

ECONOMIC CRITERIA

I Macroeconomic data

1. Please briefly comment on the main macroeconomic trends during the period 2000-2009¹⁹, based on the data requested in the attached tables 1-7²⁰:

a) real GDP growth and its breakdown by expenditures;

Having achieved real GDP growth of 5.3% in 2000 and 5.6% in 2001, GDP growth slowed down in 2002 (3.9%) and in 2003 (2.4%), while in 2004 GDP growth was recorded at the rate of 8.3%, which is at the same time the highest recorded rate in the observed period. After that, from 2005 to 2008 GDP growth was relatively equalized and amounted to 5.6%, 5.2%, 6.9% and 5.5% respectively. During 2009, there was a significant fall in the GDP and the growth rate amounted to -3.1%, which reflects the effects of the global economic crisis. Data pertaining to aggregates of GDP usage at constant prices are not available in the Republic Statistical Office. The preparation of such data is in progress and the work is expected to be completed by the end of 2011

*(*See Annex)*

b) inflation (including core inflation);

From 2000 until 2002, headline and core inflation rates were extremely high (over 70%). Starting from 2003 until present day, average annual inflation rate was around 11.1%. During this period, core inflation rate was below headline inflation rate, with exception of 2004. Starting from 2009, the NBS has started to target headline inflation, measured as the percentage change in the consumer price index (CPI).

*(*See Annex)*

c) general government deficit and debt and its breakdown by government level;

*(*See Annex)*

d) general government expenditure and revenue and its breakdown by categories;

*(*See Annex)*

e) selection of monetary and financial indicators;

In compliance with the growth of economic activity, money supply recorded constant growth; however, with spill over of the effects of the global financial crisis to Serbia at the end of 2008, such developments were completely reversed. Even after the effects of the crisis faded away, the money supply does not record signs of significant recovery.

Up until 2008, growing aggregate demand was supported with loans disbursed to the private sector, which recorded a very dynamic growth, particularly in the retail sector. Also, since 2006 companies were directly taking increasing number of cross-border loans. The crisis

¹⁹ To the extent that data are available, otherwise up to the most recent year for which data, even if estimates, are available. Please ensure consistency of the data in the tables with the data used in the text, when referring to the relevant indicators.

²⁰ To the extent that data are available, otherwise up to the most recent year for which data, even if estimates, are available. Please ensure consistency of the data in the tables with the data used in the text, when referring to the relevant indicators.

resulted in reduced availability of both, domestic and foreign funds. Even then, only slowdown, but not real reduction of credit activity recorded. Speeding up of the credit activity started again in the end of 2009, while the companies continued to net repay their foreign debt.

f) evolution of the real and nominal effective exchange rates;

Nominal effective exchange rate of the dinar²¹ in the observed period had depreciating trend. Due to relatively higher inflation rate in Serbia compared to the eurozone and the USA, the real effective exchange rate of the dinar had appreciation trend from 2000 until 2008, while in the last two years, due to higher nominal depreciation of the dinar (caused by the reduced capital inflow as a result of the global financial crisis) than the inflation differential, the real effective exchange rate has depreciated.

(*See Annex)

g) balance of payments, including trade and current account, capital and financial account and the external financing requirements.

Until 2009, balance of payments developments in Serbia were characterized by high and growing current account deficit as of the end of 2008. The current account deficit fluctuated from 7.8% of GDP in 2003 to 21.1% of GDP in 2008. Such developments were caused by rapid growth of exports and imports, where growth of imports was more rapid than growth of exports, stimulated by significant volume of foreign direct investments, growth of long-term loans from abroad and growth of remittances (current transfers). That also contributed to significant growth of foreign exchange reserves of the NBS, which ensured stability and occasional appreciation of the dinar exchange rate in the managed floating exchange rate regime.

The spill over effects of the economic and financial crisis in 2009 brought to the Serbian economy changes in the balance of payments developments. . The current account deficit was drastically decreased to 7% of GDP, due to more rapid fall of imports than the fall of exports, caused by the fall in the foreign demand, consumption and wages, as well as by fall of foreign direct investments and long-term borrowing from the abroad, while income on remittance was slightly increased. Such developments resulted in more intensive interventions of the NBS in the foreign exchange market and depreciation of the dinar exchange rate.

(*See Annex)

Please provide the last year's official report on the macro-economic developments in English.

(*See Annex) – Analysis of Macroeconomic and Fiscal Developments in 2009

II Socio-economic data

2. Please provide and briefly comment on the following data for the period 2000-2009:

a) GDP per capita in Power Purchasing Standards (PPS, in % of the EU27 average);

²¹ Weighted rates: from 2000 until 2005 - 0.7 for euro and 0.3 for dollar, from 2006 until 2010 - 0.8 for euro and 0.2 for dollar.

Serbia has participated in the European PPS Project since 2005. Data provided herein are comparable to all countries participating in the Project. Purchasing power per capita has been increasing in the observed period.

GDP per capita in Power Purchasing Standards (PPS, in % of the EU27 average);

| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
|---------------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| GDP, total, millions EUR | 25,538 | 12,820 | 16,028 | 17,305 | 19,026 | 20,305 | 23,304 | 28,784 | 33,417 | 29,967 |
| in % of the EU27 average | | | | | | | 33 | 33 | 37 | 37 |
| GDP per capita, PPS | ... | ... | ... | ... | ... | 7,100 | 7,700 | 8,300 | 9,000 | 8,800 |

b) population by sex, age and regional distribution;

Overview of population per requested characteristics is presented in Annex

c) labour market indicators: economic activity rates, employment rates and unemployment rates, long-term unemployment rate, training by education, sex, age, also in terms of regional divergences.

Table with economic activity rate (working population), employment and unemployment rate, long-term unemployment rate, professional trainings related to education level, gender, age, including regional differences is included in Annex.

TRAININGS FOR UNEMPLOYED PERSONS ORGANISED BY NATIONAL EMPLOYMENT SERVICE

| TRAININGS | Number of persons involved | Women | Education level | | | | | | | | Age | | | |
|-------------|----------------------------|-------|-----------------|-----|-----|-------|----|-----|-----|------|----------|----------|----------|---------|
| | | | I | II | III | IV | V | VI | VII | VIII | under 25 | 26 to 30 | 31 to 50 | over 50 |
| 2007 | 6.687 | 4.358 | 985 | 533 | 934 | 2.825 | 40 | 627 | 742 | 1 | 1.718 | 1.666 | 3.021 | 282 |
| 2008 | 3.976 | 2.194 | 502 | 63 | 677 | 1.728 | 16 | 504 | 484 | 2 | 1.048 | 1.090 | 1.629 | 209 |
| 2009 | 3.365 | 2.154 | 289 | 65 | 488 | 1.417 | 28 | 461 | 617 | 0 | 777 | 1.012 | 1.453 | 123 |

Source: National Employment Service

III Structural indicators

3. Please provide and briefly comment on the following indicators for the period 2000-2009:

a) sectoral economic structure (as a share of GDP and employment);

*(*See Annex)*

b) structure of enterprise ownership including an estimate of the capital stock, distinguishing between public and private capital;

The structure of the share of private and state capital is laid out in the table in Annex, pursuant to the data contained in the Register of Business Entities, which has the role of a centralized, electronic database on business entities since January 1st 2005 within the Serbian Business Registers Agency,

Overview of data is presented per years, starting from 2007, since during 2005 and 2006 the procedure of transferring business entities was still underway.

As of 3rd December 2010, there were 1.835 registered active business entities, out of 110,635 active business entities in the Republic of Serbia, in which holding of state capital was registered.

The stated record does not include joint stock companies in which the Republic of Serbia or local self-government units are the holder of shares, given that ownership over shares is recorded with the Central securities depository clearing house, while only data on total share capital is recorded with the Register of Business Entities.

c) national research capacity (in terms of research infrastructure and human resources funding of national research in terms of gross domestic expenditure on research and development and relative to GDP (see also chapter 26 – Education and culture);

As of the end of February 2010, the Government of the Republic of Serbia adopted "The National Strategy of Science and Technological Development of the Republic of Serbia for the period 2010-2015", which is one of the primary defined objectives – growth of investments into science. Actions plans for each of the research priorities have been highlighted (emphasized), and investments into science and technological development, contained in the Strategy, are the following:

Realistic plan for growth of budget appropriations for science and technological development in the next five years stipulates the annual growth rate of 0.15% of GDP. With this pace, the budget appropriations will reach 1.05% by 2015, when this Strategy will cease to be valid. This is a realistic objective that will be achieved with considerable delay: in 2003, it was planned that the percentage of budget appropriations for science of 1% of GDP will be achieved until 2007.

However, the most important contribution to investments in science will stem from the loan of the European Investment Bank, ratified in the National Assembly of the Republic of Serbia on May 15th 2010 (it was approved by the Board of Directors of the mentioned bank on December 14th 2009), as well as from EUR 25 million for science and tertiary education from the IPA funds, approved by the EU. Along with other sources, this constitutes the core of the largest investment cycle into scientific and technological infrastructure. In addition to these additional sources, it is expected that as early as 2010 the percentage of budget appropriations in science will reach 0.5-0.6% of GDP.

It is estimated that the total investments into science in the Republic of Serbia does not exceed 0.5% of GDP, which still puts the Republic of Serbia among the countries with least investments into science, both among the developed countries and among the regional countries.

In the period 2000-2010, after the painful recession period of the 1990s, the budget appropriations for science in the Republic of Serbia have been increased significantly in gross amounts, from modest EUR 28 million in 2001 to around EUR 100 million in 2008.

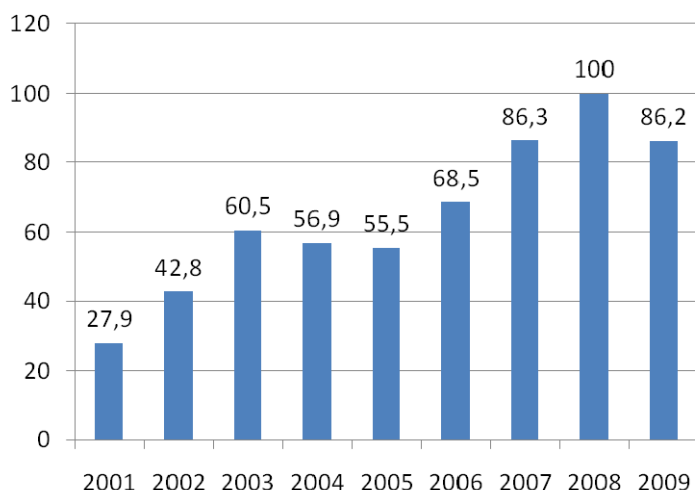


Chart 1.1. Budget appropriations for science (in millions of EUR without the National Investment Plan) (Source: Laws on the Budget System of RS).

During the seven-year period (2001-2008), the wages of researchers were increased several times, and almost EUR 30 million was invested into capital equipment for scientific researches. Nevertheless, when share of science in the GDP is observed, such share was 0.3% of GDP in 2003 and it continued to stagnate on that level until present day (Chart 1.2)

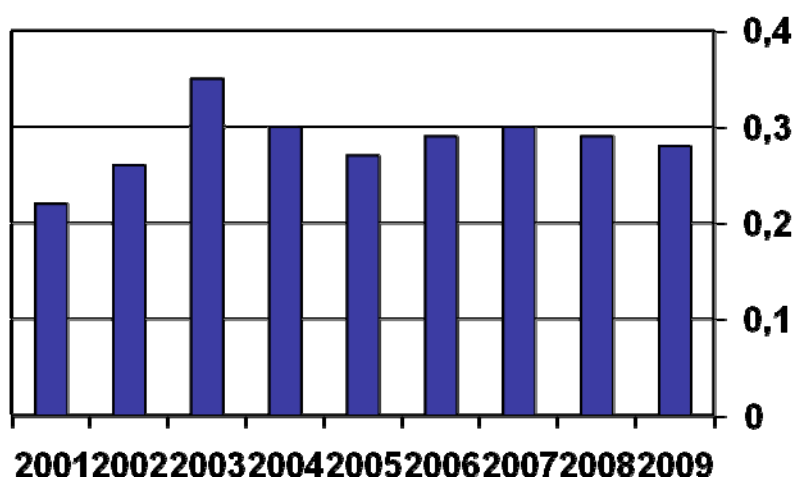


Chart 1.2. Budget appropriations in science (in % of GDP) (Source: Laws on Budget System of RS).

In addition to the budget funds of the Republic of Serbia, which are used for financing projects of the Ministry of Science and Technological Development (MSTD), there are other sources of funds for investments in science in the Republic of Serbia. There are also modest budget appropriations for science and technology in other ministries and public administration bodies, as well as in the Autonomous Province of Vojvodina.

In 2008, RSD 23 billion were allocated from the budget of the Republic of Serbia for financing higher education institutions. Scientific institutions generate income through cooperation with undertakings, and it is estimated that in 2008 income of institutions in addition to the budget of MSTD was around RSD 12.5 billion. Higher education institutions have also generated around RSD 12 billion from own income.

There is no accurate assessment of investments of the private sector in scientific and technological research. Scientific institutions and higher education institutions also participate in international programmes.

d) labour productivity; evolution by economic sectors;

In the period 2001-2008 the Serbian economy generated high real growth rates of labour productivity²² - on average of 7.8% annually. In the same period GVA was rising at an average real annual growth rate of 4.7%, while employment was falling at the rate of 2.9% annually. Labour productivity in Serbia recorded a drop (-0.2%) for the first time during the crisis year of 2009 due to a larger drop of GVA (-2.6%) than the drop of employment (-2.2%).

The sector-based analyzing suggests that in 2009 the crisis affected most Construction (the real growth rate of -10.4%), Manufacturing industry (-7.6%) and Wholesale and retail trade (-5.9%); those were the sectors that at the same time recorded the steepest GVA decline. In the sector of Financial intermediation the rise of employment (11.9%) was considerably higher than GVA growth (4.3%), which had negative effects on labour productivity (-6.8%). Regardless of worsened economic environment, labour productivity was improved in Agriculture (8.1%) and Transport, storage and communication (8.2%) but at a lower employment rate.

Real Growth Rates of Labour Productivity

| | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
|--------------------------------------------|------------|------------|-------------|------------|-------------|-------------|------------|-------------|
| SERBIA TOTAL | 5,0 | 5,3 | 10,3 | 7,0 | 11,7 | 9,3 | 6,2 | -0,4 |
| Agriculture and fishing | 2,0 | 1,1 | 26,4 | 2,4 | 9,3 | -0,7 | 20,9 | 8,1 |
| Industry | 5,9 | 3,0 | 14,9 | 5,9 | 14,1 | 11,5 | 6,4 | -5,3 |
| Mining and quarrying | 7,6 | 8,7 | 3,7 | 8,7 | 11,9 | 21,7 | 5,4 | -0,3 |
| Manufacturing | 6,1 | 1,4 | 18,1 | 5,0 | 15,4 | 12,6 | 7,1 | -7,6 |
| Electricity, gas and water supply | 1,0 | 4,1 | 1,1 | 7,4 | 6,5 | -0,7 | -0,2 | 0,2 |
| Construction | -1,6 | 14,1 | 4,5 | 2,2 | 10,9 | 14,4 | 4,8 | -10,4 |
| Services | 4,3 | 5,7 | 4,4 | 9,7 | 11,4 | 10,0 | 4,4 | 0,0 |
| Wholesale and retail trade, repairs | 16,9 | 12,4 | 13,1 | 24,1 | 14,2 | 20,8 | 5,1 | -5,9 |
| Hotels and restaurants | 6,3 | 16,8 | 7,6 | 0,4 | 0,2 | 9,2 | 3,8 | -4,1 |

²² Labour productivity is defined as gross value added at constant prices in 2002 per employee (private entrepreneurs are not included, or persons conducting self-employed activity and their employees).

| | | | | | | | | |
|---------------------------------------------------|------|------|------|------|------|------|------|------|
| Transport, storage and communication | 5,0 | 13,4 | 16,1 | 26,7 | 36,1 | 21,3 | 13,2 | 8,2 |
| Financial intermediation | 28,4 | 3,6 | 9,9 | 12,4 | 9,5 | 13,0 | 6,2 | -6,8 |
| Real estate, renting and business services | 1,9 | 5,0 | -5,5 | -3,2 | -2,3 | 3,1 | -5,8 | -4,9 |
| Other services | -0,9 | 1,1 | -0,5 | 0,2 | 0,5 | -0,5 | -0,2 | 0,3 |

Source: Calculations of the Republic Development Bureau (RDB) based on the data from the Republic Statistical Office (RSO).

Sources of data needed for the calculation of annual business performance indicators of enterprises are combined. In addition to statistical survey conducted for large and medium-sized enterprises, administrative data sources are also used (annual financial statements data and tax data).

The Value Added per Person employed (Labour Productivity) in thousands RSD

| | 2006 The Republic of Serbia | 2007 The Republic of Serbia | 2008 The Republic of Serbia | 2009 * The Republic of Serbia |
|--------------------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|-------------------------------------|
| Total | 743,0 | 951,4 | 1123,3 | 1216,4 |
| Mining and quarrying | 937,9 | 975,4 | 1183,9 | 1489,5 |
| Manufacturing | 609,4 | 781,0 | 935,8 | 972,8 |
| Electricity, gas and water supply | 1306,7 | 1397,5 | 1608,9 | 1931,6 |
| Construction | 963,2 | 1181,0 | 1441,1 | 1530,0 |
| Wholesale and retail trade, repairs | 686,3 | 940,7 | 1081,1 | 1041,9 |
| Hotels and restaurants | 386,5 | 478,7 | 563,5 | 595,7 |
| Transport, storage and communication | 972,6 | 1226,8 | 1404,4 | 1771,0 |
| Real estate, renting and business services | 762,3 | 1080,6 | 1257,3 | 1343,7 |

Source of data is Annual Structural Survey on Enterprises.

** Previous data*

Source of data is Annual Structural Research on Operations of Undertakings.

** Prior data*

e) unit labour costs, including indicators of international competitiveness (changes in relative unit labour costs, level and changes in average gross earnings, etc.);

Unit labour costs (ULC) represent an average price of labour per production unit expressed as the ratio of gross earnings and GDP, i.e. we compare the value disbursed to an employee for their work and the value generated by the employee. Higher values of ULC suggest that the rise of employees' remuneration exceeds the rise of value generated by them, which puts pressure on producer prices and leads to deterioration of international competitiveness.

In the entire observed period 2003-2009 GDP per employee was rising at an average annual rate of 6.0% but in 2009 the rise was considerably lower. Moreover, average gross earnings demonstrate the same tendencies. However, while in the period 2003-2007 the rise of average gross wages was faster than the rise of GDP per employee, which influenced the ULC rise as well, since 2008 slow growth rates of gross earnings per employee and negative ULC growth rates suggest that Serbia's competitiveness is improving.

Real Growth Rates and GDP Levels per Employees, Average Gross Wages and ULC

| | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
|-------------------------------|-------|-------|-------|-------|-------|-------|------|
| GDP per employee | | | | | | | |
| Growth rate, % | 3,7 | 7,8 | 4,7 | 7,5 | 8,1 | 5,7 | 2,5 |
| <i>In 2003 = 100</i> | 100,0 | 103,9 | 100,9 | 103,6 | 104,3 | 101,9 | 98,9 |
| Average Gross Wages | | | | | | | |
| Growth rate, % | 14,0 | 11,1 | 6,8 | 11,4 | 14,1 | 3,9 | 0,2 |
| <i>In 2003 = 100</i> | 100,0 | 97,5 | 93,7 | 97,7 | 100,1 | 91,1 | 87,9 |
| ULC | | | | | | | |
| Growth/decline rate, % | 9,9 | 3,1 | 2,0 | 3,7 | 5,5 | -1,7 | -2,3 |
| <i>In 2003 = 100</i> | 100,0 | 93,8 | 92,8 | 94,3 | 96,0 | 89,5 | 88,9 |

Source: Calculation of RDB based on the data from RSO

Relative ULC of Serbia represents the ratio of ULC of a country and ULC of Serbia. The rise of relative ULC reflects the growth of Serbia's competitiveness compared to the country of reference, and vice versa. Serbia's competitiveness had deteriorated by 2008 compared to Bulgaria, Slovenia, Croatia, and, to a lower degree, Hungary, which is indicated by declining ULC. In the markets of Macedonia (where Serbia continues to record a constantly positive foreign trade balance) and Romania, the competitiveness of Serbian products continued to rise. During the crisis-laden 2009 values of relative ULC significantly increased. This goes to affirm that the crisis hit harder the observed countries than Serbia, while the next period and the end of the crisis will show whether in this case we could talk about genuine improvement of the competitive position of Serbian economy.

Relative Unit Labour Costs (Serbia = 100)

| | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
|-----------|-------|-------|-------|-------|------|------|------|
| EU 27 | -0,04 | -2,1 | 3,3 | 4,6 | -0,1 | -0,2 | 4,5 |
| Bulgaria | 0,2 | -5,6 | 7,2 | 13,6 | 1,3 | -2,0 | 9,9 |
| Hungary | 0,1 | -1,5 | -5,5 | 7,2 | -0,1 | -0,3 | -5,7 |
| Romania | -0,2 | -14,8 | -44,9 | 19,2 | 0,4 | 0,3 | 10,2 |
| Slovenia | -0,1 | 0,4 | 3,8 | 3,8 | -0,4 | -1,1 | 11,9 |
| Croatia | -0,9 | 9,2 | 2,2 | 37,8 | -0,2 | -0,7 | 6,3 |
| Macedonia | 0,3 | -13,7 | 46,2 | -23,2 | -2,9 | 1,9 | -1,1 |

Source: Calculation of RDB based on the data from Eurostat and RSO

Unit Labour Cost Indexes

| | Unit Labour Costs | |
|------|-------------------|-------------|
| | Unit cost | Chain index |
| 2000 | 0.45 | |
| 2001 | 0.49 | 107.1 |
| 2002 | 0.54 | 111.8 |
| 2003 | 0.57 | 105.7 |
| 2004 | 0.57 | 99.2 |
| 2005 | 0.56 | 98.4 |
| 2006 | 0.58 | 102.9 |
| 2007 | 0.57 | 99.0 |
| 2008 | 0.56 | 97.5 |
| 2009 | 0.56 | 101.5 |

Average Wages and Average Wage Indexes

| | RSD | |
|-------|-----------------------|---------------------|
| | Average wages (gross) | Nominal chain index |
| 2000 | 3799 | 190.7 |
| 2001 | 8691 | 228.8 |
| 2002 | 13260 | 152.6 |
| 2003 | 16612 | 125.3 |
| 2004 | 20555 | 123.7 |
| 2005 | 25514 | 124.1 |
| 2006 | 31745 | 124.4 |
| 2007 | 38744 | 122.0 |
| 2008 | 45674 | 117.9 |
| 2009* | 44147 | 108.8 |

Source: Monthly statistical survey on employed persons and their wages and salaries (RAD-1 form)

* As of January 2009, the sample of monthly research on earnings of employees has been expanded to include earnings of employees with entrepreneurs, taken from the Ministry of Finance (Tax Administration).

f) percentage of the working population which received higher secondary education;

Percentage of the working population which received higher secondary education;

| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
|---------------|------|------|------|------|------|------|------|------|------|------|
| Employees 15+ | 48.1 | 49.9 | 49.9 | 50.1 | 54.7 | 56.1 | 57.3 | 56.9 | 55.6 | 55.9 |

Source: Labour Force Survey

g) number of pupils in primary, lower secondary, higher secondary and tertiary education;

Pupils and students within the Education System of the Republic of Serbia, 2000-2010

| | Primary Education I- IV | Primary Education V - VIII | Secondary Education | Tertiary Education |
|---------|------------------------------------|---------------------------------------|----------------------------|---------------------------|
| 2000/01 | 344346 | 367608 | 323490 | 194198 |
| 2001/02 | 338950 | 357424 | 314556 | 182941 |
| 2002/03 | 332730 | 347710 | 310235 | 197322 |
| 2003/04 | 329234 | 328836 | 302612 | 203909 |
| 2004/05 | 324913 | 334630 | 297708 | 218368 |
| 2005/06 | 312514 | 329098 | 293711 | 229355 |
| 2006/07 | 297813 | 324749 | 290387 | 238710 |
| 2007/08 | 289785 | 320293 | 288163 | 237598 |
| 2008/09 | 282395 | 315713 | 288112 | 235940 |
| 2009/10 | 283161 | 303986 | 286844 | 226772 |

h) percentage of employed persons receiving training; total number having received training and their share in the total number of employees, if possible by branch of activity; number of companies having provided training of their employees and their share in the total number of companies. Please also explain the methodology used to collect/elaborate the data;

Institution in charge of creating, monitoring and evaluation of employment policy at the national level is the Ministry of Economy and Regional Development – Department for Employment, which possesses solely data on trainings for the unemployed, and/or extra-education programmes and trainings regarding acquisition of knowledge and skills for conduct of activities within his/her profession, activities performed within the post, vocational education (interns and volunteers), retraining courses, primary education of adults, financing talented individuals etc.

The overview also includes effects of all measures of active employment policy through the National Employment Service (NES):

| | Active Employment Policy Measures | No of Persons Included in 2007 | | | No of Persons Included in 2008 | | |
|--|-----------------------------------|-----------------------------------|-------|------------------------|-----------------------------------|-------|----------|
| | | Total | Women | Employed ²³ | Total | Women | Employed |

²³ Number of employed persons can be monitored 6 months after completion of the programme; hence, it is not possible to provide accurate data.

| | | | | | | | |
|----|-----------------------------|-------|-------|-------|-------|-------|-------|
| | | | | | | | |
| 1 | Primary Education of Adults | 140 | 59 | / | 101 | 53 | / |
| 2. | Interns | 1,456 | 786 | 1,456 | 2,140 | 1,164 | 1,412 |
| 3. | Volunteers | 6,145 | 4,227 | 1,800 | 3,822 | 2,484 | 792 |
| 4. | Talented individuals | 123 | 87 | / | 92 | 70 | 38 |
| 5. | Trainings | 2,128 | 1,615 | 1,480 | 1,314 | 788 | 1,114 |
| 6. | Retraining programmes | 4,468 | 2,668 | | 2,410 | 1,231 | |

h) past and present number of students abroad.

Citizens of the Republic of Serbia study abroad on multiple bases. The Ministry of Education does not have data on the total number of students studying abroad in one school year, because such type of record is not kept.

Each year, a number of students continue their education abroad, by applying directly to foreign universities and enter into bachelor, master or doctoral studies. These students finance their studies on their own, with no obligation to inform any public authority of their departure abroad for educational purposes, nor they need to ask consent for such purposes.

Small number of students applies for scholarships of foreign governments and foundations that are approved via the Ministry of Education. Such scholarships are received by 15 to 20 students annually.

Young Talents Fund, with the Ministry of Youth and Sports, provides scholarships for studies abroad to the most successful students. Scholarship in the net amount of RSD 1,250,000 was received by 97 students in 2008, while 151 students received net amount of RSD 673,000 in 2009, and 323 students received net amount of RSD 597,000 in 2010.

