)



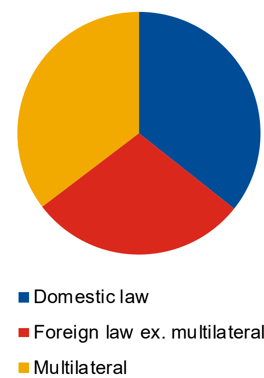
Note: The perimeter shown is general government.

Public Debt by Holder (Percent of GDP)



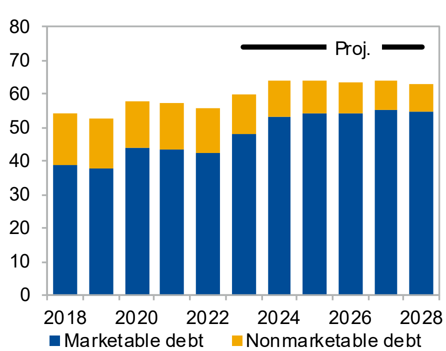
Note: The perimeter shown is general government.

Public Debt by Governing Law, 2022 (Percent)



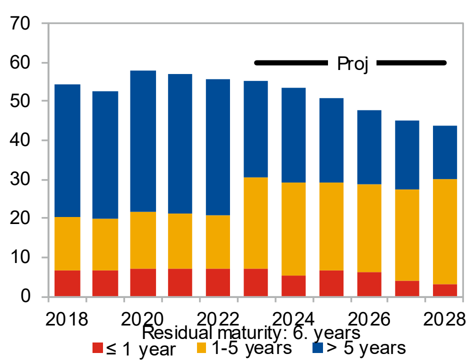
Note: The perimeter shown is general government.

Debt by Instruments (Percent of GDP)



Note: The perimeter shown is general government.

Public Debt by Maturity



Note: The perimeter shown is general government.

Commentary: Domestic and multilateral debt accounts for a large share of the debt stock and provides a relatively stable investor base. Increased debt financing in the near term is mainly expected from official creditors or with medium to long maturity. The high share of foreign currency debt represents a major risk. However, the large share of official and institutional creditors to whom external debt is owed, the long average maturity of outstanding debt, and the high share of the fixed interest rate debt (about 85%) represent important factors that mitigate the sustainability risks.

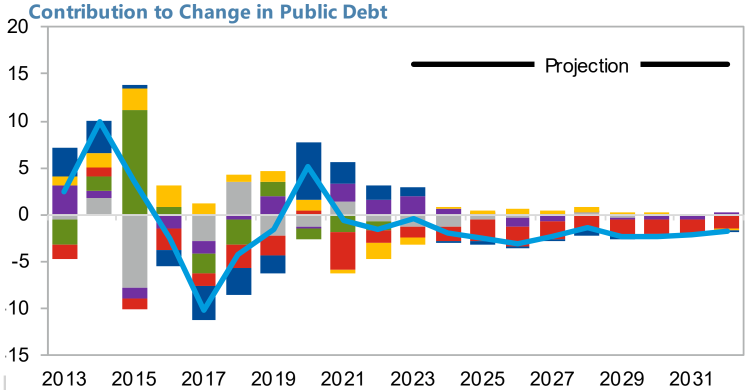
Figure 4. Baseline Scenario

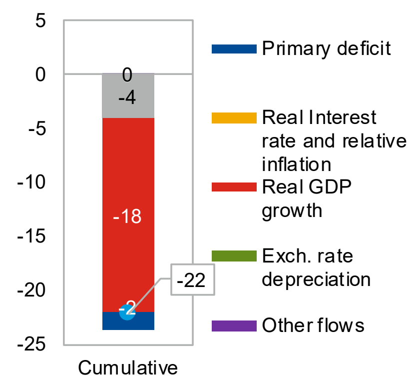
(Percent of GDP unless indicated otherwise)

	Actual	Medium-term projection						Extended projection			
	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
Public debt	55.6	55.3	53.3	50.7	47.6	45.2	43.8	41.4	39.2	37.0	35.2
Change in public debt	-1.5	-0.3	-2.0	-2.6	-3.1	-2.4	-1.4	-2.4	-2.3	-2.2	-1.8
Contribution of identified flows	-0.8	1.0	-0.8	-2.1	-2.7	-2.4	-1.6	-2.1	-2.1	-2.1	-1.6
Primary deficit	1.5	1.0	0.0	-0.3	-0.3	-0.3	-0.4	-0.3	-0.3	-0.2	-0.2
Noninterest revenues	43.4	42.1	42.1	42.4	42.4	42.4	42.4	42.3	42.3	42.3	42.3
Noninterest expenditures	44.9	43.1	42.1	42.1	42.1	42.1	42.0	42.0	42.0	42.1	42.1
Automatic debt dynamics	-4.0	-2.0	-1.4	-1.8	-1.4	-1.3	-1.3	-1.5	-1.5	-1.5	-1.5
Real interest rate and relative inflat	-1.7	-0.9	0.2	0.5	0.5	0.5	0.4	0.2	0.1	0.0	-0.1
Real interest rate	-4.4	-4.3	-0.9	-0.1	0.1	0.1	0.1	-0.1	-0.2	-0.3	-0.3
Relative inflation	2.7	3.4	1.1	0.6	0.4	0.4	0.3	0.3	0.3	0.2	0.2
Real growth rate	-1.3	-1.1	-1.6	-2.3	-1.9	-1.8	-1.7	-1.7	-1.6	-1.5	-1.4
Real exchange rate	-1.0	...	...	...	...	...	...	...	...	...	...
Other identified flows	1.6	1.9	0.6	0.0	-1.0	-0.7	0.2	-0.3	-0.3	-0.3	0.1
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other transactions	1.6	1.9	0.6	0.0	-1.0	-0.7	0.2	-0.3	-0.3	-0.3	0.1
Contribution of residual	-0.7	-1.3	-1.2	-0.5	-0.3	0.0	0.2	-0.3	-0.2	-0.1	-0.1
Gross financing needs	6.9	9.0	8.1	7.5	9.8	9.5	7.7	7.5	8.6	8.7	8.6
of which: debt service	5.4	8.0	8.1	7.8	10.1	9.8	8.2	7.9	8.9	8.9	8.8
Local currency	3.1	4.5	1.5	3.1	3.7	2.7	3.0	3.5	4.5	4.7	4.4
Foreign currency	2.3	3.5	6.6	4.7	6.4	7.1	5.1	4.4	4.4	4.2	4.4
Memo:											
Real GDP growth (percent)	2.3	2.0	3.0	4.5	4.0	4.0	4.0	4.0	4.0	4.0	4.0
Inflation (GDP deflator; percent)	10.6	12.1	5.1	3.9	3.4	3.1	3.0	3.0	3.0	3.0	3.0
Nominal GDP growth (percent)	13.1	14.4	8.3	8.6	7.5	7.3	7.1	7.1	7.1	7.1	7.1

(percent of GDP)

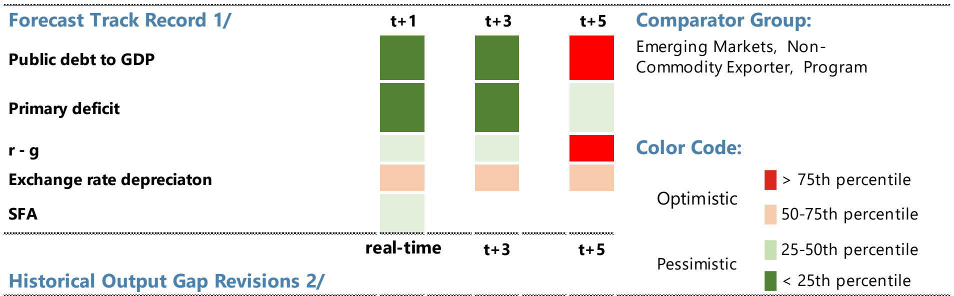
Contribution to Change in Public Debt



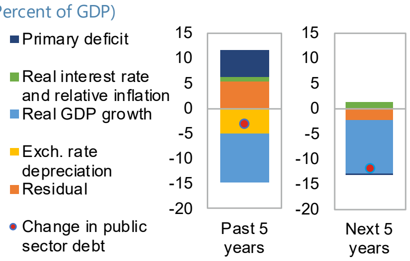


Staff commentary: Public and publicly guaranteed debt is expected to fall reflecting the effects from fiscal consolidation and a recovery in growth towards potential.

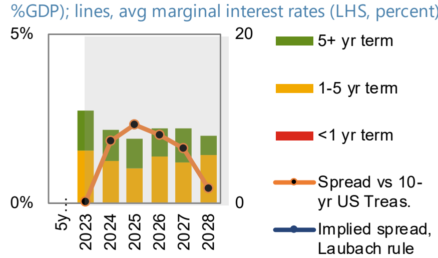
Figure 5. Realism of Baseline Assumptions



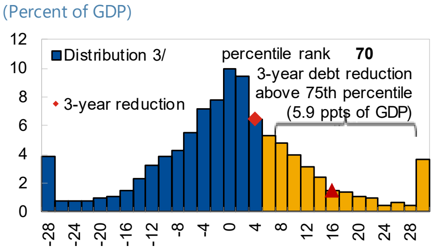
Public Debt Creating Flows
(Percent of GDP)



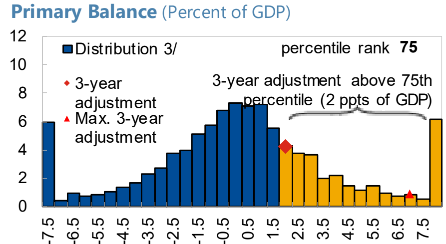
Bond Issuances (bars, debt issuances (RHS, %GDP); lines, avg marginal interest rates (LHS, percent))



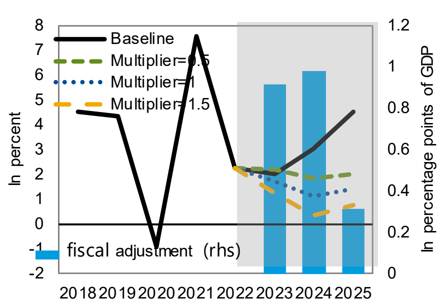
3-Year Debt Reduction
(Percent of GDP)



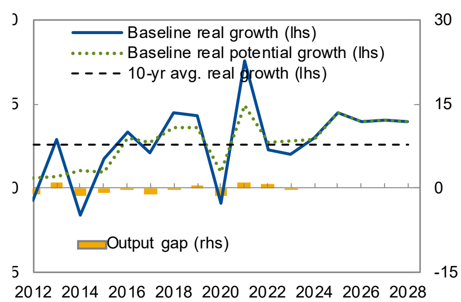
3-Year Adjustment in Cyclically-Adjusted Primary Balance (Percent of GDP)



Fiscal Adjustment and Possible Growth Paths
(lines, real growth using multiplier (LHS); bars, fiscal adj. (RHS (Percent)



Real GDP Growth



Commentary: Serbia is a converging economy with demonstrated strong growth and sound policy performance in recent years. While the recovery from COVID-19 and the recent exceptional shocks have complicated effects on the growth path, realism analysis suggests projections are broadly in line with historical performance and other countries. Past forecast errors do not reveal any systematic biases, and the projected fiscal adjustment and debt reduction are lower that what was achieved in the past. The relatively strong growth projection at t+5 reflects the expected continuation of growth convergence and some base effects as the economy recovers after the exceptional shocks, still in line with the pre-COVID growth path.

Source : IMF Staff.

1/ Projections made in the October and April WEO vintage.

2/ Data cover annual obervations from 1990 to 2019 for MAC advanced and emerging economies. Percent of sample on vertical axis.

3/ Calculated as the percentile rank of the country's output gap revisions (defined as the difference between real time/period ahead estimates and final estimates in the latest October WEO) in the total distribution of revisions across the data sample.

Figure 6. Medium-Term Risk Analysis

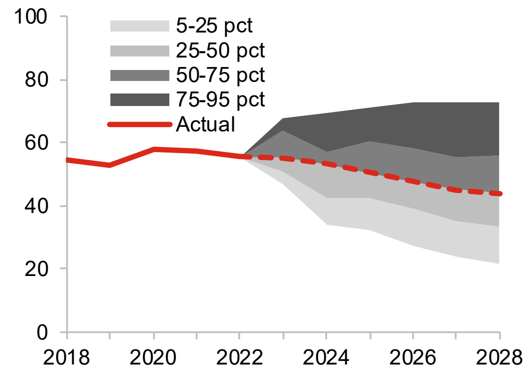
Debt Fanchart and GFN Financeability Indexes

(Percent of GDP unless otherwise indicated)

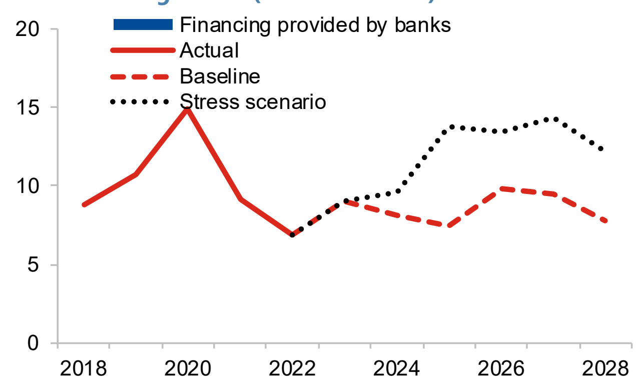
Module	Indicator	Value	Risk index	Risk signal	Adv. Econ., Non-Com. Exp, Program (0 / 25 / 50 / 75 / 100)
Debt fanchart module	Fanchart width	51.3	0.7	...	
	Probability of debt not stabilizing (pct)	0.9	0.0	...	
	Terminal debt level x institutions index	25.5	0.6	...	
	Debt fanchart index	**...**	**1.3**	**Moderate**	
GFN finance-ability module	Average GFN in baseline	8.6	2.9	...	
	Bank claims on government (pct bank assets)	18.5	6.0	...	
	Chg. in claims on govt. in stress (pct bank asset	6.0	2.0	...	
	GFN financeability index	**...**	**10.9**	**Moderate**	

Legend: Interquartile range; Serbia

Final Fanchart (Percent of GDP)



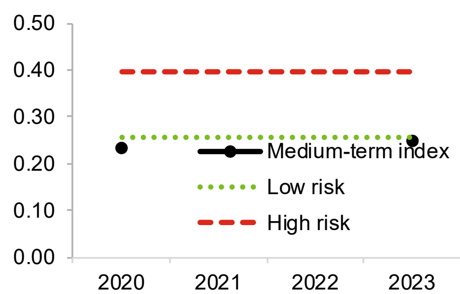
Gross Financing Needs (Percent of GDP)



Triggered stress tests (stress tests not activated in gray)

Banking crisis | Commodity prices | Exchange rate | Contingent liab. | Natural disaster

Medium-Term Index



Medium-Term Risk Analysis

Debt fanchart index	1.1	2.1	0.5	0.3
GFN finaceability index	7.6	17.9	0.5	0.2
Medium-	0.3	0.4	...	0.3, Low

Prob. of missed crisis, 2023-2028 (if stress not predicted): 9.1 pct.

Prob. of false alarm, 2023-2028 (if stress predicted): 42.0 pct.

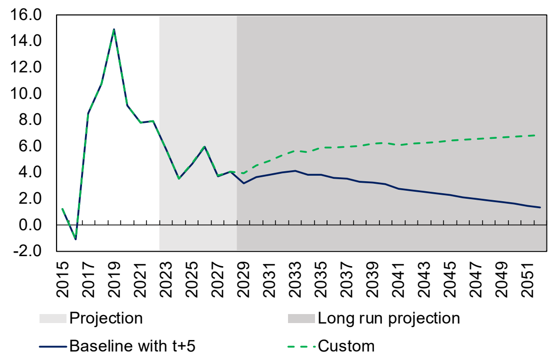
Commentary: Both medium-term tools, the Debt Fanchart Module and the GFN Financeability Module, suggest moderate levels of risk, while the medium-term index shows a low level. The relatively large banking sector and relatively low government debt mitigate domestic financing risks. In addition, the width of the fanchart is relatively narrow, reflecting a low level of shocks in the recent history, and would remain comparable to the COVID-shock scenario in a stress scenario. The GFN is at a relatively moderate level, and most financing needs are expected to be filled by official creditors in the near to medium term, further anchoring stability.

Figure 7. Long-Term Risk Analysis

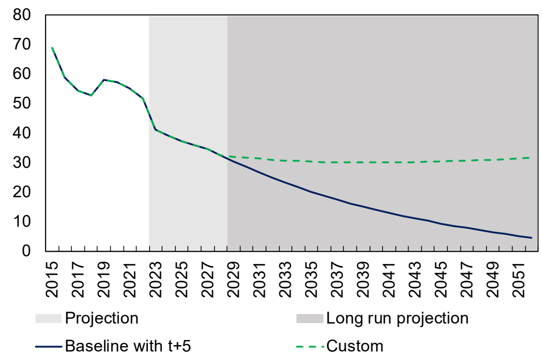
Custom

	Baseline extension of fifth projection year	Custom baseline
Real GDP growth	4.0%	4.0%
Primary Balance-to-GDP	0.5%	-0.2%
Real depreciation	-3.7%	0.0%
Inflation (GDP deflator)	4.3%	4.3%

GFN-to-GDP ratio

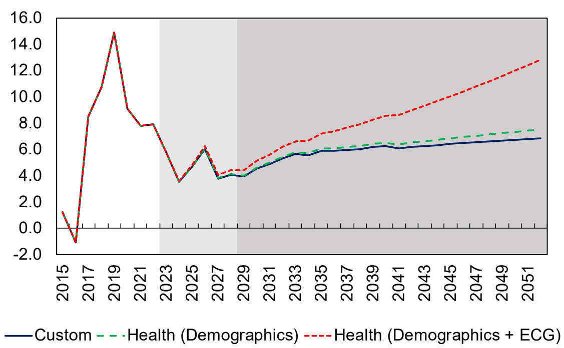


Total public debt-to-GDP ratio

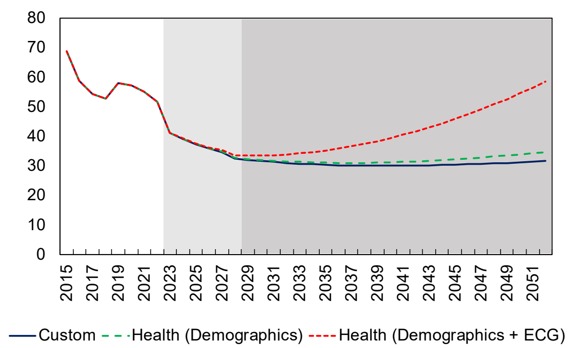


Demographics: Health

GFN-to-GDP ratio



Total public debt-to-GDP ratio



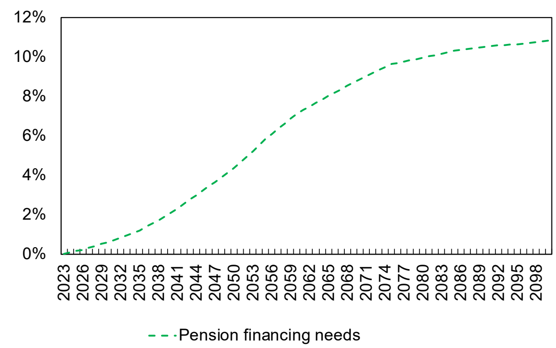
Commentary: The 'custom' scenario GFN and debt projection for 2028-52 assumes that real GDP growth and the deflator remain at the 2028 level, the real exchange rate remains constant, and a primary fiscal deficit equal to the average for 2021-25. Under this scenario, debt remains broadly stable at around 30 percent of GDP. The 'Heath (Demographics)' is a standardized shock to capture higher expenditure needs from an aging population; and the 'Health (Demographics + ECG)' shock also excludes medical inflation. The latter shock has the potential to increase debt to 60 percent of GDP by 2052, without mitigating measures.