IV The wage bargaining process and the social security system

(see also chapter 19 – Social Policy and Employment - for detailed questions)

4. Please provide quantitative and/or qualitative information for the period 2000-2009 on the following:

a) development of the average gross and net wages in the public and private sector, respectively;

Average Wages (gross) and Average Wages without Taxes and Contributions (net) in the Public and Private Sector

| | RSD | | | | Nominal indexes | | | |
|------|---------------|----------------|---------------|----------------|-----------------|----------------|---------------|----------------|
| | Gross Wages | | Net Wages | | Gross Wages | | Net Wages | |
| Year | Public sector | Private sector | Public sector | Private sector | Public sector | Private sector | Public sector | Private sector |
| 2002 | 16735 | 13634 | 11666 | 9451 | | | | |
| 2003 | 21288 | 17042 | 14757 | 11847 | 127.2 | 125 | 126.5 | 125.4 |

| | | | | | | | | |
|-------------|-------|-------|-------|-------|-------|-------|-------|-------|
| 2004 | 25725 | 20286 | 17662 | 14006 | 120.8 | 119 | 119.7 | 118.2 |
| 2005 | 30589 | 24491 | 20876 | 16852 | 118.9 | 120.7 | 118.2 | 120.3 |
| 2006 | 36996 | 31710 | 25232 | 21794 | 120.9 | 129.5 | 120.9 | 129.3 |
| 2007 | 45379 | 36229 | 32392 | 26120 | 122.7 | 114.3 | 128.4 | 119.8 |
| 2008 | 52281 | 39897 | 37284 | 28854 | 115.2 | 110.1 | 115.1 | 110.5 |
| 2009 | 54507 | 40921 | 38885 | 29587 | 104.3 | 102.6 | 104.3 | 102.5 |

*** Data pertain only to legal persons.**

b) formation of public sector wages and employment;

Wages and Employment

| Public Sector Wages and Employment | | | | Indexes | | |
|------------------------------------|--------------------|-----------|-------------------------------|-----------------------|-----------|--------------------------------|
| Year | Average wages, RSD | | No of employees, in thousands | Nominal chain indexes | | Chain index of no of employees |
| | Gross wages | Net wages | | Gross wages | Net wages | |
| 2002 | 16735 | 11666 | 507 | ... | ... | ... |
| 2003 | 21288 | 14757 | 507 | 127.2 | 126.5 | 100.1 |
| 2004 | 25725 | 17662 | 509 | 120.8 | 119.7 | 100.3 |
| 2005 | 30589 | 20876 | 505 | 118.9 | 118.2 | 99.2 |
| 2006 | 36996 | 25232 | 481 | 120.9 | 120.9 | 95.1 |
| 2007 | 45379 | 32392 | 477 | 122.7 | 128.4 | 99.2 |
| 2008 | 52281 | 37284 | 483 | 115.2 | 115.1 | 101.2 |
| 2009 | 54507 | 38885 | 477 | 104.3 | 104.3 | 98.9 |

Source: monthly statistical research on employees and wages of employees

c) formation of public administration wages and employment;

Until February 4th 2003, the Republic of Serbia existed within the Federal Republic of Yugoslavia. By Decision on Declaration of the Constitutional Charter, it was transformed into the State Union of Serbia and Montenegro which took over more than 689 federal-level employees.

On March 27th 2006, the Republic of Serbia became an independent state, and number of employees began to increase in the Ministry of Foreign Affairs, Office for Human and Minority Affairs, Coordination Centre for Kosovo, Coordination Body for Presevo, Bujanovac and Medvedja, Administration for Joint Services, Airline Service etc. Total of 2,883 employees were taken over from the federal level to authorities of the Republic of Serbia.

Executive and Legislative Branches of Government

The Law on Public Servants (*Official Gazette of RS*, No. 79/05, 81/08,... and 104/09) defines rights and duties of civil servants and certain rights and duties of general service employees

(for instance: principles of work conducted by civil servants, types of posts of civil servants, filling in available posts, assessment and promotion of civil servants, secondment of civil servants for work purposes, vocational training, responsibility of civil servants, termination of employment, rights of civil servants during change of structure of public authorities, decisions on rights and duties of civil servants, regulation of the human resources system, special provisions on general service employees, monitoring of implementation of the law).

Certain rights and duties of civil servants in certain public authorities may be defined differently by special law, if that is required by the nature of their activities.

Article 155 of the Law on Public Servants prescribes that the proposal of the human resources plan for public administration authorities and Government's services shall be prepared by the Human Resources Management Service (in charge of professional activities regarding human resources management in the public administration), and proposal of the human resources management for courts and public prosecution services shall be prepared by the ministry in charge of judicial affairs.

The Government shall define preparation of drafts and proposals of the human resources plan in all public authorities.

Article 159 of the Law on Public Servants prescribe that the central human resources records on civil servants and general service employees in the public administration authorities and Government services shall be kept by the Human Resources Management Service (central human resources records are kept as an information database).

The Law on Salaries of Public Servants and Employees (*Official Gazette* of RS, Nos. 62/06,.. and 101/07) defines wages, compensations and other emoluments of civil servants and general service employees .

The Law on Salaries in Government Bodies and Public Services (*Official Gazette* of RS, No. 34/01...and 63/06 – Corrigendum of other law) defines the manner of formation of wages, bonuses, compensations and other emoluments of elected persons in the Government and the National Assembly, state secretaries, the President of the Republic, elected, appointed and employed persons in authorities and organizations of territorial autonomy and local self-government, employees in public services financed from the budget of the Republic, autonomous provinces and local self-government units, employees of public services funded from compulsory social insurance contribution, employees of compulsory social insurance contribution organizations.

Justice

The Law on Judges and the Law on Public Prosecution (*Official Gazette of RS*, No. 116/08, 58/09 and 104/09) defines the manner of formation of wages, bonuses and compensations of judges.

Special laws regulating employment relationships and wages in public authorities or independent regulatory bodies

Manner of formation of wages, bonuses and compensations in authorities such as: Commissioner for Equal Opportunities, Commissioner for Information of Public Importance and Personal Data Protection, Ombudsman, Anti-Corruption Agency, State Audit Institution, Serbian Armed Forces, Ministry of Interior, Security-Information Agency, Diplomatic and Consular Representative Offices, Administration for Enforcement of Criminal Sanctions, Tax

Administration are regulated based on special laws, due to specific nature of jobs performed by such institutions.

Local Self-Government (elected, appointed officials and employees)

Issues regarding positions of persons employed in local self-government units relating to entry into employment relationship, rights and responsibilities, termination of employment, protection of rights are defined by the Law on Labour Relations in State Authorities (*Official Gazette of RS*, No. 48/91, 66/91, 44/98, 49/99, 34/01, 39/02, 49/05 and 79/05).

Pursuant to Article 3 of the Law on Salaries in Government Bodies and Public Services, the base for wage calculation shall be determined by the Government by means of Conclusion. The highest coefficients for calculation and payment of wages of elected and appointed persons and the highest coefficients for persons employed in authorities of local self-government units are determined by Article 9 of the Law.

Total maximum number of employees in authorities of local self-government units is defined by the Law on Maximum Number of Employees in Local Administration (*Official Gazette of RS*, No 104/09).

Note: Draft Law on Labour Relations in Local Self-Government Units is being drafted currently, which would include all work specificities at the level of local self-governments and which would, in the coming period (early next year), serve as a basis for adoption of the law for regulating wages in local self-government units in a better, more systematic and transparent manner.

Public Undertakings and Public Agencies

- Regulations on wages and employment relations stipulated for civil servants and general service employees and public services employees are not applied to public undertakings and public agencies (teachers and professors, employees in the healthcare system), but rather their wages are formed based on the Law on Labour (*Official Gazette of RS*, No 24/05, 61/05 and 54/09) and acts adopted in accordance with such Law (Rulebooks, Statutes etc.).

EMPLOYMENT

Civil Servants and General Service Employees

- Since 2007, there is an obligation to adopt Human Resources Plan within 30 days following the date of publishing the Law on the Budget of the Republic of Serbia in *the Official Gazette of the Republic of Serbia*. Human Resources Plan covers one budget year and determines the number of civil servants and general service employees that can be employed for indefinite and definite period, as well as number of interns for which funds have been secured in the budget;

The Law on Maximum Number of Employees in Public Administration (*Official Gazette of RS*, No 104/09) defines the maximum number of total employees in public administration authorities, public agencies and compulsory social insurance organizations.

Pursuant to the mentioned Law, public administration authorities mean all ministries (including all administration authorities within the ministries), special organizations and professional services of the Government, Administration for Joint Services of the Republic Bodies and professional services of administrative districts.

This Law is not applied to the Ministry of Interior, Ministry of Defence, Security-Information Agency and Administration for Enforcement of Criminal Sanctions.

Pursuant to Article 2 of this Law, the Government adopted a Decision on the Maximum Number of Employees in Public administration Authorities, Public Agencies and Compulsory Social Insurance Organizations (Official Gazette of RS, No 109/09, 5/10, ... 89/10) which applies to persons employed for indefinite period – last date of change 29th November 2010 and Conclusion 05, No: 112-4418/2010-002 from 17th June 2010, regarding to persons employed for definite period, whose number, on an average and monthly basis, can not exceed 10% of number of persons employed for indefinite period.

Stated Decision includes analytical display of number of employees per authorities, while joint display of data is presented in the following table:

| AFTER ADOPTION OF DECISION ON AMENDMENTS TO THE DECISION - 29TH NOVEMBER 2010, NO. 89 | No of employees for indefinite period | (analytical display of No of employees for indefinite period |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------|--------------------------------------------------------------------|
| The Law on Maximum Number of Employees in Public Administration | 28.400 | |
| Decision of the Government on the Maximum Number of Employees in Authorities of Public Administration, Public Agencies and Compulsory Social Insurance Organizations, namely: | 26.748 | |
| Ministries | | 15.814 |
| Administrative districts | | 285 |
| Special organizations: | | 1.629 |
| Government's services | | 1.166 |
| TOTAL I: | | 18.894 |
| Public agencies: | | 734 |
| Compulsory social insurance organizations | | 7.120 |
| TOTAL II: | | 7.854 |
| Difference (No of employees stipulated by the Law and No of employees stipulated by the Decision): | 1.652 | |

Funds for wages are planned in the budget of the Republic of Serbia, in compliance with the mentioned Law.

Public Agencies and Compulsory Social Insurance Organizations

- Number of employees is planned according to their work programmes, and/or financial plans;
- Number of employees is defined by the Law on Maximum Number of Employees in Public Administration

Local Self-Government

- Number of employees is planned by their act on classification of posts;
- Since 2010, the Law on Maximum Number of Employees in Local Administration (*Official Gazette of RS*, No 104/09) defines the maximum number of employees in local self-government.

Justice and Others

- Number of employees is planned according to their act on classification of posts and human resources plan, adoption of which started in 2007.

Ministry of Finance - the Treasury shall keep a Register that contains data on number of employees and hired persons in public and local administration and on funds paid on behalf of their wages, bonuses and compensations, within the supervision of implementation of The Law on Maximum Number of Employees in Public Administration and the Law on Maximum Number of Employees in Local Administration. Register of Employees is an electronic database, containing basic data on employees and hired persons in public and local administration on individual level. Financial data in the Register are kept at the level of budget beneficiary, per accounts on a monthly basis.

Data on funds paid on behalf of wages and data on the number of employees (for the period 2006-2010) are presented in the table in Annex.

d) share of taxes in the total wage bill, including social contributions paid by employers and employees, and the bracket structure of income taxes.

Fiscal burden on wages - share of taxes in the total wage bill, including social contributions paid by employers and employees, and the bracket structure of income taxes:

Tax base – gross income (net income increased by taxes and contributions paid by employee), reduced by non-taxable threshold (variable amount, adjusted once a year with growth of retail prices in the calendar year preceding the year when adjustment is done, according to the data of republic authority in charge of statistics, currently stands at RSD 6,554).

Contribution base – paid out, and/or realized wage, and/or gross income (net income increased by taxes and contributions paid by employee).

| No. | Description | Amount | Amount |
|------|----------------------------------------------------------|--------|---------|
| 1. | Gross Wage | 41,651 | 100,000 |
| 2. | Tax base | 35,097 | 93,446 |
| 3. | Contribution base | 41,651 | 100,000 |
| 4. | Obligations on gross income paid by employee (4.1.+4.2.) | 11,667 | 29,113 |
| 4.1. | Taxes (2* 12%) | 4,212 | 11,213 |
| 4.2. | Contributions paid by employees (3* 17.9%) | 7,455 | 17,900 |
| 5. | Obligations on gross wage paid by employer (3*17.9%) | 7,455 | 17,900 |

| | | | |
|------|-------------------------------------------------|--------|---------|
| 5.1. | Contributions paid by employer | 7,455 | 17,900 |
| 6. | Total taxes and contributions (4+5) | 19,123 | 47,013 |
| 7. | Total wage bill (1+5) | 49,107 | 117,900 |
| 8. | Net wage paid out (1-4) | 29,984 | 70,886 |
| 9. | Fiscal burden on net wage (6:8) | 63,78% | 66,32% |
| 10. | Fiscal burden on gross wage (6:1) | 45,91% | 47,01% |
| 11. | Fiscal burden pursuant to the OECD method (6:7) | 38,94% | 39,87% |

V Economic and structural developments and reforms

Please briefly describe and/or provide explanations in the following areas:

5. How has domestic consensus on the fundamentals of economic policies been secured? Please provide comprehensive information about the adoption of economic policy in the country. Please provide an English translation of Serbia's national strategy for economic policy in the medium term.

Consensus on fundamentals of economic policy is secured at the Government level, namely on tripartite level between the Government, Association of Employers and Trade Union. Political consensus at the Government level, supported by the consensus of the social partners, provides compliance of economic policy and responsibility for its implementation.

The Government of the Republic of Serbia, in compliance with the Law on the Budget System (*Official Gazette of RS*, No 54/2009), prepares and adopts economic policy for the budget year and next two years. In December 2010, the Government adopted revised Memorandum on the Budget and Economic and Fiscal Policy for 2011, along with projections for 2012 and 2013. English translation of this document is being prepared by the Government.

In compliance with the Law on Amendments and Modifications of the Law on Budget System (*Official Gazette of RS*, No 73/2010), instead of the mentioned Memorandum, the Government shall adopt a Report on Fiscal Strategy in July 2011, which is a document that will establish economic and fiscal policy of the country for the next three consecutive fiscal years.

Draft Report on Fiscal Strategy is currently being prepared by the Ministry of Finance, in cooperation with ministries and institutions in charge of economic policy and economic system, and shall submit such Report to the Fiscal Council as an independent public authority by 15th May of the current year, for purposes of obtaining an opinion thereon. On July 1st current year, the Minister of Finance shall deliver to the Government Proposal of the Report on Fiscal Strategy for adoption, along with opinion of the Fiscal Council. Until July 15th, the Government shall adopt the Report on Fiscal Strategy and shall submit such Report to the National Assembly for consideration purposes. The National Assembly shall deliver the comments and recommendations to the Government regarding the Report on Fiscal Strategy, for the purposes of including thereon into the revised Report on Fiscal Strategy. The

Government shall adopt the Report shall by October 1st current year, and submit the Report to the National Assembly prior to submitting proposal of the budget of the Republic of Serbia for the next year, Such procedure regarding preparation and adoption of the Report on Fiscal Strategy shall secure domestic consensus on fundamentals of economic policy of the country, bearing in mind that the Government, ministries, Fiscal Council, National Assembly, Social-Economic Council and consulting bodies of the Government are included in the preparation thereof.

Report on Fiscal Strategy, prepared according to the determined legal procedure, contains economic and fiscal policy, along with projections for the budget year and next two fiscal years. Report on Fiscal Strategy is the basic document of the Government, in which objectives and guidelines are determined for economic and fiscal policy in the medium term, and budget of the Republic is the main document of economic and fiscal policy for the next budget year.

Accompanying Appendix to the Report on Fiscal Strategy is the Progress Report on implementation of the defined fiscal policy, along with assessment as to what degree the Government implemented a responsible fiscal policy during the previous year, and/or whether it was in compliance with fiscal principles and fiscal rules. If the Government derogates from the fiscal principles and rules under extraordinary circumstances, it shall notify the National Assembly of that matter and state measures to be undertaken and timeframe in which the Government expects to return to fiscal principles and rules.

Adopted Report on Fiscal Strategy for the next three-year period presents a Government's document, which determines fiscal framework in the medium term, aiming to secure long-term sustainability of the fiscal policy. The document represents a basis for preparation and adoption of budgets of the Republic, autonomous provinces and local self-government units, as well as financial plans of compulsory social insurance organizations.

6. What are in your view the particular challenges/priorities for Serbia's economic policy, including in the context of the global post-crisis recovery, and how do you intend to tackle them?

The particular challenges/priorities of economic policy of the Government of the Republic of Serbia, in the context of the global post-crisis recovery, are the following:

- Macroeconomic stability
- Fast and stable recovery of the economy
- Dynamic economic growth
- Increase of investments and export
- Reduction of unemployment rate
- Improvement of living standard
- Equal regional development
- Sustainable levels of fiscal deficit and public debt

Since October 2008, economic policy of the Government during crisis period was focused on mitigating the effects of the global financial and economic crisis on the Serbian economy. Economic policy measures created conditions for macroeconomic and financial stability, as well as for lowest possible decline in production, export, employment and living standard of the population. In that respect, Serbia recorded smaller decline of GDP in 2009 (-3.1%) relative to regional and European countries. Similarly, Serbia achieved faster economic

recovery in 2010. Real GDP growth in the first half of 2010 was 1.2%, while estimates show that in 2010 Serbia will record real GDP growth of at least 1.5%, which is higher than in the regional countries.

Economic crisis has shown that the past economic growth model, based on growth of domestic consumption and import, is unsustainable and that it must be replaced by investment and export oriented economic growth model. Faster growth of domestic demand and consumption than the GDP growth in the past period resulted in the growth of current account deficit, which was covered by inflows of foreign capital, and in inflation higher than in regional countries. Sector producing non-exchangeable goods was dominant in the structure of GDP creation, while personal and public consumption were dominant in the of GDP usage structure. Change of economic growth model will also lead to changes in the structure of GDP creation and usage towards strengthening of sectors producing exchangeable goods and increase of contribution of investments, financed from national and foreign savings, and contribution of exports to the Serbian economic growth. Higher economic growth rate and significant share of investments and exports in the GDP will provide increase of employment and opening of significant number of new jobs, as well as higher living standard and reduction of poverty in the country. Thus, the credibility of the country will be increased and investment risk will be reduced.

Economic policy of the Government in the post-crisis period is oriented to fast and stable economic growth in Serbia and to creation of conditions for a dynamic economic growth, based on investment and export growth as key development elements. Robust economic growth will enable increase of employment and living standard and more equal regional development, along with reduction of poverty.

Serbian economic policy will be oriented not only to changes in the global environment and risks in external economic relations, but also to inherited social and economic problems and challenges, which define key priorities of economic policy in the post-crisis period.

The first priority is *inflation*, which is relatively high according to international standards and poses a risk for macroeconomic stability and economic growth. Inflation may be caused by overly large public spending and personal consumption, price shocks (agriculture and oil products), very high depreciation of the dinar and overly large growth of controlled prices.

Second priority is *the recovery of the real sector* from the effects of the economic crisis and inherited structural problems. Fragile economic recovery needs to be strengthened through restructuring economic branches and undertakings, completion of the privatization process and more effective implementation of bankruptcy proceedings, as well as through more business enabling environment and larger investments of domestic and foreign investors in the economic development of the country. In that sense, economic system, macroeconomic policy and sectoral policies will be adjusted to the concept of faster economic growth based on increase of investments and export and strengthening of exchangeable goods sector.

The third priority is *increase of investments*. Speeding-up of economic growth, after economic recovery from the consequences of the economic crisis, demands strong increase of investments relative to generated GDP, with slower growth of personal consumption and public spending at the same time. Financing of investments requires significant increase of domestic savings, bearing in mind that privatization proceeds are decreasing and that possibilities for new borrowings abroad are limited. That would enable dynamic economic growth, based on increase of employment and productivity, which at the same time provides internal and external macroeconomic stability and creates room for improvement of living standards on realistic bases.

The fourth priority is *increase of export*. Serbia recorded steep growth of export of goods and services in the period 2001-2008 (average growth rate was 20.9%), but did not significantly increase share of export of goods and services in the GDP (below 30%). That contributed to the fact that in the end of 2008, trade deficit share in the GDP was 24.1% and share of current account deficit in the GDP was 18.7%. Export structure is dominated by raw materials, processed materials and food with small share of new value added. Change towards development based on export include high growth rates of export of goods and services, increase of share of exports of goods and services in GDP, increase of share of exchangeable goods sectors in creation of GDP and share of exchangeable goods in the export structure with higher share of new value added and decrease of trade deficit. For strengthening of export-oriented economy, it is necessary to have the support of macroeconomic policy and active sectoral policies, above all industrial policy.

The fifth priority is *reduction of unemployment and improvement of living standard*. High unemployment rate and decline of living standard may trigger wider political and social unrest and direct orientation of economic policies towards short-term social and economic objectives. Unemployment rate in Serbia exceeded 20% according to internationally measured methodology, and average net wage declined to EUR 320. Growth of employment and wages, and consequently growth of living standard, may be provided only by speeding-up economic growth and increasing investments, for the purposes of opening new jobs. It is essential to improve education and qualifications, which define volume and quality of labour offer and its adjustment to the demand in the labour market.

The sixth priority is *equal regional development*. Serbia faces large regional development inequalities, due to unfavourable demographic trends, high regional unemployment, devastation of industry, lack of infrastructure and insufficiently developed institutional framework. New regional policy is necessary, which would target equal regional development across the country, in order to strengthen development potential of all regions, with necessary state intervention, along with increase of their competitiveness, which would thus reduce intra-regional and inter-regional inequalities that limit the aerial development in the Republic.

The Seventh priority is *sustainable level of fiscal deficit and public debt*. Increase of fiscal deficit and public debt relative to GDP is the consequence of insufficient reforms of the public sector and negative effects of the global economic crisis on Serbian public finances. Newly-introduced fiscal rules should provide significant reduction of the public spending, fiscal deficit and public debt until 2015, which should provide long-term stability of public finances and public debt, along with higher economic growth rate, change of the public spending structure towards growth of share of public investments in GDP and reforms of the pension system, education, health care and social insurance systems.

Key response of the Government's economic policy to the mentioned development challenges is speeding-up reform and transition processes within change of the economic growth model. In the post-crisis period, the Government shall speed-up economic reforms which lead Serbia towards full EU membership. Particular attention shall be paid to creation of stimulating environment for domestic and foreign investors, full property and contract protection, effective judiciary, modern tax system, harmonization of fiscal and monetary policy, effective banking system and developed financial market, private and public partnership, particularly in the area of infrastructure, regulated labour market and regulated relations between employees and employers, political stability in the country.

7. How has a co-ordination between various stakeholders (e.g. line ministries, the Ministry of Finance and/or the Central Bank) for the formulation of economic policies and their implementation been carried out? Which are the consultative bodies involved in the decision-making process? To what extent are social partners involved? If relevant, what is the time given to social partners and other consultative bodies to provide their opinion?

In the process of formulation and implementation of the Government's economic policies, coordination is ensured between line ministries, the Ministry of Finance and the National Bank of Serbia necessary for establishing and undertaking measures agreed upon.

In the process of developing the Report on Fiscal Strategy for the next medium term, in which economic policy objectives and guidelines are determined, the Ministry of Finance ensures cooperation with ministries and institutions competent for economic policy and economic system. In the same manner, the Ministry of Finance ensures inter-sectoral cooperation in the process of preparation of the budget of the Republic, as the main document in which economic policy for the budget year is determined.

NBS is an active participant in the formulation of medium-term and annual economic policy. NBS provides opinion on Government's documents, which formulate the economic policy. Opinion of the NBS on the Draft Report on Fiscal Strategy is a compulsory appendix to the Report during its adoption on the Government's session and discussion at the National Assembly. In addition, the Governor of the NBS proposes one member of the Fiscal Council who provides opinion on the Report on Fiscal Strategy and the Law on the Budget of the Republic of Serbia, and who analyzes and assesses fiscal policy and public finance management. Pursuant to the Law on the National Bank of Serbia, the Monetary Board sessions are attended by the minister in charge of financial affairs with no voting rights, and/or Director of the Treasury Administration authorized by such minister. Also, pursuant to the Law on Modifications and Supplements of the Law on the NBS, the Government shall issue consent on the Proposal of the Decision on the Dinar Exchange Rate Regime adopted by the Council of Governors of the NBS. Sessions of the Committee on Economy and Finance of the Government is attended by a representative of the NBS, and Government sessions are attended by the Governor with no voting rights.

The Ministry of Finance and the National Bank of Serbia have close coordination, through standard consultative mechanisms in the phase of implementation of economic and monetary policy and its components. Competent republic ministries undertake measures stemming from their competence, in compliance with the established economic and monetary policy frameworks, thus contributing to realization of established macroeconomic objectives.

Consultative bodies are included into the process of formulation of the Government's economic policy. In order to raise the quality of economic policy, the Government has established an Economic Council as a consultative body, which considers issues in the area of economic policy as requested by the Government or on its own initiative. Economic Council is composed of members of the Government, experts and prominent businesspeople. In the process of formulating economic policy, the Government also consults the Serbian Chamber of Commerce, as the largest economic association, as well as the Serbian Economists Association, as a professional association of economists.

In the process of formulating economic policy of the Government, social partners are included through a Social-Economic Council of the Republic of Serbia, established by special law enacted in 2004 (*Official Gazette of RS*, No 125/04), as an independent body in the territory of the Republic of Serbia, which is composed of representatives of the Government, representatives of competent associations of employers and representatives of competent trade

unions. The Council also nominates experts as members of the Council, as an addition to the members nominated by the Government, Association of Employers and Trade Union. The Council has both, consultative role in the social dialogue and negotiating role for certain economic and social issues of interest for the social development and stability of the country. The role of the Council is to secure consensus on economic policy fundamentals, contributing to its successful implementation. The Council provides opinions, proposals and recommendations on issues regarding employment policy, wage and price policy, policies of competition, productivity, privatization, work area protection, environmental protection, education and professional training, health and social protection, demographic developments, work safety, collective bargaining process etc.

The NBS provides opinion on the Memorandum on the Budget and Economic and Fiscal Policy for Medium Term Period, Draft Law on the Budget and all laws in the area of the fiscal policy. Pursuant to the Law on the National Bank of Serbia, the NBS Executive Board sessions are attended by the minister in charge of financial affairs, but with no voting rights.

The Government of the Republic of Serbia in cooperation with the NBS, determines the numerical guidelines for the growth of prices of products and services which are directly or indirectly regulated by the Government.²⁴ Moreover, the NBS in cooperation with the Government sets the inflation target.

Working group in charge of monitoring developments and plans regarding change of regulated prices, established in April 2010, is composed of representatives of the NBS and the Government (the Ministry of Mining and Energy, Ministry of Trade and Services and Ministry of Telecommunications and Information Society). Working group holds sessions four times a year, in order to analyze current developments and short-term outlook regarding regulated prices and determining numerical guidelines for growth of regulated prices, along with inflation targets in the following three-year period.

By signing the Agreement, the Government obliged itself to implement a sustainable and foreseeable fiscal policy in compliance with the targeted inflation rates, by timely notifying the public and the NBS of changes in the economic policy that may affect achievement of the targeted inflation, particularly of plans regarding market and budgetary regulation.

8. How is the co-ordination of the main producers of statistical data (Statistical office, Central Bank, Ministry of Finance, etc.) carried out? What are the plans to enhance the reliability, regularity and mutual compliance of statistical data? Does the public finances statistics comply with ESA methodology? (detailed information is required in chapter 18 – Statistics)

Republic Statistical Office (RSO), National Bank of Serbia (NBS) and Ministry of Finance (MF), being the primary producers of statistical data, have established permanent cooperation and coordination which was institutionalized by signing Memorandum on Cooperation on Macroeconomic and Financial Statistics in December 2010.

RSO, NBS and MF have developed macroeconomic and financial statistics, within their competences, and improve reliability and consistency of statistical data. Plans for improvement of methodology and data are contained in the Official Statistics Programme until 2015 and in annual statistical research plans.

²⁴ Pursuant to the Agreement signed between the NBS and the Serbian Government on inflation targeting, adopted on the Government session on 19th December 2008.

ESA 95 is still not used for calculation and presentation of fiscal operations at the general government level. However, for the purposes of national accounts, certain categories of revenue and expenditure, as well as fiscal result, are calculated and published in accordance with the ESA 95 methodology. .

Cooperation between these three institutions, regarding Council Regulation (EC No 2223/96), is implemented through allocation of functions in the following manner:

Real Sector Accounts

Within preparation of real sector accounts, which is an obligation of RSO, MF and NBS timely furnish RSO with all available data relevant for calculation of categories in compliance with requirements of RSO.