Figure 7. Long-Term Risk Analysis (concluded)

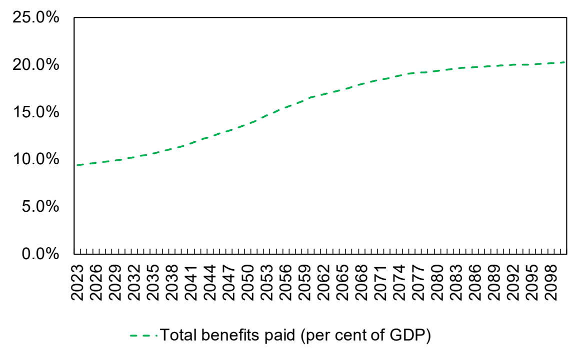
Demographics: Pension

Permanent adjustment needed in the pension system (pp of GDP per year)	To keep pension assets positive for:		
	30 years	50 years	Until 2100
	2.10%	4.65%	7.14%

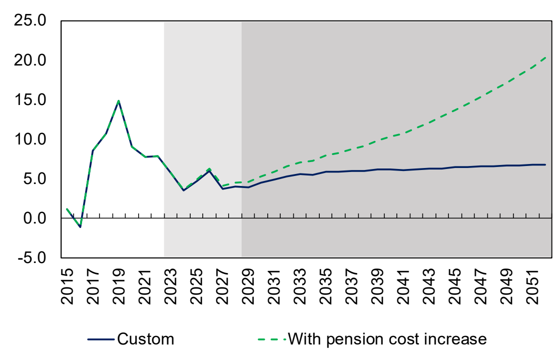
Pension Financing Needs



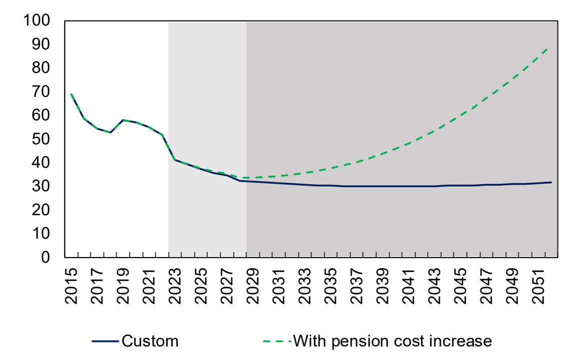
Total benefits paid



GFN-to-GDP ratio



Total public debt-to-GDP ratio



Commentary: With an aging population, Serbia's pension costs are expected to rise by around 0.1-0.2 percent of GDP a year. Unless mitigating measures are taken, either through pension reform or other fiscal measures, debt is projected to increase to around 90 percent of GDP by 2052.

Annex V. Potential Growth in Serbia

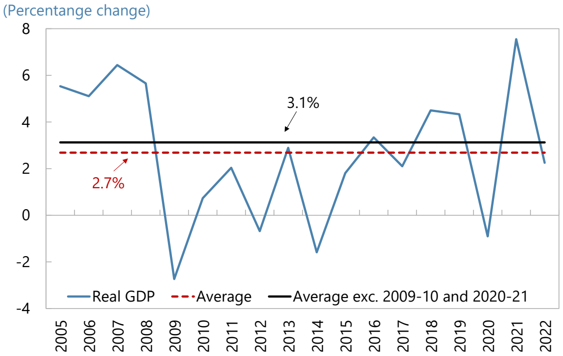
Conditional on continued prudent macroeconomic policies and targeted structural reforms, Serbia's potential growth is assessed to be around 4 percent. Continued focus on raising the labor activity rate, strengthening the investment climate, and promoting human and technological development is key to achieve such growth rates.

1. Growth in Serbia has historically been volatile. As a small, open, emerging-market economy Serbia is vulnerable to external shocks and has experienced several steep downturns over the past two decades. This makes any backward-looking assessment of potential growth difficult. Serbia is, nevertheless, projected to have one of the highest growth rates of its peers. To answer how such growth rates might be secured, a standard growth accounting framework is employed:

$$\Delta \ln(\boldsymbol{Y}) = \boldsymbol{\alpha}\Delta \ln(\boldsymbol{L}) + (\mathbf{1}-\boldsymbol{\alpha})\Delta \ln(\boldsymbol{K}) + \boldsymbol{\varepsilon}$$

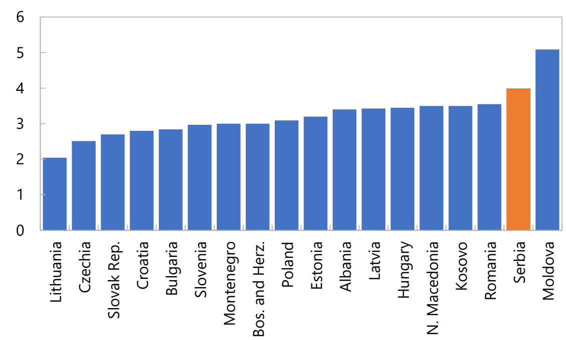
where $\boldsymbol{Y}$ represents output; $\boldsymbol{\alpha}$ the labor share of GDP; $\boldsymbol{L}$ labor; $\boldsymbol{K}$ the capital stock, and; $\boldsymbol{\varepsilon}$ the 'Solow residual'. Each will be explored in turn.

Serbia: Real GDP Growth
(Percentange change)



Sources: Haver Analytics and IMF staff calculations

Projected Growth in 2028
(Percent)



Source: IMF WEO

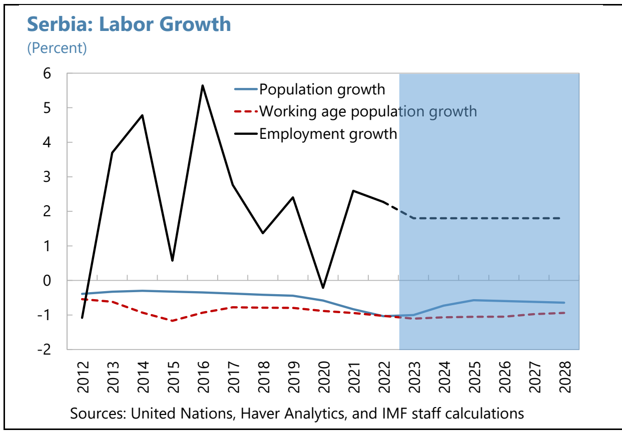
Labor

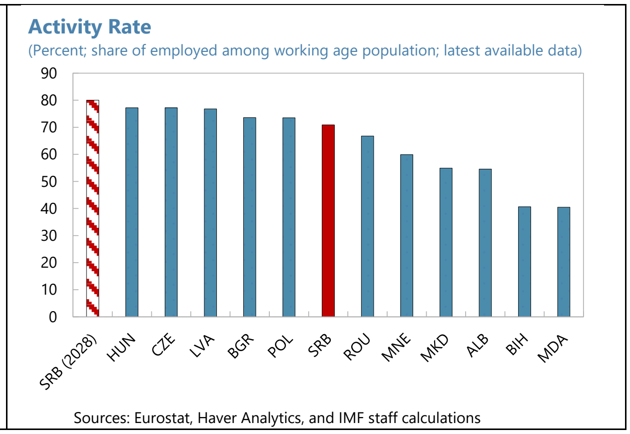
2. Despite a declining population, there is scope for employment to continue to grow. Serbia faces a shrinking population, with UN estimates suggesting an average decline of ½ percent a year. Nevertheless, employment growth has been strong, averaging over 2½ percent a year, as unemployment declined and labor force participation increased. This trend is expected to continue—supported by immigration and returning emigrants—as FDI supports employment and labor market rigidities ease. These trends imply a significant increase in the activity rate to 80 percent, close to the best performing countries in the region. Assuming employment growth of

2 percent and a labor share of 45 percent[1], this gives a labor *quantity* contribution to GDP of around 1 percent:

$$\Delta \ln(Y) = \mathbf{0.45} \times \mathbf{2}\% + (1-\alpha)\Delta \ln(K) + \varepsilon$$

$$\Delta \ln(Y) = \mathbf{1}\% + (1-\alpha)\Delta \ln(K) + \varepsilon$$





Capital

3. **Growth in the capital stock is an important component of potential growth.** Historical estimates of Serbia's capital stock and average depreciation rates are taken directly from the Total Economy Database.[2] This shows a steady increase in the real value of Serbia's capital stock, although a decline (especially in the early-2000s) when considered as a share of GDP. In recent years, much of this investment has been in the form of FDI and, to a lesser extent, public investment; a key challenge going forward will be to try to unlock domestic private investment.[3] The projected investment rate (as a share of the capital stock) is consistent with staff forecasts at 8 percent; a 5 percent depreciation rate is assumed. Taken together, this implied a contribution of the *quantity* of capital to annual growth of around 1½ percent:

$$\Delta \ln(Y) = 1\% + \mathbf{0.55} \times (\mathbf{8}\% - \mathbf{5}\%) + \varepsilon$$

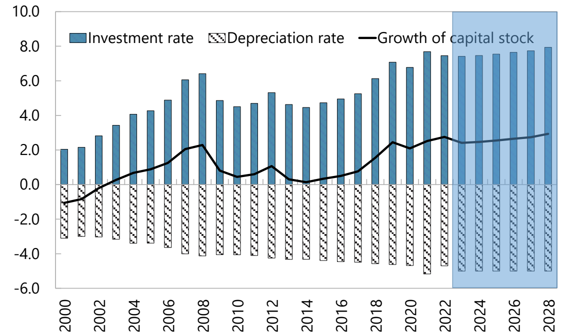
$$\Delta \ln(Y) = 1\% + \mathbf{1.5}\% + \varepsilon$$

[1] This is calculated using total compensation of employment as a share of GDP. This technique will underestimate the actual labor share as it excludes the self-employed, but nevertheless provides a reasonable approximation.

[2] Kindly supplied from The Conference Board think-tank: https://www.conference-board.org/us/

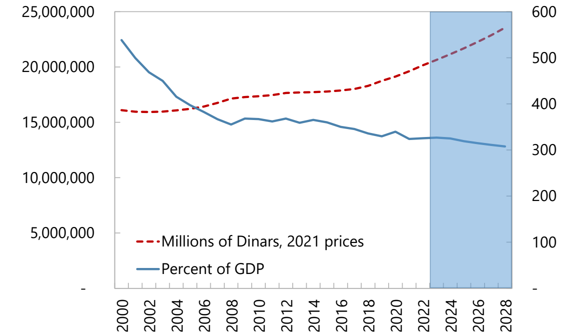
[3] See the World Bank Serbia CEM report on *Investment for Growth* (2019)

Serbia: Growth of Capital Stock
(Percent)



Sources: Total Economy Database, Haver Analytics, and IMF staff calculations

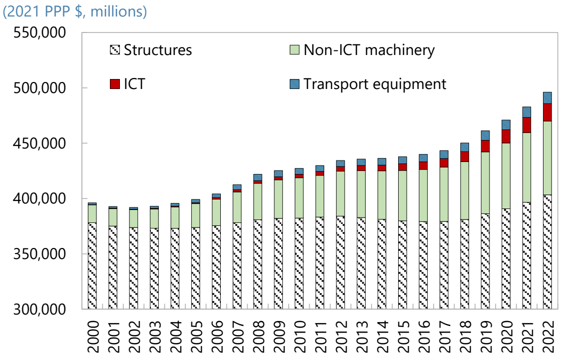
Serbia: Capital Stock
(Millions of Dinars, in 2021 prices, LHS; percent, RHS)



Sources: Total Economy Database, Haver Analytics, and IMF staff calculations

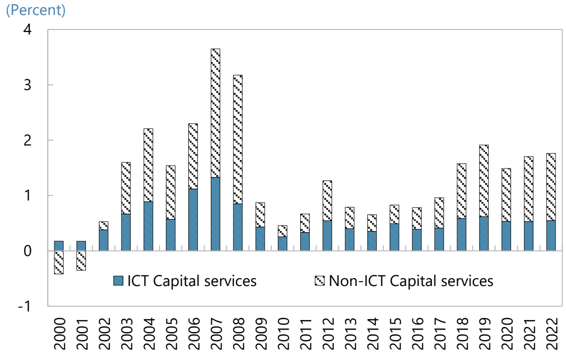
4. Information and Communication Technology (ICT) is becoming increasingly important. Structures—office buildings and factory shells, for example—make up an estimated 80 percent of the capital stock. The remainder is made up of non-ICT machinery (13 percent), ICT including software (4 percent) and transport equipment (2 percent). Despite its small share, however, ICT stands out by both its high economic return (with an estimated contribution to growth of ½ percent in 2022) and its high rate of depreciation (around 20 percent). In other words, investment in ICT enjoys high returns, but it is unlikely that a large stock of such capital will be built given that it can quickly become obsolete.

Serbia: Capital Stock
(2021 PPP $, millions)



Source: Total Economy Database

Serbia: Contribution to GDP from Capital
(Percent)



Source: Total Economy Database

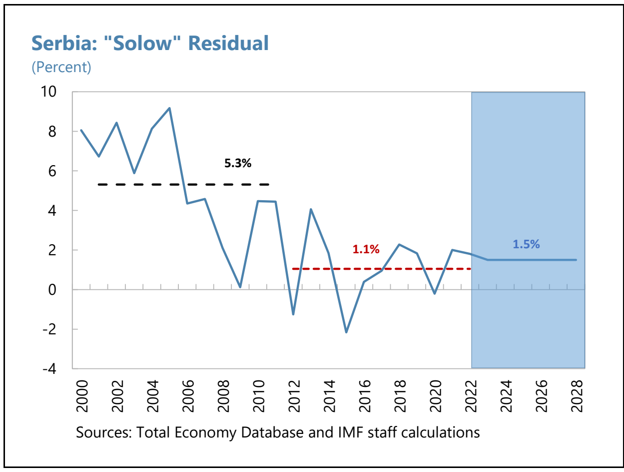
Solow Residual

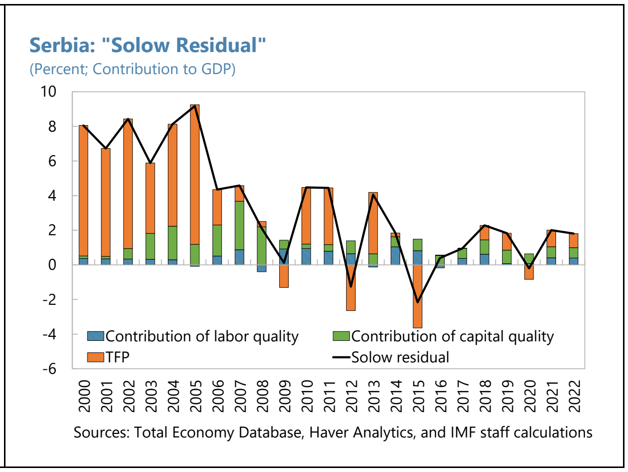
5. The "quality" of labor and capital complements total factor productivity growth. The "Solow residual" is the remainder once the contribution of labor and capital growth has been accounted for. This residual was extremely high in the 2000s as Serbia emerged from sanctions and significant economic transformation took place. The residual fell to around 1 percent over the last decade, as the country was hit by the fallout from the global financial crisis and the pandemic. It is difficult to use growth accounting to analyze any specific year. It is interesting, however, to see the important cumulative role that the *quality* of labor (better education and skills training) and the *quality* of capital (e.g., more productive equipment and machines), as estimated by the Total

Economy Database (TED), has been on growth. In contrast, total factor productivity—how efficiently different factors of production interact with each other—has been less important in recent years. Contingent on strong structural reforms, as underpinned by the SBA, the Solow residual is projected to be around 1½ percent, with overall potential growth of around 4 percent.

$$\Delta \ln(Y) = 1\% + 1.5\% + 1.5\%$$

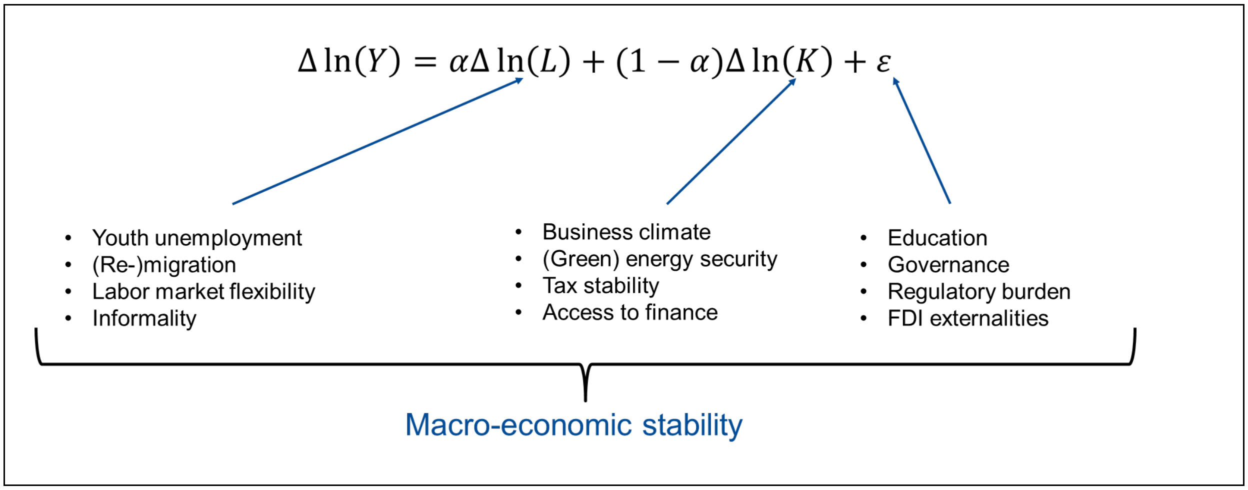
$$\Delta \ln(Y) = \mathbf{4}\%$$





The Importance of Continual Reform

6. Serbia's strong projected growth rate requires ongoing macroeconomic stability and continued strong reforms. Macroeconomic stability is a necessary condition for sustained strong growth. But strong structural reforms are important for increasing all factors of production. Staff's estimate of a 4 percent potential growth rate is contingent on active reform, as witnessed in recent years.



Annex VI. External Debt Sustainability Assessment

Serbia's external debt is assessed to be sustainable over the medium term. Despite a current account shock in 2022, external debt remained broadly stable and is projected to remain on a downward path over the medium term. Stress tests suggest that external debt dynamics are sensitive to real exchange rate shocks, given the share of external debt denominated in foreign currencies. It is important, therefore, to continue with prudent fiscal policies, maintaining adequate buffers, and structural reforms to support external resilience.

1. **After peaking in 2020, reflecting higher public borrowing during the COVID-19 pandemic, external debt declined sharply, which is projected to continue over the medium term.** Serbia's current account deficit is covered by FDI inflows, so external debt dynamics are largely a function of external government borrowing (euro bond issuances), and, to a lesser extent, private corporate sector borrowing. In line with declining debt stock ratios over the medium term, gross financing needs (about 14 percent of GDP in 2023) are projected to decline to less than 9 percent of GDP by 2028.