MF provides data to RSO regarding budgets of the Republic, Autonomous Province of Vojvodina, local self-governments and compulsory social insurance organizations on monthly, quarterly and annual basis, based on data regarding the budget of the Republic, and based on the reports that MF receives from other levels of government and funds on a monthly basis.

Pusuant to the Government Finance Statistics Manual, issued by the International Monetary Fund, MF delivers data to RSO on revenues and emoluments of budget beneficiaries, along with data on expenditures and costs of budget beneficiaries prior to implemented consolidation.

RSO publishes real sector accounts and delivers such accounts to MF and NBS.

Financial Accounts

Annual and quarterly financial accounts are developed and published by the NBS, in compliance with the accepted methodology, with exception of financial accounts for the government sector, which are under the competence of RSO.

Reports on Budget Deficit and Budget Expenditures and Revenues

MF collects data and prepares reports regarding budget deficit, expenditures and revenues of all levels of the government and also reports regarding compulsory social insurance organizations. MF is obliged to deliver prepared data and reports to the NBS and RSO.

Public Debt Reporting

MF is in charge of assessment and reporting on public debt, in compliance with the adopted EU regulations and methodologies.

Balance of Payments

NBS is in charge of drafting balance of payments, in compliance with the Balance of Payments Manual prepared by the International Monetary Fund, fifth issue (BPM5).

The primary sources of data for drafting balance of payments are the data from commercial banks and the National Bank of Serbia on international payment transactions, which is submitted electronically on the decade level (ITRS) along with data from the Republic

Statistical Office. Additional data sources are reports submitted by undertakings directly to the NBS.

RSO furnishes the NBS with data on international commodity trade transactions.

With its researches, RSO provides assistance and delivers to the NBS available information required in the process of acquiring additional sources for comprehensive monitoring of the household sector.

MF reports directly to the NBS on a monthly basis on transactions involving the Budget of the European Union and on all international transfers (help, donations) between the government sector and other international institutions and countries.

Monetary and Banking Statistical Data

NBS is in charge of monetary and banking statistical data. Monetary and banking statistics include balance sheet data of monetary and financial institutions (except money market funds), insurance undertakings, voluntary pension funds and financial lessors. Also, such statistics include interest rate statistics of monetary and financial institutions and inter-bank money market. In addition to monetary and banking statistics, the National Bank of Serbia collects data on foreign exchange reserves of the NBS and banks, dinar exchange rate and turnover in the foreign exchange market, within its statistics regarding international economic relations.

In 2007, Memorandum of Cooperation was signed between the Ministry of Agriculture, Ministry of Forestry and Water Management and RSO, with a view to improve statistical monitoring of agriculture, forestry and water management, to clearly define obligations and ensure information for an objective overview of the situation in the mentioned fields. Upon conclusion of the Memorandum, the cooperation between the two institutions has been significantly improved and is intensive regarding preparation for implementation of the upcoming agricultural inventory.

In 2007, a Memorandum was signed with the Tax Administration (which operates within the Ministry of Finance), which enables usage of administrative data as an important additional data processing source.

Some time before that, the Memorandum of Cooperation was signed with the Customs Administration (which also operates within the Ministry of Finance), with which RSO traditionally has good cooperation.

Signing similar memoranda has been planned with the Ministry of Mining and Energy, Ministry of Environment and Spatial Planning and Environmental Protection Agency, as well as with Public Health Institute of Serbia.

Also, it should be noted that in mid 2009, being a coordinator for such affairs and in coordination with the National Bank of Serbia, RSO made a decision on participating in the General Data Dissemination System. In October 2010, International Monetary Fund mission - Special Data Dissemination Standard (SDDS) – took current conditions under consideration regarding national statistics, and concluded that it can be expected that as of 3rd quarter of 2011, the Republic of Serbia may join SDDS.

9. Public finances: What is the scope of public finances system? How was it conceived? How have government revenue and expenditure developed as a share of GDP during 2000-2009, as an aggregate as well as in terms of categories?

Until the adoption of the systemic law, which provided new frameworks for preparation and execution of the budget, the 1991 Law on Public Revenues and Public Expenditures established the integrity of Republic of Serbia in the area of public revenues and expenditures and uniformly defined the public revenue system and public expenditure financing system. Adoption of the new systemic Law on the Budget System (*Official Gazette of RS*, No. 9/02, 87/02, 61/05 – other law, 66/05, 101/05 – other law, 62/06 – other law and 86/06) marked the reform of public finances in early 2002, which in a completely new and systemic bases define public spending, which include the budget of the Republic, budget of autonomous provinces and local self-governments, as well as all financial plans of compulsory social insurance organizations. The Law on the Budget System represents one of the most significant systemic laws, which fully reform the budget system and govern the area of public finance management in the entire country.

This reform law in the area of public spending marked the beginning of the reform processes in all segments of public finances and public sector in its entirety. Public finances and budget spending are important part of overall economic system, given the fact that they comprise around 45% of GDP. That being the case, they are subject of broad interest, primarily of business entities, but also of natural persons which, through allocation of funds for taxes and contributions, provide necessary public funds for financing general public services and fulfilment of public needs of general interest in any country.

The Law on the Budget System governs planning, preparation and adoption of the budget of the Republic of Serbia, budgets of territorial autonomies and local self-government units, and through establishment of the Treasury of the Republic, and/or of local authorities, execution of the budget has been regulated, along with borrowing, issuing of guarantees, debt management, budgetary accounting and reporting. Also, this Law governs the control and audit of the budget, as well as control and audit of official services and other indirect budget beneficiaries, public undertakings and legal persons founded by public undertakings, and/or legal persons over which the Republic, and/or local authority has direct or indirect control with more than 50% of capital or more than 50% of voting rights in the management board.

One of the innovations regarding public finances reform is that the Law regulates preparation and adoption of financial plans, borrowing, accounting, reporting, control and audits of financial plans of compulsory social insurance organizations. That is, the Law on the Budget System places the procedure of preparation and adoption of financial plans of compulsory social insurance organizations into the same systemic framework, thus encompassing the overall budget system of the Republic. Budget process has included all types of public revenues and expenditures and integrated all revenues and expenditures of local self-government units and compulsory social insurance organizations. Since the compulsory social insurance organizations (Republic Pension and Disability Fund of Employees, Republic Pension and Disability Fund of Self-Employed Activities, Republic Pension and Disability Fund of Farmers, Republic Health Insurance Bureau and National Employment Service) did not conduct their financial activities entirely in compliance with regulations applied to budget issues until the adoption of the Law on the Budget System, this represents a significant improvement, and obligatory delivery of reports on financial activities to the National Assembly strengthens the control over Government.

The Law has established new institutions as well, which contributed to more effective functioning of the entire public finance system. The most significant innovations in that

respect are the establishment of macroeconomic model of fiscal planning of public finances, which uses the Treasury for budget execution and public finance management. That is, implementation of the new budget system provides the establishment of macroeconomic discipline, which resulted in the fact that budget acts and financial plans of compulsory social insurance organizations are in compliance with the sustainable macroeconomic and fiscal framework.

For the purposes of stabilization of overall public finances, a medium-term planning framework has been introduced through adoption of a memorandum on the budget and on economic and fiscal policy for the budget year and the next two fiscal years, as well as acts based on which budgets and financial plans of compulsory social insurance organizations are adopted. Such novelty is in compliance with the formulation of budget objectives under preparation and budget execution regarding: macroeconomic stability, sustainable and stable economic growth and reduction of financial risk of the country.

Integrity of the budget system is secured by joint legal basis, uniform budget classification, use of uniform budget documents for development of draft budget and financial plans, uniform budget accounting system, uniform criteria for budget control and audit, transfer of statistical reports and data from one budget level to the other and principles on which budget procedure is based. During budget preparation and execution, principles of efficiency and economics must be observed, along with principles of completeness, accuracy and uniform budget classification.

Budget is carried in compliance with uniform international methodology of revenues and expenditures, namely according to: economic, functional and organizational classification, as well as according to financing sources (it carries revenues and emoluments, expenditures and costs based on asset realization).

Adoption of the Law on the Budget System introduced establishment of the Treasury that represents a completely new thing in the public finance system, which manages the Treasury consolidated account through introduction of information-technology system of the Treasury, establishment of the general ledger and budget execution system. Monitoring of public finances and their consolidation through Treasury, in addition to improvement of daily liquidity of public spending, increased efficiency and transparency in planning and managing public spending as well, while the system enabled daily monitoring of budget execution and cash management planning through appropriations and quotas.

In subsequent reform process of public finances and adjustment to the modern principles, amendments were made to the Law on the Budget System. Namely, the Law on the Budget System generally governed issues pertaining to debt and guarantees, while adoption of the Law on Public Debt (*Official Gazette of RS*, No 62/05 and 107/09) in 2005 regulated in detail all issues regarding all aspects of Republic of Serbia's public debt, and particularly defined what is considered a public debt of the Republic of Serbia, obligations of the Republic of Serbia on public debt as well as what such obligations represent for the Republic of Serbia. Reasons for adoption of such Law are, primarily, the need to define conditions, manner and procedure according to which the Republic of Serbia may borrow, as well as the need to prescribe manner and procedure according to which borrowings may be made by a territorial autonomy and local self-government, Republic Health Insurance Bureau, republic funds for pension and disability insurance and National Employment Service, as well as to clearly define that all public undertakings, as well as all legal persons founded by the Republic of Serbia, may ask the Republic of Serbia to provide a guarantee, where such legal persons must fulfil certain conditions to receive such guarantee, and to clearly define guarantees of the

Republic, manner and procedure of public debt management, record-keeping on public debt and establishment of Administration for Public Debt.

For the purposes of allocational, technical and operational efficiency of the public finance system, in 2006 the amendments to the Law on the Budget System created legal framework for programme and medium-term budget planning, which include allocating largest appropriations for investment programmes that contribute to faster realization of economic policy objectives, through faster economic growth, higher employment rate and more effective investment programmes.

Programme part of the budget represents one of the significant components of a broader reform process implemented in public finance management. Amendments and Modifications of the Law on the Budget System enabled introduction of more effective mechanism for monitoring realization of objectives in three key strategic processes, which the Government defined for the purposes of implementation of the economic and fiscal policy, which are Poverty Reduction Strategy, European Union accession process and development policy and programmes. Public finance management in the past has shown that it was hard to translate the abovementioned objectives into operational plans that could be linked to budget appropriations; hence, it was important to improve connections between financial plans and strategies, in order to provide appropriate mechanisms for monitoring success rate of their implementation and consideration of the future needs. The conditions for that have been created by adoption of the mentioned amendments.

Through programmes, as a transparent mechanism for monitoring budget revenues and expenditures, which enables efficient allocation of funds to solving specific problems and which enables decision-makers to easily understand the link between the requested funds, strategies, programmes and results, the budget should become more effective instrument of economic and other government's policies, because it improves the manner in which financial plans are drafted and analyzed. In that manner, the budget enables to pinpoint and analyze various programme measures in finding the most effective manners, and/or methods (activities) used for solving detected problems and role of various stakeholders, and/or defining competences and responsibilities for solving problems, and/or achieving desirable objectives.

However, implementation of the mentioned legal framework, although it enabled gradual approach, did not have desirable results, given that the programme-based budgeting model is reduced to five pilot ministries; also, the programme-based model included only listing of activities without even stating evaluation of the outputs, thus omitting the feedback to the Government necessary for further implementation of its policies.

Also, changes were made that contributed to better public finance management through payments of all expenditures, both direct and indirect budget beneficiaries, via uniform treasury system. Namely, the amendments established the obligation for the direct budget beneficiaries to allocate available appropriations, carried jointly in the budget, to beneficiaries within their competences, after the budget has been adopted. That practically means that financial plans for indirect budget beneficiaries are prepared, within approved appropriations, which created conditions for indirect payments to be made by Treasury to the indirect budget beneficiaries.

For the purposes of improving public finance management, since 2008 a permanent Treasury system was established, which provides for exchange of information that contribute to better synchronisation of inflow and spending of money through financial planning, electronic links between beneficiaries and the Treasury Administration, which enables beneficiaries to submit direct requests for taking on obligations, payment request, and which also enables adjustments

of budget execution to the legislation, as well as improvement of accounting functions in compliance with the international standards.

An integral part of financial statements of all budgets and financial plans of compulsory social insurance organizations is the external audit report, which is the competence of the State Audit Institution pursuant to its constituent instrument.

The Government has demonstrated its orientation towards embracing modern trends by implementing the Law on the Budget System (*Official Gazette of RS*, No 54/2009) in 2009. Further amendments to the Law were necessary, in order to achieve more effective implementation of budget objectives, particularly efficiency, economics and effectiveness in the budget preparation and execution, and in order to implement further improvement of the treasury-type operations and improvement of the system that recognizes responsibility in public spending. However, given the past large amendments to the Law and the need for new amendments, it was estimated that the new law should be adopted.

The new Law on the Budget System created legal framework for use of development aid from the European Union, and stipulated obligations of Serbia to establish its own adequate institutions for management of European Union funds through, so called, decentralized system of EU fund management.

Applicable provisions of the 1991 Law on Public Revenues and Public Expenditures were incorporated into the new Law on the Budget System, and such Law ceased to be valid.

Public revenues and emoluments are the following:

Revenues:

- 1) Taxes;
- 2) Contributions on compulsory social insurance;
- 3) Charges for usage of goods of general interest;
- 4) Fees;
- 5) Voluntary local tax;
- 6) Donations and transfers;
- 7) Other public revenues.

Government's emoluments:

- 1) Emoluments on sale of non-financial assets;
- 2) Emoluments on borrowings;
- 3) Emoluments on sale of financial assets, namely:
 - a. Received payments on principles of disbursed loans,
 - b. Emoluments on sale of securities,
 - c. Emoluments on sale of shares and holdings.

The Law provides for introduction of the following: value added tax, excise duties, personal income tax, corporate income tax, property tax, inheritance and gift tax, tax on transfer of absolute rights, tax on using, holding and carrying certain goods, international trade and transaction tax and other taxes in compliance with special law.

The Law provides for introduction of the following fees: administrative, court, communal, registration, residence fees and fee for special products and activities.

The Law provides for introduction of the following charges for usage of goods of general interest: water charges, forestry charges, road charges, land charges, charge for fishing zones, charge for using tourist area, charge for using natural medical factors, charge for using mineral raw material, environmental protection charge, charge for using air space, charge for listening to radio frequency and so called channels, tourist charge and other charges in compliance with special law.

Funds received from the mentioned charges are used in compliance with the law that introduced such charges.

The Law introduces contributions on compulsory social insurance, namely on:

- 1) Pension and disability insurance;
- 2) Health insurance;
- 3) Insurance in case of unemployment.
- 4) Public expenditures and costs are the following:

Expenditures:

- 1) Expenditures for employees;
- 2) Expenditures for goods and services;
- 3) Depreciation and use of professional means;
- 4) Repayment of interest and related borrowing costs;
- 5) Subsidies;
- 6) Donations and transfers;
- 7) Compulsory social insurance and social protection;
- 8) Other expenditures (taxes, compulsory fees, pecuniary sanctions, penalties etc.).

Government's costs:

- 1) Costs for acquisition of non-financial assets;
- 2) Costs for repayment of principal;
- 3) Costs for acquisition of financial assets.

Provisions of the Law on the Budget System precisely define public revenues and emoluments that belong to the Republic of Serbia, autonomous provinces, local self-

government units and compulsory social insurance organizations for financing activities stemming from their competence.

Adoption of the new Law on the Budget System introduces modern and efficient instruments into the public finances, along with medium-term framework of expenditures and public investment, possibility of introducing three-year budget, adoption of priority financing areas, new budget objectives, such as maintaining overall fiscal discipline, allocational efficiency, technical, and/or operational efficiency, low inflation rate and economic development, stimulating regional development, along with effectiveness, which must be followed during budget preparation and execution etc.

New Law stipulates even stronger obligation of medium-term planning for budget beneficiaries, on all levels of the government. As one of important components of a wider reform process in public finance management, a medium-term plan is defined as a comprehensive budget beneficiary's plan, containing detailed development of all programmes, projects and activities for the budget year, along with projections for the next two years, pursuant to the determined medium-term objectives and priorities. The Law establishes deadlines for gradual procedure of preparing medium-term plans, and/or programme-based display of the budget (in its entirety for adoption of the Law on the Budget of the Republic of Serbia, and/or budgets of local authorities for 2015).

For the purposes of strengthening the stability of public finances, the results of the public finance reforms in this sector should be linking strategic planning, as well as achieving a level of integrity of the budget system in which several thousand budget beneficiaries participate on all levels of government.

Implementation of a medium-term budget framework, and/or introduction of the limit for budget beneficiaries in a multi-year period, within reform of the budget preparation and planning process, shall be done as of the day of adoption of the 2011 budget. For the purposes of stable and sustainable fiscal policy, it is necessary to strengthen the awareness of budget beneficiaries on the need to determine priorities, in order to improve ability of the Government to allocate funds in compliance with its policy.

There were problems in the past period on understanding how the public funds are spent regarding legal persons that do not have the status of neither direct nor indirect budget beneficiary in the current system, which prevented record-keeping nor control of such public funds. Legal persons in questions were agencies founded in compliance with the Law on Public Agencies, regulatory bodies and other beneficiaries. For such reasons, it has been assessed that it is necessary to include them into the consolidated Treasury account, which would enable high-quality and more efficient information on such public funds beneficiaries, better control and rational spending of public funds, which was made possible by the Law on the Budget System. Including those beneficiaries into the consolidated Treasury account is in compliance with GFS standards.

Innovations in the provisions pertaining to internal financial control of the public sector aim to clearly define internal financial control, in compliance with international standards for internal audit, international standards for internal controls and best practices of the European Union. In this way, obligations stemming from the Plan for the Implementation of Priorities Contained in the European Partnership are executed, which include principles, priorities and conditions regarding financial control, adopted by the Government on 7th April 2006.

Inadequacy of the size and structure of public spending in Serbia has been especially evident during the economic crisis. During years of high economic growth rates, fiscal policy was pro-cyclical, through increase of public spending on one side and reduction of fiscal capacity

through decrease of certain tax rates, cancellation of certain taxes and introduction of numerous facilities on the other hand. That prevented fiscal policy to act more in a counter-cyclical manner during recession, because the room for fiscal stimuli to the economy was limited.

Bearing in mind such developments, the need was recognized to expand the existing Law on the Budget System with provisions pertaining to definition of fiscal responsibility and strengthening of fiscal discipline, in order to ensure sustainability of public finances in the medium term, which was accomplished by Amendments and Modifications of the Law on the Budget System, in October 2010.

Developments of General Government Revenue and Expenditure in the Period 2005-2009

In 2005 and 2006, the Republic of Serbia generated high public revenues of around 45% of GDP in average. In 2007 and 2006, the generated public revenues were somewhat lower, around 44.2% of GDP. Somewhat lower public revenues in 2007 were the consequence of change in the tax policy, namely in the area of income tax (reduction of wage tax rate from 14% to 12% and introduction of non-taxable part of wages), and also change of policies regarding other taxes (reduction of tax on transfer of absolute rights from 5% to 2.5%, transferring certain products from higher to lower VAT rate, VAT exemption when buying first apartment etc.), In 2008, there were no significant changes in the tax policy, but spill-over of economic crisis to Serbia in the last quarter brought significant fall in revenues.

Revenue, Expenditure, Result and Public Debt of General Government in % of GDP

| | 2005 | 2006 | 2007 | 2008 | 2009 |
|---------------------|------|------|------|------|------|
| PUBLIC REVENUE | 44,9 | 46,1 | 45,4 | 43,9 | 42,7 |
| PUBLIC EXPENDITURE | 43,9 | 47,7 | 47,3 | 46,5 | 47,0 |
| CONSOLIDATED RESULT | 1,0 | -1,6 | -1,9 | -2,6 | -4,3 |
| PUBLIC DEBT | 50,2 | 36,2 | 29,4 | 25,6 | 31,3 |

In 2009, there was further deterioration of economic developments, and generated public revenues stood at 42.7% of GDP. Main orientation of fiscal policy during the crisis year of 2009 was decrease of public spending, in order to avoid significant increase of fiscal burden on the economy. Within tax policy, changes included increase of excise duties, namely on oil products two times during 2009, as well as increase of excise duties on cigarettes. Such combination of measures kept fiscal deficit in 2009 to slightly lower level than the one agreed with the IMF.

In the period 2005-2009, the Republic of Serbia recorded high share of public expenditure in the GDP. High growth rate of expenditure was recorded in 2006, in the amount of 3.8% relative to 2005. In the period 2007-2009, the share of public expenditure in GDP decreased and amounted to 47% of GDP.

Having recorded a surplus in 2005, fiscal position of the Republic of Serbia deteriorates and public sector records high levels of fiscal deficit, which was financed with borrowings since

the privatization process ended that marked end of inflow on that basis, which lead to relatively high growth of public debt share in GDP.

| | 2005 | 2006 | 2007 | 2008 | 2009 |
|----------------------|------|------|------|------|------|
| PUBLIC REVENUE | 44,9 | 46,1 | 45,4 | 43,9 | 42,7 |
| 1. Operating revenue | 44,7 | 46,0 | 45,1 | 43,8 | 42,4 |
| Tax revenue | 39,8 | 40,4 | 39,6 | 38,6 | 37,5 |
| Personal income tax | 5,6 | 6,0 | 5,0 | 5,0 | 4,7 |
| Corporate income tax | 0,6 | 0,9 | 1,3 | 1,4 | 1,1 |
| Value added tax | 12,8 | 11,5 | 11,5 | 11,1 | 10,5 |
| Excise duties | 4,2 | 4,4 | 4,3 | 4,0 | 4,8 |
| Customs duties | 2,3 | 2,3 | 2,5 | 2,4 | 1,7 |
| Other tax revenue | 1,4 | 1,5 | 1,4 | 1,3 | 1,3 |
| Contributions | 12,7 | 13,6 | 13,6 | 13,4 | 13,3 |
| 1.2. Non-tax revenue | 5,0 | 5,6 | 5,4 | 5,1 | 4,9 |
| 2. Capital income | 0,0 | 0,0 | 0,2 | 0,1 | 0,1 |
| 3. Donations | 0,2 | 0,1 | 0,1 | 0,1 | 0,2 |

Revenue of General Government, broken down by categories, in % of GDP

Personal income tax In 2005 and 2006, the share of income tax in GDP was 5.3% of GDP on average. Reduction of the wage tax rate from 14% to 12% and introduction of non-taxable part of wages permanently reduced these revenues by around 1% of GDP. During the crisis period in the end of 2008 and in 2009, further decline of share of personal income tax revenue occur, primarily due to decrease of employment and slowing down of average wage growth. Annual average wage growth in the 2005-2008 period were 21.5%, while the growth in the January-December period in 2009 was 8.8% nominally relative to the same period previous year. Decline of employment in 2009 relative to 2008 was 5.5%²⁵.

Corporate income tax. In the observed period, the share of corporate income tax in GDP is relatively low. Significant growth of revenue on corporate income tax occurred in 2006, 2007 and 2008. Cause for such growth is the result of positive economic developments in this period, as well as commencement of implementation of international accounting standards for undertakings, which contributed to more realistic results being carried²⁶.

²⁵ RSO revised the data on the number of private entrepreneurs and employees of entrepreneurs' since March 2010.

²⁶ International accounting standards have been applied since 2005, which affected the profit carried for 2005 and corporate income tax calculated and paid out in 2006.

Value added tax. Value added tax was introduced in the Republic of Serbia in 2005, which replaced the turnover tax, applied until then. In 2006 and 2007, the share of the VAT in GDP stabilizes and amounts to slightly more than 11% of GDP. In the last quarter of 2008 and during 2009, export declined significantly (decline of export, expressed in EUR in the period January-December in 2009 relative to the same period previous year, was 29.3%) along with domestic demand, which affected the reduction of share of VAT in GDP.

Excise duties. In the observed period, the revenue on excise duties had relatively stable share in GDP. Significant growth of excise duties share in 2009 is the consequence of changes in excise duty policy, and/or increase of excise duties on oil products and cigarettes.

Customs duties. In the period 2005-2008, the average share of customs duties revenue was 2.2% of GDP. Reduction of customs duties to 1.7% of GDP was the consequence of, partly reduced import, and partly reduction of customs duties' rates, in compliance with liberalization plan contained in the Interim Trade Agreement with the EU.

Other tax revenue. In the observed period, other tax revenues had relatively stable share in GDP. Other tax revenues consist of property tax, tax on using, holding and carrying certain goods and other tax revenues.

Contributions on compulsory social insurance. Contributions represent an item that has the single largest share in GDP. In the observed period, the contributions recorded share of 13.3% in GDP on average.

In period 2005-2009, non-tax revenue and capital income and donations had stable share in the GDP of slightly more than 5% ,on average.

Expenditure of General Government, Broken Down by Categories, in % of GDP

| | 2005 | 2006 | 2007 | 2008 | 2009 |
|-------------------------------------------|------|------|------|------|------|
| II PUBLIC EXPENDITURE | 43,9 | 47,7 | 47,3 | 46,5 | 47,0 |
| 1. Operating expenditure | 40,7 | 43,0 | 41,8 | 41,9 | 42,9 |
| Expenditures for employees | 12,0 | 12,3 | 12,2 | 12,7 | 12,7 |
| Purchase of goods and services | 7,4 | 8,0 | 8,3 | 7,5 | 7,5 |
| Repayment of interest | 1,0 | 1,5 | 0,8 | 0,6 | 0,8 |
| Subsidies | 3,3 | 2,8 | 2,8 | 2,9 | 2,2 |
| Social assistance payments and transfers; | 17,0 | 18,4 | 17,8 | 18,2 | 19,7 |
| Out of which: pensions | 11,1 | 11,6 | 11,3 | 13,0 | 13,8 |
| 2. Capital expenditure | 2,7 | 4,1 | 4,9 | 3,9 | 3,3 |
| 3. Net budget borrowings | 0,5 | 0,6 | 0,7 | 0,7 | 0,7 |

In the period 2005-2009, the Republic of Serbia recorded high share of public expenditure in GDP. High growth rate of expenditure was recorded in 2006, in the amount of 2.3% relative to 2005. In the period 2007-2009, the share of public expenditure in GDP decreased and amounted to 47% of GDP.

In 2006, there was a growth of operating and capital expenditure, while in 2007 structure of public spending was somewhat improved through decrease of operating expenditure by 1.2%, with further growth of public investments by 0.8%. In 2008, there was no growth of operating expenditure, but the reduction of total public spending is the result of reduced public investments. In 2009, operating expenditure was higher by around 1% relative to 2008, regardless of freezing the largest spending categories (wages and pensions). Growth of operating expenditures in 2009 is the result of increase of social assistance payments and other transfers to citizens, in order to maintain living standard of the citizens facing poverty risk, which were particularly affected by the crisis. Growth of **public investments** in 2006 and 2007 is the result of implementation of the National Investment Plan, adopted in 2006.

Individually, the largest part of public spending pertains to **social assistance payments and transfers to citizens**, and the largest item within this category is **pensions**. The largest increase of share of pensions in GDP occurred in 2008, when the pensions were subject to one-off increase by 10% in October, after regular indexations (two times during the year in compliance with the Law on Pension and Disability Insurance). In 2009, the pensions were frozen in compliance with agreed IMF programme (with no regular adjustment), but the growth of share in GDP is the result of the effects of pension increase carried over from 2008 and increase of number of beneficiaries.

Expenditures for employees. The second largest expenditure item, observed individually within public spending, is wages of employees. In the observed period, average share of wages of employees in GDP was around 12.3% annually.

In the observed period, **subsidies and net budget borrowings** make 3.4% of GDP on average. Their share in GDP decreased during the observed period, so that in 2009 it was 0.8% of GDP lower relative to 2005.

10. Extra-budgetary funds: Please list and provide information on extra-budgetary funds. What is the relationship between the budget and the extra-budgetary funds? Which are the implemented/planned steps to integrate the extra-budgetary funds in the government budget? Please provide balance sheet indicators for these funds. Please describe major activities to improve the management of extra-budgetary funds.