Table 1. Serbia: External Debt Sustainability Framework, 2018-28

(In percent of GDP, unless otherwise indicated)

	Actual							Projections						
	2018	2019	2020	2021	2022	10-Year Historical Average	10-Year Standard Deviation	2023	2024	2025	2026	2027	2028	Debt-stabilizing non-interest current account 6/
Baseline: External debt	64.0	65.8	75.8	68.2	64.8			**66.0**	**62.3**	**58.1**	**54.2**	**49.9**	**47.8**	**-3.9**
Change in external debt	-9.0	1.8	10.0	-7.6	-3.5			1.2	-3.6	-4.2	-3.9	-4.4	-2.1	
Identified external debt-creating flows (4+8+9)	-6.8	3.7	0.0	-9.2	-2.4			3.0	2.2	0.9	1.2	1.0	1.1	
Current account deficit, excluding interest payments	3.3	5.5	2.7	2.9	5.5			5.0	4.8	4.2	4.2	3.7	3.8	
Deficit in balance of goods and services	9.5	10.0	8.8	8.5	11.7			9.1	8.2	7.3	7.0	6.4	6.1	
Exports	49.3	50.8	47.6	53.6	63.0			60.2	59.9	59.3	59.4	59.9	60.9	
Imports	58.9	60.8	56.3	62.1	74.7			69.3	68.1	66.6	66.3	66.4	67.1	
Net non-debt creating capital inflows (negative)	-2.3	-2.1	-1.9	-1.8	-1.7			-1.8	-1.7	-1.6	-1.6	-1.5	-1.5	
Automatic debt dynamics 1/	-7.7	0.3	-0.8	-10.3	-6.2			-0.1	-0.9	-1.7	-1.4	-1.2	-1.2	
Contribution from nominal interest rate	1.6	1.4	1.4	1.4	1.3			1.1	0.9	0.9	0.8	0.8	0.7	
Contribution from real GDP growth	-2.9	-2.7	0.6	-4.8	-1.4			-1.2	-1.8	-2.6	-2.2	-2.0	-1.9	
Contribution from price and exchange rate changes 2/	-6.5	1.6	-2.8	-6.8	-6.2			-1.4	-3.6	-2.9	-2.4	-2.0	-1.4	
Residual, incl. change in gross foreign assets (2-3) 3/	-2.2	-1.9	10.1	1.6	-1.1			-0.4	-2.2	-2.2	-2.7	-3.4	-1.9	
External debt-to-exports ratio (in percent)	129.7	129.6	159.3	127.3	102.8			109.6	104.0	98.0	91.4	83.2	78.4	
Gross external financing need (in billions of US dollars) 4/	8.3	10.0	7.7	9.0	11.1			10.1	10.7	9.0	9.9	11.9	9.5	
in percent of GDP	16.5	19.5	14.4	14.2	15.7			13.7	13.2	10.2	10.3	11.5	8.6	
Scenario with key variables at their historical averages 5/								**66.0**	**62.9**	**59.8**	**56.2**	**51.9**	**49.3**	**-3.4**
Key Macroeconomic Assumptions Underlying Baseline														
Real GDP growth (in percent)	4.5	4.3	-0.9	7.5	2.3	2.6	2.6	2.0	3.0	4.5	4.0	4.0	4.0	
GDP deflator in US dollars (change in percent)	9.7	-2.5	4.5	9.9	9.9	2.7	8.5	2.3	5.7	4.8	4.3	3.8	2.8	
Nominal external interest rate (in percent)	2.5	2.2	2.2	2.2	2.2	2.7	0.5	1.8	1.5	1.6	1.4	1.6	1.5	
Growth of exports (US dollar terms, in percent)	14.8	4.6	-2.9	33.2	32.1	12.5	14.3	-0.4	8.4	8.5	8.6	8.9	8.6	
Growth of imports (US dollar terms, in percent)	18.5	5.0	-4.0	30.3	35.2	10.2	15.1	-3.2	7.1	7.1	8.1	8.0	8.0	
Current account balance, excluding interest payments	-3.3	-5.5	-2.7	-2.9	-5.5	-3.1	1.7	-5.0	-4.8	-4.2	-4.2	-3.7	-3.8	
Net non-debt creating capital inflows	2.3	2.1	1.9	1.8	1.7	2.2	0.3	1.8	1.7	1.6	1.6	1.5	1.5	

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

2. **Serbia's external debt composition is strong, mostly long-term and owed by the public sector.** As of end-December 2023, about 82 percent of Serbia's external debt was long term on a

residual maturity basis, with 60 percent issued by the public sector and 40 percent by the private sector. Short-term external debt is manageable at about 18 percent of GDP, but more than 84 percent is private sector exposure. Almost 40 percent of Serbia's external debt is held by IFIs and official bilateral creditors and less than 60 percent by private creditors, which includes a substantial portion of euro bonds. Local currency debt held by nonresidents stands at less than 3 percent of GDP.

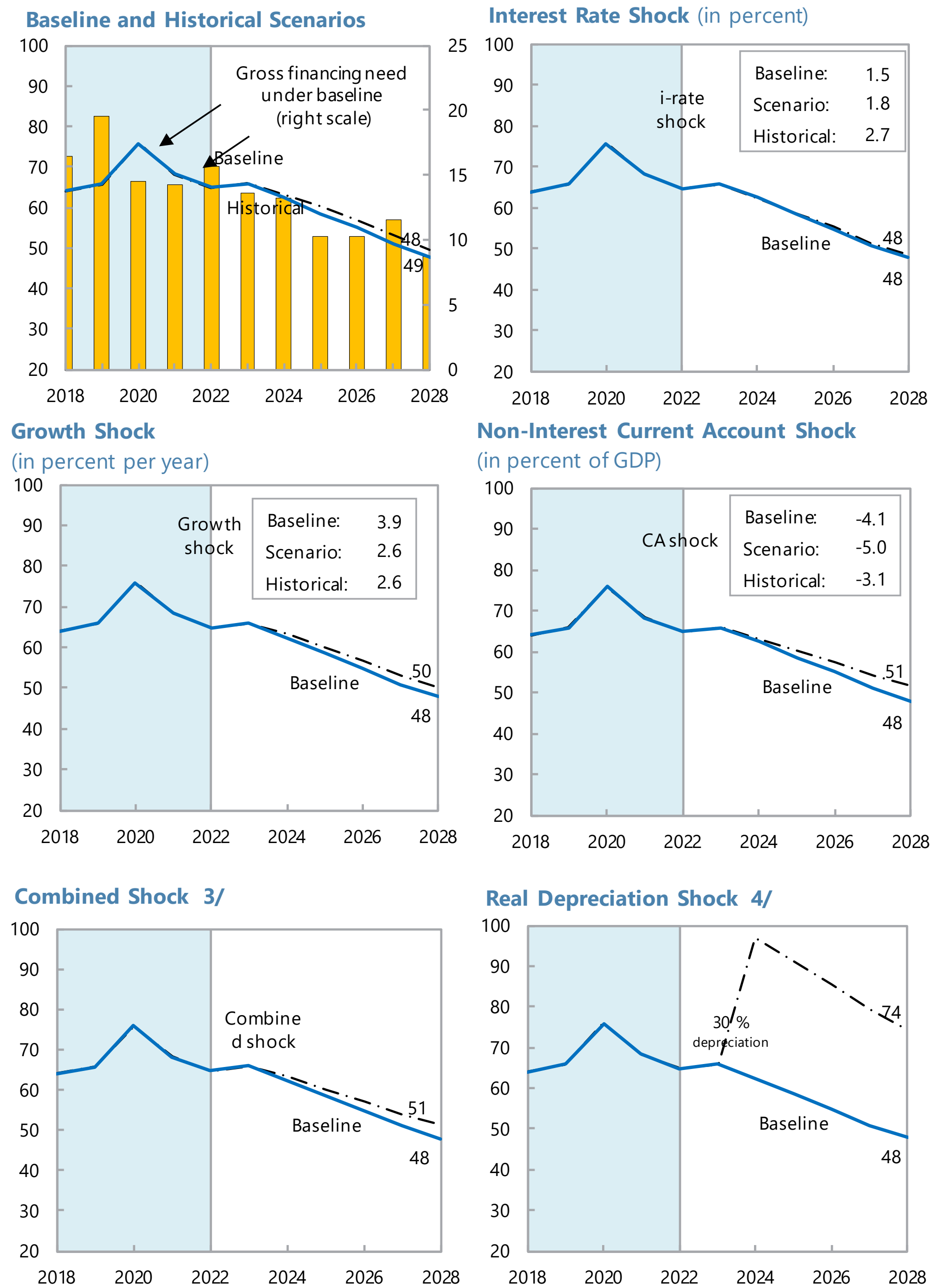
3. **Projected economic growth, a narrowing current account deficit, and strong net FDI inflows, as well as automatic debt dynamics are key factors driving the expected decline in Serbia's external-debt-to-GDP ratio.** Real GDP growth, while expected to fall to 2 percent this year, is projected to move back to its potential of around 4 percent over the medium term. After expanding in 2022 and 2023, the current account deficit is expected to narrow to between 5 and 4 percent of GDP over the medium-term, driven by a narrowing goods deficit and continued robust service surplus. Net FDI inflows are projected to decline gradually relative to GDP over the projection period, from elevated levels, but should continue to cover the current account deficit.

4. **The external debt path is sensitive to potential real exchange rate depreciation shocks.** As shown in the shock scenarios figure below, a 30 percent real depreciation of the dinar in 2023 would cause the external debt-to-GDP ratio to exceed 90 percent in 2024, before falling to 74 percent by 2028.

5. **Continued prudent fiscal policy and reforms of energy SOEs will help strengthen the external debt outlook.** The fiscal deficit has declined steadily since the COVID-19 crisis and is expected to fall to 1 percent of GDP over the medium term. In addition, financial risks from energy SOEs should decline as tariff rate increases and other SOE reforms are put in place. Furthermore, structural reforms to improve competitiveness and increase productivity and higher value-added investment would facilitate higher real growth and increase resilience against shocks.

Figure 1. External Debt Sustainability: Bound Tests 1/ 2/

(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2023.

Annex VII. Risk Assessment Matrix

Source of Risk[1]	Relative Likelihood	Time Horizon	Impact if Realized	Policy Response
		Global conjunctural risks		
Intensification of regional conflict(s) and regional geopolitical tensions.	**High** Escalation of Russia's war in Ukraine or other regional conflicts, further sanctions resulting from the war, along with a failure to make progress in resolving regional geopolitical issues, disrupt trade (e.g., energy, food, tourism, and/or critical supply chain components), remittances, refugee flows, FDI and financial flows, and payment systems.	Short to medium term	**High** Adverse spillovers and commodity price shocks would reduce trade, lower investor confidence and FDI, while giving rise to further inflationary pressures, and demands for fiscal support programs and a weaker fiscal position. Serbia's current preferential economic relations with the EU (Serbia is a candidate country) could be downgraded which would reduce trade, lower investor confidence and stall FDI. **Medium** Supply of contracted gas volumes to Serbia may be curtailed in transit.	• Further monetary tightening if there are stronger signs of second-round inflation effects. • Intensify efforts to secure alternative energy sources and allocate supplies in accordance with a national rationing plan. • Allow automatic stabilizers to operate. • Targeted support to vulnerable households.

[1]The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path. The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. The conjunctural shocks and scenario highlight risks that may materialize over a shorter horizon (between 12 to 18 months) given the current baseline. Structural risks are those that are likely to remain salient over a longer horizon.

Source of Risk	Relative Likelihood	Time Horizon	Impact if Realized	Policy Response
Abrupt global slowdown or recession.	**Medium** Global and idiosyncratic risk factors combine to cause a synchronized sharp growth downturn, with recessions in some countries, adverse spillovers through trade and financial channels, and markets fragmentation. • **U.S.:** (...) inflation remains elevated, prompting the Fed to keep rates higher for longer and resulting in dollar strengthening, (...) and "hard landing". **Medium** • **Europe:** Intensifying fallout from the war in Ukraine, worsening energy crisis and supply disruptions, and monetary tightening exacerbate economic downturns (...). **High** • **China:** (...) disrupt economic activity. **Medium** • **EMDEs:** A new bout of global financial tightening, possibly combined with volatile commodity prices, leads to spiking risk premia (...) and sudden stops**.** **Medium**	Short to medium term	**High** Sharp growth slowdown, and weaker fiscal and external position. Serbia may also face near-term challenges in accessing the Eurobond market, but with fairly closed capital markets and a high share of FDI, the scope for capital outflows from non-residents appears limited in the near term.	• Tightening in the event of aggregate supply shocks if there are signs of second-round inflation effects. • Allow automatic stabilizers to operate. • Targeted support to vulnerable households. • Purchase under the precautionary tranches of the SBA.
Commodity price volatility.	**Medium** A succession of supply disruptions (e.g., due to conflicts and export restrictions) and demand fluctuations (e.g., reflecting China reopening) causes recurrent commodity price volatility (...)	Short to medium term	**High** Cost push inflation resumes, leading to decline in real income. Sharp increases in energy prices could make some businesses unviable.	• Adjust energy tariffs further to help offset changes in costs. • Further monetary tightening if there are stronger signs of second-round inflation effects.

Source of Risk	Relative Likelihood	Time Horizon	Impact if Realized	Policy Response
			Inflation expectations could worsen and lead to a wage-price spiral. **Medium (positive)** Near-shoring to Serbia could intensify.	• Targeted support to vulnerable households. • Accelerate efforts to secure greater energy diversification.
Monetary policy miscalibration.	**Medium** Amid high economic uncertainty and volatility, major central banks slow monetary policy tightening or pivot to loosen monetary policy stance prematurely (…)	Short to medium term	**High** Global inflation stays higher for longer, increasing imported inflation in Serbia, worsening inflation expectations. Risk premia for Serbia could increase along with premia for other EMDEs. **Medium (positive)** Search for yield could incentivize investment in Serbia, but fairly closed financial markets may reduce the importance of this channel.	• Further monetary tightening if there are signs of stronger second-round inflation effects.
Systemic financial instability.	**Medium** Sharp swings in real interest rates, risk premia, and assets repricing amid economic slowdowns and policy shifts trigger insolvencies (…), markets dislocations and adverse cross-border spillovers.	Short to medium term	**Medium** Parent banks may become more risk averse in their Serbian operations.	• Further strengthen already robust and vigilant banking supervision. • Intensify surveillance of developments in home economies of parent banks.

Source of Risk	Relative Likelihood	Time Horizon	Impact if Realized	Policy Response
Global Structural Risks				
Deepening geo-economic fragmentation.	**High** Broader and deeper conflict(s) and weakened international cooperation lead to a more rapid reconfiguration of trade and FDI, supply disruptions, technological and payments systems fragmentation, rising input costs, financial instability, a fracturing of international monetary and financial systems, and lower potential growth.	Short to medium term	**High** Similar impact as described in conjunctural risks, but deeper and longer-lasting. **Medium (positive)** Serbia may benefit from near-shoring, and inward migration or relocation of businesses.	• Take measures to ensure a globally diversified economic structure for imports, exports and financing. • Enhance efforts to ensure a business-friendly environment while continuing to combat the grey economy.Prioritize reforms that support a reputation for evenhandedness in a market and rules-based economy.
Cyberthreats.	**Medium** Cyberattacks on critical domestic and/or international physical or digital infrastructure (including digital currency and crypto ecosystems) trigger financial and economic instability	Short to medium term	**Medium** While digitalization of the economy and government operations is progressing, it is not yet at the stage where the impact of cyberattacks would appear to have a generalized macro-critical impact.	• Further strengthen standards of IT security for government and public IT infrastructure, taking advantage of expertise in the local IT sector. • Develop and activate a cyberattack emergency response capacity.
Extreme climate events.	**Medium** Extreme climate events cause more severe than expected damage to infrastructure (…) and loss of human lives and livelihoods, amplifying supply chain disruptions and inflationary pressures, causing water and food shortages, and reducing growth.		**Medium** Serbia is exposed to some climate risks including droughts, landslides, waterlogging and earthquakes.	• Strengthen disaster preparedness, including contingency reserves in the budget. • Build further capacity for fiscal risk management, and link the insights into government planning and budgeting.

Source of Risk	Relative Likelihood	Time Horizon	Impact if Realized	Policy Response
Domestic Risks				
Domestic policy errors or loss of fiscal discipline.	**Low** Structural reform delays or looser fiscal policies.	Short to medium term	**High** Loss of fiscal discipline would undermine market confidence. Structural reform delays would undercut growth prospects.	• Take corrective measures to restore fiscal discipline and adhere to new fiscal rule. • Re-focus on a prioritized set of structural reforms with well-defined action plans with front-loading of corrective actions.
Energy sector reform delays.	**Medium** Delays in energy sector reforms. Electricity production remains unreliable, and coal and electricity imports remain elevated.	Short to medium term	**High** Financial viability of the energy companies is not restored, and fiscal costs and risks persist. Energy security and environmental sustainability remain at risk over the medium term	• Take corrective actions. • Further adjust energy tariffs to restore full cost recovery. • Further strengthen management of key energy SOEs. • Reach consensus on an energy sector strategy with well-defined roles for the government, SOEs and private sector, and implement it.

Annex VIII. Illustrative Adverse Scenario

1. This illustrative adverse scenario represents an intensification and extension of the ongoing shocks arising from the war in Ukraine and high global uncertainty. —Similar to the adverse scenario at the time of SBA approval, it involves another bout of high energy prices that remain elevated for longer, and even lower growth in advanced economy trading partners. In addition, it includes higher financing needs for the government and energy companies. While the magnitude of shocks is similar to the adverse scenario at the time of SBA approval, the baseline has improved noticeably since then, inter alia due to lower oil, natural gas and electricity prices.

2. This shock is set against Serbia's solid record on strong macroeconomic policies. Given high uncertainty on the duration and intensity of the external shocks faced by Serbia, this illustrative adverse scenario aims to balance the impact of additional adverse developments with Serbia's proven track record of solid macroeconomic policies and meaningful adjustment under IMF programs. It assumes that Serbia will fully draw the approved SBA resources, while continuing to implement policies to contain external and fiscal financing needs, including by increasing domestic energy prices to ensure cost recovery over the medium-term. The adverse scenario can be assessed against developments in 2020–22, while it is important to note that this reference period already includes two severe global shock years (2020—with the outbreak of the Covid-19 pandemic, and 2022—with the start of the war in Ukraine). Moreover, the recent sharp increase in global inflation and trade prices distorts nominal (including euro-based) historical comparisons.