The adoption of the new Law on the Budget System marked the beginning of the process of addressing the issue of extra-budgetary funds. Most extra-budgetary funds in Serbia operate in the form of agencies which, in compliance with the Law on Public Agencies, are not subject to the rules governing the budget beneficiaries, and/or the budget system. For now, agencies are not covered by the reporting on the general government fiscal position. Article 8 of the Law on the Budget System provides that the coverage of the general government shall be defined by the Republic Statistical Office, in cooperation with the Ministry of Finance and in compliance with the international standards. With the application of this Article the coverage of the general government will be extended, which means that a part of the fiscal activities performed by extra-budgetary funds will be included in the reporting on the general government fiscal position.

At the moment, there are four extra-budgetary funds in the Republic of Serbia which are included in the general government: Republic Fund for Pension and Disability Insurance,

Republic Health Insurance Bureau, National Employment Service, and the Public Enterprise (PE) "Roads of Serbia". Compulsory social insurance organizations are extra-budgetary funds in the sense that they are individual legal entities, they have separate accounts and separate management bodies, but their operation is entirely regulated by the Law on the Budget System. In compliance with the Law on Budget System, compulsory social insurance organizations apply budgetary procedures prescribed for the budget of the Republic, even though they do not form an integral part of the budget. PE "Roads of Serbia" operates in compliance with the Law on Public Enterprises, but it is part of the general government and prepares regular monthly reports in compliance with the budget accounting rules.

Basic Information about the Republic Fund for Pension and Disability Insurance

Pursuant to Article 63 of the Law on Amendments and Modifications of the Law on Pension and Disability Insurance (*Official Gazette of RS*, No. 85/2005), the Republic Fund for Pension and Disability Insurance of Employees, the Republic Fund for Pension and Disability Insurance of Self-Employed Persons, and the Republic Fund for Pension and Disability Insurance of Farmers were integrated into a single fund on 1 January 2008 - the Republic Fund for Pension and Disability Insurance, organized as a single legal person with the status of a compulsory social insurance organization where the rights arising from pension and disability insurance are exercised and funds for this type of insurance are provided. The provisions of the mentioned Article stipulate that the financial operations of the Fund shall be conducted through three sub-accounts: sub-account for employees, sub-account for the self-employed persons and the sub-account for farmers, until 1 January 2011; as of this date the operations shall be conducted through single account.

The Fund provides pension and disability insurance to all persons that are covered by the compulsory insurance under the Law and are participating in the insurance, irrespective of whether they are employees, self-employed persons or farmers; determines contribution bases in compliance with the Law; ensures special-purpose and economical usage of funds; ensures direct, efficient, cost-effective and lawful exercise of rights arising from pension and disability insurance and organizes the activities necessary for the implementation of insurance; controls the insurance application, as well as all the data pertaining to eligibility, exercise and termination of rights; organizes and administers pension and disability insurance, under the Law; implements international agreements; performs the disbursement of pension benefits, allowances and other payments.

The Fund has approximately 2,767 million insured persons from all categories (around 2.2 million employees, 328,000 self-employed persons and 233,000 insured farmers), as well as 1.58 million pensioners. Out of the total number of pensioners, around 1.3 million are former employees, 52,400 are self-employed pensioners, and around 224,000 are retired farmers.

With the aim to perform its activities successfully and in a cost-effective manner, as well as to ensure the accessibility of rights related to pension and disability insurance, the Fund established its organizational units by relevant functions and across the entire territory of the Republic.

The Fund is managed by the representatives of the insured persons, the employers and the beneficiaries of rights.

The bodies of the Fund are: Management Board, Supervisory Board and the General Manager.

Indexation

From April 2003 to January 2006, pension benefits and compensations were indexed on a quarterly basis - on 1st January, 1st April, 1st July and 1st October, according to the so called Swiss formula that takes into account 50% of the wage growth and 50% of the growth of the costs of living recorded in the previous quarter. Since 2006, the emoluments were indexed on 1 April and 1 October according to the indicators from the previous six months, but the share of wages was gradually reduced, while the share of the costs of living was increased. Notwithstanding, in 2009 and 2010 the pension benefits will not be indexed, the amounts determined in October 2008 will be disbursed (in compliance with the changes to the pension system). The amended Law on the Budget System also regulates the indexation of pension benefits stipulating that the benefits shall be indexed to the general government wages.

Contribution payers

Contribution payers for pension and disability insurance are insured persons in compliance with the law governing the compulsory pension and disability insurance, as follows:

- 1) Employees;
- 2) Elected, nominated and appointed officials who earn remunerations in addition to salaries or wages;
- 3) Persons who perform temporary and occasional work under the contract concluded directly with the employer;
- 4) Persons receiving wage compensation under the law governing financial support for families with children;
- 5) Persons receiving wage compensation under the law governing compulsory health insurance;
- 6) Entrepreneurs;
- 7) Founders, and/or members of a company;
- 8) Farmers;
- 9) Persons earning a contracted fee;
- 10) Independent artists;
- 11) Priests and religious officials;
- 12) Persons receiving financial compensation under the law regulating employment and insurance in case of unemployment;
- 13) Serbian nationals employed abroad;
- 14) Persons participating in the compulsory insurance, in compliance with the law;
- 15) Other insured persons, under the law regulating the system of compulsory pension and disability insurance.

For the insured persons referred to under points 1) to 5), the contribution payers shall also be the employers and/or other payers of income, at the same rate and according to the same base as the mentioned insured persons.

Contribution rate for the mandatory pension and disability insurance is set at 22%, pursuant to Article 44 of the Law on Contributions for Mandatory Social Insurance (*Official Gazette of RS*, Nos. 84/04, 61/05, 62/06, 7/08, 5/09, 7/09 and 3/10).

Contribution base is regulated by the same law, Articles 13 to 35, and it is different for various categories of insured persons (for employees - the wage and remuneration, for farmers - agriculture income taxable under the law regulating personal income tax, for entrepreneurs - taxable profit...)

Attendance allowance

Attendance allowance is provided for the pension beneficiaries and insured persons who, due to the nature of their illness or injury, need the help of other people for everyday activities. Under the Pension and Disability Insurance Law, practically the only persons entitled to this allowance are immobile persons, the blind, dementia sufferers, and the persons who are not able to eat, dress or move indoors without other people's help, as well as the persons undergoing dialysis. In cases when a disability commission concludes that the medical condition can improve, a medical examination is scheduled.

Bodily injury benefit

Bodily injury benefit is provided to the insured persons who, due to the injury at work or occupational disease, have lost or suffered a severe damage of organs or body parts.

Domestic pension benefits abroad

Pension benefits earned in Serbia are disbursed in 20 countries across the world (former Yugoslav republics excluded). More than half of the total of 10,322 such pension beneficiaries live in Germany, followed by Austria, Hungary, France, Czech Republic, Switzerland, Sweden, USA... These pension benefits are disbursed on a quarterly basis due to great administrative costs and relatively small benefit amounts.

Former republics

Pension Fund disburses pension benefits for approximately 24,016 of its beneficiaries living in the former SFRY republics (Croatia - around 5,751; Republika Srpska - around 6,243; Macedonia - around 4,243; Bosnia and Herzegovina - around 4,541; Montenegro - around 3,235). The total monthly amount of these benefits equals approximately RSD 316 million.

International agreements

Serbia has concluded social insurance agreements with 25 countries governing the issues of recognition of the years of service, health insurance, disbursement of pension benefits, child allowances and other benefits.

The text of the agreement with Canada has been agreed upon.

Planned agreements – with Greece, Russia, Cyprus, Australia, New Zealand, Ukraine, Quebec.

Contribution limit

The highest annual base for the payment of the pension and disability insurance equals five average wages. The contribution is paid for every income, including honoraria, special service

agreements, contracts on temporary and casual work, compensation for the membership in management and supervisory boards

Basic information about the Republic Health Insurance Bureau

Republic Health Insurance Bureau is a legal person established pursuant to the Law on Health Insurance (*Official Gazette of RS*, No. 18/92...45/05) with the status of a compulsory social insurance organization where the rights arising from health insurance are exercised and funds for mandatory health insurance are provided, in compliance with the law.

The Republic Institute for Health Insurance is a national, public and non-profit organization through which Serbian citizens exercise their health insurance rights.

The Bureau is funded through the payment of health insurance contributions. Thus, the Serbian citizens are enabled to finance their healthcare services through the Republic Bureau.

The contribution rate is set at 12.3%.

All citizens generating income (wages, pension benefits, fees...) are legally bound to pay health insurance contributions. Health insurance contributions for citizens who do not generate income and who cannot be insured as family members of persons generating income are paid from the budget of the Republic of Serbia.

The healthcare rights laid down in the Law also include the right to use healthcare services abroad.

Pursuant to Article 22 of the Law on Health Insurance (*Official Gazette of RS*, No. 107/05 and 109/05 – Corrigendum), the insured persons shall also include all persons belonging to population groups at higher risk of illness, persons whose healthcare is needed with respect to prevention, curbing, early-stage diagnosis and treatment of diseases of higher social and medical importance; as well as persons belong to socially vulnerable population categories, if not covered by insurance in accordance with Article 17 of this Law or if such persons do not exercise rights arising from compulsory health insurance as family members.

The Law also provides that the insured persons shall include the persons to whom the competent Republic authority has assigned the status of a refugee or a displaced person from former Yugoslav republics, if they meet legally prescribed conditions and reside in the territory of the Republic.

The Law also lays down the right of military invalids to receive healthcare.

The Serbian healthcare system conforms to the principles of equality and solidarity. Citizens pay health insurance contributions by percentage, according to their income and financial capacity, and they use healthcare services according to their needs.

Rights, obligations and liability of the Bureau are governed by the Law on Health Insurance and the Statute of the Bureau.

The bodies of the Bureau are: Management Board, Supervisory Board and the General Manager.

Compulsory health insurance includes:

- 1) Insurance in case of illness and injuries sustained outside of work;
- 2) Insurance in case of injury at work or occupational disease.

Compulsory health insurance rights include:

- 1) Right to healthcare;
- 2) Right to wage compensations during temporary work disability (wage compensation);
- 3) Right to reimbursement of travel costs related to using healthcare services (travel costs reimbursement).

The Bureau performs the following activities:

- 1) Passes the Statute;
- 2) By the authority specified in the Law, passes general acts that regulate in more detail the administration of the mandatory health insurance;
- 3) Plans and provides financial assets for the administration of the compulsory health insurance;
- 4) Within the available financial assets, plans and ensures conditions for the balanced administration of the compulsory health insurance in the territory of the Republic, and provides solidarity funds equalizing the conditions for the granting of rights arising from the compulsory health insurance in the territories of branch offices;
- 5) Ensures financial and other conditions for the exercise of the right to receive healthcare services abroad and/or to be sent to the medical treatment abroad;
- 6) Passes the work plan for granting of rights arising from the compulsory health insurance in line with the activity plan of branch offices;
- 7) Passes the financial plan, in compliance with the Law;
- 8) Concludes contracts with the providers of healthcare services in compliance with the Law, and provides resources for the implementation of the healthcare on the basis the contracts;
- 9) Transfers funds for the administration of compulsory health insurance to the branch offices, in compliance with Article 202 of this Law;
- 10) Ensures lawful, special-purpose and economical usage of funds and makes sure that the resources are increased on economic grounds;
- 11) Ensures direct, efficient, economic and lawful exercise of health insurance rights and organizes activities needed for the administration of health insurance that is directly administered in the Bureau;
- 12) Organizes activities needed for the administration of health insurance that is directly administered in the Bureau;
- 13) Coordinates the work of branch offices and the Provincial Bureau;
- 14) Organizes and controls the work conducted by branch offices, the lawful and special-purpose usage of funds transferred to branch offices for the exercise of rights arising from the mandatory health insurance;
- 15) Controls the implementation of the contracts concluded between the branch offices and the providers of healthcare service, and controls the exercise of rights arising from the mandatory health insurance;
- 16) Establishes and organizes the central records and controls the related activities;
- 17) Organizes, controls and harmonizes the work of the first and second degree medical commissions;

- 18) Ensures the implementation of international agreements pertaining to compulsory health insurance;
- 19) Keeps records and monitors the collection of contribution, exchanges data with the competent authorities regarding the health insurance contribution payers, as well as other data pertaining to the contribution;
- 20) Performs other tasks specified in the Law and the Bureau's Statute.

The Republic Bureau for Health Insurance contracts the provision of healthcare services to its insured persons with the medical institutions included in the so called Network of Medical Institutions. The Network is adopted by the Government of the Republic of Serbia, at the proposal of the Ministry of Health.

The Institute can also enter into contracts with the institutions outside the Network, but only for the volume and type of medical services that cannot be provided within the existing capacities of the medical institutions included in the Network.

The opinion regarding the justification of concluding the contract for the volume and type of services with the institutions outside the Network is provided by the Serbian Institute for Public Health "Dr Milan Jovanovic-Batut", while the consent for the conclusion of the contract is given by the Ministry of Health.

Voluntary insurance

The Republic Bureau for Health Insurance administers voluntary health insurance with the aim to enable the citizens to exercise the rights not covered by the compulsory health insurance under the most favourable conditions.

By concluding a contract on voluntary health insurance, the insured persons can exercise a different type and/or a greater volume, content and standard of rights than the rights guaranteed under the compulsory insurance.

The rights arising from the voluntary health insurance also include the rights exercised within the compulsory health insurance, but in a different manner and according to the different procedure (e.g. the rights arising from the compulsory insurance that require the doctor referral letter can be exercised without such referral letter).

Number of insured persons

As of 31st December 2009, there were 6,786,333 insured persons under the compulsory health insurance in Serbia.

Total of 2,958,668 persons were insured on the basis of employment, which make up 43.60% of the total number of insured persons under the compulsory insurance. The above figure is followed by the number of insured persons on the basis of retirement, 1,842,066 insured persons, and/or 27.14%, which is followed by the number of persons whose insurance is financed from the Republic of Serbia Budget that stands at 1,210,157, and/or. 17.83%.

Basic information about the National Employment Service

The National Employment Service was established pursuant to the Law on Employment and Unemployment Insurance, published in the *Official Gazette of RS*, No. 71/03 dated 15th July

2003. The National Employment Service, as the legal successor of the Republic Bureau for Labour Market, was entered into the registry of the competent court on 16th March 2004, and the new Law on Employment and Unemployment Insurance (*Official Gazette of RS*, No. 36/09 and 88/10) confirms the continued existence of the National Employment Service as an institution competent for employment affairs. The Service has existed for over 90 years as an institution dealing with employment affairs

In line with the Rulebook on Organization and Classification of Jobs in the National Employment Service, the Service set up its organizational units by relevant functions and across the entire territory of the Republic, and all the activities falling under its scope of work are performed in the National Employment Service – the Directorate – Belgrade, the Provincial Employment Service AP Vojvodina, the Provincial Employment Service of AP Kosovo and Metohija, and 34 branch offices comprised of services, departments and branches located in approximately 180 premises across the Republic of Serbia.

The National Employment Service conducts employment affairs, affairs related to the insurance in case of unemployment, activities regarding the exercise of unemployment insurance rights and other rights pursuant to the law, as well as employment related record keeping, professional and organizational, administrative, economic and financial and other general affairs in the field of employment and insurance in case of unemployment, in compliance with the law, this Statute and other acts passed by the National Employment Service.

The scope of work of the National Employment Service includes:

- 1) Notification on employment opportunities and conditions;
- 2) Implementation of active employment policy measures: Job matching for persons seeking employment in the country and abroad; vocational guidance and career counselling; employment subsidies; support to self-employment; further education and training; incentives for users of unemployment benefit; public works and other measures designed for the persons seeking employment;
- 3) Issuing work permits to foreigners and stateless persons, pursuant to the law;
- 4) Exercise of rights arising from insurance in case of unemployment;
- 5) Insurance in case of unemployment;
- 6) Employment related record keeping in line with the Law;
- 7) Employment abroad;
- 8) Protection of persons employed abroad;
- 9) Adopting decisions regarding the assessed working capacities and possibilities for employment, or maintenance of employment of the persons with disabilities;
- 10) Stimulating the employment of persons with disabilities;
- 11) Professional rehabilitation of persons with disabilities;
- 12) Other activities specified in the law.

The bodies of the National Employment Service are: Management Board and the General Manager of the National Employment Service.

Management Board manages the work of the National Employment Service.

The General Manager represents and acts on behalf of the National Employment Service.

The Funds of the National Employment Service are used for the purposes specified in the National Employment Action Plan, work programme and financial plan of the Service, in compliance with the law and the Statute.

The Law on Employment and Unemployment Insurance (*Official Gazette of RS*, No. 36/09 and 88/10), inter alia, stipulates that the mandatory insurance shall involve following unemployment rights:

- 1) Unemployment benefit;
- 2) Health insurance and pension and disability insurance in compliance with the law;
- 3) Other rights in compliance with the law.

The person covered by compulsory insurance shall be entitled to unemployment benefit if he/she was insured for at least 12 months continuously or intermittently within the past 18 months.

Insurance with an interruption shorter than 30 days shall also be deemed continuous insurance.

Contribution rate for compulsory pension and disability insurance is set at 1.5 %, pursuant to Article 44 of the Law on Contributions for Mandatory Social Insurance (*Official Gazette of RS*, No. 84/04, 61/05, 62/06, 7/08, 5/09, 7/09 and 3/10).

The base for computation of unemployment benefit shall be the average salary or wage, or wage compensation of the unemployed person, as appropriate, received in the last six months prior to the month in which his/her employment contract or insurance was terminated.

The unemployment benefit shall equal 50% of the base and may not be higher than 160% or lower than 80% of the minimum wage determined pursuant to labour regulations for the month in which the unemployment benefit is paid. Such amount of the benefit represents the base for the computation of contributions for the pension and disability insurance, as well as for the health insurance. The amount of the benefit representing the base for the computation of contributions shall be reduced by the amount of the contribution determined according to the applicable rates and such reduced amount shall be paid to the benefit user.

The number of benefit users receiving the benefit stood at 81,190 in February, while the average amount of the paid unemployment benefit equalled RSD 21,910.

On the basis of the Conclusion of the Government of Republic of Serbia No. 02-4586/2003-001 passed on 17th July 2003, the National Employment Service is obligated to pay the benefits to the persons temporarily displaced from the territory of the AP Kosovo and Metohija.

The number of persons from K&M receiving the benefit for the employed stood at 20,900 in February, while the average amount of the paid benefit equalled RSD 15,000.

Within the active employment policy measures, determined by the Government at the proposal of the Ministry of Economy and Regional Development and in compliance with the Law on Employment and Insurance in Case of Unemployment, the National Employment Service implements programmes and plans resources for their implementation.

For these purposes the following allocation of funds is planned:

- 1) For job matching measures (vocational guidance and career counselling, active job seeking, job seeking club and job fairs);

- 2) For further education programmes and trainings aimed at acquiring additional knowledge and skills (interns, re-training, additional vocational training);
- 3) For incentive measures aimed at supporting and developing entrepreneurship, subsidies for self-employment, job-creation subsidies and organization of public works.

PE “Roads of Serbia”

The management system in the field of roads has been changing. Since the political changes introduced in 2000, the road management system in the Republic of Serbia experienced various institutional forms. Until 22nd February 2006, the management of roads in the territory of the Republic of Serbia was under the competence of the Republic Directorate for Roads, a separate Republic organization with the status of a budget beneficiary. Pursuant to the new Law on Public Roads (*Official Gazette of RS*, No. 101/05 and 123/07) and on the basis of the Decision of the Republic of Serbia Government (*Official Gazette of RS*, No. 115/05), the public enterprise “Roads of Serbia” was established and started operating on 23rd February 2006. In view of the sources of financing (the percentage of the excise duties on oil derivatives, road toll and transfers from the budget), as well as due to the particular business activity of this public enterprise - management of national roads, this public enterprise is treated as an extra-budgetary fund, and as such it is included in the fiscal reports at the general government level.

The procedure for the adoption of the Business Plan of the public enterprise “Roads of Serbia” is as follows: Management Board of the PE “Roads of Serbia” adopts the annual Business Plan which is then submitted to the line ministry (Ministry of Infrastructure). The opinion to the plan is given by the following ministries: Ministry of Finance, Ministry of Economy and Regional Development, Ministry of Labour and Social Policy, Ministry for the National Investment Plan and the Secretariat for Legislation. After the positive opinions are obtained, the Plan is submitted to the Government for approval. Government's approval to the Business Plan is published in the *Official Gazette of RS*.

Sources of financing the construction, reconstruction and maintenance of public roads are defined in the Law on Public Roads (*Official Gazette of RS*, No. 101/05 and 123/07), and these are:

- 1) Tolls for the usage of public roads;
- 2) Fees for the maintenance of public roads set as a percentage of the excise duty on oil derivatives and liquid petroleum gas in the amount of:
 - a. 10% - from February 2006 to the end of 2007;
 - b. 15% - from January 2008 to the end of 2008;
 - c. 20% since 1 January 2009;
- 3) Loans;
- 4) Investments by domestic and foreign persons;
- 5) Budget of the Republic of Serbia;
- 6) Other sources in accordance with the Law.

Funds collected from above sources are used for the maintenance of roads, construction, reconstruction and rehabilitation of roads, preparation of studies and projects, loan repayment, as well as for covering the costs of PE “Roads of Serbia”.

Being a public enterprise, "Roads of Serbia" prepares financial statements in accordance with the rules of corporate accounting, but also provides the Ministry of Finance with monthly reports on generated revenues and executed expenditures, in conformity with the principles and rules of budget accounting. On the basis of these reports, the data on revenues and expenditures, as well as data on the borrowing and loan repayment of the PE "Roads of Serbia" are included in the fiscal reports prepared at the general government level.

In the course of public finance management reforms, several areas have been identified as areas where changes should be made in order to fully align these areas to the applicable international standards. One such area is the coverage of the general government, which should be defined as specified in the Government Finance Statistics Manual 2001 - GFSM2001, with the aim to enable a more comprehensive overview of the fiscal policy effects. At the moment, in addition to the budget of the Republic of Serbia, as central government level, the general government includes budgets of the local governments, and four extra-budgetary funds: Republic Fund for Pension and Disability Insurance, Republic Health Insurance Bureau, National Employment Service, and the Public Enterprise (PE) "Roads of Serbia".

As there are numerous entities (institutions) that have the features of extra-budgetary funds but are currently not included in the general government and are not subject to the rules laid down in the Law on Budget System, the first step in this reform process is to identify all extra-budgetary funds at the central government level and draw up a list of all these funds.

The new Law on Budget System (Article 1) provides that certain provisions of the Law may also be applied to the extra-budgetary funds as soon as the conditions for the better regulation of these funds are created and the adoption of their financial plans is aligned with the budget process to the greatest extent possible.

Article 1

"This Law shall regulate the following: planning, preparation, adoption and execution of the Republic of Serbia Budget; planning, preparation, adoption and execution of the budgets of the Autonomous Provinces and local government units (hereinafter: local government budget); preparation and adoption of financial plans of the Republic Pension and Disability Insurance Fund, Republic Bureau for Health Insurance and National Employment Service (hereinafter: compulsory social insurance organizations); budget accounting and reporting, financial management, control and audit of users of public funds and Republic of Serbia Budget beneficiaries, local government budgets and financial plans of compulsory social insurance organizations; competence and organization of the Treasury Administration, as an authority within the Ministry of Finance (hereinafter: the Treasury) and local government treasuries; other issues of importance for the functioning of the budget system.

Certain provisions of this Law shall regulate budget relations and rules applied to extra-budgetary funds, business entities and other legal persons in which the government, on all government levels, has a decisive influence on management, and especially on the following: drafting of financial plans, management of funds, borrowing and issuing of guarantees, accounting, drafting and submission of reports and execution of budget control, which, owing to the sources of financing and control, are included in the general government (hereinafter: extra-budgetary beneficiaries)."

Following the identification of all extra-budgetary beneficiaries, a systemic revision of all funds shall be conducted in order to determine which funds should exist in the form of extra-budgetary funds due to economic or political reasons and are not part of the budget as such,

but consolidated when general government data are reported, and which funds must be fully integrated into the budget process.

11. Budgetary system: Please describe the features of the planning, programming and execution process of the government budget. Please indicate policy objectives, developments and achievements as regards budgetary policy. Are the social partners consulted at the planning/programming stage of the budget cycle? How is the efficiency and effectiveness of government spending ensured? What are the implemented/imminent (in 2011) systemic reforms to enhance the long-term fiscal sustainability?

The Law on the Budget System (*Official Gazette of RS*, No. 54/09) regulates planning, preparation, adoption and execution of the budget of the Republic of Serbia, autonomous provinces, units of local self-government and preparation and adoption of financial plans of the Republic Fund for Pension and Disability Insurance, Republic Institute for Health Insurance and the National Employment Service (mandatory social insurance organisations).

Article 31 of the Law

The process of preparation and adoption of the budget and financial plans of mandatory social insurance organisations shall be carried out according to the budget calendar, as follows:

1) Calendar for the level of the Republic of Serbia:

15 March – direct beneficiaries of the Republic of Serbia budget shall submit to the Ministry proposals for determining priority areas of financing for the budget year and the two following fiscal years;

1 April – the Government, according to the proposal agreed upon by the Ministry and the special Government body, shall determine priority areas of financing, including national investment priorities for the budget year and the two following fiscal years;

10 April – the Government shall organise a public debate on the priority areas of financing, including national investment priorities for the budget year and the two following fiscal years;

30 April – the Minister, in cooperation with ministries and institutions in charge of economic policy and economy system, and taking into account the public debate, shall prepare the Memorandum containing economic and fiscal policy of the Government, with projections for the budget year and the two following fiscal years;

15 May – the Government shall adopt the Memorandum;

1 June – the Minister shall adopt the instruction for the preparation of the draft budget of the Republic of Serbia;

1 June – the Minister shall submit the Memorandum to the local government and organisations for mandatory social insurance;

1 September – direct beneficiaries of the Republic of Serbia budget and organisations for mandatory social insurance shall submit proposal for the medium-term and financial plan to the Ministry;

1 October – the Government, at the proposal of the Minister, shall adopt the revised Memorandum, together with information on financial and other effects of new policies, taking into account the updated macroeconomic framework after 30 April;

15 October – the Minister shall submit to the Government the Draft Law on Budget of the Republic of Serbia, draft decisions on giving consent to financial plans of organisations for mandatory social insurance together with financial plans of organisations for mandatory social insurance;

1 November – the Government shall adopt Proposal for the Law on Budget of the Republic of Serbia and shall submit it, together with the revised Memorandum, the proposals for decisions on giving consent to financial plans of organisations for mandatory social insurance and financial plans of organisations for mandatory social insurance, to the National Assembly;

15 December – the National Assembly shall adopt the Law on Budget of the Republic of Serbia and decisions on giving consent to financial plans of organisations for mandatory social insurance;

2) ***Calendar for the local government budget:***

15 June – local government finance authority shall issue the instruction for the preparation of the draft local government budget;

1 September – direct beneficiaries of the local government budget shall submit proposal of the financial plan to the local government finance authority for the budget year and the two following fiscal years;

15 October – local government finance authority shall submit Draft Decision on Budget to the local government executive authority;

1 November – local government finance authority shall submit Draft Decision on Budget to the local government executive authority;

20 December – local government assembly shall adopt the Decision on the Local Government Budget;

25 December – local government finance authority shall submit to the Minister the Decision on the Local Government Budget.”

On the basis of the regulated budget calendar, individual provisions of the Law on the Budget System regulate, in detail, the process of planning and preparation, whose overview follows further in the text.

After the priority areas of financing have been determined, including national investment priorities for the budget year and the two following fiscal years, the Government adopts the Memorandum on the Budget and Economic and Fiscal Policy, an act determining medium-term macroeconomic and fiscal framework, on the basis of which budgets and financial plans of budget beneficiaries and organisations for mandatory social insurance are to be adopted.

After the Memorandum has been adopted, direct beneficiaries of the Republic of Serbia budget are being provided with the Instruction for the Preparation of the Budget of the Republic of Serbia, whose contents are prescribed by Article 35 of the Law on the Budget System, as follows:

“Following the adoption of the Memorandum, the Ministry shall provide direct beneficiaries of the Republic of Serbia budget with the instruction for the preparation of medium-term and financial plans for the preparation of the budget of the Republic of Serbia.

The instruction referred to in paragraph 1 hereof shall contain:

- 1) basic economic assumptions and guidelines for the preparation of the budget beneficiary financial plan proposal and the draft budget of the Republic of Serbia;
- 2) volume of funds which can be contained in the financial plan proposal of a direct beneficiary of the Republic of Serbia budget for the budget year, with projections for the two following fiscal years, determined by the medium-term expenditure scope from the Memorandum;
- 3) guidelines for the preparation of medium-term plans of direct beneficiaries of the Republic of Serbia budget;
- 4) guidelines and requests for elaboration, medium-term quantification and estimation of the effects of new policies and investment priorities;
- 5) procedure and schedule for the preparation of the Republic of Serbia budget and for the preparation of financial plan proposals of direct beneficiaries of the Republic of Serbia budget;
- 6) the manner in which the beneficiaries shall present expenditures and outflows in the financial plan proposal.”

Article 37

According to the instruction for the preparation of the draft Republic budget and medium-term plans, direct budget beneficiaries shall prepare medium-term and financial plan proposal.

Financial plan proposal referred to in paragraph 1 hereof shall contain:

- 1) expenditures and outflows for a three-year period, presented according to budget classification;
- 2) a detailed written explanation of the expenditures and outflows, as well as sources of financing.

Budget beneficiary financial plan proposal shall be submitted in the amount equal to the amount of the scope of funds of the first year of medium-term expenditure framework, defined in the Memorandum.

Parts of the financial plan proposal referred to in paragraph 2 hereof shall consist of a written explanation, including also elaboration, medium-term quantification and estimation of new policies and investment priorities effects, according to the Instruction for the Preparation of the Budget of the Republic and medium-term plans of beneficiaries of the Republic of Serbia funds, and financial request.”

Article 39 of the Law, which regulates consideration of budget requests, says:

The Ministry shall consider the requests of budget beneficiaries and organisations for mandatory social insurance contained in their financial plan proposals taking into account the following:

- 1) targeted revenues and inflows and expenditures and outflows;

- 2) data and explanations according to the Article 37 hereof;
- 3) compliance with the guidelines set forth by the Memorandum and priorities determined by the Government.

Prior to the preparation of the draft budget, the Minister shall notify the direct budget beneficiaries on the proposed amounts of revenues and inflows and expenditures and outflows, and the organisations for mandatory social insurance shall be notified on the proposal for a financial plan that is not compliant with the guidelines set forth by the Memorandum.

Direct budget beneficiaries shall submit their opinion to the Minister regarding the amount of funds and the notification referred to in paragraph 2 hereof, and the organisations for mandatory social insurance shall submit their opinion to the competent direct budget beneficiary.

In case the agreement indicated in paragraphs 2 and 3 hereof cannot be reached, the Government shall instruct that the irregularities in the financial plan of the organisation for mandatory social insurance be removed.

The competent authority of the organisation for mandatory social insurance indicated in Article 6, paragraph 6 shall be obliged to modify financial plan in accordance with the Government's stance."

Article 36 of the Law, which regulates recommendation to the local government, organisations for mandatory social insurance and indirect budget beneficiaries, states that:

"The Minister shall submit the Memorandum to the local government and the mandatory social security organisations.

Line ministries shall inform indirect beneficiaries of the Republic of Serbia budget about basic economic assumptions and guidelines for the preparation of the Republic of Serbia budget.

Local government finance authority shall inform direct beneficiaries of the local government budget about the basic economic assumptions and guidelines for the preparation of the local government budget, while the direct beneficiary of the local government funds shall inform indirect beneficiaries of the local government budget.

Article 38

Organisations for mandatory social insurance shall be obliged to prepare financial plans according to the guidelines set forth by the Memorandum.

Line ministries shall be obliged to ask the organisations for mandatory social insurance to submit the data necessary for the evaluation of their submitted financial plan proposals, in accordance with the guidelines and time limits prescribed by the Minister.

The Minister can ask directly the organisations for mandatory social insurance to submit the data related to their financing, necessary for the preparation of the draft budget of the Republic of Serbia and for evaluation of their submitted financial plan proposals.

Line ministry shall be obliged to submit the financial plan of an organisation for mandatory social insurance to the Minister, who shall submit it to the Government, together with the draft budget of the Republic of Serbia and draft decisions on giving consent to financial plans of organisations for mandatory social insurance, and/or proposed Government act on rejection of said financial plans.

The financial plan indicated in paragraph 4 hereof shall be submitted by the Government to the National Assembly, together with the Proposal for the Law on Budget of the Republic of Serbia and proposal for decisions on giving consent to the financial plans of organisations for mandatory social insurance.

The financial plan of an organisation for mandatory social insurance shall be adopted pursuant to Article 6 paragraph 3 of this Law.

Financial plan proposals of indirect beneficiaries of the Republic of Serbia budget shall be prepared according to the guidelines set forth by the Memorandum.

Instruction for the preparation of the local government budget is regulated **under Article 40 of the Law**, as follows:

"Following the reception of the Memorandum, the local government finance authority shall submit the instruction for the preparation of the local government budget to direct beneficiaries of the local government budget.

The instruction referred to in paragraph 1 hereof shall contain:

- 1) basic economic assumptions and guidelines for the preparation of the draft local government budget;
- 2) description of the local government planned policy;
- 3) estimated revenues and inflows and expenditures and outflows of the local government budget for the budget year and the two following fiscal years;
- 4) volume of funds which can be contained in the financial plan proposal of a direct beneficiary of the local government budget for the budget year, with projections for the two following fiscal years;
- 5) guidelines for the preparation of medium-term plans of direct beneficiaries of the local government budget;
- 6) procedure and schedule for the preparation of the local government budget and for the preparation of financial plan proposals of direct beneficiaries of the local government budget."

Article 41

According to the instruction for the preparation of the draft local government budget, the local budget direct beneficiaries shall prepare financial plan proposal and submit it to the local government finance authority.

In terms of the content of the financial plan proposal of the local government budget direct beneficiaries, provisions of Article 37 of this Law shall be duly applied.

Indirect beneficiaries of the local government budget are obliged to prepare proposal of the financial plan in accordance with the guidelines pertaining to the local government budget.

Direct beneficiaries of the local government budget shall be obliged to ask indirect budget beneficiaries under their responsibility to submit the data necessary to prepare financial plan proposal of the direct budget beneficiary, in accordance with the guidelines and time limits prescribed by the competent local government executive authority.

Local government finance authority can ask directly the indirect budget beneficiaries to submit the data on their financing, necessary for the preparation of the proposal of the local government budget.”

Preparation of the budget proposal and proposal of decisions on giving consent to financial plans of organisations for mandatory social insurance and their submission to the National Assembly, and/or to the local government assembly, is regulated **under Article 42 of this Law**, as follows:

The Minister shall submit to the Government the Draft Law on Budget of the Republic of Serbia and draft decisions on giving consent to financial plans of organisations for mandatory social insurance, together with financial plans of organisations for mandatory social insurance.

The Government may ask the Minister to submit additional information or explanations regarding the Draft Law on Budget of the Republic of Serbia, draft decisions on giving consent to financial plans of organisations for mandatory social insurance and financial plans of organisations for mandatory social insurance.

The Government shall decide on the amendments of the Draft Law on Budget of the Republic of Serbia, adopt the Proposal for the Law on Budget of the Republic of Serbia, evaluate financial plans of organisations for mandatory social insurance, prepare proposals of decisions on giving consent to financial plans of organisations for mandatory social insurance and submit them to the National Assembly together with the Memorandum;

Local government finance authority shall submit Draft Decision on Budget of the local government to the local government executive authority and at the same time inform the citizens on the Draft Decision on Budget.

Competent local government executive authority can ask directly the local government finance authority for additional information or explanations regarding the Draft Decision on Budget of the local government.

Competent local government executive authority shall prepare Proposal for the Decision on Budget of the local government and shall submit it to the local government assembly, within time limits determined by the budget calendar.

If the competent local government executive authority does not submit Proposal for the Decision on Budget to the local government assembly within the time limits determined by the budget calendar, the local government assembly may adopt the budget.”

The National Assembly and the local government assembly adopt the Law on Budget of the Republic of Serbia and the Decision on Budget of the local government, respectively. Also, the National Assembly adopts decisions on giving consent to financial plans of organisations for mandatory social insurance.

With the aim of strengthening the stability of public finances, the result of the public finance reform in this sector should be integration of strategic planning, as well as establishing integrity of the budget system, in which several thousand beneficiaries participate on all levels of government (over 9500 beneficiaries).

Within the reform of the budget planning and preparation process, the implementation of the medium-term budget framework and introduction of limits for budget beneficiaries in the several-year period shall be applied in the process of adopting the budget for 2011. In order to maintain stable and sustainable fiscal policy it is necessary that the budget beneficiaries

become fully aware of the need to identify priorities, so that the capability of the Government to allocate resources according to its policy could be improved.

Deadline for the full implementation of programme budgeting, in accordance with the Law on the Budget System, is the year 2015.

With the aim of further improvement of public finance management, the Law on Amendments and Modifications of the Law on the Budget System (*Official Gazette of RS*, No. 73/10) sets forth fiscal principles, rules and procedures, on the basis of which the fiscal framework is to be determined, and, accordingly, the respective Article of the Law, regulating the budget calendar, has been changed. This Article will be in force as of 1 January 2011:

Article 31 of the Law

The process of preparation and adoption of the budget and financial plans of mandatory social insurance organisations shall be carried out according to the budget calendar, as follows:

1) *Calendar for the level of the Republic of Serbia:*

(1) 15 February – the Minister shall give instruction for the proposal of the priority areas of financing;

(2) 15 March – direct beneficiaries of the Republic of Serbia budget shall submit to the Ministry proposals for determining priority areas of financing for the budget year and the two following fiscal years, according to the instruction indicated under item (1);

(3) 30 April – the Minister, in cooperation with ministries and institutions in charge of economic policy and economy system, shall prepare the Report on Fiscal Strategy, which contains economic and fiscal policy of the Government with projections for the budget year and the two following fiscal years;

(4) 15 May – the Minister shall submit Draft Report on Fiscal Strategy to the Fiscal Council;

(5) 15 June – the Fiscal Council shall give their opinion on the Draft Report on Fiscal Strategy;

(6) 1 July – the Minister shall submit Proposal for the Report on Fiscal Strategy to the Government for adoption;

(7) 15 July – the Government shall adopt the Report on Fiscal Strategy and submit it to the National Assembly for consideration;

(8) 1 August – the Minister shall submit instruction for the preparation of the draft budget of the Republic of Serbia;

(9) 1 August – the Minister shall submit the Report on Fiscal Strategy to the local government and organisations for mandatory social insurance;

(10) 31 August – the National Assembly shall submit to the Government comments and recommendations in relation to the Report on Fiscal Strategy;

(11) 15 September – direct beneficiaries of the Republic of Serbia budget and organisations for mandatory social insurance shall submit their proposals for medium-term and financial plan to the Ministry;

(12) 1 October – the Government, at the proposal of the Minister, shall adopt the revised Report on Fiscal Strategy, together with information on financial and other effects of new policies, taking into account the updated macroeconomic framework after 30 April;

(13) 5 October – the Government shall submit to the National Assembly the revised Report on Fiscal Strategy;

(14) 15 October – the Minister shall submit to the Government the Draft Law on Budget of the Republic of Serbia, draft decisions on giving consent to financial plans of organisations for mandatory social insurance together with financial plans of organisations for mandatory social insurance;

(15) 1 November – the Government shall adopt Proposal for the Law on Budget of the Republic of Serbia and shall submit it, together with proposals for decisions on giving consent to financial plans of organisations for mandatory social insurance and financial plans of organisations for mandatory social insurance, to the National Assembly;

(16) 15 December – the National Assembly shall adopt the Law on Budget of the Republic of Serbia and decisions on giving consent to financial plans of organisations for mandatory social insurance;

2) *Calendar for the local government budget:*

(1) 15 August – local government finance authority shall issue the instruction for the preparation of the draft local government budget;

(2) 15 September – direct beneficiaries of the local government budget shall submit proposal of the financial plan to the local government finance authority for the budget year and the two following fiscal years;

(3) 15 October – local government finance authority shall submit Draft Decision on Budget to the local government executive authority;

(4) 1 November – local government executive authority shall submit Draft Decision on Budget to the local government assembly;

(5) 20 December – local government assembly shall adopt the Decision on the Local Government Budget;

(6) 25 December – local government finance authority shall submit to the Minister the Decision on the Local Government Budget.

Dates indicated in the paragraph 1 hereof shall mean the final dates in the budget calendar.”

The process of preparation and planning of the budget and financial plans of organizations for mandatory social insurance shall be carried out in accordance with changes laid down in the Law on Amendments and Modifications of the Law on the Budget System.

Participation of social partners in the planning phase of the budget cycle

In the Republic of Serbia, the right to participate in collective bargaining process is granted to a trade union or an association of trade unions on one side, and an employer or several employers or an association of employers on the other side, them being social partners in the bargaining (decision-making) process.

The Social-Economic Council of the Republic of Serbia has been founded by the Law on Social-Economic Council (*Official Gazette of RS*, No. 125/04) with the aim of establishing and developing social dialogue regarding issues of importance for realisation of economic and social freedoms and human rights, material, social and economic position of employees and employers and their living and working conditions, development of bargaining culture, promotion of amicable resolution of collective labour disputes and development of democracy. The Council consists of trade union representatives, association of employers' representatives as well as Government representatives (the Government being the largest individual employer in the Republic).

The Law on Labour (*Official Gazette of RS*, No. 24/05...54/09) as a general regulation sets forth the obligation of collective bargaining, but also the obligation of fulfilling responsibilities determined by such collective bargaining process (General Collective Agreement, Special Collective Agreements, Individual Collective Agreements, etc.). Partners participating in the preparation of collective agreements define: rights and obligations of the agreement parties, implementation of the collective agreement, dispute resolution, interpretation, cancellation, renewal and modification of a collective agreement, as well as other issues related to employment relations, and maintenance of social peace.

Pursuant to Article 29 of the Law on Government of the Republic of Serbia (*Official Gazette of RS*, No. 5/91 and 45/93), on 24 April 2003 the Government has adopted a Conclusion by which it has adopted the Strategy for Bargaining with Civil Servants' Trade Unions regarding wage policy. The objectives that the Government has achieved by adopting this strategy are: ensuring that the unique policy regarding wages is pursued by the Government of the Republic of Serbia during bargaining process with civil servants as well as including into the bargaining process all representative trade unions of civil servants, so that collective agreements could be concluded on the basis of which all participating parties would realise their rights and obligations by voluntary collective bargaining.

Initiative for collective bargaining process usually comes from the side of a trade union, in the course of which the agreement parties debate on the base for calculation and payment of wages as well as on the correction of the coefficient if necessary. The base for calculation of wages is agreed upon not later than 15 November of the current year for the following year, and before the Budget of the Republic of Serbia has been adopted. If circumstances and assumptions according to which the base for wage calculation has been set should change in the course of the calendar year, the agreement parties are obliged to begin the bargaining process. Bargaining with trade unions on the base and coefficients for calculation and payment of wages of civil servants, which are financed from public funds, can be preformed only within limits set forth by the Budget of the Republic of Serbia, which is in accordance with provisions of the Law on the Budget System (*Official Gazette of RS*, No. 54/09 and 73/10) stating that the financial obligations from the budget can be undertaken only up to the approved limits for specific purposes. Article 27e of the aforementioned Law clearly defines in what manner individual wages in the public sector may be changed. This provision clearly defines fiscal responsibility in the public sector setting forth fiscal rules aimed at changing the structure of public spending in the direction of decreasing public expenditures and increasing investments so that the medium-term sustainability of public finances could be maintained.

Agreements concluded between the Government and the social partners (trade unions) are the following:

- General Collective Agreement (*Official Gazette of RS*, No. 50/08...8/09),
- Special Collective Agreement for state bodies (*Official Gazette of RS*, No. 95/08),
- Special Collective Agreement on Amendments and Modifications of the Special Collective Agreement for state bodies (*Official Gazette of RS*, No. 11/09),
- Special Collective Agreement for employees of cultural institutions founded by the Republic of Serbia (*Official Gazette of RS*, No. 97/09),
- Special Collective Agreement for employees of elementary and high schools and student homes (*Official Gazette of RS*, No. 12/09),
- Special Collective Agreement for tertiary education (*Official Gazette of RS*, No. 12/09),
- Special Collective Agreement for employees in student standard institutions (*Official Gazette of RS*, No. 14/07),
- Special Collective Agreement for health institutions founded by the Republic of Serbia (*Official Gazette of RS*, No. 36/10).

The bargaining process between representative trade unions of police and representatives of the Government of the Republic of Serbia regarding preparation of the collective agreement for police officers is taking place at this point.

System reforms ensuring long-term fiscal sustainability

Inadequacy of volume and structure of public spending in the Republic of Serbia has become particularly significant in the crisis period. In the years of the high economic growth the fiscal policy had a pro-cyclic effect, by increasing public spending on one side, and decreasing fiscal capacity by reduction of some tax rates, elimination of certain taxes, and introduction of numerous benefits on the other side. It rendered fiscal policy incapable of having an anti-cyclic effect to a larger extent in the recession period, because the possibilities for fiscal stimulations to the economy are limited.

Bearing in mind such developments, the need to add provisions to the Law on the Budget System related to determining fiscal responsibility and strengthening fiscal discipline has been identified, in order to ensure that the medium-term sustainability of the public finances is maintained.

Introduction of fiscal rules reduces the degree of discretion in conducting fiscal policy, which shall ensure the long-term sustainability of the fiscal policy, as well as just and fair distribution of expenditures and benefits between present and future generations.

Establishing fiscal responsibility, in the first place by introducing ceilings for deficit and public debt, represents main condition for conducting a responsible fiscal policy aimed at maintaining fiscal fairness between generations.

In addition to this, significant improvement of the management of public funds and control will have a positive effect on the whole public sector.

The aim of the Law is conducting a responsible fiscal policy, decreasing public spending and fiscal deficit, which will speed up economic growth.

Implementation of the Law should not produce additional expenditures to citizens and economic entities; it should contribute to significant savings and bring about a stable, predictable and sustainable fiscal policy. The introduction of fiscal rules in the Republic of

Serbia will reduce the degree of probability of fiscal expansion, as well as chances of its realisation. Fiscal rules would, in this way, contribute to the strengthening up of the macroeconomic stability and increasing the credibility of macroeconomic policy. Direct benefits could be improvement of the Republic of Serbia credit rating and lowering of interest rates for economic entities from the Republic of Serbia in the international financial market.

In addition to the aforementioned, introduction of fiscal rules is an obligation assumed by the Republic of Serbia within the existing arrangement with the IMF. Therefore, the introduction of fiscal rules can be considered an integral part of the Republic of Serbia EU integration process.

The Law stipulates that the Government and/or the local government executive authority are responsible for implementing fiscal policy.

Principles, procedures and rules of a responsible fiscal management have been proposed. Fiscal principles have been defined as general and special. General principles are the principles of: accountability, fairness, responsibility, stability and transparency, and special principles are: sustainability of the state debt, regular servicing of the debt, predictability of tax rates' and tax bases' levels for the following year, responsible fiscal risk management, management of public assets and liabilities, natural resources in a manner that will not burden the future generations and stimulating economic growth.

The document containing objectives of the Government fiscal policy and evaluation of the sustainability of fiscal policy is the Fiscal Strategy Report. The report shall replace the existing document – Memorandum on Budget and Economic and Fiscal Policy, with additions in the form of new mandatory elements in accordance with proposed reasons for Law amendments: opinion of the Fiscal Council on the Draft Fiscal Strategy Report, opinion of the National Bank of Serbia on the Draft Report and the Progress Report on the implementation of fiscal policy laid down in the Fiscal Strategy Report.

The new element is Progress Report, containing report on the progress in the implementation of fiscal policy laid down in Fiscal Strategy Report, adopted in the preceding fiscal year. This report shall contain the following elements: updated assessment of medium-term macroeconomic and fiscal trends and projections contained in the Fiscal Strategy Report which the Progress Report refers to; a section containing progress assessment against the defined fiscal policy and indicators laid down in the Fiscal Strategy Report which the Progress Report refers to; a section containing assessment of the extent to which the Government has, in the course of the preceding fiscal year, pursued the fiscal policy compliant with the principles and rules of responsible fiscal management, set forth in the Law.

Fiscal rules have been introduced with the aim of achieving fiscal responsibility so that the pro-cyclic effect of the fiscal policy could be reduced. Fiscal rules pertain to the general level of the state (including budget of the Republic of Serbia, local government budgets, extra-budgetary funds, social insurance funds at all levels of government, as well as non-commercial and non-profit institutions controlled and financed by the state at all government levels) and they can be general and special.

The proposed general fiscal rules are the rules referring to: (a) determining target share of the annual fiscal deficit in GDP in the medium term (1%) and (b) determining maximum ratio of the general state level debt to GDP (45%).

These rules are closely interconnected - once the maximum ratio of the debt to GDP is set, it is possible to realise the level of fiscal deficit which is in accordance with the debt. On the basis of fiscal deficit and adequate assumptions related to public revenue trends, it is possible to set the ratio of public expenditures to GDP.

Fiscal deficit would, from year to year, fluctuate around the targeted average amount, which would result in the anti-cyclic effect of the fiscal policy on the economic activity and employment. This means that in the recession periods fiscal deficit would be higher than 1% of GDP, and in the expansion periods it would be lower than 1% of GDP or there would be a surplus. With this objective a formula has been proposed, so that the real fiscal deficit in the medium term could be equal to the targeted deficit, with the possibility of the realisation of an anti-cyclic fiscal policy at the same time.

$$d_t = d_{t-1} - a(d_{t-1} - d^*) - b(g_t - g^*)$$

where d_t and d_{t-1} represent deficit in years t and $t-1$, d^* is the target fiscal deficit set at the level of 1% of GDP, g_t is the real GDP growth rate in year t , and g^* is a potential GDP medium-term real growth rate.

According to the proposed formula, the fiscal deficit in a specific year will depend on the fiscal deficit from the preceding year, on the degree of deviation of the preceding-year fiscal deficit from the targeted deficit, as well as on the extent to which the current year GDP growth rate deviates from the medium-term GDP growth rate. The pace of the adjustment of fiscal deficit to the targeted level is determined by the coefficient A , whose value for the three following years equals 0.3. This numerical value of coefficient A means that, under all other conditions unchanged, the deviation of the real fiscal deficit from the preceding-year targeted level is reduced by 30% in a certain year. The final element in the formula ensures that the level of fiscal deficit adapts to the conditions in the economy, measured by the extent to which the GDP growth rate in a certain year diverges from the GDP medium-term growth rate. This element creates the possibility for fiscal deficit to be higher than the targeted level in the recession years, and in the expansion years it can be lower than the targeted level or a surplus can be made. The coefficient of adjustment B equals 0.4%, meaning that, under other conditions unchanged, the fiscal deficit in the year T can be higher by 0.4% GDP from the targeted level, if the GDP growth rate in the year T is by one percentage point lower than the targeted level. On the other hand, if the GDP growth rate in a certain year is by 1% higher than the medium-term growth rate, the fiscal deficit shall be, under other conditions unchanged, lower by 0.4% GDP from the targeted level. The value of the coefficient B is set so as to correspond, approximately, to the ratio of consolidated public revenues to GDP of 40%. When determining the value of the coefficient B , the implicitly used assumption has been that the coefficient of elasticity of public revenues in relation to GDP equals (1), meaning that if GDP increases by 1%, the fiscal revenues shall increase by 1% as well. The assumption that the public revenue elasticity coefficient in relation to GDP equals (1) is adequate when the domestic demand equals GDP, which is mandatory in the long-term – it is not possible to produce external deficit infinitely. The value of the public revenue elasticity coefficient in relation to GDP of (1) is additionally justified by the fact that there is no significant progression in the tax system of the Republic of Serbia.

Targeted medium-term fiscal deficit of the Republic of Serbia (1% of GDP) is lower than the one set forth by the Maastricht criteria (3% of GDP) mainly because the Maastricht criteria determine the maximum fiscal deficit (except in extreme circumstances, such as the current crisis), while the proposal for the Republic of Serbia sets forth the average fiscal deficit in the medium term.

The reason for proposing a lower level of the general state debt than the one prescribed by the Maastricht criteria (60% of GDP) is a relatively high uncertainty in terms of the Republic of Serbia GDP growth in the following years, which is partly a result of uncertainty in terms of the recovery of the world economy. In addition to this, it is almost certain that the process of denationalisation shall result in the increase of the general state level debt of the Republic of Serbia. With the addition of debt created by the denationalisation process, total general state level debt of the Republic of Serbia shall approach the limit set forth by the Maastricht criteria, but it is necessary that it stays well below that limit. A high level of the general state level debt implies high expenditures for the servicing of interests, which could not be incorporated into the public spending level of 40% of GDP without difficulties.

Special fiscal rules shall ensure that the fiscal deficit reduction against GDP is predominantly achieved by means of reduction of current public expenditures, in terms of the regulation of wages in the public sector and pensions.

The objective of special fiscal rules is also to change the structure of public spending in terms of reducing current expenditures and increasing public investments, which is confirmed by the proposal to exclude, when calculating deficit in 2011, the part of total public investments exceeding 4% of GDP, and to exclude the part of public investments exceeding 5% of GDP in years 2012 – 2015. The part of public investments above the ceilings, in the amount of which, according to the general fiscal rule, the consolidated general state deficit can be increased, must not exceed 2% of GDP.

Introduction of special rules pertaining to public investments has been proposed in terms of intergeneration fairness – increase in the public debt ratio to GDP from the current level of 32% is justified only if the future generations are left, in addition to the increased debt, assets of higher value which could directly and indirectly facilitate the burden of servicing the debt. It means that the government will, entirely or mainly, increase its debt in order to realise public investments.

This Law also proposes fiscal rules for the local government in terms of setting the upper limit of the local government fiscal deficit, so that in a certain year it cannot exceed 10% of the local government revenues in the same year, and the deficit of local government units can only be a result of public investments. Exceptionally, fiscal deficit can exceed the upper limit if the local government has previously obtained consent of the Minister of Finance.

Apart from limitations related to the general state level debt, it was necessary to determine corrective measures referring to fiscal deficit and public spending, which would be implemented in cases of natural disasters and external shocks that result in endangering citizens' health, national security and drop of the economic activity. Corrective rules would allow, in the aforementioned circumstances, that the general state level debt, fiscal deficit and public spending be above the limits set by the existing rules.

Efficiency and effectiveness of government spending

The Law on the Budget System (*Official Gazette of RS*, No. 54/09 and 73/10) regulates budget goals.

“Budget goals

Article 4

The budget system shall achieve the following goals:

- 1) overall fiscal sustainability and control, which shall imply the implementation of policies without significant changes in the consolidated government budget, with a comprehensive control of total budget funds, through the establishment of expenditure and outflow upper limits guaranteed by the law, both at the overall level and at the budget beneficiary level;
- 2) allocation efficiency which shall imply the possibility of establishing priorities within the budget, allocation of funds in line with the Government priorities within the budget, as well as a possibility of transferring funds from old to new or from less productive to more productive priorities;
- 3) technical or operational efficiency which shall imply the use of budget funds and possibility of their application with the lowest possible costs.

The budget system shall provide comprehensive, relevant and reliable information on the Government activities.

Priority budget goals in the course of budget preparation and execution shall also be macroeconomic stability, low inflation, economic development, stimulation of regional development and reducing the financial risk of the Republic of Serbia.