Table 1. Serbia: Assumptions Underlying the Illustrative Adverse Scenario

	2020-22	2022	2023			2024			2025		
	Average Baseline	Estimate	Baseline	Adverse	Adverse over baseline	Baseline	Adverse	Adverse over baseline	Baseline	Adverse	Adverse over baseline
Oil price 1/											
APSP price (USD/bbl)	69.1	96.4	73.1	87.8	20.0 %	68.9	79.2	15.0 %	67.0	72.3	8.0 %
Growth rate (percent, yoy)	24.3	39.2	-24.1	-8.9		-5.8	-9.7		-2.8	-8.7	
Trading partner developments											
AE trading partners real GDP (growth rate, percent) 1/	1.0	3.3	0.6	-0.2	-0.8 ppt	1.4	0.4	-1.0 ppt	2.0	1.5	-0.5 ppt
Serbia growth differential (ppt)	1.9	-1.1	1.4	1.2	-0.2 ppt	1.6	1.1	-0.5 ppt	2.5	1.0	-1.5 ppt
Advanced economy inflation (growth rate, percent)	3.7	7.3	4.7	5.7	1.0 ppt	2.6	3.1	0.5 ppt	2.1	2.6	0.5 ppt
Serbia developments											
Real GDP (growth rate, percent)	3.0	2.3	2.0	1.0	-1.0 ppt	3.0	1.5	-1.5 ppt	4.5	2.5	-2.0 ppt
CPI inflation (growth rate, percent)	5.9	12.0	12.4	15.4	3.0 ppt	5.3	6.8	1.5 ppt	3.5	4.0	0.5 ppt
Current account balance (Euro bn)	-2.8	-4.1	-3.3	-4.8	-48.0 %	-3.5	-5.4	-55.4 %	-3.7	-4.9	-31.4 %
Current account balance (percent of GDP)	-5.1	-6.9	-4.7	-7.2	-2.4 ppt	-4.6	-7.5	-2.9 ppt	-4.5	-6.4	-1.8 ppt
Trade balance, goods (Euro bn)	-6.8	-9.4	-8.2	-9.4	-14.2 %	-8.1	-9.3	-15.2 %	-8.0	-8.8	-10.7 %
Exports, goods (Euro bn)	21.3	26.9	29.6	29.6	0.2 %	32.7	32.4	-1.0 %	36.0	35.3	-2.0 %
Exports, goods, real (growth rate, percent)	5.4	4.2	6.8	6.0	-0.8 ppt	6.9	5.1	-1.8 ppt	7.1	5.8	-1.3 ppt
Imports, goods (Euro bn)	28.1	36.3	37.8	39.0	3.2 %	40.8	41.7	2.2 %	43.9	44.1	0.3 %
Imports, goods, real (growth rate, percent)	6.6	5.5	4.1	4.1	0.0 ppt	4.6	4.6	0.0 ppt	5.3	4.4	-0.9 ppt
Current transfers private, incl. remittances (Euro bn)	4.2	5.4	5.6	5.5	-3.1 %	5.7	5.3	-7.2 %	5.7	5.5	-3.8 %
FDI (net) (Euro bn)	3.6	4.3	4.2	3.9	-7.2 %	4.2	3.6	-14.1 %	4.4	4.3	-2.2 %
Fiscal balance (RSD bn)	-306	-216	-228	-267		-176	-254		-145	-192	
Fiscal balance (percent of GDP)	-4.9	-3.0	-2.8	-3.3	-0.5 ppt	-2.0	-2.9	-0.9 ppt	-1.5	-2.0	-0.5 ppt
Structural primary fiscal balance (percent of GDP) 2/	-2.3	0.1	-0.1	-0.2	-0.1 ppt	0.2	-0.4	-0.6 ppt	0.4	0.1	-0.3 ppt
GDP (Euro bn)	53.5	60.3	68.9	67.3	-2.3 %	74.8	71.4	-4.6 %	81.5	76.5	-6.2 %

Sources: SORS, Ministry of Finance, NBS, and IMF staff estimates.

1/ IMF WEO, WEO GEE and IMF staff esitmates and assumptions.

2/ Excludes one-offs, notably Covid-related programs, and net lending to Srbijagas and EPS during the present energy crisis.

3. Oil Prices and Energy Supply. Compared to the baseline, oil prices would be higher by 20, 15, and 8 percent, respectively, in 2023, 2024 and 2025. Price spikes in the natural gas and electricity spot markets are a key risk for energy import costs. The recent expansion of gas storage capacity and forward contracting of energy imports have increased the authorities' ability to smooth these risks, and additional buffer capacities are expected to be put in place over the course of 2023. Currently, the risk of severe gas supply disruptions seems to have abated, and no such disruptions are assumed.

4. Export Growth. Real GDP in Serbia's advanced economy trading partners (mostly EU countries, which account for about 60 percent of trade and FDI) is assumed, under the illustrative adverse scenario, to be lower by 1.8 percentage points in 2023–24, and to remain lower through 2025. This contributes to lower real export growth by 2½ percentage points in 2023–24, which nevertheless remains robust, reflecting Serbia's continuing integration into global supply chains and strong FDI inflows.

5. Remittances. While remittances (and other current private transfers) have been resilient in the past, they are assumed to grow more slowly because of weaker growth in the source economies. The assumed total loss is €½ bn or about 0.3 ppt of GDP in 2023–24, a drop by about 5 percent relative to the baseline.

6. Foreign Direct Investment. While FDI (net) has been approximately 6–8 percent of GDP every year since 2017 and remained resilient in 2022, the baseline assumes a stabilization in nominal terms, implying a declining path relative to GDP: 6.1 percent of GDP in 2023 and 5.7 percent of GDP in 2024. The adverse scenario assumes further weakening (10½ percent decline during 2023–24 relative to the baseline). FDI in 2023–25 would be more than 1 percentage point of GDP lower each year than in 2020–22. These assumptions are conservative as the ongoing near-shoring and Serbia's open access to EU markets should support continued robust FDI inflows.

7. External Market Financing. During 2020–22 Serbia placed, on average, Eurobonds of around €1.9 billion per year, while for 2022 no Eurobond issuance was planned. In January 2023, Serbia placed Eurobonds worth about € 1.6 bn in two heavily oversubscribed issuances. Nevertheless, in the adverse scenario it is assumed that no additional Eurobond issuances are made through 2024.

8. Fiscal Deficit. The adverse scenario assumes that higher energy-related costs for imports, maintaining electricity generation or securing energy supplies will require additional liquidity support for the energy SOEs in 2024 and 2025 of 0.3 and 0.2 percent of GDP, respectively. The fiscal impact would be contained, inter alia through larger tariff increases. Moreover, additional expenditure of around 0.5 percent of GDP per year are assumed that could be allocated for support to vulnerable households or efficiency-improving energy infrastructure investments. For 2023 it is assumed that the deficit would stay below the quantitative performance criterion (QPC) on the overall fiscal balance agreed at SBA approval (equivalent to 3.3 percent of GDP, and 0.3 percent of GDP higher than the revised QPC). After 2023 there is a modest increase in the deficit through 2025, while the overall deficit is kept on a downward path. Adherence to the deficit ceiling under the new fiscal rule (1.5 percent of GDP when general government debt and guaranteed debt is between 55–45 percent of GDP) would be delayed by one year to 2026.

9. Outlook. For Serbia, as a result of these additional shocks compared with the baseline, the economic outlook would be weakened, and external financing needs increased.

10. Growth. Real GDP would be lower by 2½ percentage points by 2024, reflecting weaker consumption due to higher inflation eroding real incomes, weaker investment due to lower FDI, and lower export growth due to weaker external demand. As the shocks to the global economy dissipate, Serbia is expected to return to stronger growth while some scarring is assumed. Potential growth would be lower, and the growth differential to trading partners could narrow from 2 percentage points in the reference period to around 1 percentage point through 2025.

11. Current Account. The current account is affected by several opposing forces. Real export growth in 2023–25 is assumed to decline relative to the baseline (-4 percentage points, cumulatively). Higher energy prices raise imports in nominal terms. While these effects would be partly offset by lower demand for imports, the current account deficit would widen to 7.2 percent of GDP (4.7 percent of GDP in the baseline) in 2023 and 7.5 percent of GDP (4.6 percent of GDP in the baseline) in 2024, before declining to 6.4 percent of GDP (4.5 percent of GDP in the baseline) in 2025.

12. Policy Response. Despite the adverse shock to growth, the scenario assumes a moderately contractionary policy response overall. While the fiscal deficit increases, as the IMF arrangement and other credible financing options from development partners provide external and fiscal financing space, the fiscal impulse remains moderately negative. Monetary policy is assumed to tighten, with the policy rate increasing in line with higher inflation. This policy response would help to dampen the adverse impact on the balance of payments and forestall capital outflows. Given that the shocks included in the adverse scenario are mostly Europe-wide, the euro-exchange rate, against which the dinar is assumed to remain de facto stabilized, would be expected to depreciate in real terms. This would moderate the impact of the real appreciation of the dinar vis-à-vis the euro.

Table 2. Serbia: External Financing Requirements

(Billions of euros, unless otherwise indicated)

	2021	2022	2023		2024		2025		2026		2027	2028
	Actual	Estimate	Baseline	Adverse	Baseline	Adverse	Baseline	Adverse	Baseline	Adverse	Baseline	Baseline
Gross financing needs	7.5	8.6	7.9	9.4	9.0	11.4	7.7	8.8	8.8	9.2	11.0	8.1
Current account deficit	2.3	4.1	3.3	4.8	3.5	5.4	3.7	4.9	3.8	4.3	4.0	4.2
(As a percent of GDP)	*4.3*	*6.9*	*4.7*	*7.2*	*4.6*	*7.5*	*4.5*	*6.4*	*4.4*	*5.3*	*4.3*	*4.2*
Debt amortization (excl. FDI)	5.2	4.5	4.6	4.6	5.5	6.1	4.0	3.9	5.0	4.9	7.0	3.9
Public	2.5	2.1	1.8	1.7	2.8	3.3	1.5	1.4	2.4	2.3	4.6	1.9
Private	2.7	2.4	2.9	2.9	2.8	2.8	2.5	2.5	2.5	2.5	2.3	2.0
Financing sources	10.2	10.6	9.3	9.0	10.8	8.0	9.3	9.1	11.0	10.8	12.8	10.5
FDI (net)	3.7	4.3	4.2	3.9	4.2	3.6	4.4	4.3	4.8	4.7	5.1	5.4
Debt disbursements (excl. FDI)	7.7	5.9	6.0	6.0	7.0	4.9	5.4	5.3	6.1	6.0	7.4	4.5
Eurobond	2.7	0.0	1.6	1.6	2.1	0.0	0.5	0.5	1.0	1.0	2.2	1.0
Public MLT	1.8	3.2	1.8	1.8	1.9	1.8	2.2	2.1	2.3	2.2	2.5	1.2
Private	3.1	2.7	2.6	2.6	3.1	3.1	2.7	2.7	2.8	2.8	2.7	2.3
Other 1/	-1.2	0.4	-0.9	-0.9	-0.5	-0.5	-0.5	-0.5	0.1	0.1	0.3	0.6
Net change in reserves (+: increase)	2.6	2.9	2.6	0.7	2.0	-2.0	1.7	0.3	1.7	1.0	1.0	2.1
Remaining financing need	0.0	1.0	1.2	1.2	0.2	1.4	0.0	0.0	-0.6	-0.6	-0.8	-0.3
SBA	0.0	1.0	0.6	0.6	0.0	0.8	0.0	0.0	-0.6	-0.6	-0.8	-0.3
Other	0.0	0.0	0.5	0.5	0.2	0.5	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items												
Gross international reserves (GIR)	16.5	19.4	22.0	20.2	24.0	18.1	25.7	18.4	27.3	19.4	28.3	30.4
GIR as percent of ARA metric	131.5	134.0	143.1	131.7	145.3	114.3	138.9	104.8	138.6	103.9	135.0	139.6

Sources: NBS, and IMF staff estimates.

1/ Including the capital account balance, trade credits and advances, currency and deposits, other portfolio investments, and net errors and omissions.

13. Financing sources. With all these shocks combined, reserves would be expected to decline in nominal terms in 2023–24 from the current historically high level while the authorities would make all purchases under the SBA (SDR 1,898.92 bn, about €2.4 bn). Reserves are expected to bottom out at about €18 billion in 2024, before increasing gradually over the projection horizon. Reserves fall to 104 percent of the ARA metric in 2026, before building up to 113 percent of the ARA metric in 2028. If the authorities were not to make the two precautionary purchases under the SBA (96.66 percent of quota, about €0.8 bn) in 2024, reserves would fall below 100 percent of the ARA metric in 2025-26. As the energy sector continues to contribute to the balance of payments challenges, additional access to loans from other official creditors including the World Bank and the EBRD for liquidity support and/ or more rapid transformation would be expected, also given that such contingent augmentations are already under discussion. Nonetheless, out of caution, only modest additional financing from other official creditors is assumed under the adverse scenario in 2024 (€0.3 bn).

Table 3. Serbia: Indicators of Capacity to Repay the Fund (Adverse Scenario), 2021–28[1]

(In billions of euros, unless otherwise indicated)

	2021	2022 Est.	2023 Proj.	2024 Proj.	2025 Proj.	2026 Proj.	2027 Proj.	2028 Proj.
Fund repurchases and charges 2/								
In millions of SDRs	-	4	36	71	102	530	777	545
In millions of euro	-	5	46	90	130	681	1,007	716
In percent of exports of goods and NFS	-	0.0	0.1	0.2	0.3	1.3	1.8	1.2
In percent of GDP	-	0.0	0.1	0.1	0.2	0.8	1.1	0.8
In percent of quota	-	0.6	5.6	10.9	15.6	81.0	118.7	83.2
In percent of total external debt service	-	0.1	0.8	1.3	2.8	12.3	13.2	14.5
In percent of gross international reserves	-	0.0	0.2	0.5	0.7	3.5	4.8	3.0
Fund credit outstanding (end-period)								
In millions of SDRs	-	786	1,266	1,899	1,899	1,465	753	237
In millions of euro	-	987	1,595	2,407	2,428	1,887	982	314
In percent of exports of goods and NFS	-	2.6	3.9	5.4	5.1	3.7	1.8	0.5
In percent of GDP	-	1.6	2.4	3.4	3.2	2.3	1.1	0.3
In percent of quota	-	120.0	193.3	290.0	290.0	223.8	115.0	36.2
In percent of total external debt	-	2.3	3.5	5.2	5.1	3.9	2.0	0.6
In percent of gross international reserves	-	5.1	7.9	13.3	13.2	9.7	4.7	1.3
Memorandum items:								
Exports of goods and NFS	28,583	38,000	41,320	44,538	48,052	51,309	54,654	58,183
Quota (in millions of SDRs)	654.8	654.8	654.8	654.8	654.8	654.8	654.8	654.8
GDP	53,329	60,309	67,323	71,388	76,460	81,992	88,505	94,445
Total external debt service	5,978	5,306	5,425	6,783	4,701	5,532	7,627	4,950
Public sector external debt	22,293	23,724	26,183	25,771	26,916	27,778	27,843	27,747
Total external debt	39,687	43,489	46,074	46,231	47,615	48,736	49,129	49,310
Total external debt stock excluding IMF	39,687	42,475	44,442	43,783	45,167	46,847	48,158	49,004
Gross international reserves	16,455	19,416	20,151	18,102	18,430	19,449	20,934	23,505

Source: IMF staff estimates.

1/ Assumes purchase of the full authorized access under the SBA arrangement including precautionary tranches.
2/ Includes GRA basic rate of charge, surcharges, service fees, and SDR charges.

Appendix I. Letter of Intent

Ms. Kristalina Georgieva
Managing Director
International Monetary Fund
Washington, D.C., 20431
U.S.A.

Belgrade, June 15, 2023

Dear Ms. Georgieva:

The Serbian economy has proven itself to be resilient in the face of large adverse external shocks in recent years and strong headwinds from the adverse global and regional environment. While economic activity has softened, the labor market remains strong. Sharp declines in regional energy prices have supported better-than-expected external and fiscal outcomes. Gross international reserves have continued to increase, exceeding by end-May 2023 €22 billion, their highest end-of-month level on record. While headline inflation stood at around 16 percent in 1Q 2023 due to the pass-through of high-cost push pressures from the prior period, it started declining in April-May on the back of our appropriate macroeconomic policy response and base effects. Financial stability has been maintained and close monitoring of the financial sector continues.

Our economic program, supported by the Stand-By Arrangement (SBA) that was approved by the IMF Executive Board on December 19, 2022, aims at preserving macroeconomic and financial stability, boosting the economy's resilience to energy shocks, and fostering higher, greener, and inclusive sustainable growth over the medium term. The program is off to a good start. All end-December 2022 quantitative performance criteria (QPCs) were met. The standard continuous performance criteria and other March 2023 indicative targets were also met. The structural reform agenda has been progressing well, albeit there were minor delays in implementing the end-December 2022 SB for approving a new SOE governance law and the end-February 2023 SB on the conversion of the EPS to a joint stock company that allowed time for more consultation and for stronger reforms.

In the attached update to the Memorandum of Economic and Financial Policies (MEFP) from December 1, 2022, we reiterate our commitment to the policies and objectives of the SBA-supported economic program and update the reform agenda that we intend to implement in 2023-24.

Considering our strong performance and commitments made under the program, we request completion of the First Review under the SBA, which would allow us to purchase the equivalent of SDR 163.7 million (25 percent of quota). As with the initial purchase under the program, we plan to use the purchase for budget financing. Going forward, if the external environment continues to be supportive, we may consider treating the SBA as precautionary at the time of the Second Review, earlier than expected at the SBA approval. To this end, we request modification of the (i) end-June 2023 and end-December 2023 performance criteria on the floor on net international reserves (NIR) and (ii) the end-

December 2023 QPC on the fiscal deficit. In addition, should reserves remain strong, we will consider requesting raising the NIR floor at the next review.

Our program will continue to be monitored through quantitative performance criteria, standard continuous conditionality, structural benchmarks, and an inflation consultation clause, as described in the MEFP and the Technical Memorandum of Understanding (TMU). Reviews by the IMF will continue to be conducted on a semi-annual basis to assess program implementation and reach understandings on any further program reforms needed. While we believe that the policies set forth in the MEFP are adequate to achieve the economic objectives under the program, we will promptly take any additional measures that may become necessary for this purpose. We will also consult with the IMF in advance of any revisions to the policies contained in our MEFP or any new policies that may affect program objectives, in accordance with the IMF's policies on such consultations; and we will provide IMF staff with all the data and information necessary for the purpose of monitoring the program.

In line with our commitment to transparency, we intend to make this letter available to the public, along with the MEFP, TMU, and the IMF staff report for the First Review Under the SBA and the 2023 Article IV Consultation. 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
Deputy Prime Minister
Minister of Finance

Attachments: Memorandum on Economic and Financial Policies
Technical Memorandum of Understanding

Attachment I. Memorandum of Economic and Financial Policies

1. This memorandum supplements our memorandum of December 1, 2022, provides information on recent developments, and presents our economic program for the remainder of 2023 and 2024. The program aims to (i) preserve macroeconomic and financial stability by tailoring our policy response to ongoing economic shocks; (ii) boost the economy's resilience to energy shocks by pursuing approriate energy policies and reforms to tackle domestic energy sector challenges, while protecting the most vulnerable; and (iii) foster higher, greener, and inclusive sustainable growth over the medium term by implementing comprehensive structural reforms. The goals of the program are compatible with our aspirations to join the EU.

Recent Economic Developments and Outlook

2. Serbia's economic activity has softened, but sharp declines in regional energy prices have supported better-than-expected external and fiscal outcomes.

- **Growth.** Serbia's real GDP growth was 2.3 percent in 2022. While real GDP growth was strong in the first half of 2022, at 4.0 percent year to year, it slowed to 0.7 percent in the second half because of subdued external demand, global cost push pressures, and a domestic drought that led to lower crop yields. For 2023, we project real GDP growth to range between 2 and 3 percent because of the adverse international environment, while beyond 2023 we expect growth to return to precrisis levels, as the effects of the Ukraine conflict on external demand fade and as planned investment infrastructure projects are implemented.

- **Inflation.** Headline inflation stood at around 16 percent in 1Q 2023, due to the pass-through of high-cost push pressures from the prior period. Such inflation movements were dictated by the increased contribution of food prices and the expected adjustment of administered prices, while a lower contribution of petroleum products worked in the opposite direction. Core inflation stayed considerably lower, at about 11 percent on average, in 1Q 2023. The National Bank of Serbia (NBS) continued to tighten monetary conditions through June 2023 to respond to ongoing inflationary pressures, while the relative stability of the dinar exchange rate against the euro, supported by active NBS policy, has limited the spillover of rising import prices onto domestic prices. Headline inflation declined to 15.1 percent in April and further to 14.8 percent in May. We expect that inflationary pressures would continue subsiding in the coming months, more substantially so as of the middle of this year. We expect inflation to end the year at half the March level. By mid-2024, inflation is projected to fall within the bounds of the NBS's target tolerance band. Inflationary pressures are expected to ease on the back of past monetary tightening, the waning effects of global factors that drove the energy and food price growth in the prior period, and by lower external demand amid an anticipated slackening of global economic growth. But the inflation outlook remains highly uncertain, and we will continue to monitor developments closely, adjusting policy as needed.