In the course of budget preparation and execution, the principles of efficiency, cost effectiveness, effectiveness, transparency, comprehensiveness, accuracy and unique budget classification must be observed.”

Efficiency and effectiveness of government spending is ensured, in addition the aforementioned law provisions, by fiscal principles as well.

“Fiscal principles

Article 27b

General principles of the responsible fiscal management shall be:

- 1) the principle of accountability shall mean that the Government and the local government executive authority are accountable to the National Assembly and the local government assembly, respectively, for the execution of their competencies related to the fiscal policy management;
- 2) the principle of fairness shall mean that the fiscal policy management shall take into account its impact on the wellbeing of present and future generations;
- 3) the principle of responsibility shall mean that the management of public assets, liabilities, natural resources and fiscal risks shall be preformed in the manner that strengthens fiscal sustainability;
- 4) the principle of stability shall mean that the fiscal policy shall be implemented in such a manner as not to cause sudden changes in the development of macroeconomic and fiscal indicators;
- 5) the principle of transparency shall mean that the tasks and responsibilities of different government authorities, local government authorities and officials related to fiscal policy management have been clearly identified and defined; that the updated financial and non-financial information related to fiscal policy management have been prepared and are at public disposal, so that an effective

public control of the fiscal policy management and state of public finances can be preformed; that those responsible for publishing such information shall not withhold such information, unless disclosure thereof could incur significant damage to national security, defence or international relations of the Republic of Serbia."

The Law also regulates the obligation of establishing financial management and control.

Article 81

Public funds beneficiaries shall establish financial management and control, implemented through policies, procedures and activities, with the task of providing reasonable assurances that they shall achieve their objectives through:

- 1) operation in accordance with regulations, internal acts and agreements;
- 2) truthfulness and integrity of financial and business reports;
- 3) economical, efficient and effective use of funds;
- 4) protection of funds and data (information).

Financial management and control shall include the following elements:

- 1) control environment;
- 2) risk management;
- 3) control activities;
- 4) information and communication;
- 5) system monitoring and assessment.

Financial management and control shall be organised as a system of procedures and responsibilities of all persons in an organisation.

The manager of a public funds beneficiary shall be responsible for the establishment, maintenance and regular updating of the financial management and control system. The manager of a public funds beneficiary may delegate his/her responsibility for the establishment, maintenance and regular updating of the financial management and control system to the person he/she authorises.

The manager from paragraph 4 hereof shall report to the Minister on the adequacy and functioning of the financial management and control system in the prescribed manner, not later than 31 March of the current year for the preceding year.

The Minister shall establish joint criteria and standards for the establishment, functioning and reporting on the financial management and control system in the public sector."

Control of the efficiency of budget spending is ensured by establishing the State Audit Institution. In the course of auditing the financial statements, the following is observed:

- 1) The principle of cost-effectiveness shall mean minimum spending of funds for a particular activity, without compromising the expected quality thereby;
- 2) The principle of efficiency shall mean the ratio between achieved results in production of goods or rendering of services and utilised resources for the production or rendering services;

- 3) The principle of effectiveness (performance) shall mean the level of the achievement of the set objectives, as well as the ratio between the planned and achieved effects of a particular activity.²⁷

The integral part of annual financial statements of all budgets and financial plans of mandatory social insurance organisations is the external audit report, which the State Audit Institution is in charge of, by nature of its constitution.

Effectiveness of government spending is additionally ensured by the amendments of the Law on the Budget System, by which the Fiscal Council has been founded. The main task of the Fiscal Council is to independently assess whether the Government is implementing fiscal policy in compliance with the rules.

Fiscal Council is an independent body founded in order to improve the culture of fiscal responsibility in the Republic of Serbia, by performing independent analysis of the fiscal policy and encouraging professional debates regarding fiscal policy. The Fiscal Council has three members chosen by the National Assembly, at the proposal of the President of the Republic, Minister of Finance and the Governor of the National Bank of Serbia, and is accountable for its activities to the National Assembly.

"Functions and tasks of the Fiscal Council

Article 92g

The Fiscal Council shall:

- 1) verify macroeconomic and fiscal presumptions used for preparing the Fiscal Strategy Report by the Government;
- 2) provide independent and credible assessment of the economic policy measures proposed by the Government with the aim of achieving quantitative fiscal targets set by the Government;
- 3) assess basic fiscal risks and probability level that the Government shall achieve its fiscal targets in the future;
- 4) assess the extent to which the Government abided by its own fiscal rules in the past;
- 5) assess the need for the activation of any provision pertaining to exceptional circumstances and the probability with which the Government harmonisation plan will facilitate abiding by the fiscal rules;
- 6) verify the adequacy of economic classifications, including the regular classification of capital expenditures, in order to provide for the adequate measuring of quantitative fiscal targets.

Article 92h

²⁷ The Law on State Audit Institution

The Fiscal Council shall perform the following tasks:

- 1) prepare the opinion on the Draft Fiscal Strategy Report;
- 2) prepare and submit to the National Assembly the analysis on:
 - revised Fiscal Strategy Report of the Government for the corresponding fiscal year;
 - Proposal for a Law on Budget of the Republic of Serbia, including also the proposal for budget revision, and amendments submitted during National Assembly debate;
- 3) prepare and submit to the National Assembly the analysis of the Proposal for a Law on the Annual Financial Statement of the Budget of the Republic of Serbia and analysis of the consolidated balance sheet of the general state level;
- 4) prepare and submit to the National Assembly assessments of the fiscal impact of other law proposals, as well as amendments submitted during National Assembly debate.

The Fiscal Council shall submit analyses indicated in paragraph 1 item 2) hereof to the National Assembly within 15 days from the day on which the Government has submitted to the National Assembly the revised Fiscal Strategy Report, or Proposal for a Law on Budget of the Republic of Serbia or proposal for the budget revision.

Article 92i

The Fiscal Council may, at any moment, on its own initiative or upon request, provide advice to the Government about issues related to the fiscal policy and management of public finances.

All analyses, reports, recommendations and advice prepared by the Fiscal Council shall be made publicly available within five working days from the date of their submission to the Minister, Government or the National Assembly.

Reports, analyses and assessments of the Fiscal Council shall be available to the general public through the Internet page of the Fiscal council.

Reports, analyses and assessments of the Fiscal Council shall be, when needed, published in the "Official gazette of the Republic of Serbia", as well as on the Internet page of the National Assembly, Government, Ministry of Finance, or relevant unit of local government.

In order to secure a higher level of effectiveness of government spending, the Law on the Budget System has also introduced the Progress Report.

“Progress Report

Article 27f

The Fiscal Strategy Report shall contain, in the form of a mandatory Annex, the Progress Report on the implementation of fiscal policy defined in the Fiscal Strategy Report that was adopted in the preceding fiscal year.

The Report on Progress shall contain the following mandatory elements:

- 1) updated assessment of medium-term macroeconomic and fiscal trends and projections contained in the Fiscal Strategy Report which the Progress Report refers to;
- 2) section containing assessment of the progress against defined fiscal policy and indicators specified in the Fiscal Strategy Report which the Progress Report refers to;
- 3) section containing assessment of the extent to which the Government has, during the preceding fiscal year, conducted the fiscal policy in compliance with the principles and rules of the responsible fiscal management, laid down in this Law;
- 4) other information as specified by the Minister.”

Execution of the republic budget is realised through the budget execution system, into which budget beneficiaries enter payment orders.

So far, the common practise has been the practice of entering payment orders into the system with a very short deadline for execution (a day or two in advance). In such conditions, it is not possible to have precise information on the daily level of expenditures; therefore, the Treasury Administration has started working on the project of financial planning, which has been in use since 2010. With the introduction of financial planning, it is possible to secure a more efficient and rational use of republic funds, since all direct budget beneficiaries shall be obliged to plan their expenditures three months in advance. In this way, the liquidity management shall be improved.

Also, as of 01 January 2011, the Rulebook on the Budget Execution System for all budget beneficiaries of the Republic of Serbia (*Official Gazette of RS* No. 83/2010, from 09 November 2010) shall be applied. The Treasury Administration plans budget cash-flow liquidity for the budget year based on the planned expenditures, or inflows, and expenditures, or outflows, laid down in plans for budget execution prepared by budget beneficiaries. Within ten days from the day the Law on Budget or Act on Temporary Financing has been adopted, the budget beneficiary shall be obliged to submit to the Treasury plan for budget execution, on a monthly basis, for the period which the Law or the Act on Temporary Financing refers to. Budget beneficiaries are obliged to submit the plan for budget execution to the Treasury every month, by the 5th day in a month for the following three months, with the possibility of amending previously submitted plans for the following months.

12. Tax policy: Which are the tax authorities in central government, and possibly other levels of government (local governments, public institutions -if any- collecting taxes)? Which fiscal responsibilities do these various authorities have (nature of the taxes collected)? How has the tax regime changed over the last five years (amendments of tax rates, introduction of new taxes and contributions etc)? Is there an adequate flow of revenue for municipalities in order to finance their competences? Is there a mechanism of redistribution of sources among municipalities? Is the central budget expected to finance municipalities? (*detailed information is required in chapter 16 – Taxation*)

Which are the tax authorities in central government, and possibly other levels of government (local governments, public institutions -if any- collecting taxes)? Which fiscal responsibilities do these various authorities have (nature of the taxes collected)?

Tax Administration determines and collects the following taxes:

- VAT (value added tax)
- Excise tax
- Personal income tax (tax on wages and salaries, tax on revenues from agriculture and forestry, tax on revenues from self-employment, tax on revenues from copyrights, rights related to copyrights and industrial property rights, tax on real estate revenues, tax on revenues from yield on capital, tax on capital gains, tax on other revenues (tax on revenues from movable goods, tax on revenues from games of chance, insurance revenues, athletes and sports experts revenues, other revenues), annual personal income tax);
- Corporate income tax (tax, after deduction, on revenues from yield on capital – dividends and share in the corporate profit, revenues from copyright and rights related to copyright and industrial property rights, interests and revenues from fixed and movable assets, capital gain);
- Contributions;
- Tax on absolute rights transfer;
- Tax on inheritance and gift;
- Other tax revenues (fees, penalties for not fulfilling obligations related to employing persons with disability...).

Customs Administration determines and collects the following taxes:

- excise tax on imported goods;
- VAT on imported goods;
- Customs duties.

Local Tax Administration determines and collects the following taxes:

- property tax;
- fees (administrative, communal, sojourn);
- charges
- road charges (land charges, charge for the use of tourist grounds (determined by the local self-government and collected by business entities registered for tourism-related business), charge for the use of natural healing factor, charge for environmental protection, charge for the use of air space, charge for the use of radio frequencies and TV channels, tourist charge (determined by the local self-government and collected by business entities registered for tourism-related business)).

Competent ministries and other public enterprises:

- water charges (ministry in charge of environmental protection, TA – for natural persons, public water-policy enterprises)
- forest charges (Public Enterprise “Srbijasume”)
- fishing areas charges (fund for environmental protection?)
- charge for the use of mineral raw materials (ministry in charge of mining)

How has the tax regime changed over the last five years (amendments of tax rates, introduction of new taxes and contributions etc)?

1. In the Republic of Serbia, until **31 December 2004**, the taxation of consumption was regulated by the Law on Sales Tax (*Official Gazette of RS*, No. 22/01 ... 84/04).

Since **1 January 2005**, the taxation of consumption has been made in line with the Law on Value Added Tax (*Official Gazette of RS*, No. 84/04 ... 61/07 – hereinafter: Law on VAT).

From the very beginning of its implementation, the Law on VAT has prescribed taxation at the general VAT rate of 18% and the special VAT rate of 8%.

1.1. According to the current Law, the special VAT rate of 8% is applied on the supply of goods and services and the imports of: bread and other bakery products, milk and dairy products, flour, sugar, edible sunflower oil, maize, rape, soybean and olive oil, edible fats of animal and vegetable origin and honey; drinking water other than bottled; fresh, cooled and frozen fruits, vegetables, meat, including innards and other slaughterhouse products, fish and eggs; cereals, sunflower, soy, sugar beet and rape; medicines, including those for veterinary purposes; orthotic and prosthetic aids, as well as medical aids – products surgically implanted in the organism; dialysis materials; fertilisers, pesticides, seed stock, nursery stock, compost with mycelium, complete fodder mixtures and live stock; textbooks and teaching aids; personal computers and their components; daily newspapers; monographs and serial publications; firewood; accommodation services in hotels, motels, resorts, dormitories and camps; public utility services; services paid through tickets for cinema and theatre performances, fairs, circuses, amusement parks, concerts (music events), exhibitions, sports events, museums and galleries, botanical gardens and zoos, provided the supply of such services is not exempt from VAT; natural gas and the first transfer of the disposal right to residential properties – apartments.

1.2. Since **8 July 2007**, i.e. since the day the Law on Amendments and Changes to the Law on Value Added Tax entered into force (*Official Gazette of RS* No. 61/07), the taxation at the special VAT rate of 8% has applied to the supply and import of: personal computers and their components and the first transfer of the disposal right to residential properties – apartments not used for living purposes (the obligation of paying the difference between general and special VAT rate if the purpose of the residential property – apartment has changed within a period shorter than five years from the day the disposal right was acquired has been abolished)

1.3. Since **26 July 2005**, i.e. since the day the Law on Amendments and Changes to the Law on Value Added Tax entered into force (*Official Gazette of RS* No. 61/05), the taxation at the special VAT rate of 8% has applied to the supply and import of the following goods and services: honey, drinking water (other than bottled), frozen fruits, vegetables, meat and fish, cereals, sunflower, soy, sugar beet and rape, medicines for veterinary purposes and medicines exempt from the list of medicines prescribed and paid for by the health insurance, compost with mycelium, complete fodder mixtures and livestock (since the Law on VAT entered into force, only breeding stock was taxed at the special VAT rate of 8%), services paid through tickets for cinema and theatre performances, fairs, circuses, amusement parks, concerts (music events), exhibitions, sports events, museums and galleries, botanical gardens and zoos, provided the supply of such services is not exempt from VAT, natural gas (regardless of who it is distributed to, since the Law on VAT prescribed the special VAT rate of 8% only for natural gas distributed to individual consumers through gas distributive network), the first transfer of the disposal right to residential properties and equity shares in such properties (with the obligation of the person acquiring such right to pay the difference

between general and special VAT rate if they should change the purpose of the property within five years of the day the disposal right was acquired).

1.4. Under the Law on Amendments and Changes to the Law on Value Added Tax (*Official Gazette of RS* No. 61/05), the right of reimbursement of VAT was granted to traditional churches and religious communities.

1.5. Under the Law on Amendments and Changes to the Law on Value Added Tax (*Official Gazette of RS* No. 61/05), the right of reimbursement of VAT was granted the buyer of the first apartment.

2. Since 1 January 2005, tax on premiums in non-life insurance was introduced into the tax system of the Republic of Serbia under the Law on Tax on Non-Life Insurance Premiums (*Official Gazette of RS* No. 135/04). This tax is paid at the rate of 5% on the total amount of the insurance premium specified in the insurance contract.

3. Taxes on the use, possession and carrying of goods are prescribed by the Law on Taxes for Using, Possessing and Carrying Goods (*Official Gazette of RS*, No. 26/01, 80/02, 43/04, 132/04, 112/05, 114/06, 118/07, 114/08, 31/09 and 106/09) in the absolute amount (tax on the use of motor vehicles, tax on the use of vessels, tax on the use of aircrafts and spacecrafts and tax on the registered firearms) have been harmonised every year with the retail prices growth rate, in December – for the following year. In addition to this, the amounts of taxes have been changed in the last five years, tax exemptions have been expanded for tax on the use of motor vehicles, and there have been changes related to the types of taxable vessels which are subject to tax on the use of vessels.

Since **1 June 2009** tax on the use of mobile phones is paid through mobile telephony services.

4. The Property Tax Law (*Official Gazette of RS* No. 26/01, 80/02, 135/04, 61/07 and 5/09) specifies three tax forms: property tax, inheritance and gift tax and absolute rights transfer tax.

Property tax:

Property tax refers to the following property rights: right to property; right of occupancy; right to a lease on a dwelling or residential building in accordance with the law governing housing, for a period longer than one year or an indefinite period; right of using urban building land and/or public building land or other building land owned by the government, exceeding the area of 10 acres.

These revenues are primary revenues of the local self-government units (however, until 31 December 2006, this tax had been administered by the Tax Administration; after this date, this fiscal form went into the competence of the local self-government units on whose territory the taxed property lies).

Until 31 December 2006 the tax rate was specified by the Law; since **1 January 2007** the Law prescribes the maximum tax rate, up to which local self-government units can specify tax rate for properties within their territory.

Since **1 January 2009** the tax credit for an apartment or a building in which a member of the family of a tax payer lives has been abolished (the amount of credit was 10% for every member of the tax payer's family and every member of his/her household, up to the maximum of 30% of the determined tax amount).

Inheritance and gift tax:

Inheritance and gift tax refers to certain property transfers without compensation.

Since **8 July 2007** financial income exempt from the taxation and that taxable in accordance with the law regulating individual income tax are not subject to gift tax, and neither is transfer of gains from the organiser of games of chance to the winner.

Also, tax rates have been reduced by replacing tax rate of 3% with that of 2% for tax base up to 300,000 RSD, and for tax base higher than 300,000 tax rate of 5% was replaced with that of 2.5%.

Since **30 January 2009** there has been no inheritance and gift tax related to shares in capital of legal entities and securities.

Absolute rights transfer tax:

Transfers of certain absolute rights with compensation are subject to absolute rights transfer tax.

Since **July 8 2007** the absolute rights transfer tax has also been paid for giving building land owned by the government into lease, for a period longer than one year or for an indefinite period.

The tax rate has been reduced from 5% to 2.5%.

Tax exemption for the buyer of the first apartment has been introduced – up to a specified apartment area.

Since **30 January 2009** there has been no tax related to the transfer of shares in capital of legal entities and securities with compensation.

5. In relation to the Law on Excises (*Official Gazette of RS* No. 22/01, 73/01, 80/02, 43/03, 72/03, 43/04, 55/04, 135/04, 46/05, 101/05 – other law, 61/07, 5/09 and 31/09), we are attaching Parallel Overview of Excise Amounts and Rates in the period 2005 – 2010, classified by periods of application.

6. Pursuant to the Corporate Income Tax Law (*Official Gazette of RS*, No. 25/01 ... 18/10) the corporate income tax rate, which is proportional and unique and equals 10%, has not changed in the last five years, given that the last change of the corporate profit tax happened in 2004 under the amendments and changes to the Corporate Income Tax Law.

Tax rate after deductions (when taxing revenues of a non-residential legal entity realised within the territory of the Republic of Serbia), amounting to 20%, unless otherwise regulated by an international agreement on the elimination of double taxation, has also not been changed in the last five years.

7. Personal income tax rates applicable to different revenues of natural persons, in line with the Personal Income Tax Law (*Official Gazette of RS*, No. 24/01, 80/02, 135/04, 62/06, 65/06 – correction, 31/09, 44/09 and 18/10), in the period from 2005 to 2010 have been changing in the following way:

Tax rate on wages and salaries: under the Law on Amendments and Changes to Personal Income Tax Law (*Official Gazette of RS*, No. 62/06) tax rate on wages and salaries has been changed, so that since **1 January 2007** the tax rate of 12% has been applied. Previously used tax rate, up to this date, used to be 14%.

Tax rate on revenues from agriculture and forestry: under the Law on Amendments and Changes to Personal Income Tax Law (*Official Gazette of RS*, No. 31/09) tax rate on revenues from agriculture and forestry has been changed, so that since **8 May 2009** the tax rate of 10% has been applied. Previously used tax rate on revenues from agriculture and forestry, up to this date, used to be 14%. We would like to point out that tax on revenues from agriculture and forestry on cadastre revenues does not exist since 2004.

Tax rate on revenues from self-employment: under the Law on Amendments and Changes to Personal Income Tax Law (*Official Gazette of RS*, No. 135/04) tax rate on revenues from self-employment has been changed, so that since **1 January 2005** the tax rate of 10% has been applied. Previously used tax rate on revenues from self-employment, up to this date, used to be 14%.

Tax rate on revenues from yield on capital: under the Law on Amendments and Changes to Personal Income Tax Law (*Official Gazette of RS*, No. 18/10), tax rate on revenues from yield on capital has been changed, so that since **27 March 2010** the tax rate of 10% has been applied. Previously used tax rate on revenues from yield on capital, up to this date, used to be 20%.

Tax rate on capital gains: under the Law on Amendments and Changes to Personal Income Tax Law (*Official Gazette of RS*, No. 18/10), tax rate on capital gains has been changed, so that since **27 March 2010** the tax rate of 10% has been applied. Previously used tax rate on capital gains, up to this date, used to be 20%.

Tax rate on revenues from personal insurance: under the Law on Amendments and Changes to Personal Income Tax Law (*Official Gazette of RS*, No. 18/10), tax rate on revenues from personal insurance has been changed, so that since **27 March 2010** the tax rate of 10% has been applied. Previously used tax rate on revenues from personal insurance, up to this date, used to be 20%.

Tax rate on annual individual income: under the Law on Amendments and Changes to Personal Income Tax Law (*Official Gazette of RS*, No. 62/06), annual personal income tax rate has been changed, so that since **1 January 2007** the progressive tax rates of 10% and 15% have been applied. Previously used tax rate on annual personal income, up to this date, used to be 10%.

Tax rate on revenues from copyrights, rights related to copyrights and industrial property rights, revenues from real estate and other revenues, has not changed in the last five years, and amounts to 20%.

Units of Local Self-Government are financed from 3 main groups of revenues:

1. Transferred revenues – these are taxes and other revenues levied by central government through laws; central government determines the base to which the tax is paid as well as tax rate and possible tax exemptions.

These taxes are administered by tax administration on the Republic level. A part of these revenues is transferred to ULSG for financing their competencies. This part can even be 100% of tax collected on the territory of a ULSG, as is the case in Serbia, with the exception of tax on wages and salaries which is distributed between the Republic and ULSG at 60% - 40% respectively.

In the territory of APV, ULSG also receive 40% from collected tax, 18% belongs to the budget of APV and the remaining 42% to the budget of the Republic.

2. Primary revenues – revenues specified by decisions of Units of Local Self-Government, in relation to which they have the possibility of determining base or rate, and/or amount of tax, fees and charges paid by tax obligor.

3. Transfers from the Republic budget

Mechanism of distribution between Units of Local Self-Government

This mechanism is realised through a system of unconditional transfers regulated by the Law on Local Self-Government Financing, by which, among other things, an equalisation of revenues of ULCG is being performed (equalising transfer). The equalisation is performed up to the limit of 90% of transferred revenues. Primary revenues are not being considered when calculating equalisation needs, in order to stimulate Units of Local Self-Government to collect their revenues up to the maximum, while at the same time they should not be punished by reduced transfers in case they manage to increase their revenues; also, vice versa - they should not be stimulated to create a decrease in their primary revenues on purpose in order to ask for deficient funds from transfers (overflow of tax burden between different ULSG).

A mechanism of direct transfers between different Units of Local Self-Government, apart from participation in mutual projects, does not exist.

The central budget participates in financing of ULSG through the aforementioned system of unconditional transfers, and the funds are spent by ULSG according to their needs set forth in their budgets. There are also the so-called conditional transfers for financing specific projects but these transfers are of a significantly lower volume and importance than unconditional transfers, which has a positive effect on a higher degree of autonomy of USGL from central government.

Detailed answer is given in the chapter 16-Taxation and chapter Political Criteria – question number 31

13. Public debt: How was budgetary financing secured since 2000 (main instruments etc.)? Please provide detailed information on the present stock of public debt (foreign/domestic creditors, currency, instruments, etc.), guarantees and arrears.

| | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
|------------------------------------------------|-----------|----------|----------|-----------|-----------|-----------|-----------|
| III BUDGET | | | | | | | |
| SURPLUS/DEFICIT | -27,271.6 | -3,143.6 | 8,193.9 | -35,568.3 | -38,171.7 | -50,796.5 | -90,461.5 |
| Financing | | | | | | | |
| OUTFLOWS FOR FINANCING (1 + 2) | 19,262.3 | 21,833.5 | 25,807.7 | 52,310.0 | 36,030.3 | 43,643.7 | 144,160.3 |
| 1. Payment of principle (1.1 + 1.2 + 1.3) | 19,262.3 | 21,833.5 | 25,807.7 | 52,310.0 | 35,909.2 | 40,845.9 | 144,160.3 |
| 1.1 Payment of principle to domestic creditors | 18,923.1 | 21,430.6 | 23,770.2 | 21,901.3 | 31,247.6 | 30,075.3 | 131,412.3 |

| | | | | | | | |
|---------------------------------------------------|----------|----------|----------|-----------|-----------|-----------|-----------|
| 1.2 Payment of principle to foreign creditors | 339.2 | 323.2 | 2,037.5 | 29,918.3 | 4,145.1 | 4,885.6 | 8,957.9 |
| 1.3 Payment of principle for activated guarantees | 0.0 | 79.7 | 0.0 | 490.4 | 516.5 | 5,885.0 | 3,790.1 |
| 2. Procurement of financial assets | 0.0 | 0.0 | 0.0 | 0.0 | 121.1 | 2,797.8 | 0.0 |
| INFLOWS BY TYPE OF FINANCING (1 + 2) | 48,741.5 | 35,059.1 | 51,100.9 | 177,013.0 | 43,246.0 | 36,917.4 | 270,493.0 |
| 1. Inflows from borrowing (1.1 + 1.2) | 9,212.5 | 18,609.4 | 17,200.2 | 24,785.6 | 3,189.9 | 10,076.3 | 250,345.6 |
| 1.1 Inflows from domestic borrowing | 2,032.9 | 9,141.9 | 5,398.5 | 19,612.7 | 1,035.8 | 9,278.9 | 205,607.9 |
| 1.2 Inflows from foreign borrowing | 7,179.6 | 9,467.5 | 11,801.7 | 5,172.9 | 2,154.1 | 797.4 | 44,737.7 |
| 2. Inflows from privatisation | 36,094.0 | 14,594.3 | 31,174.7 | 150,828.3 | 39,310.3 | 26,096.2 | 14,191.8 |
| ACCOUNT BALANCE | 2,207.6 | 10,082.0 | 33,487.1 | 89,134.7 | -30,956.0 | -57,522.8 | 35,871.2 |
| NET FINANCING | 27,271.6 | 3,143.6 | -8,193.9 | 35,568.3 | 38,171.7 | 50,796.5 | 90,461.5 |

14. Labour Market (*detailed information is required in chapter 19 – Social Policy and Employment*):

a) Unemployment: How has unemployment developed over time and sectors? What are the main causes of unemployment? What are the main categories concerned? What is the percentage of long term unemployment?

Negative trends of decrease in employment and increase in unemployment present in the 1990s have been continued throughout the main part of this decade, even in the years of the highest economic growth. The citizens felt the benefits of economic growth through rise of salaries, not through increase of employment. The developing private sector was not able to absorb labour force that was made redundant during the process of restructuring of socially-owned and state-owned companies, or to generate enough job positions in the labour market for other unemployed. Unemployment was partly mitigated by the employment in informal economy which, according to the Labour Force Survey from April 2010, amounted to approximately one third of total employment (19.8% for citizens 15+), mainly by absorbing unqualified labour force.

A very high unemployment rate is present in Serbia, given that 20.1% of working age population (15-64 years of age) or 572,500 of them were unemployed in April 2010 according to the LFS. The number of the unemployed, as well as the unemployment rate, was significantly reduced in the period 2005-2009, which is partly a result of the better inclusion of persons from groups of low employability, reducing consequentially the number of the

unemployed.²⁸ A decrease in unemployment in this period was only partly a consequence of new employments, since there was a significant number of those discouraged to look for new employment who had become inactive. However, it should be noted that the number of the unemployed, as well as the unemployment rate, have continually increased since 2008, as a consequence of the impact of economic crisis on the labour market.

The main problems Serbia is facing in the area of employment are a lack of job positions as a consequence of insufficient economic activity and low employment rate.