- **Balance of Payments.** The current account deficit was below 7 percent of GDP in 2022. This better-than-anticipated outturn primarily reflected lower-than-expected energy prices, lower energy imports because of a relatively mild winter, strong FDI-related exports, and somewhat stronger demand from our main trading partners in Europe through the end of 2022. In addition, remittance inflows continued to be buoyant. The current account deficit was fully covered by net FDI inflows for the eighth year in a row, supporting the sustainability of Serbia's external position. Despite heightened global uncertainty, in 2022 FDI inflows reached a new record high of €4.4 billion. In 2023, the current account deficit is projected to continue improving to under 5 percent of GDP based on continued strong exports of goods and services (much of which is FDI-related), and to gradually decline further over the medium term, reflecting ongoing strong export performance based on strong investment and the recovery of external demand.

- **Fiscal Outcome.** The fiscal deficit ended at 3.2 percent of GDP in 2022, despite the need to accommodate budget spending on the energy companies of about 2½ percent of GDP. This strong outcome reflected mainly tight administrative controls on all areas of spending in the Republican budget. The 2023 budget was approved in December 2022 in line with the SBA targets.

3. Although outturns have been strong, the outlook is subject to much uncertainty. Yet, in our view, the risks to the projections seem to have moderated compared to the time of program approval as international energy prices have declined sharply, uncertainty over the supply of gas to Europe has diminished, and economic activity indicators in the euro area for Q4 2022 and early 2023 are better than expected. Key risks from the international environment continue to include the global growth outlook, international energy and primary commodity prices, and the degree of monetary policy tightening by leading central banks. To this has been added financial distress in advanced markets, although Serbia appears to be well insulated from these developments. At home, the risks to the projections are associated primarily with the energy sector, the outcome of this year's agricultural season, FDI inflows, and recovery of the energy and construction sectors.

4. Yet, the Serbian economy has considerable buffers against these uncertainties. The buffers include strong foreign exchange reserves, relatively low public debt, sustainable external debt dynamics, and a well-capitalized and liquid banking system. Another important anchor is Serbia's attractiveness as a destination for increasingly diversified FDI, reflecting its strong track record of agile policy responses to various shocks. The Stand-By Arrangement provides an additional buffer, while we adjust policies and implement reforms to tackle the crisis and strengthen the economy's performance and resilience. In this regard, Serbia's medium-term outlook remains favorable, supported by our commitment to continued responsible macroeconomic policies and to an ambitious structural reform agenda.

Economic Policies

5. We continue monitoring domestic and external developments closely and stand ready to tailor our policy responses as needed. In the context of earlier sharp increases in food and global energy prices, we introduced a set of administrative measures to cushion the impact of price shocks on Serbia's households and firms. We introduced export restrictions on some basic food items, that were later phased out. In February 2023, we introduced import duties on milk and cheese to protect local farmers. We have also implemented price regulations on gasoline and diesel, which we are committed to reverse once the global energy situation stabilizes, and in any event no later than end-March 2024. These administrative measures are strictly temporary with the goal of moderating the social and economic strains while we develop a comprehensive set of policy measures and reforms to further reduce Serbia's vulnerability to external shocks.

A. Energy Sector Policies

6. We are committed to addressing the deep-rooted weaknesses in Serbia's energy sector by continuing to implement a comprehensive set of much-needed reforms. Our policy decisions in the following areas are critical both for ensuring energy security and maintaining fiscal and external sustainability:

Tariff Adjustments

7. Higher gas and electricity tariffs are needed to achieve medium-term cost recovery of the energy companies and to promote energy conservation. We consider that a continued gradual increase in energy tariffs will facilitate the adjustment to higher costs while keeping Serbia's international attractiveness as an investment destination intact. In calibrating further tariff adjustments, we will continue accounting for ongoing expenses and higher investments needs for maintaining reliable electricity generation, bolstering energy security, and greening the energy supply.

8. We are committed to deliver the necessary gas tariff adjustments during the program period to ensure full cost recovery for Srbijagas over the medium term.

- We raised the average gas tariff by 11 percent effective from January 1, 2023, and by a further 10 percent effective from May 1, 2023 (the latter an **end-April 2023 SB**). We will implement additional increases in the average gas tariff by 10 percent effective from November 1, 2023 (a new **end-October 2023 SB**), and May 1, 2024. In the context of the Second Review under the SBA, the adequacy of the May 2024 programmed tariff increase will be re-assessed.

- The SBA includes a consultation clause in case market prices for gas exceed €250/MWh, on average, during a two-week period, to initiate a discussion on an appropriate policy response, if relevant, and help contain risks to the budget. Current prices fall well short of this market price.

9. We are committed to deliver the necessary electricity tariff adjustments during the program period to ensure full cost recovery for EPS.

- We raised electricity tariffs for households by 8 percent and the cap for electricity prices for the corporate sector by 8 percent effective from January 1, 2023, and further by 8 percent from May 1, 2023 (the latter an **end-April 2023 SB**). We will implement additional increases by 8 percent effective from November 1, 2023 (a new **end-October 2023 SB**), and May 1, 2024. In the context of the Second Review under the SBA, the adequacy of the May 2024 tariff increase will be re-assessed.

Social Protection

10. We will strive to soften the impact of tariffs adjustments on the most vulnerable. We will maintain the existing system of block tariffs, with a lower electricity price for households up to a certain electricity consumption threshold. We also expanded the energy-vulnerable consumer protection program by increasing eligibility criteria while targeting the poor and energy-vulnerable households. In our effort to raise the share of households benefitting from the reduced energy bill to about 10 percent in 2023, we have launched an information campaign to actively inform citizens about the eligibility criteria for the program and coordinate closely with local municipalities in doing so.

Structural Reforms

11. We are committed to implementing urgent reforms to resolve the deep-rooted structural weaknesses in the energy sector. We have involved the Norwegian company Rystad Energy to help with our reforms. We will also benefit from access to loans from official creditors including the EBRD and the KfW for liquidity support to the energy companies as we transform the energy sector.

- We have prioritized restructuring of the large state-owned energy companies to enhance efficiency and contain fiscal costs and risks. In April 2023, we changed the legal status of the EPS to a joint stock company aiming to professionalize its management and strengthen the company in the long term (end-February 2023 SB). The implementation of this structural benchmark was delayed in consultation with the IMF staff to allow time to align the new EPS statutes with the new draft Law on ownership management for SOEs (¶43). We are proceeding with setting up a revised two-tier governance structure in line with the new EPS statutes and are further professionalizing EPS management. In early June, we replaced the previous Supervisory Board of the EPS with new Board members. These new members have strong professional credentials, and three of the seven new members are foreign experts. The next step is to choose the executive directors and a permanent new general director of EPS following an open and transparent procedure. For Srbijagas, we will ensure completion of its unbundling by end-2024.

- We are working on a well-specified strategic restructuring plan for the EPS **(end-December 2023 SB)**. The plan, which is needed to address EPS's many problems, will outline the companies' stabilization and transformation steps, and will specify the reform priorities in the EPS governance and organizational structure, including managerial and sectorial layout, audit processes, internal controls, and compliance procedures.

- In line with our commitment to transparency, we will publish all strategic and financial plans for EPS and Srbijagas. We will also continue with the publication of monthly reporting of overdue receivables to Srbijagas and EPS from their top-20 debtors including changes in overdue receivables since January 2022.

- Another priority is the adoption of the National Energy and Climate Plan (NECP). The Plan will define the goals and strategies of the Republic of Serbia for reducing greenhouse gas emissions, increasing the share of renewable energy sources in gross final energy consumption, and setting goals for greater energy efficiency. The first draft of the NECP will be prepared by mid-2023 with a goal of having it adopted by government by end-2023.

- We have developed a prioritized investment plan for the energy sector with projects that will be implemented over the next 2–5 years and that will enhance energy security, stabilize electricity generation, and conserve energy **(end-May 2023 SB)**. The plan was adopted by the government in mid-June. For the first two years, the plan identifies those entities that will bear the costs of these investments and how exactly they are to be financed. For the outer years, the plan lays out options for financing of the priority projects.

- We will also adopt by government a new Energy Development Strategy of the Republic of Serbia by end-2023, which will be aligned with this investment plan. The strategy will include projections through 2050 that will be harmonized with the NECP and with the strategic development and business plans for the energy SOEs. Investment expenditure allocated to the Republican budget will be included in the capital budget.

- We are setting up a framework to ramp up private investment in renewables through auctions and other measures, working closely with international development partners. Currently, we are preparing a three-year auction plan for wind and solar projects. We aim to launch the first renewables auction already in 2Q2023 and are currently revising the relevant legislation to create the regulatory conditions for these auctions.

B. Fiscal Policies

12. We commit to delivering the 2023 fiscal deficit in line with the approved budget. According to our updated projections, the approved budget is consistent with a deficit of 3 percent of GDP. The expected stronger performance is also reflected in our revised and more ambitious quantitative performance criteria on the fiscal deficit (see below). During the first five months of 2023, however, revenue collection was higher than expected. In addition, a better-than-expected financial situation in the domestic energy SOEs resulting from higher energy tariffs, favorable hydroelectric generation, and lower energy imports have reduced budget subsidies to the EPS and Srbijagas. Thus, we have decided to use this additional fiscal space to finance several priority areas without jeopardizing the agreed deficit and expenditure limits for 2023. The new fiscal package includes a) increasing wages for teachers and nurses by 5.5 percent starting from September 2023 to address structural imbalances in public wages, b) enhancing Serbia's resilience to food shocks by increased agriculture subsidies, c) raising pensions by 5.5 percent starting from October 2023, beyond the existing pension indexation formula, as the already-low real pension income has been further eroded by high inflation, and d) providing support to families with children ahead of the new school year, as well as a few other measures. For 2023, the fiscal cost of this new fiscal package is estimated at about 0.9 percent of 2023 GDP. Going forward, we will refrain from any additional untargeted transfers to the population even if room arises from stronger revenue performance. Instead, such room will either be saved or used for investment purposes. Should new economic disruptions arise that warrant support to affected groups or activities, the additional expenditures will be accommodated by reprioritizing the budgeted current and capital spending. Reflecting ongoing strong fiscal performance, public debt is expected at about 55 percent of GDP by end-2023.

13. We are cognizant that some of the new fiscal measures will have a permanent impact on expenditure and we are committed to design and implement offsetting measures. For 2024, the fiscal cost of the new measures is estimated at about 1 percent of GDP. Specifically, we will redesign our excise policy to deliver additional 0.4 percent of GDP in revenue in 2024 and cut non-priority current and capital expenditure.

14. We are successfully implementing our fiscal financing strategy for 2023. We received a bilateral loan from the UAE of USD 1 billion in late 2022, which boosted the Ministry of Finance cash holdings, which is important in these uncertain times. In January 2023, we tapped international capital markets placing USD 1.75 billion of Eurobonds in two heavily oversubscribed issuances. After hedging into euro, the final interest rates were 6M EURIBOR plus about 3 ppts, on par with, or better than, neighboring peers. We finalized discussions with the World Bank, KfW and ADF for a budget-support loan of about €430 million. In addition, we have signed an agreement with the EBRD on €300 million liquidity support loan to EPS for 2023. We are continuing discussions on additional loans with development partners. We will continue relying on budget financing under the SBA, although, if the external environment is supportive, we may consider treating the SBA as precautionary at the time of the 2nd review, one review earlier than originally planned. Our financing strategy also envisages borrowing domestically and drawing as appropriate on the government's substantial cash deposits.

15. We will continue to contain fiscal risks and prepare contingency measures as needed. We will continue to closely monitor revenue and expenditure risks related to ongoing external and domestic challenges and their economic impact. We will maintain adequate liquidity buffers and will not accumulate public sector external debt payment arrears (continuous target). We will also refrain from accumulating domestic payment arrears (indicative target). Our efforts to contain public spending will continue to be monitored through a program ceiling on current primary spending of the Republican budget, excluding capital spending and interest payments (quantitative performance target). Any financial support to public enterprises will be delivered in a transparent and timely manner and channeled through the government budget. In the meantime, any additional expenditure on state-owned enterprises (SOEs) in the energy sector beyond that currently budgeted for 2023 (now considered unlikely) would be accommodated by reprioritizing the budgeted current and capital spending.

16. We are committed to strictly limiting the issuance of state guarantees. In 2023, we issued new state guarantees for Srbijagas' commercial loans (of €105 million, €225 million, and RSD 2.3 billion) to provide liquidity support and refinance previous commercial borrowing. We have also issued new state guarantee (€300 million) for the EPS loans from the EBRD and additionally up to €300 million from the KFW. We will not issue any new state guarantees for liquidity support to the

SOEs other than IFI of official bilateral loans to Srbijagas and EPS, or state guarantees for any company in the portfolio of the former Privatization Agency. The Government will also refrain from issuing any implicit state guarantees. We will continue to issue guarantees for project loans provided by multilateral financial organizations in support of our investment and reform agenda.

17. We are committed to maintaining fiscal discipline over the medium term. Supported by the new fiscal rule (see below), we plan to narrow the fiscal deficit further in coming years and to reduce public debt to below 50 percent of GDP over the medium term, further building up fiscal buffers. For 2024, we will target a further reduction in the fiscal deficit to 2.2 percent of GDP. We expect that the combination of tariff increases (¶8 and 9) and lower gas import prices will significantly reduce the need for fiscal support for the energy sector over the medium term. To help support growth, we will maintain high levels of capital spending, while containing current spending.

C. Structural Fiscal Policies

18. A new set of fiscal rules, incorporated into the budget system law in late-2022, will help anchor fiscal discipline over the medium term. Upcoming upgrades to fiscal data and government finance statistics (GFS) will require a review of the numerical fiscal parameters in 2024–25. With Fund technical assistance (TA) support, we are working on automating the preparation of monthly GFSM 2014-compliant fiscal data, expanding the coverage of indirect budget users and extrabudgetary units, and developing data for the compilation of financial accounts. We have formed coordination committees between SORS, the MoF and the NBS to ensure the necessary coordination between all participating government bodies. Moreover, comprehensive improvements to the GFS are expected with the next 5-yearly revision of national account statistics in 2024. We will update fiscal rules definitions and parameters in the Budget System Law accordingly to align them with statistical definitions, revisions to the national accounts and other improvements to fiscal data (**end-November 2024 SB**).

19. We will continue to enhance public financial management (PFM), which will help strengthen adherence to the fiscal rule. Our priority is to strengthen the medium-term budgetary framework. We will work on complementing our focus on annual budgets with a medium-term perspective that will form the starting point for next year's budgeting exercise. We will develop an action plan (**end-July 2023 SB**) to make medium-term budgeting more effective and binding beginning from 2025. To facilitate this process, a new IT system that consolidates budget preparation, execution and reporting will become functional in 2023. In the meantime, we will continue to ensure strict adherence to the budget calendar and to the transparency of the budget process, inter alia expanding the content of our within-year budget reports.

20. Strengthening the role and capacity of the Fiscal Risks Monitoring Department (FRMD) at the MOF is important.

- Following the adoption of the Unified Methodology for Fiscal Risks Monitoring, we will sign the remaining Protocols with the relevant institutions to establish a formal basis for the MOF to collect the data that is needed for monitoring fiscal risks by mid-2023.

- We are developing models and tools to operationalize the use of the new methodology to monitor fiscal risks stemming from SOEs, local governments, litigation, and natural disasters with World Bank support.

- We will provide expanded reporting on fiscal risks in the November update of Fiscal Strategy for 2024. We will also continue using the methodology that was developed with IMF TA support for managing fiscal risks associated with the state-guarantee schemes.

21. We are further strengthening our public investment management (PIM) framework.

- We strive to establish a single project pipeline to cover all ongoing and future investment projects by end-2023. With his in mind, the MOF has reached general agreement with the Ministry of European Integration (MOEI) on redesigning the pre-implementation stage regarding the strategic relevance evaluation to overcome the dualism between the Capital Investment Commission and the National Investment Committee. We will revise the relevant decree accordingly. The MOF and MoEI have already exchanged data on projects, thus creating a consolidated list. We are currently updating data at the level of individual projects.

- We have made progress in developing a Public Investment Management System (PIMIS)—including an integrated database of public investment projects. The overarching goal is to automate the evaluation and monitoring of capital projects, thus lowering related fiscal risks. The new system has become fully operational in June 2023 for projects in the implementation phase. As a next step, after streamlining the legal framework by end-September 2023, we will also incorporate projects in the pre-implementation phase starting from the project idea stage. We will expand PIMIS's usage to the national level by end-March 2024 (e.g., to line ministries and relevant special organizations), and aim to have local information systems compatible with PIMIS by early 2025.

- Following the amendment of the PIM Decree to incorporate indicators for environmental impact assessments in the PIM process, we are currently developing the relevant rulebooks and forms.

- We will remain committed to the following PIM processes to support public investment and capital budget planning: (I) we will ensure full implementation of the strategic relevance assessments of projects in line with the Decree on Capital Projects; (II) we will continue informing the Government on the projects monitored and appraised by local and provincial governments to the extent possible until the legal framework and the IT systems are in place; (III) we will continue to monitor the projects of special importance in the implementation stage and inform the government about PPP projects; (IV) we will continue including all project loans of the general government in the budget.

22. We remain committed to further modernizing our tax administration in line with our 2021-25 Transformation Program. This program provides strategic guidance in deepening the modernization of the tax administration by ramping up our use of electronic business processes, improved taxpayer services, and a risk-based approach to compliance. Our reforms will reflect the updated Tax Administration Diagnostic Assessment Tool review and will continue to be supported by IMF TA and the World Bank Tax Administration Modernization Project.

- We successfully introduced in May 2022 a new e-fiscalization model and have completed a first round of audits and enforcement activities drawing on the new information. We expect that general taxpayer compliance will increase and will consider a reduction in adverse audit findings a success. An electronic invoice exchange system became fully operational in the beginning of 2023.

- We will adopt the new reengineered business model and will aim at finalizing the recently launched tender for procuring a new commercial-off-the shelf-system (COTS) system by end-2023. Once the COTS provider has been selected, we will adopt an action plan for implementation. The system, which is expected to become operational gradually over several years will facilitate the effective implementation of key reform activities, including the modernization of business processes.

- We have initiated a VAT gap analysis and are now working on addressing data gaps and adjusting the analytical tools. The preliminary results suggest that the VAT gap has fallen considerably since 2018. We plan to improve the VAT gap estimations further to better identify the sources of non-compliance.

- Our recently formed dedicated unit to analyze the level of noncompliance of high-net-worth individuals has been collecting the relevant data and is ready to launch the first audits. We commit to launch the first audits by end-October 2023. We expect that this new enforcement activity will have a positive impact on general taxpayer compliance of high-net-worth individuals. To smooth the transition, we already amended our legal framework such that taxes on previously non-reported assets arising from legal activities will be assessed according to the standard tax regime plus interest, while taxes on non-reported assets where the origin cannot be documented will be taxed at a rate of 75 percent.

- Developing a new HR strategy for the tax administration and accelerating hiring procedures remains a high priority to ensure continued adequate staffing levels. Staffing in the STA has declined significantly over the recent years. With an impending retirement wave of many staff and considering our transformation agenda that implies a shift to higher skilled work, it is imperative to hire new well-skilled staff in a timely manner and at adequate pay levels.

23. The transition to the new general government employment framework for all public sector entities is being planned. The new system should ensure medium-term workforce planning by all public sector institutions according to their specific requirements as well as alignment with budgetary constraints. The work on a methodology to harmonize personnel and financial planning in state administration bodies continues. Currently, the Employment Commission allows public sector entities to replace up to 70 percent of the staff leaving the institution or retiring, within the institutions' budget limits, without approval of the Commission. At the same time, we maintain a limit on overall hiring approvals, such that the total number of permanent staff in the public sector cannot exceed the end-December 2020 level by more than 1 percent.

24. The phased establishment of a central electronic public wage and employment registry continues. This central registry *Iskra* will allow for better planning, executing, and controlling wage spending. The registry is expected to be completed by early 2024 and cover all public sector (except Ministry of Defense, Ministry of Internal Affairs, Security Information Agency BIA and higher education institutions) with more than 450 thousand public sector employees. The system already covers (1) direct budget users; (2) judiciary sector; (3) culture sector; (4) labor employment and social affairs sector; (5) education sector except higher education institutions. The next step is to further expand the system and make it fully operational for the health sector (new **end-January 2024 SB).** The ISKRA system will help with implementing a comprehensive reform of the public wage system, which is becoming urgent, because severe wage compression and competition from the private sector make it increasingly difficult to attract essential high skilled employees such as engineers, IT specialists and managers in the public sector.

25. We will aim to strengthen the application of the public procurement system to improve competition and transparency. Reforms in this area are particularly important given the large size of the public investment program. The current Law on Public Procurement, prepared with support from the EU, is aligned with the EU acquis and is set to enhance competition and transparency. We will also ensure regular public reporting through the Public Procurement Office on all procurements that were exempted from the regular procurement regime under this law, as well as a comprehensive justification of the basis for those exemptions. Going forward, we will ensure continued alignment of the entire procurement framework with the EU acquis. We will also ensure that all procurement transactions in the public sector are conducted using the e-procurement portal and strive to create conditions to increase the number of bids per procedure. With this in mind, we have been working on improving the functionalities of the Public Procurement Portal to facilitate the application of the provisions of the Public Procurement Law (PPL) and its use. We have also been conducting trainings for public procurement officers, and for police officers regarding monitoring of public procurement and the most frequent irregularities in the field of public procurement in Serbia.

D. Monetary and Exchange Rate Policies

26. The primary objective of the NBS's monetary policy is to achieve and maintain price stability. This plays a crucial role in contributing to financial system stability and in fostering sustainable economic growth. An important pillar of this objective is relative exchange rate stability of domestic currency vis-à-vis the euro. The National Bank of Serbia (NBS) stands ready to use all available policy instruments to deliver on its objectives.

- Our current policies are consistent with the objective of putting inflation on a declining path in 2023 and bringing it within the NBS's tolerance band (3 percent ±1½ percentage points) by mid-2024. We were tightening monetary conditions since 4Q2021 in a gradual and continuous fashion, at first by tightening liquidity conditions, and afterwards by raising key policy rate by 525 bps cumulatively from April 2022 to reach 6.25 percent in June 2023. We also raised the interest rates on deposit and lending facilities to 5 and 7.5 percent, respectively. While at the monetary policy decision meeting in May the NBS decided to keep the key policy rate unchanged, we raised the key policy rate further in June, having concluded that it is necessary to continue to moderately tighten monetary conditions to contain inflation expectations and make sure that inflation strikes a downward path and returns to within the target tolerance band in the projection horizon. We will continue to sterilize dinar liquidity (injected mainly through foreign exchange purchases) to support NBS policy of achieving price stability.

- Depending on movements of key monetary and macroeconomic factors at home and abroad, as well as the global geopolitical situation, the NBS will assess whether there is a need to tighten monetary conditions further and to what extent, taking into account the expected effects of past monetary tightening on the future inflation profile. The NBS underscores the need to pursue a cautious monetary policy, notably in light of uncertainties around the duration of the Ukraine conflict and energy availability and prices going forward. Uncertainties are also associated with developments in core inflation in a number of countries. An important factor will also be the future monetary policy decisions of leading central banks, given their impact on conditions in the international financial markets and capital flows to emerging economies.

- In the context of the SBA, inflation developments will continue to be monitored through a consultation clause with consultation bands set around the program's central inflation projections (Table 1a). As envisaged by the TMU (¶21), in case of deviations we will discuss with the IMF staff the reasons for the deviation and the appropriate policy response.

27. We are committed to sustaining relative exchange rate stability through this period of heightened uncertainty. With this in mind, we have been strengthening the reserves buffers. At end-May 2023, gross and net FX reserves stood at €22.1 billion and €18.1 billion, respectively. In the context of the SBA, we are committed to maintaining the international reserves above the NIR floor envisaged under the program. We are cognizant that uncertainty remains high, and in a context of relative exchange rate stability, reserves take the first hit in case of shocks. Accordingly, and consistent with our existing policies, we aim at preserving a substantial and prudent reserves buffer well above this floor, aligned with the IMF reserves adequacy metric. In addition, should reserves remain strong, we will consider raising the net international reserves (NIR) floor at the next review. To protect reserves, we will adjust monetary and fiscal policies as needed.

28. Promoting dinarization remains an important objective. Our dinarization strategy has three pillars: (i) maintaining overall macroeconomic stability; (ii) creating favorable conditions for developing the dinar bond market; and (iii) promoting hedging instruments.

- In April 2023, deposit and credit dinarization stood at 40.7 and 34.3 percent, respectively. Having recorded a decline in 1H2022 amid the adverse global developments, dinar savings increased to RSD 106,3 bln as of end-April 2023. Importantly, and as another sign of confidence in the system, the share of time deposits in total dinar savings increased to 76.6 percent while the share of demand deposits declined.

- Beyond pursuing policies that support macroeconomic stability, several specific measures to foster dinarization have been put in place, such as higher reserve requirements on FX deposits, mandatory down-payment ratios for FX loans, and systemic risk buffers. Higher capital requirements on banks' FX-indexed lending to corporates will be required for loans disbursed from July-2023.

- We have signed an agreement with Euroclear to create a Euroclearable link to be able to auction dinar-denominated securities through Euroclear's system. While we have already established the necessary software architecture, we have postponed launching the Euroclearable link and auctioning dinar-denominated securities through Euroclear's system due to the unfavorable market conditions. In addition, the negotiations with Euroclear on the right model of the primary distribution for the benchmark bonds are yet to be finalized.

29. During the Fund-supported program period we will not impose or intensify restrictions inconsistent with the IMF's Articles of Agreement. Specifically, 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 (Table 1b).

E. Financial Sector Policies

30. Maintaining financial stability is a key priority and we will continue monitoring risks in the banking sector while promoting financial inclusion. The banking system remains stable owing to adequate capitalization, ample liquidity, and strong profitability. Banks' average capital adequacy ratio stood at 20.52 percent in March 2023, well above the regulatory prescribed minimum of 8 percent. The average monthly liquidity ratio amounted to 2.3 in March 2023 which is more than double the regulatory prescribed threshold of 1. In December 2022, bank average ROA and ROE outturns stood at 1.9 and 13.9 percent, respectively.

31. In 2022–23 the NBS introduced regulations to address the impact of shocks and to preserve financial stability and support the economy and its citizens under pandemic conditions.

- In June 2022, the NBS adopted a regulation enabling banks to mitigate the negative effects of the change in government bond prices on bank capital by excluding 70 percent of the net unrealized losses and gains from the valuation of the bonds from the calculation of CET 1 capital until the end of 2022. Subsequently, this measure was extended through 2023.

- In October 2022, in response to severe drought, we allowed registered agricultural producers to postpone the settlement of their liabilities under the loans by six to twelve months, depending on their preferred grace period, but with the contracted interest rate still being paid. Such a rescheduling does not trigger automatic reclassification of the loans. In January 2023, this measure was extended to borrowers engaged in the purchase and cold storage of fruit, with an application deadline of end-April 2023.

- In December 2022, the NBS extended the temporary measure to ease repayment conditions of housing loans through end-2023. Under this measure, banks can offer relief by extending the repayment period of housing loans for a maximum of five years, without affecting the regulatory treatment of these claims.

- In December 2022, by the Decision Amending the Decision on Capital Adequacy of Banks, we adopted a permanent measure enabling banks to restructure their receivables from financially distressed natural persons in respect of consumer, cash, or similar loans by extending the maturity of these loans by up to three years relative to the current regulatory arrangement, consequently restructured loans would have stage 2 treatment under IFRS9.

32. We will continue to strengthen financial sector regulatory and supervisory frameworks to fully align them with international standards. We continue to enhance the prudential framework for banks and insurance companies to ensure full compliance with international standards and EU requirements. We will further harmonize our financial legal framework with the EU acquis, considering the specificities of the Serbian financial market. We are also conducting a gap analysis of the domestic legal framework for banks with those in EU, that we aim to conclude by end-2023.

33. We continue enhancing financial safety nets. The work on harmonization of the deposit insurance scheme with the EU acquis remains a priority for the Deposit Insurance Agency (DIA).

34. NPL ratios have remained low, but we continue to monitor asset quality closely. Despite unfavorable global developments, NPLs fell to an historical low of 3 percent as of end-March 2023. Yet, the current context of changing interest rates and inflationary pressures warrants continued close monitoring. To resolve the residual assets of the DIA portfolio of bad assets, we launched the third and final tendering process with a nominal value of about €318 million in December 2022. The closing is expected by H1 2023.

35. We will continue to implement reforms of state-owned financial institutions. We will further strengthen our oversight of state-owned financial institutions.

- We will continue to implement the government strategy for Banka Poštanska Štedionica (BPS) for the period 2021–25. We will continue to closely monitor risks related to new lending to medium-size companies, SOEs and local governments.

- We will adopt a plan for the future of Srpska Banka before end-2023, the preparation of which was delayed due to the COVID-19 pandemic, 2022 elections and the current policy focus on the energy-crisis.

- The Development Fund and AOFI will continue 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, prevent further deterioration in asset quality, and resolve impaired assets.

36. We continue to enhance Serbia's capital markets and to diversify sources of long-term financing in line with the Capital Market Development Strategy. Our initial focus is on plain vanilla financial instruments, followed by more complex instruments, including covered bonds. As planned, the new Law on Capital Markets that aligns the Serbian regulatory framework with the EU acquis and the MiFID II requirements has become effective since 2023. We continue to focus on the existing tax system's compatibility with capital market development and will make changes as needed. In addition, we have been working on creating the so-called One Stop Shop internet platform that will provide market participants with information needed to reach an investment or issuing decision.

F. Structural and Governance Policies

37. We are committed to enhancing the existing social protection programs to protect vulnerable groups, reduce inequality, and fight poverty. In 2022, we launched a new Social Cards Register that envisages a single, centralized, and electronic record with up-to-date data on the socio-economic status of individuals and persons related to them to improve the consistency and efficiency of social protection programs. We plan to integrate the Social Card register with the information system SOZIS which envisages adding the module for social benefits and services at the local level, the module for the payment of rights at the republic level, the integration of the Republic and Provincial Institute for Social Protection, the Chamber of Professional Social Protection of Workers, and creation of modules for reporting by system management levels and interested users.

38. We will continue developing a comprehensive agenda for green growth, to support the economic recovery and ensure a more sustainable and environmental-friendly development. This is essential to prepare for the EU CBAM and to continue to attract strong FDI to Serbia. We have adopted the Low-Carbon Development Strategy for 2023-2030 period with the 2050 outlook, which will be harmonized with the Integrated National Energy and Climate Plan and the Energy Development Strategy of the Republic of Serbia, that are under development (¶11). In the meantime, we have been prioritizing green investments, including in renewable energy and energy efficiency, making progress on green budgeting, and we will consider carbon pricing mechanisms once the overarching goals and principles have been designed.

39. We will continue to support reforms to strengthen the rule of law and fight corruption. Over the past months, we have been working on broadening the definition of persons with top executive functions (PTEFs) to include Ministerial chief of cabinets and advisors to strengthen our asset declaration regime, and have improved coordination and data exchange between relevant agencies and the Agency for the Prevention of Corruption. This includes verification processes to cross reference information, including beneficial ownership. We will continue to address outstanding GRECO recommendations outlined in the 5th evaluation report by September 2023, when the next mutual evaluation report is due. We will continue to build the human capacity at the Agency for the

Prevention of Corruption and commit to providing it with sufficient budgetary resources to fulfill its mandate.

40. We will also continue to address the grey economy. Building on the successful implementation of the previous program for countering the shadow economy, we have adopted a new program for 2023–25 that lists 23 measures aimed at (1) strengthening the capacity of inspections and misdemeanor courts; (2) improving the tax oversight and reporting procedure; and (3) facilitating fiscal and administrative relief for legal businesses. The program was prepared with the private and civil sectors.

41. We remain committed to resolving enterprises in the portfolio of the former Privatization Agency in accordance with the Privatization Law.

- We will not reopen MSK.
- We will continue exploring options for potential strategic investments or partnerships for Lasta.
- We remain committed to a time-bound action plan for Resavica mines, developed with the assistance of the World Bank, that foresees the closure of several unviable mines, while developing a voluntary social program and labor optimization plan. We will ensure sufficient resources in the budget to transparently support Resavica through subsidies and to prevent further accumulation of arrears to EPS.

42. We will continue strengthening the AML/CFT framework. We will continue strengthening the AML/CFT framework and accelerate ongoing reforms.

- We will continue our regular reporting under the EU agenda, both as part of negotiating chapters (e.g., Chapters 24 and 4) and sub-committees of monitoring the implementation of the Stabilization and Association Agreement. We will ensure the adequate and timely implementation of the requirements of all AML/CFT related EU Directives and Regulations, in line with the FATF Standards and with EU implementation deadlines.
- The competent AML/CFT authorities, including the Administration for Prevention of Money Laundering and Law Enforcement Authorities (LEA), will continue with all their regulatory, supervisory, and other activities, as well as continuous strengthening of their capacities through adequate external and internal trainings, especially concerning the emerging AML/CFT trends and risks. Importantly, we have re-assessed and modified our National AML/CFT Strategy and Action Plan (2022-2024) which focuses, among other areas, on retention and further improvement of human, financial and technical resources.
- Transparency of Beneficial Ownership of legal entities operating in Serbia, including the implementation of the recent updates from March 2022 to FATF's R.24, will also be further strengthened by enacting a new law that will enhance Serbia's capacities in ensuring adequate, accurate and up-to-date information on beneficial owners. We will also continue closely

monitoring the implementation of targeted financial sanctions by regulated entities in order to prevent potential spillovers related to the Ukraine conflict.

43. We will continue improving the quality and transparency of national statistics. We remain committed to comprehensive, timely, and automatic data sharing across relevant compiling agencies (including MOF, SORS and NBS) for statistical purposes. NBS and SORS will coordinate on the compilation and dissemination of annual financing data on an accrual basis consistent with GFSM 2014. Meanwhile, coordinated and phased work will continue to migrate annual revenue and expenditure data to an accrual basis.

G. SOE Reforms

44. We are fully committed to changing the operation of SOEs in Serbia, spearheaded by a new ambitious SOE law. The important new Law on ownership management for SOEs was adopted by the government in May 2023. While the first draft of the law was completed before end-December 2022 **(end-December 2022 SB)**, its approval was delayed providing more time to align the draft more closely with the OECD Guidelines on Corporate Governance of SOEs. Accordingly, the new Law mandates that supervisory boards appoint general managers at arms' length from the government, defines mechanisms for setting and monitoring SOE mandates and objectives, defines the main principles for covering costs of public policy objectives, and prescribes strong disclosure and transparency requirements. The governance structure envisaged by the new SOE law will be instrumental for addressing the excessive reliance on acting directors in state-owned companies. Given strong interest by the public in the new Law, we embarked on a public communication campaign to explain the goals of the new law and elaborate on how it will address the deep-rooted problems of Serbia's SOE sector. We expect the campaign to last three weeks after which the Law will be resubmitted to the National Assembly for adoption. We expect the Law to be adopted by the National Assembly before end-July 2023. In the meantime, we will prepare the necessary bylaws to make the Law fully operational one year after the law enters into force.

Program Monitoring

45. Progress in the implementation of the policies under this program will continue to be monitored through quantitative performance criteria (QPCs), indicative targets (ITs), including an inflation consultation clause and natural gas prices consultation clause, continuous performance criteria (CPCs) and structural benchmarks (SBs). These are detailed in Tables 1a, 1b, and 2, with definitions provided in the attached Technical Memorandum of Understanding (TMU). Reviews by the IMF will be conducted on a semi-annual basis to assess program implementation and reach understandings on any further reforms needed. The second review is scheduled to be completed soon after December 19, 2023, the third review is scheduled to be completed soon after June 1, 2024.

46. The April 2023 safeguards mission confirmed that the NBS has a strong safeguards framework and internal controls and financial reporting environment and recommended some steps for further enhancement. As required by the IMF's safeguards policy, we will continue to engage independent external audit firms to conduct the audit of the NBS in accordance with international standards. We will also provide Fund staff with the necessary NBS's audit reports and authorize representatives of the external audit firm of the central bank to hold discussions related to their reports with Fund staff.

Table 1a. Serbia: Quantitative Performance Criteria and Indicative Targets Under the SBA 2022–24[1]

	2022			2023									2024	
	end-Dec.			end-Mar.			end-Jun.		end-Sep.		end-Dec		end-Mar.	end-Jun.
	QPC	Adj. Prog.	Actual	IT 5/	Adj. Prog.	Actual	QPC	Rev. QPC	IT 5/	Rev. IT 5/	QPC	Rev. QPC	IT 5/	QPC
	CR 22/384			CR 22/384			CR 22/384		CR 22/384		CR 22/384			
I. Quantitative Performance Criteria (QPCs, semi-annually)														
1 Ceiling on the general government fiscal deficit (in billions of dinars) 2/ 3/	272.0	270.0	221.2	70.9	73.5	24.9	86.9	86.9	121.7	121.7	264.0	245.0	82.0	102.4
2 Ceiling on current primary expenditure of the Serbian Republican Budget including net lending, excluding capital expenditure and interest payments (in billions of dinars) 2/	1,415.0	1,410.9	1,405.8	375.3	364.4	326.8	736.6	736.6	1,079.9	1079.9	1,497.5	1,497.5	374.3	767.8
3 Floor on Net International Reserves (in billions of euros) 4/	6.5		14.0	5.5		16.0	5.5	6.2	5.6	6.3	5.9	6.4	6.6	6.8
II. Indicative Target (IT) 5/														
4 Ceiling on accumulation of domestic payment arrears by the consolidated general government except local governments, the Development Fund, and AOFI (in billions of dinars) 6/	1.0		0.9	1.0		0.6	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
III. Continuous Performance Criterion														
5 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	0.0	0.0
IV. Inflation consultation band (quarterly) 7/														
Upper band limit (1.5 percent above center point)	17.3			17.0			15.5	15.5	11.5	11.5	9.7	9.7	7.7	6.8
End of period inflation, center point 8/	*15.8*		15.1	*15.5*		16.2	*14.0*	*14.0*	*10.0*	*10.0*	*8.2*	*8.2*	*6.2*	*5.3*
Lower band limit (1.5 percent below center point)	14.3			14.0			12.5	12.5	8.5	8.5	6.7	6.7	4.7	3.8

1/ As defined in the Memorandum of Economic and Financial Polices, 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/ Calculated consistent with Gross International Reserves at 80 percent of the ARA metric (see TMU).
5/ Indicative targets include (i) the items under I. Quantitative Performance Criteria at end-March and end-September, and (ii) the targets under II Indicative Target (IT). ITs are not monitored as part of program conditionality.
6/ Net cumulative change since the start of the year, measured as the change in the stock at the test date and at the start of that year.
7/ Staff level consultation is required upon breach of the band limits at the specific test date.
8/ Defined as the change over 12 months of the end-of-period consumer price index, as measured and published by the Serbian Statistics Office.