General characteristics of the labour market in the period 2007-2009 were: mismatch between supply and demand of labour force (on one hand, a certain number of empty job positions advertised by employers remained unfilled, while, on the other hand, there was a large number of persons with occupations not needed in the labour market), a high share of the long-term unemployed and a large inflow of redundant workers from enterprises in the process of restructuring and privatisation (the process of privatisation of enterprises and public institutions is still ongoing; in 2009 a the process of forced liquidation was initiated), unfavourable age- and qualification-related structure of the unemployed, a high rate of unemployment of young persons, large differences between regional labour markets and low degree of mobility of labour force (the situation is less favourable in the south of the country than in the north, and in the rural areas in comparison to urban areas), a large number of the unemployed belonging to low-employability groups (persons with disabilities, the Roma, women, the young, etc.), as well as a large number of those employed within the grey economy.

Unemployment in Serbia has a long-term character. Many of those employed, once they become unemployed, keep this status for a very long period. International experiences show that the probability of finding a job declines proportionately to the length of the unemployment period, which can bring about a permanent exclusion from the labour market and an increase in the risk of poverty. The share of long-term unemployment (persons looking for a job for one year and longer) in the unemployment of the working age population (15-64) is extremely high and it amounted to 79.4% in 2005. In the period 2005-2009 this share fell to 65.1%. Long-term unemployment rate of the working age population (15-64) in April 2010 equalled 13.4%. It should be pointed out that, as with the overall rate of unemployment, a significant part of this decrease is owned to the change in the methodology of calculating employment/unemployment in LFS.

A special problem in the Republic of Serbia labour market is still a large surplus of employees. Government has helped financially in solving the problem of the surplus of employees in enterprises that have begun the process of rationalisation and restructuring as a preparation for privatisation. From 2002 until October 2010, funds for resolving the labour-related legal status of the surplus of 209,795 employees were secured from the budget of the Republic of Serbia.

According to age, almost one half of the unemployed belong to two youngest age groups (15-24, 25-34), whose share in the total unemployment (15+) in April 2010 amounted to 19.6% and 29.6% respectively. In the period 2005-2010, a decline was recorded in the share of the youngest population in total unemployment, which can be partly attributed to the prolonged

²⁸ Almost one half of the recorded growth rate of employment in 2008 in comparison to 2007 is the result of the change in methodology (Mehran, 2010). In other words, if the same methodology had been used as in 2008, the unemployment rate of 15+ in 2007 would have been 16.2% instead of 18.1%. This means that the fall of unemployment rate of 4.5 percentage points in 2008 in comparison to 2007 (from 18.1 % to 13.6%) is a result of the changed methodology (1.9 percentage points) and real changes (2.6 percentage points).

period of education in conditions of low employment, and an increase was recorded in the share of middle-aged (45-54) and older population (55-64).

Unemployment rate significantly declines with age – the highest rate is present among the youngest age group (15-24). After the unemployment rate of the young (15-24) had declined between 2005 and 2007, it began to rise again, and in April 2010 it reached 46.4%. In comparison to the adult population, the position of the youth in the Serbian labour market worsened, since the gap between the unemployment rate of the young and the unemployment rate of overall population deepened in the observed period.

Structure of the unemployed according to the education level has been stable in the observed period. Unemployment rate is the highest among those with secondary education, since more than two thirds of all unemployed finished secondary school (68% in 2005 and 69% in April 2010).

There are significant differences in economic development between regions in the Republic of Serbia. The situation is less favourable in the south than in the north of the country, and in the rural areas in comparison with the urban areas. Insufficient economic activity and lack of job positions in certain regions has as a consequence the migration of labour force to the regions with better employment possibilities. Region-wise, two sub-periods brought about divergent migration of unemployment. In the first sub-period (2005-2007), there was a decline of unemployment in all three regions, in the largest extent in Belgrade and the smallest in Vojvodina, while in the second sub-period (2008-2009) unemployment increased in Vojvodina (30.1%) and Central Serbia without Belgrade (21.4%). The number of the unemployed in Belgrade remained the same as in 2008. These regional migrations of unemployment are in accordance with the regional migrations of employment, Belgrade being in the best situation and Vojvodina and Central Serbia in a significantly worse situation.

Even though there are no records of the number of persons with disabilities, it is estimated that more than 500,000 persons with different sorts of disability live in Serbia, but only 20,470 of them were registered with the National Employment Service in October 2010. According to the Living Standards Measurement Survey (LSMS) from 2007, unemployment rate of persons with disability amounted to 13.6% and was approximately at the same level as was the average unemployment rate from the same study (13.9%). The main reason standing behind such a low unemployment rate of persons with disability is a high rate of inactivity, amounting to 69%. This can be attributed to the fact that the majority of them are discouraged in finding a job, so that they are not looking for it at all. A very small number of persons with disability registered with the National Employment Service points to this as well. The main reason for such a high degree of discouragement of persons with disabilities in looking for a job is related to prejudices of employers and their lack of willingness to adapt work environment to the needs of persons with disabilities. In addition to this, persons with disabilities fear losing social security rights once they find employment.

According to the last census in 2002, the Roma population contributed to only 1.4% of the total population. The unemployment rate of the Roma in 2007 was 31.6% according to the Living Standards Measurement Study, which was much higher than the unemployment rate of general population (13.9%), signifying a considerably more difficult position of the Roma in the labour market in comparison to the overall population. It is important to point out that the Roma from illegal Roma settlements (urban favelas) have not been included in LSMS, and they are by all means a more severely affected group than the Roma integrated in the general population. A high unemployment rate and a low rate of inclusion and employment are the main reasons standing behind extensive poverty present among the Roma. In 2007, poverty of the Roma population was several times more wide-spread, and also substantially deeper and

more severe compared to the general population. Almost a half of the Roma population (49.2%) were poor, and 6.4% extremely poor. The majority of working age Roma lack adequate education in order to participate successfully in the labour market. A special problem concerning the unemployment of Roma is the same problem relating to the overall population, which is its long-term character. Many of the employed Roma, once they become unemployed, keep that status for a very long period, which can bring about their permanent exclusion from the labour market and an increase in the risk of poverty.

The unemployment of women in the Republic of Serbia is more prominent than the unemployment of men. In April 2010, the activity rate of women was approximately 50.9% and of men 67.4%. The lowest employment rate of women was recorded in 15-24 age group, because young women, more often than young men, take over the responsibility of taking care of household and family thus postponing the entry into the labour market. Main reasons for the inactivity of women (with the exception of university students) are personal reasons, family reasons or "other" reasons. The gap between the employment rate of men and women in April 2010 dropped to 1.5 percentage points. Although the gaps between employment and activity rates are still huge, there is a trend of their gradual decreasing.

Unemployment of the young belonging to the 15-24 age group in the Republic of Serbia is very high and is substantially above the overall unemployment rate. The low activity rate of the young (28.2% in April 2010) is mostly attributed to extended education and to the fact that the majority of university students do not work while studying. The employment rate of the young in April 2010 dropped to 15.1% (by 5.9 percentage points compared to April 2008), while the unemployment rate rose to 46.4% (by 13.7 percentage points compared to April 2008). The recorded drop in the employment rate of the young was much less sharp than the rise of the unemployment rate of the same group. Data from April 2010 show that there was a significant drop in the employment of the young in the category of assisting household members (share of this age group in the overall employment in October 2009 was 16.5%, while in April 2010 the share dropped to 12.2%, by 4.3 percentage points). According to the definition of the International Labour Organisation, household members assisting in household tasks are a part of the informal economy, and these developments can be regarded as a positive sign of the labour market recovery, or inclusion of the young into the formal labour market trends.

According to the LFS data from April 2010, employment (15-64) in the informal economy in April 2010 amounted to 17.2%. Employment in the informal sector is highest among the young (15-24) and it equals 28.8%. The lowest employment rate in the informal sector is recorded in the 25-35 age group and it equals 13.7%. Employment within grey economy in the Republic of Serbia is characterised by low salaries and low productivity, low level of work safety, bad working conditions, and very often such jobs are characterised by the absence of basic health and social insurance. The possibility of losing one's job is higher among the informally employed than among those with formal employment, which is shown in the LFS data. This means that in spite of all expectations that the crisis would bring about a rise of the informal employment, it has been confirmed that the possibility of losing one's job is higher in the informal than in the formal sector.

b) Employment: How is the division of employment between the public, the privatised and the private sector? What have been the main sectors of job creation? How do you assess the relationship between economic growth and employment?

In the Republic of Serbia, the employment by sectors (sectors according to the type of ownership: private, state, social and other types of ownership) for the employed population is being monitored through Labour Force Survey which is carried out by the Republic Statistical Office. This category does not include self-employed persons and the assisting household members. The data given here are for the period 2004 – 2009 due to a change in methodology of the Labour Force Survey in 2004 and difficulties arising from this concerning data comparison.

For the privatised sector, the data given are the data of the Republic Development Bureau and the Serbian Business Registers Agency.

According to the data for 2009, the private sector employed the majority of employed workers – 55.0% of the overall employed, 40.2% worked in the state-owned sector, 3.1% in socially-owned enterprises and 1.7% in enterprises not classified by type of ownership, or belonging to some sort of mixed ownership (Table X).

Table X. Structure of the employed working age population by the type of ownership, 2004-2009

| 15-64 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
|--------------------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Private ownership | 38.7 | 44.1 | 48.2 | 52.5 | 56.3 | 55.0 |
| State ownership | 33.1 | 33.5 | 36.0 | 35.0 | 36.9 | 40.2 |
| Social ownership | 21.8 | 17.0 | 12.2 | 8.2 | 4.5 | 3.1 |
| Other types of ownership | 6.5 | 5.4 | 3.5 | 4.3 | 2.3 | 1.7 |
| Total | 100 | 100 | 100 | 100 | 100 | 100 |

Source: Republic Statistical Office, Labour Force Survey

Notes:

- 1) Data refer to the employed workers, without self-employed persons and assisting household members
- 2) Until October 2008 RSO used to carry out LFS once a year, in October every year, but since 2008, LFS has been carried out twice per year, in April and in October, so that data after 2008 represent average values.

The number of employees in the private sector had been recording a constant growth between 2004 and 2008, when, due to the negative impact of the world economic crisis on the country's economy, a decline in the overall number of employees occurred, especially in the private sector. Employment in the private sector had recorded a growth of the number of employed persons from 38.7% of all employed in 2004 to 56.3% in 2008; however, due to the influence of the world economic crisis, this share dropped to 55.0% in 2009.

Due to the process of transition and restructuring, the social sector experienced a substantial drop in employment, from 21.8% in 2004 to 1.7% in 2009. Privatisation of the socially-owned capital is in its final phase, so that further drop of employment is expected, until final disappearance of the social sector in the end.

Sector "Other types of ownership", including, among other things, cooperatives and NGOs which belong to the concept of social entrepreneurship, also recorded a drop in the number of those employed²⁹ in the period 2004-2009, from 6.5% of the total number of employed

²⁹ Employed persons, without the self-employed and assisting household members.

persons in 2004 to 1.7% in 2009. Key problems³⁰ identified in the development of the social entrepreneurship sector are: inadequate legal framework, insufficient investment in the human capital, difficult access to the sources of financing, tax treatment, lack of statistical tracking³¹, all of which is characteristic for other countries in the region.³²

State-owned sector which includes state-owned public enterprises and local public enterprises recorded a slight growth between 2004 and 2009, from 33.1% to 40.2% of overall employment.

Increase in the employment in this sector in the overall employment is a consequence of the overflow of employees from socially-owned enterprises (due to privatisation and restructuring) and enterprises belonging to other types of ownership into the state-owned enterprises, given that the number of employed persons in these sectors was constantly decreasing.

As far as the privatised sector is concerned, i.e. the privatised enterprises, we shall present the findings from the analysis of the Republic Development Bureau entitled "The Economy of Serbia in 2009" from July 2010. It should be noted that for the purposes of this analysis the Republic Development Bureau used data from financial reports of enterprises made available by the Serbian Business Registers Agency (SBRA), so the total number of employed persons is not the same as in the Labour Force Survey of the Republic Statistical Office. The differences are caused by the employed entrepreneurs who are not legally bound to submit financial reports to SBRA, as well as by persons employed within informal economy.

According to this analysis, the Agency for Privatisation data for the period 2002-2010 (until 25 May) show that 2,453 enterprises have been privatised: 106 by tender privatisation, 1,631 by auction privatisation and 716 by sale of minority share packages from the portfolio of Share Fund.

There were 181,426 employees in privatised enterprises in 2009. In relation to 2002 the number of employees had been reduced by 210,322 (from 391,748 in 2002 to 181,426 in 2009). The crisis had negative consequences on the business operations of privatised enterprises to a far larger extent than on economy as a whole.

The share of the number of employed persons in privatised companies in the total number of employed persons was reduced from 19.0% in 2008 to 17.1% in 2009, according to financial reports of these enterprises.

Regarding the period 2004-2009, we can see that the creation of the majority of new job positions was recorded in private sector. However, it should be noted that in the period 2008-2009, the socially-owned sector aside, the sharpest decline was recorded in the very same private sector (-1.3 percentage points). In time of economic crisis the private sector was adjusting by laying off the employees (downsizing job posts), while the state-owned sector was adjusting by freezing or reducing employee salaries.

The quick economic development of the Republic of Serbia in the period 2001-2008 with the average annual real GDP growth of 5.4% did not have sufficient effects on the labour market

³⁰ First national Draft Report on Social Inclusion and Reduction of Poverty

³¹ The first initiative for tracking down the importance of cooperatives and other types of social economy in line with the concept of satellite accounts has been launched by RDB http://webzrzs.stat.gov.rs/axd/en/EU_projects3.php

³² Innovative Social Enterprise Development Network in Serbia (ISEDE – NET), European Movement in Serbia, 2010

in terms of the increase in employment due to transition and restructuring processes as well as to serious inherited difficulties. The indicator of employment elasticity makes it possible to understand the relationship between economic growth – measured by GDP, employment and productivity. Economic growth can be shown as a sum of the growth of employment and growth of productivity. The higher the share of employment growth in economic growth, the higher the intensity of employment shall be.

Namely, during the period between 2001 and 2008, this indicator generally had a negative prefix; in other words, GDP growth was accompanied by the employment drop. Since the beginning of the economic crisis, the employment elasticity to GDP has unfortunately become positive and larger than 1 – i.e. GDP decline has been accompanied by an even stronger decline in employment³³. Since the beginning of the crisis, the decline in employment had been much sharper than the decline in economic activity. During the crisis (the first quarter of 2008 – the first quarter of 2010), GDP had declined in total by 4.7% while the employment had declined in total by 12.5%, which makes employment elasticity of 2.6³⁴.

Such developments in the employment intensity in relation to growth over the past decade in Serbia can be largely explained by the influence of transitional restructuring through intensive dismissal of "redundant" employees in privatised enterprises, as was the case in many countries of Central and East Europe in 1990s³⁵. An important additional role in reinforcing this effect had a current model of growth, in which the employment has been neglected as an important goal of socioeconomic development. In addition to this, after the global economic crisis had arrived in Serbia at the end of 2008, structural factors in the labour market, and the extreme dual nature thereof (the private sector adapted to new market conditions by downsizing the staff, especially those without formal employment, while the public sector adapted by freezing employee salaries), influenced – in a parallel perspective - an unexpectedly rapid and extreme reaction of employment to GDP decline³⁶.

c) Describe the government policy concerning the labour market. What are the main steps taken/to be taken to improve the unemployment situation and/or the mismatch between labour supply and demand?

Creation and implementation of employment policy is under the competence of the Ministry of Economy and Regional Development.

The legal framework for creating and implementing programmes and measures for the promotion of employment comprises the Law on Employment and Unemployment Insurance (*Official Gazette of RS*, No. 36/09 and 88/10) and the Law on Professional Rehabilitation and Employment of Persons with Disabilities (*Official Gazette of RS*, No. 36/09). The employment activities and the active policy of employment are defined by law as a system of plans, programmes and measures aimed at increasing employment and reducing unemployment.

In accordance with the strategic orientation toward EU accession, in April 2005 the Government of the Republic of Serbia adopted the National Employment Strategy for the

³³ Post-crisis model of growth

³⁴ FAE (Foundation for the Advancement of Economics)

³⁵ Saget, 2000

³⁶ Post-crisis model of growth

period 2005-2010, which deals with the area of employment in the context of sustainable economic growth and development as well as increase in employment. Its key purpose is to point to the specific directions for solving the problem of unemployment during the transition process, and to offer solutions appropriate to the process, taking into account available human and financial resources.

The main instrument for implementing the employment policy is the National Employment Action Plan, adopted by the Government of the Republic of Serbia, on an annual basis. In addition to this, legal provisions offer the possibility of employment policy decentralisation and creation of local employment action plans.

The Government Conclusion dated 11 February 2010, sets forth the National Employment Action Plan for 2010 (*Official Gazette of RS*, No. 7/2010). The Plan defines priorities and objectives of employment policy and determines measures to be realised in 2010 in order to achieve determined goals and attain sustainable growth of employment.

Priorities of the active employment policy in 2010 are mainly aimed at investing in human capital, stimulating social inclusion in the labour market and creation of new job posts. Therefore, in line with the guidelines and recommendations of the European employment policy, the priorities of employment policy laid down in the National Employment Action Plan for 2010 are:

- 1) supporting the creation of new jobs, reducing the impact of economic crisis on existing jobs and encouraging formal employment in the private sector, with significant participation of social partners;
- 2) reduction of youth unemployment and promotion of youth employment, especially those affected by decreased employment possibilities;
- 3) decentralisation of employment policy and encouragement of the development of regional and local employment policy through proactive approach of local authorities;
- 4) greater investments in human resources by improving education and training in order to harmonise supply and demand in the labour market;
- 5) promotion of social inclusion and equal opportunities in the labour market.

In the Budget of RS for 2010, RSD 3.7 billion was set aside for financing the measures of active employment policy.

These funds are higher than in the preceding year, but still much smaller than needed (the RS budget funds, allocated for active employment policy, amount to only 0.1% of GDP), which is why a good planning and optimal use of funds is necessary in order to include a large number of different target groups in these measures. In addition to this, it is important to point out that the support of international community and donors is very important and significant for the realisation of planned activities.

In 2010, a special emphasis has been placed on professional training and employment of young persons under the age of 30, without professional working experience, in the form of "First Chance 2010" programme. This programme of youth employment is designed for private sector employers who, by engaging interns, have an opportunity to have all expenses for their salaries and social insurance contributions reimbursed.

The emphasis has also been placed on public works, which are aimed at hiring low employability persons and the unemployed in social need, at preserving and improving the working skills of the unemployed, as well as at achieving particular social interest.

In February 2010, with the aim of encouraging employment of the Roma, the National Employment Service announced special open calls as follows:

- open call intended for persons of Roma ethnicity, for granting subsidies for self-employment in one lump sum of RSD 160,000.00, and
- open call intended for employers, for granting subsidies for the opening of new job posts for persons of Roma ethnicity. The subsidy to an employer hiring a person of Roma ethnicity is to be paid in the amount of RSD 160,000.00 in one lump sum, regardless of the degree of development of the municipality in which the employer performs his/her business operations.

**Allocation of funds for realisation of active employment policy measures
in 2010**

| Number | Active employment policy measure | Funds (in RSD) | Number of persons included |
|-----------------------------------------------------|-------------------------------------------|---------------------------|-------------------------------------------|
| 1 | Active job seeking | 5,000,000 | 86,840 |
| 2 | Additional education and trainings | 2,095,000,000 | 20,000 |
| 2.1 | Interns | 1,800,000,000 | 16,000 |
| 2.2 | Trainings | 295,000,000 | 4,000 |
| 3 | Subsidies for employment | 900,000,000 | 6,075 |
| 3.1 | Subsidies for self-employment | 300,000,000 | 1,875 |
| 3.2 | Subsidies for creation of new jobs | 600,000,000 | 4,200 |
| 4 | Public works | 700,000,000 | 5,000 |
| Total funds and persons included in measures | | 3,700,000,000 | 117,915 |

Taking into account the objectives, priorities and guidelines of the European Strategy – Europe 2020, as well as objective circumstances in the labour market in the Republic of Serbia, the National Employment Action Plan for 2011 (adopted by the Government Conclusion from 29 July 2010, *O. Gazette of RS* No. 55/2010) lays down the objectives and priorities (increase in employment, investment in human capital and social inclusion). Therefore, the activities defined by NEAP for 2011 are in line with the activities set forth by the preceding action plan and represent a continuation of activities carried out over a longer period of time.

Drafting of the National Employment Strategy for the period 2011 -2020 is currently under way, in line with the guidelines of the European Strategy – Europe 2020.

15. Price regime: How has the price control regime been liberalised since 2000? In what sectors are prices still administered (i.e. set explicitly by government) or regulated (i.e. subject to approval by independent regulator)? Please indicate the broad categories of prices which are administered/regulated and the share of administered/regulated prices in total, including quantitative indicators. What is the strategy for completing price liberalisation, in particular in the energy sector?

Since 2000 the liberalisation of prices has been done gradually and in accordance with developments of all economic activities, situation on the market and trends concerning purchasing power of population, in line with the current legislation.

Certain energy products, some infrastructural products and services, medicines used in human medicine, and, occasionally, a few industrial food products vital for the standard of the population have been under direct control. For example, in a certain period, the government controlled prices of milk, oil, and bread made of 850-type flour (the so-called "people's bread"). All these measures were of temporary character and were aimed at eliminating disturbances in the market.

Since 2000 the Government of the Republic of Serbia has chosen the direction of price liberalisation and deregulation, leaving the price policy up to the market, in order to ensure free operation of market mechanisms.

Pursuant to Article 36 of the Law on Trade (*Official Gazette of RS*, No. 53/09), by which the Law on Prices, as well as the Law on Conditions of Conducting Trade in Goods, Rendering Services in the Trade of Goods and Inspection Surveillance were put out of force, since 1 January 2001, the prices of products and services are to be formed freely according to market conditions, except in case of products and services whose prices are to be formed in a different manner as prescribed by a special regulation. If a law stipulates that the Government is to give its consent to a certain price, it shall decide on such matters at the proposal of the minister competent for trade-related issues and minister competent for the area in question.

The Government or an independent regulatory body, or the competent ministry, or a unit of local self-government (depending on a special regulation), shall set forth criteria for price formation or give their consent to the decision on the change of price for the following products and services: medicines for human consumption, petroleum products, oil transport, electricity, natural gas, coal for industry and general consumption, rail transport of goods and passengers, reserved postal services, a special charge for the use of a public road (toll), other charges for the use of a public road, airport services, ski-pass prices, technical inspection of vehicles, charge for removing vehicles from the road, collection of protected plant and animal species, services in fixed telephony and prices of products and services of public companies founded by a local self-government unit.

It is difficult to give the statistical scope because until 2008, the measure of inflation used to be the list of retail prices index. Since 1 January 2009, the Retail Price Index has been replaced by the Consumer Price Index. The contents of the consumer prices index list differs considerably from the contents of the retail prices index list, so comparing of the two would give a wrong picture of the scope.

Energy

Within the energy and mining sector, since 2000 the Government of the Republic of Serbia has controlled prices of basic oil derivatives, electric energy and natural gas, and since 2007

also prices of oil pipeline transport, while the retail prices of coal have been liberalised at the end of 2004.

Control of prices of basic petroleum products was based on Article 8a of the Law on Conditions for Conducting Trade in Goods, Rendering Services in the Trade of Goods and Inspection Surveillance (*Official Gazette of RS*, No. 39/96, 20/97, 46/98, 34/01, other Law, 80/02-other Law and 101/05). The Government used to give consent to prices of electricity, natural gas and oil pipeline transport pursuant to Article 27 of the Law on Public Enterprises and Performance of Activities of General Interest (*Official Gazette of RS*, No. 25/00, 25/02, 17/05 and 108/05), and since 2004 pursuant to Articles 36 and 66 of the Law on Energy (*Official Gazette of RS*, No. 84/04), according to which the Government shall give consent to an act on prices of an energy operator with the previously obtained opinion of the Republic of Serbia Energy Agency, which, in the process of price regulation of electric energy, natural gas and oil pipeline transport determines the economically justified level of prices based on the methodology for price and tariff system calculation.

In the period between 2000 and 2003, pursuant to the Regulation on the Prices of Crude Oil and Petroleum Products (*Official Gazette of RS*, No. 22/01, 34/01, 70/01, 16/02 and 24/02) retail prices of basic petroleum products were under direct control and were formed on the cost-based criteria, mainly crude oil prices. From May 2003 until October 2004, pursuant to the Regulation on the Prices of Petroleum Products (*Official Gazette of RS*, No. 54/03) the model applied for forming prices used, as a criterion, harmonisation of petroleum products prices with the change in the average price of petroleum products in 15 EU states. However, at the end of 2004, the Government adopted Regulation on the Prices of Petroleum Products (*Official Gazette of RS*, No. 103 and 117/04) that brought back the cost-based model of balancing petroleum products prices with quoted crude oil prices, but it also introduced a formula by which the amount of refinery processing costs oscillated depending on oil price. In spite of the fact that the Law on Energy prescribed a free formation of petroleum products prices, in May 2005, with the aim of securing funds for modernisation of refineries and preparation of “Naftna industrija Srbije” (“Petroleum Industry of Serbia”) for privatisation, the Government adopted Regulation on the Prices of Petroleum Products (*Official Gazette of RS*, No. 42/05, 111/05, 77/06, 05/09, 84/09 and 24/10) which enabled periodical adjustment of highest production prices of petroleum products (without fiscal expenditures) with trends in oil price, including the calculation of fixed costs of oil processing and costs of transport.

In the period 2000-2007, the Government, at the request of energy operator, gave consent to the correction of electricity price for all consumer categories, as well as natural gas price for households and heating plants (the price of gas for industry was formed freely). However, since 2008, after the operations related to electricity and natural gas were separated, the Government has given consent to the regulated price of electric energy and natural gas transmission, transport and distribution as well as to prices of electric energy and natural gas for tariff consumers, at the request of energy operator and with the previously obtained opinion of the Agency. The electricity and natural gas prices for non-tariff (qualified) buyers, determined by the contract concluded between a qualified buyer and a supplier, are free.

Until 2007, the oil pipeline transport price used to be included in the production price of petroleum products and was not under direct control, but since 2007 it has been regulated in the way that the Government gives consent to the decision on oil transport price for energy operator, with the previously obtained opinion of the Energy Agency of the Republic of Serbia.

From 2000 on, pursuant to the Law on Public Enterprises and Performance of Activities of General Interest, the Government gave consent to production prices of coal for industry and households. This rule stopped being valid for “Kolubara” and “Kostolac” coalmines in the middle of 2005 at which point they were separated from the Public Company EPS, resulting in the liberalisation of production prices for these two coalmines, so that until today this rule has referred only to Public Enterprise for Subterranean Exploitation of Coal “Resavica”, to whose production prices the Government gave consent last time at the end of 2008. However, in November 2004, the Government has, by putting out of force the Regulation for Determining Maximum Domestic Coal Retail Prices (*Official Gazette of RS*, No. 28/03 and 122/04) liberalised industry and household coal prices for all market participants and since that moment the coal retail prices have been formed freely.

As far as completing of price liberalisation process in the energy sector is concerned, it has been estimated that full opening of market for free import of oil derivatives (from 1 January 2011) shall contribute to increased competition, and therefore also to better quality of fuel, and, in the long run, to lower prices. In the electricity and natural gas market in the next five years it is expected that the process of liberalisation shall continue, and that, gradually, the regional and the domestic markets shall be included in the European electricity and gas market; the competition is expected to be stronger and the price of, mainly, electricity is expected to reach the economically justified level. Until the complete liberalisation of energy market has been achieved, the consumer category of “households” shall have a privileged status of a tariff buyer, so the prices of electricity and natural gas for households shall be regulated. This is especially important regarding electricity price, where any abrupt opening of market would cause a substantial price increase which would have an extremely negative effect on the population’s standard.