Table 1b. Serbia: Standard Continuous Performance Criteria Under the SBA

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: Structural Benchmarks Under the SBA

	Description	Target Date	Status	Objective
	Fiscal			
1	Expand and fully operationalize the central electronic public wage and employment registry for the education sector.	End-March 2023	Met	This reform would help rationalize, pay and improve incentives across public sector.
2	Adopt an action plan to make medium-term budgeting more effective and binding.	End-July 2023		Continued strengthening of public financial management practices in support of achieving fiscal objectives.
3	Expand and fully operationalize the central electronic pubic wage and employment registry for the health sector.	End-January 2024	New, continuation of a multi-year reform agenda	This reform would help rationalize pay and improve incentives across public sector.
4	Finalize a review of the quantitative indicators of the fiscal rule to reflect, as needed, revisions to the national account/ GFS methodology and other improvements to fiscal data.	End-November 2024		Continued strengthening of public financial management practices in support of achieving fiscal objectives, and improved fiscal data.
	Energy			
5	Change the legal status of Elektroprivreda Srbije (EPS) to a joint stock company.	End-February 2023	Not met, completed in April 2023. Legal status was changed following changes to EPS' statutes.	This target is line with the ongoing corporate restructuring process and financial consolidation of EPS, aiming to improve the viability of the company and ensure its professional management.
6	A decision to increase average electricity tariffs by at least 8 percent, effective May 1, 2023.	End-April 2023	Met	Move energy tariffs towards cost recovery, and control fiscal risks.
7	A decision to increase average natural gas tariffs by at least 10 percent, effective May 1, 2023.	End-April 2023	Met	Move energy tariffs towards cost recovery, and control fiscal risks.
8	Adopt by government a prioritized and costed investment plan for the energy sector for projects to be implemented over 2 - 5 years.	End-May 2023	Not met, completed in June 2023	Address near-term challenges in the energy sector to enhance energy security, stabilize energy production, and conserve energy.
9	A decision to increase average natural gas tariff by at least 10 percent, effective November 1, 2023.	End-October 2023	New, as foreshadowed in the MEFP of December 1, 2022 at SBA approval	Move energy tariffs toward cost recovery, and control fiscal risks.
10	A decision to increase average electricity tariffs by at least 8 percent, effective November 1, 2023.	End-October 2023	New, as foreshadowed in the MEFP of December 1, 2022 at SBA approval	Move energy tariffs toward cost recovery, and control fiscal risks.
11	Adopt by the government a restructuring plan for EPS.	End-December 2023		Address the medium- to long-term viability of the company and the security of electricity production.
	Other			
12	Adopt a new law on ownership management for SOEs.	End-December 2022	Not met, completed in May 2023	Adopting this law is critical to advance reforms aimed at strengthening SOE governance and management.

Attachment II. 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 October 31, 2022, except as noted below. The quantitative performance criteria and structural benchmarks for assessing program performance are shown in Tables 1a, 1b and 2 of the Memorandum of Economic and Financial Policies (MEFP). Definitions and adjustments of these targets are outlined below.

2. For program purposes, the consolidated general government comprises the Serbian Republican government (without indirect budget beneficiaries that are not included in the budgetary execution system), local governments (including the Province of Vojvodina), 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. Reflecting the ongoing work program to expand the coverage of the general government sector in within-year reporting, consolidated general government data for 2023 and beyond include service institutions like dormitories in the education sector now included in the budgetary execution system, and health sector institutions reported by the Health Fund. Any new extra budgetary fund or subsidiary established over the duration of the program would be consolidated into the general government.

A. Fiscal Conditionality

3. The general government fiscal deficit is defined as the difference between total general government expenditure (irrespective of the source of financing) and total general government revenue (including grants). General government expenditure includes expenditure financed from foreign and domestic project loans and grants; payments of called guarantees, cost of bank resolution and recapitalization, cost of debt takeover if debt was not previously guaranteed, all budget loans provided to public sector enterprises in the energy sector, and any other budget loans if they have not been repaid by the end of the calendar year; repayments of called guarantees, debt takeovers, budget loans previously recorded "above the line"; and payment of arrears (irrespective of the way they are recorded in the budget law). 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.

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

5. For program purposes, any financial support (other than loan guarantees) from the Republican or local government budgets for public enterprises in the energy sector will be recorded "above the line" at the time it is given. Financial support includes, but is not limited to, subsidies, budget loans for liquidity support, capital expenditure or capital grants for financing or co-financing energy sector projects. This is irrespective of the way these transactions are recorded in the budget law. The energy sector covers electricity production and supply, transmission and distribution including associated activities like coal mining; natural gas supply, transportation and storage; district heating; and transport of crude oil and oil products pipelines. Public enterprises in the energy sector include but are not limited to EPS, EMS and EDS and their subsidiaries; Srbijagas and its subsidiaries; and district heating companies; and any public enterprise that may be created by unbundling or be newly founded.

6. Quantitative fiscal targets (MEFP Table 1b) are specified cumulatively from the beginning of each calendar year except where defined otherwise. This includes in particular the quantitative performance criteria and indicative targets on the general government fiscal deficit and the current primary expenditure of the Republican budget, and the reference values for adjustors.

Adjustors

- The quarterly ceilings on the general government fiscal deficit and on primary current expenditure of the Republican budget will be adjusted upward by 90 percent of the excess in actual net lending from the Republican budget to Srbijagas relative to the amount indicated in the table below provided that the average of market prices at the TTF Dutch market (closing prices "Close*", as reported on https://finance.yahoo.com/quote/TTF%3DF/history/) since the beginning of the year exceeded €130 per MWh by no less than 10 percent.

- The quarterly ceilings on the general government fiscal deficit and on primary current expenditure of the Republican budget will be adjusted downward by 90 percent of the shortfall in actual net lending from the Republican budget to Srbijagas relative to the amount indicated in the table below provided that the average of market prices at the TTF Dutch market (closing prices "Close*", as reported on https://finance.yahoo.com/quote/TTF%3DF/history/) since the beginning of the year fell short of €130 per MWh by no less than 10 percent.

Cumulative Programmed Net Lending from the Republican Budget to Srbijagas 1/
(In billions of dinars)

	End-Dec. 2022	End-Mar. 2023	End-Jun. 2023	End-Sept. 2023	End-Dec. 2023	End-Mar. 2024	End-Jun. 2024
Programmed Net Lending	130	40	54	54	54	30	30

1/ Cumulative from the beginning of each calendar year.

- 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, debt recovery receipts, debt issuance premiums, and concession and Public Private Partnership (PPP) receipts recorded above-the-line exceed (fall short of) 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 1/

(In billions of dinars)

	End-Dec. 2022	End-Mar. 2023	End-Jun. 2023	End-Sept. 2023	End-Dec. 2023	End-Mar. 2024	End-Jun. 2024
Programmed cumulative dividends	18.5	13.5	13.5	13.5	13.5	13.5	13.5
Programmed cumulative debt recovery receipts	4	4	4	4	4	4	4
Programmed cumulative debt issuance at a premium	4	0	0	0	0	0	0
Programmed concession and PPP receipts recorded above the line	0	0	0	0	0	0	0

1/ Cumulative from the beginning of each calendar year.

- 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 1/

(In billions of dinars)

	End-Dec. 2022	End-Mar. 2023	End-Jun. 2023	End-Sept. 2023	End-Dec. 2023	End-Mar. 2024	End-Jun. 2024
Programmed cumulative ear-marked grants receipts	19.2	19.2	23.2	31.2	50.5	4.0	9.0
Programmed cumulative receipts from small-scale disposal of assets	0	0	0	0	0	0	0

1/ Cumulative from the beginning of each calendar year.

7. 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 an indicative 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. This indicative target will be measured as the change in the stock of domestic arrears at the test date relative to the stock at the end of the previous calendar year. Within 45 days of the end of the calendar year, the authorities will report the stock of domestic arrears on December 31, 2022

8. 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. Public Debt

9. Public debt is defined as debt and guaranteed debt incurred by the general government.

10. The term "debt" will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debt will include SDRs used for financing of the Republican budget, and restitution bonds. Debts can take a number of forms, the primary ones being as follows:

(i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);

(ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and

(iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of these guidelines, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property.

11. Guaranteed public debt is debt guaranteed by the general government, i.e., a contingent liability.

C. Floor on Net International Reserves

12. For purposes of the program, all foreign currency-related assets and liabilities will be valued in euros at **program exchange rates** as specified below. The program exchange rates are those that prevailed on October 31, 2022. Monetary gold will be valued at the average London fixing market price that prevailed on October 31, 2022.

Table 1. Serbia: Cross Exchange Rates and Gold Price for Program Purposes, October 31, 2022

Valued in:

Currency:	**RSD**	**Euro**	**USD**	**SDR**	**GBP**	**Yuan**
RSD	1.0000	0.0085	0.0085	0.0066	0.0073	0.0617
Euro	117.3088	1.0000	0.9953	0.7756	0.8581	7.2379
USD	117.8628	1.0047	1.0000	0.7792	0.8622	7.272
SDR	151.2522	1.2894	1.2833	1.0000	1.1064	9.3322
GBP	136.7076	1.1654	1.1599	0.9038	1.0000	8.4348
Yuan	16.2076	0.1382	0.1375	0.1072	0.1186	1.0000
Gold	193,177.13	1,646.74	1,639.00	1,277.19	1,413.07	11,918.92

Source: International Monetary Fund and NBS.

13. Net international reserves (NIR) of the NBS are defined as the difference between reserve assets and reserve-related, short-term liabilities, measured at the end-of-business day.

14. Reserve assets are readily available claims on nonresidents denominated in convertible foreign currencies (see Balance of Payment Manual, 6.64). They include the NBS holdings of monetary gold,[1] foreign exchange balances (foreign currency cash, foreign currency securities, deposits abroad), holdings of SDRs, and the country's reserve position at the Fund. Excluded from reserve assets are any assets that are pledged, collateralized, or otherwise encumbered (e.g., pledged as collateral for foreign loans or through forward contracts, guarantees and letters of credit), claims in foreign exchange arising from derivatives in foreign currencies vis-à-vis domestic currency (such as futures, forwards, swaps, and options), precious metals other than monetary gold, domestically

[1] See BPM6, 6.78: monetary gold is gold (i) to which the NBS has title, (ii) is held as a reserve asset by the NBS, and (iii) is certified to be at least 995/1000 pure.

acquired gold without international certificates, assets in nonconvertible currencies, and illiquid assets.

15. Reserve-related liabilities are defined as all foreign exchange denominated liabilities to nonresidents and residents, excluding deposits from the general government, with a maturity of less than one year, including commitments to sell foreign exchange arising from derivatives (such as futures, forwards, swaps, and options, including any portion of the NBS gold that is collateralized), and the stock of all IMF credit outstanding to the Republic of Serbia. If the NBS conducts swaps as an intermediate between two banks, commitments to sell foreign exchange arising from swaps in foreign currencies vis-à-vis domestic currency are included in foreign exchange denominated liabilities after netting with claims in foreign exchange arising from these swaps.

16. Monitoring. NIR data will be reported to the Fund on a monthly, end-of-month basis, within 14 days after the end of each month.

17. Adjustors. For program purposes, the NIR target will be adjusted:

- Downward and upward by any shortfall/excess of exceptional financing compared to program amounts outlined in the table below.

Table 2. Serbia: Identified Exceptional Financing in 2023 and 2024[1]

(Millions of euros)

	2023			2024	
	Q2	Q3	Q4	Q1	Q2
General government	0	149.9	149.9	240.0	240.0
Public enterprises	200.0	200.0	400.0	0.0	0.0

1/ Cumulative from the beginning of the year.

D. Gas Price Consultation Mechanism

18. Gas prices are defined as the spot prices for natural gas at the Dutch TTF market (closing price “Close*”) as reported on. https://finance.yahoo.com/quote/TTF%3DF/history/. The 14-day average is the equally weighted average of those prices actually reported during the 14 calendar days ending one day before the reporting day.

19. Exceeding the gas prices means, the 14-day average of natural gas prices exceeds the reference values specified in the table below. The reference gas price applies continuously during the entire quarter. Exceeding the gas price would trigger consultation with staff on the proposed policy response, including any potential additional liquidity support from the budget to Srbijagas and potential tariff increases, as needed. The consultation would take place at least once a month until one month has elapsed after gas prices drop below the reference price.

Table 3. Serbia: Reference Values for Natural Gas Price
(Millions of euros)

	2023			2024	
	Apr.-Jun.	**Jul.-Sept.**	**Oct.-Dec.**	**Jan.-Mar.**	**Apr.-Jun.**
Natural gas price upper bound (EUR/ MWh) 1/	250	250	250	250	250

1/ Consultation is required if the 14-day average Dutch TTF spot natural gas price (EUR/ MWh) exceeds the upper bound specified. The upper bound price applies continuously during the entire quarter.

E. Ceiling on External Debt Service Arrears

20. 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. 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.

21. 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.

F. Inflation Consultation Mechanism

22. 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.

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

G. Reporting

24. General government revenue data and the Treasury cash position table will be submitted weekly; and the stock of spending arrears as defined in ¶6 will be reported 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.

25. The stock of spending arrears (> 60 days past due) as reported in the MOF Invoice central registry system (CRF) and Registry for Settlement of Monetary Obligations (RINO) will be submitted within 14 calendar days after the end of each month.

26. 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.

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

28. Borrowing by the Development Fund and AOFI will be submitted within 35 days of the end of each month.

29. 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 35 days of the end of each month.

30. 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.

31. Detailed balance of payments data on a value basis provided on a monthly basis, 45 days after the end of the month or after publication, which is traditionally available on the NBS website and downloaded by the IMF team.

32. Gross international reserve data will be submitted within one business day after the respective period end as defined in the data reporting table below**.**

33. Volumes and prices of trade in goods data, on a monthly basis, 8 weeks after the end of the month, which is traditionally available on the SORS website and downloaded by the IMF team

34. Production and consumption data, and cash flow data (actuals and revised projections to the end of the year) for EPS and Srbijagas will be submitted at the end of each quarter, within 20 calendar days, in the agreed templates, until end-September 2023. Starting end-October 2023, this data will be provided at the end of each month, within 20 calendar days. In the interim, until end-September 2023, readily available data for EPS and Srbijagas (profit and loss statements) will be provided at the end of each month, within 20 calendar days.

35. Any support provided from the Republican budget or local government budgets to public enterprises in the energy sector will be reported monthly within 35 calendar days after the end of each month in the template agreed. This will also include any guarantees extended.

36. Data on public debt and publicly guaranteed debt will be submitted monthly within 35 calendar days after the end of each month; except that data on suppliers' credit, leases and obligations arising from the receipt of advance payments will be provided to the extent available on a quarterly basis, and data on guaranteed debt will cover guarantees issued by the Republic of Serbia.

Table 4. Serbia: 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
Statistical Office and NBS	Trade in goods data, volumes and prices 1/	Monthly, within 8 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	Cumulative net lending from the Republican Budget to Srbijagas	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
NBS	Detailed balance of payments data, value basis 2/	Monthly, within 45 days of the end of the month
	Gross international reserves	Weekly, at the end of the first business day in the following week 3/
	Gross international reserves, composition details	Every two weeks, at the end of the first business day in the following week
	GIR and reserve-related liabilities (FX liabilities with a maturity of 1 year or less). Reserve-related liabilities projections for 4 quarters forward.	End of quarter, within 14 days after the end of the quarter.

1/ Sufficient to notify IMF that data is available on SORS website.
2/ Sufficient to notify IMF that data is available on NBS website.
3/ If gross reserves decline by more than 5 percent in one day or by more than 10 percent on a cumulative basis for any two-week period, reporting frequency shall be increased to daily, by the end of the subsequent business day, until the NBS and IMF staff mutually agree to return to weekly reporting.

INTERNATIONAL MONETARY FUND

REPUBLIC OF SERBIA

June 15, 2023

STAFF REPORT FOR THE 2023 ARTICLE IV CONSULTATION, FIRST REVIEW UNDER THE STAND-BY ARRANGEMENT, AND REQUEST FOR MODIFICATION OF PERFORMANCE CRITERIA—INFORMATIONAL ANNEX

Prepared By	European Department (in consultation with other departments)

CONTENTS

FUND RELATIONS

(As of April 30, 2023)

Membership Status

Joined December 14, 1992 (succeeding to membership of the former Socialist Federal Republic of Yugoslavia); accepted Article VIII on May 15, 2002. Serbia continues the membership in the Fund of the former state union of Serbia and Montenegro—previously the Federal Republic of Yugoslavia—since July 2006.

General Resources Account:

	SDR Million	Percent Quota
Quota	654.80	100.00
IMF's Holdings of Currency	1,393.80	212.86
Reserve Position	46.78	7.14

SDR Department

	SDR Million	Percent Allocation
Net cumulative allocation	1,072.63	100.00
Holdings	68.46	6.38

Outstanding Purchases and Loans

	SDR Million	Percent Quota
Stand-By Arrangements	785.76	120.00

Latest Financial Commitments

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-By	Dec 19, 2022	Dec 18, 2024	1,898.92	785.76
Stand-By	Feb 23, 2015	Feb 22, 2018	935.40	0.00
Stand-By	Sep 29, 2011	Mar 28, 2013	935.40	0.00

Projected Payments to Fund

	Forthcoming (SDR Million)				
	2023	**2024**	**2025**	**2026**	**2027**
Principal				392.88	392.88
Charges / Interest	55.13	74.99	74.92	69.82	51.82
Total	**55.13**	**74.99**	**74.92**	**462.70**	**444.70**

Implementation of HIPC Initiative

Not applicable.

Implementation of Multilateral Debt Relief Initiative (MDRI)

Not applicable.

Implementation of Catastrophe Containment and Relief (CCR)

Not applicable.

Exchange Arrangement

Serbia accepted the obligations under Article VIII, Sections 2, 3, and 4, on May 15, 2002, and maintains a system free of restrictions on payments and transfers for current international transactions, except with respect to blocked pre-1991 foreign currency savings deposits. In accordance with the revised IMF classification system of exchange rate arrangements, the de jure exchange rate arrangement is a floating system since January 1, 2001. The current Decision on the Dinar Exchange Rate Regime of the National Bank of Serbia (NBS) stipulates "managed floating." The de facto exchange rate arrangement is classified as stabilized; it was reclassified from crawl-like effective March 2, 2018.

Last Article IV Consultation

Concluded on June 18, 2021 (IMF Country Report No. 21/132).

FSAP Participation

Serbia participated in the Financial Sector Assessment Program in 2005, and the Executive Board discussed the Financial System Stability Assessment in February 2006 (IMF Country Report No. 06/96). An update under the Financial Sector Assessment Program was conducted in 2009 and the Executive Board discussed the Financial System Stability Assessment (FSSA) in March 2010 (IMF Country Report No. 10/147).

FSSA recommendations informed subsequent program engagements in the 2010s under Stand-By Arrangements (SBAs) and Policy Consultation Instruments (PCIs), as well as Article IV recommendations. Important financial sector reforms have been completed (see, e.g., the 2021 Article IV consultation (IMF Country Report No. 21/132)). Today there is only one sizable state-owned bank - Banka Poštanska Štedionica (BPS) with a share of assets in the banking system of 6.4 percent, which operates under a well-defined government strategy 2021–25 (MEFP ¶34). The Deposit Insurance Agency (DIA) is expected to complete the third and final sale of legacy asset in the first half of 2023. The bank resolution framework was upgraded with MCM assistance, and successfully applied to mitigate international spillovers at the start of the war in Ukraine by resolving speedily the local branch Sberbank Srbija (IMF Country Report No. 22/201). Capital market development is now guided by the October 2021 strategy, and a new Law on Capital Markets, which aligns the regulatory framework with the EU acquis and MiFID II requirements, was adopted and applied from Jan 2023.

Technical Assistance since Last Article IV consultation (June 2021)[1]

Department	Timing	Purpose
STA	June–September 2021 (virtual)	Government Finance Statistics
STA	February–April 2022 (virtual)	Government Finance Statistics
STA	November 2022	Government Finance Statistics
FAD	August 2021	Tax Administration: Large Taxpayers
FAD	August 2022	Green Budgeting
FAD	November 2022	Tax Administration: Risk Analysis
FAD	November–December 2022 (blended)	VAT Gap Analysis
FAD/ LEG	January 2023 (virtual)	SOE Governance Law
FAD	April 2023	Workshop: Management of the Tax Administration Transformation Program
FAD	April 2023	Tax Administration Organization
FAD	April 2023	Tax Administration Reform Strategy

In addition, technical assistance was available through regional advisors covering tax administration, public financial management, and government finance statistics.

Resident Representative

Mrs. Yulia Ustyugova assumed her position as Resident Representative in August 2021.

[1] The list does not include visits by regional advisors.

COLLABORATION WITH OTHER INTERNATIONAL INSTITUTIONS

As of March 31, 2023, Serbia has collaborations with the World Bank Group, the European Bank for Reconstruction and Development (EBRD), the European Investment Bank, and the Council of Europe Development Bank.

International Financial Institution	**Hyperlink**
The World Bank Group	https://www.worldbank.org/en/country/serbia/overview#2
The European Bank for Reconstruction and Development (EBRD)	https://www.ebrd.com/serbia.html
The European Investment Bank	https://www.eib.org/en/projects/regions/enlargement/the-western-balkans/serbia/index.htm
Council of Europe Development Bank	https://coebank.org/en/about/member-countries/serbia/

STATISTICAL ISSUES

(As of May 12, 2023)

I. Assessment of Data Adequacy for Surveillance

General

Data provision has some shortcomings while it is broadly adequate for surveillance. There are some key data shortcomings in the government finance statistics.

Statistical data improvements are ongoing. The current statistical development strategy and activities are set out in the latest quinquennial "Program of the Official Statistics 2021–2025." The European Commission (EC) in its reports on the accession negotiations with Serbia (negotiation chapter 18) provides a regular external view on Serbia's statistical systems and progress toward fully meeting the standards of the European Statistical System (ESS) and the transmission program for the European Sector Accounts 2010 (ESA 2010).

National Accounts[2]

The real sector data are compiled by the Statistical Office of the Republic of Serbia (SORS). The GDP data are compiled using expenditure and production methods. The compilation of annual national accounts is based on the principles and definitions established by the ESA 2010 as well as other relevant methodological manuals prepared by Eurostat and the IMF. Seasonal adjustments and working day corrections are made with the JDemetra+ software, which is the officially recommended software for the members of the ESS and the European System of Central Banks. Data on GDP and its components are disseminated at current prices, previous year's prices in absolute values (RSD millions), and as chain-linked volume measures (reference year 2015). Quarter-to-quarter growth rates are derived from seasonally adjusted data.

Annual and quarterly GDP data are available from the first quarter of 1995 onwards. From 1999 onwards, data coverage for the Republic of Serbia does not include Kosovo and Metohija. A GDP flash estimate is available after 30 days, the first quarterly GDP estimate at t+60 days, followed by scheduled routine revisions and benchmark revisions about every five years.[3] The last benchmark revision was published in 2018–2019, and revised the time series for 1995–2017.

Procedures for the compilation of annual GDP estimates by production are in line with internationally recommended practices. Production account estimates are compiled with an

[2] A "GDP Methodology – Sources and Methods" for annual GDP was published in March 2023 (https://publikacije.stat.gov.rs/G2023/PdfE/G202321003.pdf) and for quarterly GDP in April 2023 (https://publikacije.stat.gov.rs/G2023/PdfE/G202321004.pdf). Time series data are published here: https://data.stat.gov.rs/?caller=090202&languageCode=en-US.

[3] The National Accounts Revision Policy is published here: (https://www.stat.gov.rs/media/5461/national-accounts-revision-policy-statistical-office-of-the-republic-of-serbia.docx)

adequate methodology and at very detailed levels. Sources and method for the compilation of GDP by expenditures are in general, adequate. Reconciliation between the independent annual GDP estimates based on the production and expenditure approaches is being made at an aggregate level, although the original differences are not significant. There are no reliable independent estimates of changes in inventories and net acquisition of valuables on a quarterly basis. These components are estimated as the residual between quarterly GDP by the production approach, which is considered more reliable, and the remaining components of GDP by expenditure.

Efforts to enhance the national accounts compilation process and produce more robust and accurate GDP estimates are ongoing, including under EU funded projects in cooperation with Eurostat. The next benchmark revision of GDP is anticipated in 2024.

Price Statistics

The SORS compiles and disseminates monthly indices for consumer prices, producer prices, industrial production, as well as unit-value indices for imports and exports. Concepts and methods used to compile the CPI, as well as other price statistics, broadly reflect international standards and best practices.

Other Real Sector Statistics

A population and housing census was conducted in October 2022 and first results released in December 2022. Digital data collection helped with the quick processing of the information gathered.

The methodology of the Labor Force Survey was changed from 2021, and the data are no longer comparable with data published in the statistical data release of the same name before 2021. For comparability, revised time series data of the most important labor market indicators are available in the database on the SORS website.

An agriculture census will be conducted in 2023.

External Sector Statistics

The National Bank of Serbia (NBS) compiles monthly and quarterly balance of payments (BOP) statistics as well as quarterly international investment position (IIP) data. They are reported to STA for re-dissemination in the IFS and the Balance of Payments Statistics Yearbook. Since April 2014, BOP data have been compiled in accordance with the Sixth Edition of the Balance of Payments and International Investment Position Manual (BPM6), with data starting from Q1 2007 (BOP) and Q4 2013 (IIP). Work on further improving the quality of external sector statistics is ongoing in preparation for implementing the changes in the BPM6 methodology in 2025. Serbia participates in the Coordinated Direct Investment Survey (CDIS) but the last reported data are for 2019.

Government Finance Statistics

Monthly fiscal data on budgetary general government are compiled and published by the Ministry of Finance (MoF) on a cash basis, using a bridge table from the chart of accounts to the methodology of the Manual on Government Finance Statistics 2014 (GFSM 2014) that was developed with IMF technical assistance. GFSM 2014 data were first published in October 2021, with time series extending back to 2015. The current sector coverage captures most of the fiscally relevant general government, including the Republican budget, the local governments, the autonomous Province of Vojvodina, the four social security funds, the Putevi Srbije (Road of Serbia Fund), and Koridori Srbije (the Corridors of Serbia Fund). However, coverage is not fully in line with the definitions of central and general government in GFSM 2014. Monthly central government data exclude own resources and related expenditure of some indirect budget users like universities. Only the law on the final account of the budget, reporting annual fiscal data, includes the own resource revenues and related expenditures of the indirect budget users. General government data do not yet include extrabudgetary public agencies, other public bodies and public enterprises that have been classified by SORS as belonging to the general government sector.

Fiscal data improvements to achieve full compliance with GFSM 2014 are underway. The authorities have adopted a program—legislated in the Budget System Law—to expand the coverage of monthly cash-basis GFS data in phases and include all statistically material general government entities by 2025. This will be accomplished by bringing most central government entities directly into the Treasury Accounting system, and by Treasury setting up as needed new IT systems for regular data collection from all other general government entities. Data processing for verification, compilation, and consolidation will also be further standardized and automated, and it is intended that Treasury will take over the responsibility for fiscal data publication from the MoF's Macro-fiscal Unit. As a first step, monthly data from 2023 onward include student dormitories and other institutions providing student services, and beneficiaries of the Health Insurance Fund.

In a related move, in January 2021, SORS resumed reporting of cash-based annual revenue and expenditure data for the budgetary general government to the GFS Yearbook of the IMF Statistics Department. The data use the same data sources as used in the monthly fiscal reporting supplemented by the final annual accounts of the budget and other sources, and own resources of indirect budget beneficiaries are included.

In parallel, SORS—in collaboration with the NBS and MoF, and supported by technical assistance from the IMF and Eurostat—is improving the GFS data compilation on accrual basis, which is an integral element of the compilation of the national accounts and a requirement under the ESA 2010 transmission program. SORS provides notification tables to the EC twice a year for the excessive deficit procedure (EDP). The EC assesses[4] that progress was made in completing the questionnaire

[4] European Commission: *Serbia 2022 Report*, SWD (2022) 338 final, pp. 80 (https://neighbourhood-enlargement.ec.europa.eu/system/files/2022-10/Serbia%20Report%202022.pdf)

related to the EDP notification tables, but that the quality and completeness of the EDP notification data and the government finance statistics need to be further improved.

The Public Debt Management Agency (PDA) publishes comprehensive data on central government debt and guaranteed debt on its website as well as some elements of general government debt such as local government debt and guaranteed debt.

Since January 2019, the NBS is reporting budgetary central government debt data on loans and securities to the World Bank/IMF Quarterly Public Sector Debt Database. Although source data are available, NBS has not committed to expand reporting to cover all debt instruments and to the public sector nor even general government.

Monetary and Financial Statistics

Monetary and financial statistics are compiled by the NBS, broadly following the methodology set forth in Monetary and Financial Statistics Manual and Compilation Guide 2016 (MFSMCG), and meeting the Enhanced General Data Dissemination System (e-GDDS) recommendations with respect to periodicity and timeliness for financial sector data. Monetary data are reported to the Fund using Standardized Report Forms beginning December 2013.

The coverage of monetary statistics includes the central bank and the other depository corporations (ODCs) and could be improved by including remaining ODCs (including banks in liquidation) and other financial corporations.

Serbia reports data on several series and indicators of the Financial Access Survey (FAS), including mobile and internet banking and the two indicators (commercial bank branches per 100,000 adults and ATMs per 100,000 adults) adopted by the UN to monitor Target 8.10 of the Sustainable Development Goals (SDGs). Serbia doesn’t currently report gender-disaggregated data.

Financial Soundness Indicators are published on the NBS website[5] while Serbia has yet to submit these data for publication on the IMF website.

II. Data Standards and Quality

Serbia participates in the Enhanced General Data Dissemination System (e-GDDS), the first tier in the IMF Data Standards Initiatives aimed at promoting data transparency, and launched the National Summary Data Page, a data portal for official macroeconomic and financial statistics, on June 8, 2018.

Release calendars are available for macroeconomic statistics on the websites of the SORS, the NBS, and the MoF. The PDA publishes debt issuance data and regular monthly and quarterly reports.

A ROSC report on Fiscal Transparency was published in May 2009.

[5]Financial Soundness Indicators: https://nbs.rs/en/ciljevi-i-funkcije/finansijska-stabilnost/pokazatelji/

Serbia: Table of Common Indicators Required for Surveillance

(As of May 12, 2023)

	Date of latest observation	Date received	Frequency of data [4]	Frequency of reporting [4]	Frequency of publication [4]
Exchange rates	May 12, 2023	May 12, 2023	D and M	D and M	D and M
International reserve assets and reserve liabilities of the monetary authorities [1]	April 2023	May 12, 2023	D	W	M
Reserve/base money	May 2023	May 5, 2023	D and M	W and M	W and M
Broad money	March 2023	April 27, 2023	M	M	M
Central bank balance sheet	March 2023	April 27, 2023	M	M	M
Consolidated balance sheet of the banking system	March 2023	April 27, 2023	M	M	M
Interest rates [2]	May 5, 2023	May 8, 2023	D	D	D
Consumer price index	April 2023	May 12, 2023	M	M	M
Revenue, expenditure, balance and composition of financing – general government	March 2023	May 5, 2023	M	M	M
Revenue, expenditure, balance and composition of financing – central government	March 2023	May 5, 2023	M	M	M
Stocks of central government and central government-guaranteed debt [3]	March 2023	May 4, 2023	M	M	M
External current account balance	February 2023	April 19, 2023	M	M	M
Exports and imports of goods and services	February 2023	April 19, 2023	M	M	M
GDP/GNP	2022, Q4	February 28, 2023	Q	Q	Q
Gross external debt	March 2023	April 30, 2023	M	M	M
International investment position [5]	March 2023	April 30, 2023	Q	Q	Q

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Including currency and maturity composition.
[4] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Semi-annually (SA), Annually (A), Irregular (I), or Not Available (NA).
[5] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

Statement by Mr. Marcel Peter, Executive Director for the Republic of Serbia
June 23, 2023

Driven by firm political resolve and supported by successive arrangements with the Fund, Serbia recorded an impressive economic performance over most of the previous decade. Standards of living improved, employment grew steadily, and macroeconomic imbalances were effectively addressed. These economic gains were made possible by broad macroeconomic policy improvements that stabilized the economy, lowered inflation, consolidated public finances, and strengthened resilience.

Since 2015, Serbia has benefited from continuous engagement with the Fund, first through a precautionary Stand-By Arrangement (SBA), followed by two consecutive Policy Coordination Instruments (PCI). Over this period, a substantial fiscal adjustment lowered the public debt-to-GDP ratio from about 76 percent to slightly above 55 percent at present, notwithstanding the Covid-19 and energy price shocks. These results and the strong track record of reform implementation testify to the authorities' resolve, prudent approach to macroeconomic policy making, and capacity to implement difficult reforms.

The Serbian economy weathered the Covid-19 shock well, bolstered by an early and resolute policy response and sizable policy buffers. Post-pandemic economic policy was geared toward restoring buffers, most notably by continuing consolidation efforts, while attracting FDI and addressing lingering pandemic-related scarring. The authorities concur that the reforms implemented under the successive Fund-supported programs over the past eight years are yielding dividends in terms of stability, growth, and capacity to deal with future shocks.

The current SBA is key to help bridge transitory balance of payments (BOP) and budget financing needs. The sharp rise in energy prices, global inflationary pressures, regional and global uncertainty, and the substantial tightening of global credit conditions, compounded by unexpected shortcomings in domestic electricity production, resulted in rising BOP and fiscal financing pressures in 2022. These events prompted the authorities' decision to cancel the PCI and request a two-year SBA with the Fund—the first Fund financing arrangement in more than a decade. The program's four-pronged objectives hinge on stabilizing and addressing the shortcomings and structural deficiencies in the Serbian energy sector, while facilitating the resolution of macroeconomic imbalances and restoring macroeconomic stability. The authorities consider that the SBA remains instrumental in guiding reforms and overseeing policy implementation, especially under the currently prevailing uncertainty.

Fiscal policy

The authorities concur that continued tight fiscal policy is needed to help contain inflationary pressures, further reduce public debt, and, over the medium term, align fiscal policy with the fiscal rule. At the same time, given the current headwinds and prevailing uncertainty, they see a need for flexible policy implementation and smoothing the impact of the cost-of-living crisis on vulnerable populations, commensurate with the available fiscal space and in line with program objectives. Strong revenues in the first half of the year, paired with lower-than-planned budgetary outlays for energy imports as a result of a benign winter and a decline in regional energy prices, created space for targeted spending measures of about 0.9 percent of GDP, including (i) an increase in wages for teachers and nurses by 5.5 percent (to address structural imbalances in public wages), (ii) higher agricultural subsidies, and (iii) an increase in public pensions by 5.5 percent aimed at cushioning the impact of eroding real incomes on this vulnerable group. As some of these measures will be permanent, the authorities plan to adjust the excise policy going forward to generate additional revenue of about 0.4 percent of GDP.

Notwithstanding the increase in current spending addressing the cost-of-living situation, an overall restrictive fiscal stance in 2023 will contribute to a tight policy mix and to taming inflation. The fiscal outturn is projected to be below the revised target of 3 percent of GDP, about ⅓ of a percentage point lower than envisaged at SBA approval, implying a negative fiscal impulse of about 0.4 percent of GDP. Under the conservatively projected baseline, the public debt ratio will remain on a firm downward path over the course of the program and will decline to about 53 percent by the end of 2024. Over the medium term, the fiscal path will be guided by a revamped deficit-based fiscal rule that also incorporates a debt anchor.

On the back of moderate public debt and a prudent borrowing strategy, the government's gross financing needs remain manageable. Supported by liability management operations, an extended maturity of new bond placements, and an improved currency composition of debt—implemented before the tightening of external credit conditions—the gross financing needs declined from about 11 percent in 2019 to below 9 percent at present and are projected to decline further over the medium term. Serbia successfully tapped the international sovereign debt market in February, raising USD 1.75 billion in a heavily oversubscribed issuance. The 2023 fiscal financing is further supported by the 2022 USD 1 billion bilateral loan from the UAE, budgetary support from IFIs—including the World Bank, KfW, ADF, and the Fund—as well as high government deposits.

Continued implementation of structural fiscal reforms is critical to support program objectives. Key reforms include (i) advancing e-fiscalization and digitization of tax administration, supported by the World Bank and Fund TA, (ii) further strengthening public investment management, and (iii) further enhancing public sector employment and the payroll system "Iskra" to include the health sector. In addition, fiscal rules will be underpinned by a reassessment of the coverage of the general government sector and improved statistics, supported by Fund TA.

Energy sector policies

Addressing shortcomings in the Serbian energy sector and limiting the related fiscal risks remain key pillars of the program. A decline in regional energy prices and restored electricity generation allowed for a substantial reduction of budget transfers to energy SOEs. The cash flows of these companies benefited from two consecutive increases in gas and electricity tariffs, lower energy prices and imports, restored electricity production, and new generation capacity. During the winter, EPS—the SOE responsible for electricity generation and distribution—recorded a net export of electricity, as opposed to large and expensive imports over 2022. The authorities agree on the need to continue raising energy tariffs to levels that secure cost recovery.

The authorities are well aware that sectoral reforms and the restructuring of energy SOEs will be critical to ensure a stable supply, minimize energy security risks, and foster green energy generation. The government recently adopted a new law on ownership management for SOEs, changed the legal status of EPS to become a joint-stock company, and appointed a new supervisory Board of EPS, including three international experts. These measures are key to strengthening EPS governance and aligning it with the OECD guidelines on corporate governance, thus paving the way for modernizing the company's management and operations. Concurrently, the government adopted a new energy investment plan, to be published as a part of the Energy Sector Development Strategy, aimed at enhancing energy security and stabilizing electricity production. This investment plan is fully costed for the first two years, with clearly delineated investments and financing needs between the government, SOEs, and the private sector.

Monetary policy and financial sector

Following its peak in March, headline inflation continued to decline, reaching 14.8 percent y-o-y in March, in line with the projections of the National Bank of Serbia (NBS). After a pause in raising the key reference rate in May, the monetary council of the NBS resumed the tightening cycle in June, increasing the key reference rate by 25 basis points to 6.25 percent. Since January, the reference rate has been cumulatively increased by 125 basis points. The rate hike aimed at anchoring inflation expectations while ensuring a downward path of inflation and its return to within the target band by mid-2024. Core inflation in May fell more than headline inflation, to 10.4 percent, reflecting still high food price inflation and a relatively large weight of food in the consumption basket. The authorities note that the relative stability of the exchange rate is a key factor in curbing core inflation and keeping it well below headline inflation. Furthermore, the ongoing monetary tightening by the ECB is positively contributing to the NBS' disinflation efforts as it is translated into higher interest rates on euro-indexed loans in Serbia.

International reserves are high and projected to exceed 140 percent of the Fund's ARA metric by the end of the year. The Serbian dinar has been exposed to almost continuous appreciation pressures since May 2022. Over the first four months of 2023, the NBS purchased more than one billion euros on the FX market and further strengthened FX reserves, which stood at EUR 21.6 billion at the end of April. International reserves are projected to exceed 140 percent of the Fund's ARA metric by year-end.

The Serbian financial sector is dominated by banks, which remain resilient and profitable, with strong balance sheets, ample liquidity, and low shares of non-performing loans. However global headwinds, tightening monetary conditions, and potential adverse spillovers call for enhanced vigilance. The authorities are well aware of these risks and are closely monitoring developments related to banks' liquidity, deposits, and asset quality, while further strengthening the already robust banking supervision.