The share of controlled prices of electricity for households and basic petroleum products in the list of retail prices in the period between 2003 and 2008, declined from 18.7% to 16.5%. However, parallel with the migration of monitoring inflation through retail prices list to monitoring it through consumer prices list, the total scope of controlled prices within energy sector in 2009 was reduced to 11.5%, and the same value refers to 2010 (the share of oil derivatives is 4.5%, of electric energy 6.6% and of gas 0.4%). Increase in the degree of energy prices liberalisation in 2009, even with additional expansion of the scope of controlled prices pertaining to natural gas for households, is a consequence of a significant decrease in the share of prices of basic petroleum products and electric energy in the list of consumer prices, in relation to its share in the retail prices list.

Amending Law to the Law on Excise (“Official Gazette of RS”, No. 101/10) of 1 January 2011 determines the amount in RSD of the excise on petroleum products as follows;

- 1) all types of motor gasoline, except EURO BMB 98 and EURO Premium BMB 95, in the amount of 45.00 rsd/l;
- 2) motor gasolines EURO BMB 98 and EURO Premium BMB 95 in the amount of 49.50 rad/l;
- 3) all types of diesel fuels, except EURO diesel, in the amount of 35.00 rsd/l;
- 4) EURO diesel in the amount of 37.00 rsd/l;
- 5) other petroleum products derived from oil fractions which have a distillation range of up to 380 degrees Celsius in the amount of 53.34 rsd/kg;
- 6) liquid oil gas for powering of motor vehicles in the amount of 17.95 rsd/kg.

Infrastructure

The prices of services in domestic rail, postal, telegraph and telephone traffic (fixed and mobile telephony) in the period between 2000 and July 2003 were controlled in accordance with the Decision on the Obligation of Pre-Informing on the Change of Prices of Services in Domestic Rail Traffic and Domestic PTT Traffic (*O. Journal of FRY*, No. 8/00, 36/00, 5/01, 37/01, 3/02, 39/02 and 3/03), adopted pursuant to Article 14 of the Law on the System of Social Price Control (*O. Journal of SFRY*, No. 84/89 and *O. Journal of FRY*, No. 32/93 and 28/96), which specifies that the Federal Government prescribes measures for direct control of prices of products and services that are of general interest to the whole of country. Enterprises operating in these areas were obliged to inform in writing federal ministry competent for domestic trade on the prices, at least eight days prior to the change of prices in the market. In case the competent ministry should decide that the proposed prices are not in compliance with the economic policy, they would inform the applicant that the prices cannot be changed.

In this period, the prices of transportation of passengers and goods by airplanes in domestic traffic within scheduled flights and prices of airport services were formed in compliance with the Instruction on Informing on Price Changes for Monitoring Purposes (*O. Journal of FRY*, No. 12/96 and 52/97), adopted pursuant to Article 16 of the Law on the System of Social Price Control, according to which, among other groups of products and services, companies rendering this type of services are to form prices freely, with the obligation of informing federal ministry competent for domestic trade on the change of prices on the day of that change.

Since 2003, pursuant to the Constitutional Chart of the State Union of Serbia and Montenegro, prices of these services came within the competence of the republic level bodies and they have been formed according to the Law on Public Enterprises and Performance of Activities of General Interest (*Official Gazette of RS*, No. 25/00, 25/02, 107/05, 108/05 and 123/07), which prescribes that rail, postal and air traffic and telecommunications, as well as the issuance of the official gazette of the Republic of Serbia, are activities of general interest. In order to perform these activities, the state has founded public enterprises. Pursuant to Articles 27 and 28 of the same law, the Government of the Republic of Serbia shall give consent to the tariff (decision on prices, tariff system, etc.) for the purposes of securing general interest in public enterprises, and securing general interest in other types of enterprises performing activities of general interest for the Republic. The proposal to the Government for giving its consent is submitted by the competent ministry.

The Law on Prices, adopted in September 2005 and in force until the Law on Trade (*O. Gazette of RS*, No. 53/10) entered into force stipulated that the prices of products and services were to be formed freely according to market conditions, except in case of products and services whose prices were to be formed in a different manner as prescribed by a special regulation. In this way, the manner of formation of prices of certain products and services regulated by laws already adopted within respective areas was respected. This formulation is now contained in paragraphs 2 and 5 of Article 36 of the Law on Trade, which has been in force since 1 January 2011.

In August 2005, the Law on Telecommunications (*Official Gazette of RS*, No. 44/03, 36/06 and 50/09) entered fully into force and by that the formation of fixed telephony prices went into the competence of the Republic Agency for Telecommunication (RATEL). The Law on Telecommunications envisaged specifying conditions for the introduction of a special tariff regime and criteria for determining tariffs (Article 43 and Article 44) in cases where certain telecommunication services are provided by only one public telecommunication operator, or when the operator has a significant market share or uses revenues from these services in order

to subsidise or co-finance another telecommunication network or service of their own. Since the Managing Board of RATEL determined that there are public telecommunication operators with significant market shares in public fixed telephony network services and in services of distribution of radio and television channels via cable distribution network, the correction of prices of fixed telephony services have been done since 2006 (Company for Telecommunications "Telekom" a.d.) and correction of prices of cable distribution network services since 2009 (Serbia Broadband – Srpske kablovske mreze d.o.o.) in compliance with the given consent of this body. In conditions when there is competition in the market between public telecommunication operators, tariffs for their services are formed freely.

At the end of June 2010, the Law on Electronic Communications (*O. Gazette of RS*, No. 45/10) was adopted, according to which the Agency for Electronic Communications, based on the previously conducted market analysis, shall, in the form of a decision, designate the operator with significant market power-SMP (Article 62), on whom at least one obligation from Article 63 shall be imposed, which could relate to price control and cost-based accounting. By imposing this obligation, the operator with SMP could be the target of one of the measures laid down in Article 68 of this law. In this year, the prices have not been corrected on account of this law.

Concerning the area of air traffic, at the end of the first half of 2010 the public enterprise for rendering airport services, founded by the Republic of Serbia, was transformed into a closed joint stock company, and in October the same year the Law on Air Traffic (*O. Gazette of RS*, No. 73/10) was adopted, stipulating that the amount of airport charges is to be determined by the airport operator for every individual service, with the previously obtained consent of the airport owner.

By adopting laws from different areas, the following activities have been defined as activities of general interest: managing of railway infrastructure and public railway transport of passengers and goods (Article 7 and Article 70 of the Law on Railway – *O. Gazette of RS*, No. 18/05); managing of public roads (Article 7 of the Law on Public Roads - *O. Gazette of RS*, No. 101/05 and 123/07) and designing, equipping, maintaining, using and managing of public ski resorts, as well as grounds adequate for ski resorts (Article 5 of the Law on Public Ski Resorts – *O. Gazette of RS*, No. 46/06).

The Law on Public Roads prescribes charges for the use of a public road (Article 17), as well as charges set forth by this Article specified by the public road operator, with the consent of the Government (Article 18).

The Law on Postal Services (*O. Gazette of RS*, No. 18/05 and 30/10) prescribes that the Government shall give consent to an Act of the public postal operator, by which postal fees for reserved postal services are determined (Article 23). Reserved postal services include letter parcels up to a limited mass and price, money orders in classical and electronic form and in written form in legal, administrative and misdemeanour proceedings, regardless of limits (Article 19).

Taking all this into account, the obligation of the Government of the Republic of Serbia to give its consent to the prices of public enterprises founded by the Republic of Serbia pertains to reserved postal services, services of domestic railway passenger and goods transport, use of public roads, tourist infrastructure (ski-pass), forms and issues of the "Official Gazette of the Republic of Serbia". Since 2009, the Government has given consent to the services of overtaking, transport and temporary storage of radioactive waste, given that pursuant to Article 48a of the Law on Ionizing Radiation Protection and Nuclear Safety (*Official Gazette of RS*, No. 36/09) managing nuclear facilities in the Republic of Serbia is an activity of general interest. Also, since 2010, the Government has given consent on ticket prices for

entering the Avala Tower facility, in accordance with the concluded agreement on transferring the rights of the usage of Avala tower to a public enterprise from the area of emission infrastructure and the Decision on Establishing Public Enterprise for Managing Emission Infrastructure in the Territory of the Republic of Serbia (*O. Gazette of RS*, No. 84/09), pursuant to which the Managing Board of the Public Enterprise “Emisiona tehnika i veze” (“Emission Technique and Communications”) shall decide on the prices of services rendered.

The share of services in consumer prices under government control in 2010 equals 0.07% (railway passenger transport, an ordinary letter, postcard), and under RATEL control 2.08% (fixed telephony in domestic and international traffic, telephone subscription, public phone booths), which is almost the same as in the preceding year.

Gradual liberalisation of prices in the area of postal services was done in September 2006, when express services were exempted from then existing decision, and in February 2007, when the consent was given only to reserved postal services, resulting in the liberalisation of parcel prices, as they belong to non-reserved services.

The share of liberalised prices is insignificant and in all consumer prices it amounts to 0.01% (parcels) in 2010 and 2009.

Liberalisation of telecommunication market began in 2009. In mid-2009, the Managing Board of RATEL granted two licences for fixed wireless access to the public telecommunication network and services within specific frequency band for the territory of the Republic of Serbia, and companies (Telekom Srbija and Media Works) were obliged to start commercial provision of services at the latest six months after the licenses had been granted. In the beginning of 2010, a license for public fixed telecommunication network and services for the territory of the Republic of Serbia was granted, and Telenor, who was granted the license, is obliged to start commercial provision of services within one year from the date the license had been granted. Market liberalisation creates conditions for better competition and market price formation, with the obligation of financing certain services of general interest by applying cost-based model.

Utility products and services

The prices of public utility services (water, water waste and sewage, waste management and central heating) and public city transport (bus transport of passengers and monthly subscription tickets) are still under control, regardless of the institutional competence and concept. The share of these prices in the retail prices list increased, from 6.4% in 2000, to 8.6% in 2003 and finally to 11.7% in 2008. The moment of transition to new methodology caused the first decrease in the share of these prices in the same year to 3.8%, and after that to 3.7% in 2010, due to the change of the number of weights in the overall weight list. As opposed to the change in the share of these prices from 2000 to 2010, their number remained the same.

Even though these prices had been increasing in the major part faster than the inflation from 2000 to 2005, it was not possible to bring the prices of public utility services and city transport to the economic level, due to the low starting point. In 2000, the “Antimonopoly Regulation” (the Regulation on Measures for Prevention and Elimination of Market Disturbances Caused by the Abuse of Monopoly Position, *O. Gazette of RS*, No. 42/95) was put out of force, thus putting out of force the regime that the local self-government shall determine these prices with the consent of the Ministry of Trade. The first significant change in the normative regulation of price regime in the area of public utility services and public city transport happened in 2002, when the Regulation on Prices of Certain Products and Services

(*O. Gazette of RS*, No. 2/02 and 39/02) was adopted (and subsequently repealed six months later), by which the Government of the Republic of Serbia had intervened by prescribing prices for these services. Repealing the Regulation on Prices of Certain Products and Services virtually meant the return to the implementation of the previously adopted Law on Public Utility Services (*O. Gazette of RS*, No. 16/97 and 42/98), or the return to the regime of the local self-government being competent for deciding on prices of basic utility services. The last change happened in 2006, when, pursuant to the Law on Amendments and Changes to the Law on Public Enterprises and Performance of Activities of General Interest (*O. Gazette of RS*, No. 107/05), a new regulation was introduced at the Republic level – the Regulation on the Procedure of Temporary Suspension of Transfers from the Budget of the Republic to Units of Local Self-Government and Transfer of the Corresponding Share of Wages Tax and Corporate Profit Tax to Autonomous Province (*O. Gazette of RS*, No. 6/06 and 108/08), which laid down the permitted scope of price increase of these services. Sanctions for local self-governments and autonomous province should they exceed the permitted scope for price increase can be the termination of these transfers. (More details are given in the answer to question 33 in Chapter 1: Free Movement of Goods)

Medicines

Prices of medicines for use in human medicine issued on prescription and medicines for use in human medicine issued without prescription have been controlled throughout the whole observed period from 2000 on.

Prices of medicines are administered in accordance with the Law on Medicines and Medical Devices (*Official Gazette of RS*, No. 84/04 and 85/05-other law). The Regulation on the Criteria for Pricing of Medicines (*Official Gazette of RS*, No. 37/08, 84/08, 88/08, 113/08 and 18/09) prescribes the criteria for medicine pricing. From October 2008 until April 2009 changes to this regulation were done twice, in order to create a legal framework for the harmonisation of medicine prices with the change of EUR-RSD middle exchange rate. On the calculation day, the National Bank of Serbia middle exchange rate of EUR to RSD is used in order to calculate the comparative and CIP prices into RSD.

In December 2008, the Decision on Prices of Medicines for Human Consumption (*Official Gazette of RS*, No. 113/08) was adopted, specifying wholesale prices for 3100 medicines for human consumption. In March 2009, the Regulation on Amendments and Changes to the Regulation on the Criteria for Pricing of Medicines (*Official Gazette of RS*, No. 18/09) was adopted, changing the criteria for wholesale pricing of medicines and prescribing the date on which comparative and CIP prices are to be calculated into RSD, thus creating the legal framework for the harmonisation of medicine prices with changes in EUR-RSD middle exchange rate. In March 2009, the Decision on Prices of Medicines for Human Consumption (*Official Gazette of RS*, No. 18/09) was adopted, specifying wholesale prices for 3189 medicines for human consumption.

In October and December 2009, two Decisions on Amendments and Changes to the Decision on Prices of Medicines for Human Consumption (*Official Gazette of RS*, No. 88/09 and 102/09) were adopted, specifying, mainly, prices of new medicines with circulation permits. In March 2010 the Regulation on Amendments and Changes to the Regulation on the Criteria for Pricing of Medicines (*Official Gazette of RS*, No. 13/10) and the Decision on Prices of Medicines for Human Consumption (*Official Gazette of RS*, No. 14/10) were adopted.

The share of medicines in retail prices index in 2009 amounted to 2.2% and was slightly lower than in 2008. The share of medicines in consumer prices index in 2009 equalled 2.72%.

The share of medicines in retail prices index was slightly higher in 2010 in comparison with 2009 (it went from 2.72% to 2.87%) although the list containing medicines whose prices are statistically monitored was not changed.

Under the Law on Medicines and Medical Devices (*Official Gazette of RS*, No. 30/10), which was adopted in May 2010, prices of medicines for human consumption that are issued without prescription (around 11% of medicines for use in human medicine) were liberalised. Pursuant to Article 58 paragraph 1 of the Law, the Government determines the criteria for the formation of prices of medicines that have obtained circulation permit, that are used in human medicine and issued on prescription, as well as maximum prices for these medicines, based on joint suggestions of the minister competent for health issues and minister competent for trade issues.

In compliance with the Law, in June 2010 the Decision on Maximum Prices of Medicines for Use in Human Medicine Issued on Prescription (*Official Gazette of RS*, No. 45/10) was adopted, determining maximum wholesale prices only for medicines used in human medicine, which are issued on prescription. Adoption of this decision provided for a free formation of medicine prices for use in human medicine which are issued without prescription, since 352 medicines issued without prescription were excluded from the List of Medicine Prices that accompanies this decision and is its integral part. Liberalisation of prices of medicines issued without prescription reduced the scope of medicines whose prices are determined by the Government from 2.87% to 2.33% within consumer prices index.

Adoption of the aforementioned decision created conditions for launching into Serbian market of 108 new medicines for use in human medicine that are issued on prescription and that had obtained circulation permit from Medicines and Medical Devices Agency of Serbia.

Current prices of medicines for use in human medicine issued on prescription have been formed according to the Regulation on Criteria for Pricing of Medicines for Use in Human Medicine Issued on Prescription (*Official Gazette of RS*, No. 87/10) and the Decision on Maximum Prices of Medicines for Use in Human Medicine Issued on Prescription (*Official Gazette of RS*, No. 87/10), adopted in November 2010 in line with the Law on Medicines and Medical Devices (*Official Gazette of RS*, No. 30/10). The main reasons for the adoption of a new regulation are bringing it into compliance with the aforementioned law, and/or prescribing criteria for pricing of medicines for use in human medicine issued on prescription and creation of legal framework for harmonisation of medicine prices with prices of comparative medicines in specified reference countries according to data from 2010 and harmonisation with the changes in EUR-RSD exchange rate.

The scope of medicines in Consumer Price Index in 2009 equalled 2.72%, in the first part of 2010 2.87%, and after the liberalisation, the scope of medicines in Consumer Price Index was reduced and it approximately amounted to 2.33%.

Other

At the end of 2009 the Government adopted decisions specifying the price for technical inspection of vehicles and charge for removal of vehicles (*Official Gazette of RS*, No. 109/09) thereby extending the scope, or the list of products and services whose prices are administered, by 0.3%. However, in this case it is not forbidden to form a price of technical inspection of vehicles above, but only below the prescribed level, which, in fact, does not breach the concept of price liberalisation.

The Law on Publishing Laws and Other Regulations and General Acts and Issuing of "Official Gazette of the Republic of Serbia" (*O. Gazette of RS*, No. 72/91, *O. Journal of FRY*, No. 11/93 and *O. Gazette of RS*, No. 30/10) prescribes that the Government shall give consent to retail and subscription prices for the "Official Gazette of the Republic of Serbia" and retail prices of forms, determined by the Managing Board (Article 18).

Since 2009, the Government has given consent to the services of overtaking, transport and temporary storage of radioactive waste, given that pursuant to Article 48a of the Law on Ionizing Radiation Protection and Nuclear Safety (*O. Gazette of RS*, No. 36/09) managing nuclear facilities in the Republic of Serbia is an activity of general interest.

Article 17 of the Regulation on Controlling Exploitation and Trade of Wild Plant and Animal Species (*O. Gazette of RS*, No. 31/05, 45/05, 22/07, 38/08, 9/10) which was adopted pursuant to Article 27 paragraph 6 of the Law on Environmental Protection (*O. Gazette of RS*, No. 135/04, 36/09, 72/09) prescribes that prices of protected species are determined by the ministry competent for environmental protection, with the previously obtained opinion of the ministry competent for trade issues.

The Law on Publishing Laws and Other Regulations and General Acts and Issuing of "Official Gazette of the Republic of Serbia" (*O. Gazette of RS*, No. 72/91, *O. Journal of FRY*, No. 11/93 and *O. Gazette of RS*, No. 30/10) prescribes that the Government shall give consent to retail and subscription prices for the "Official Gazette of the Republic of Serbia" and retail prices of forms, determined by the Managing Board (Article 18).

Notes:

Answers given to question 15 in chapter V Economic and Structural Developments and Reforms, are related to prices of those products and services for which the following refers:

- 1) The Government of the Republic of Serbia gives consent to acts of public enterprises on their prices, with the previously obtained opinion of the ministry competent for trade or it determines prices, on the basis of the proposal of the ministry competent for trade-related issues and ministry competent for the area in question.
- 2) The ministry competent for the area in question determines prices, with the previously obtained opinion of the ministry competent for trade issues.
- 3) Units of local self-government, as founders of public utilities, have an obligation to harmonise growth of prices of public utility services with the policy of projected general growth of prices specified by an act of the Government of the Republic of Serbia for every year, and
- 4) Independent regulatory body gives its consent.

16. Privatisation: (detailed information is required in chapters 4 – Free movement of capital and 20 – Enterprise and industrial policy):

a) Please provide an overview of the privatisation process since year 2000 for state-owned and socially owned companies, respectively. What have been the main methods of privatisation? How many enterprises have been privatised/liquidated/sent into bankruptcy procedures? Please provide information on the size, employment and activity of these enterprises. In which cases have the sales contracts been revoked? Please explain the factors and the process. Have any enterprises been re-nationalised

after their initial privatisation? Is the government considering potential cases for re-nationalisation given the impact of the global economic crisis? What activities are necessary to finalise the privatisation process? What is the current status and portfolio of the agency in charge of privatisation? What are the prospects for the further disinvestment and termination of activities of the same agency?

a) So far, the privatisation process has taken place under two concepts, adhering to the regulations of the Law on Ownership Transformation ("Official Gazette of the RS", no. 32/97 and 10/01) and the Law on Privatisation ("Official Gazette of the RS", no. 38/01, 18/03, 45/05, 123/07, 123/07 – other law and 30/10 – other law).

The first concept, incorporating the application of the Law on Ownership Transformation, involved implementation of the ownership transformation procedure in two rounds; the first round consisted of distribution of the social capital through allocation of free shares to employees and former employees in the amount of 60% of the share capital of the privatised entity, whereas 10% of the capital was transferred to the Pension and Disability Insurance Fund (PDI Fund). The remaining social capital for the issuers not announcing calls for the second round of ownership transformation according to one of the 3 models (1. sale of the shares with and without discount; 2. recapitalization with discount, and 3. debt conversion into shares with discount), was being transferred to the Share Fund of the Republic of Serbia. This privatisation model had been applied until July 2001, when the Law on Privatisation took effect, generating the application of the new privatisation concept. Application of the new Law on Privatization did not compromise those privatisations undertaken according to the earlier law, thus securing legal protection for the participants of the privatisation. Likewise, this model of the sale of the privatised entity social capital is performed as one-off, thus overcoming the problem of partial privatisation and privatisation with delayed effects, aiming to shorten the total time of the privatisation and to have its effects reflected in the development of the privatised entity and the general economy growth as soon as possible.

In view of the provision of the Law on Privatisation, the most important activities in 2010 and in the period ahead would be:

- 1) to finalise the social and state capital privatisation, according to the Law on Privatisation, through tenders and auctions, on the capital market, and through liquidation/bankruptcy;
- 2) to sell the shares and stakes from the Share Fund portfolio (capital market);
- 3) . to privatise the social capital in the undertakings organized according to Regulation on protection of the property of companies that had headquarters on the territory of the former SFRY ("Official Gazette of the RS", no. 31/01, 61/08, 109/08, 14/09, 40/09, 79/09, 111/09 and 67/10).
- 4) to participate in the development of the privatisation strategies for big public enterprises and to finalize the restructuring strategy for public-communal enterprises;

1. In the period from the adoption of the Law on Privatisation (in July 2001) until 30 November 2010, totally 2,405 enterprises were privatised.

There were 1,589 enterprises with 130,789 employees sold at auctions, with total income from the sale of EUR 903 million, and compulsory investments of EUR 203 million.

In the same period, 93 big enterprises with 75,120 employees were sold through tenders, accomplishing income from the sale of EUR 1.1 billion, and compulsory investments of EUR 973 million.

As regards the capital market, the accelerated sale procedure continued for shares from the portfolio of the Share Fund, as well as the withdrawal of the Government's participation in the private sector capital, thus selling minority shares of 723 enterprises, with income of EUR 624 million.

Table 1 – Privatisation results as of 30 November 2010

| Description | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 1.1.- 30.11. 2010. | Total 2002-2010 |
|---------------------------|-------|--------|--------|--------|--------|--------|--------|-------|--------------------------|--------------------|
| Number of sold companies: | 211 | 638 | 237 | 317 | 281 | 316 | 277 | 94 | 34 | 2.405 |
| Number of employees | 37.32 | 76.927 | 38.808 | 58.931 | 45.962 | 45.011 | 27.187 | 9.119 | 1.634 | 340.899 |
| In millions of EUR | | | | | | | | | | |
| Selling price | 319 | 840 | 154 | 371 | 240 | 434 | 253 | 49 | 13 | 2.673 |
| Investments | 320 | 320 | 100 | 99 | 152 | 104 | 62 | 25 | 2 | 1.184 |
| Welfare programme | 146 | 128 | 3 | 0 | 0 | 0 | 0 | 0 | 0 | 277 |

Source: Privatisation Agency

In 2010, the capital and the property of 2 undertakings were sold by public tender, and 25 undertakings were sold at auctions. Privatisation Centre's plan was to successfully finalize the privatization procedure – negotiations on the sale of the capital and/or property of 4 undertakings by the end of 2010. Public call is also underway for the sale of the capital of six undertakings at auctions, which have been appointed for December 2010. Five bidding procedures for the sale of the property entities and shares have been appointed for December. The appointed bidding procedures represent the continuing sale of the property and property entities, as well as of the shares of the restructuring undertakings with majority social capital.

Furthermore, the Privatisation Centre portfolio presently includes 221 companies whose privatisation procedure has been interrupted for several reasons.

Of this number, 174 operate with majority social capital and 47 with state capital. Likewise, the procedure is underway before the Property Directorate of the Republic of Serbia relating to 41 socially-owned companies as to ascertain the state property share in the assets used by

companies, complying with Article 48, of the Law on Assets Owned by the Republic of Serbia (of this number 26 companies' main business is water management and 15 did not have a public call announced by the legal deadline because they had unresolved ownership/legal relations).

Almost all undertakings are expected to find the state property share to be around 100%, resulting either in termination, or continuation of the privatisation procedure, subject to the decision of the Government of the RS.

Moreover, 21 undertakings, tourist services providers, spas, companies for the employment and vocational training of invalids, whose founders are syndicates, sport associations, and others, are in the termination procedure. In this connection, privatization is scheduled to begin for sports societies, after adoption of the Law on Sports. Similarly, privatisation procedure for special hospitals, or spas in Serbia is expected to continue once property and legal issues have been resolved.

In accordance with the Conclusion of the Government of the RS, 47 state-owned companies are in the termination procedure, primarily electronic media broadcasting national minority programmes, veterinarian stations, those in publishing and other businesses, whose continued privatisation procedure shall be conducted once the competent ministries have presented their opinions.

With regard to bankruptcy procedures, the Bankruptcy Centre, of the Privatisation Agency, has been appointed the bankruptcy administrator in 877 cases of bankruptcy debtors. Of this number, 236 were under the category of inherited cases, or the cases initiated according to the earlier law, where bankruptcy administrators were dismissed from duty, and Privatisation Agency was appointed, while 641 were the bankruptcy procedures initiated after the date of the initial application of the The Law on Bankruptcy ("OG of the RS", no. 84/04 and 85/05 – other law), or after 02/02/2005, including the bankruptcy procedures instigated according to the provisions of the Law on Bankruptcy ("OG of the RS", no. 104/2009). There were 310 bankruptcy cases concluded, where assets from the sale of the property of the bankruptcy debtors reached in total RSD 52,284,960,152.14. Inclusive the beginning of December 2010, the Privatisation Agency has been acting as bankruptcy administrator in 481 cases of active bankruptcy debtors. There are indications that in 2011 the Privatisation Agency, could be appointed the bankruptcy administrator for 400 undertakings (from the forced liquidations portfolio, insolvent entities under regular procedure, undertakings with terminated sale/purchase agreements and opened respective bankruptcy procedures...).

Adoption of the new Law on Bankruptcy ("Official Gazette of the Republic of Serbia", no. 104/2009) and adoption of the by-law acts (the Rulebook on the Requirements and the Manner of the Appointment of the Bankruptcy Administrator by Random Selection; The Rulebook on the Manner of the Issuance and the Renewal of the Bankruptcy Administrator Licence; the Code of Ethics; National Standards for Bankruptcy Mass Management; the Rulebook on the Form and the Content of the Official Identification Document; the Rulebook on the Content, the Manner of Subscription and the Maintenance of the Bankruptcy Mass Register and the Regulation on the Type and the Amount of the Remuneration for the Registration and Other services provided by the Business Registers Agency in the procedure of maintaining the bankruptcy mass registers), this matter has been regulated in detail and in an appropriate manner.

Its priority target is the collective settlement of the creditors, accomplishing the highest possible bankruptcy debtor's value, or of his property, in a significantly shorter time, than was the case before, thus eliminating many deficiencies of the earlier law.

2. In November 2010 the Share Fund portfolio contained the shares and stakes from about 870 companies (not counting the shares in companies where shareholders renounced the shares). Attention should be paid that the number of companies in the Share Fund portfolio changes practically on a daily basis. On the one hand, shares and stakes from the Share Fund portfolio are being sold, and on the other hand, shares and stakes remaining after the sale of the capital in the privatisation procedure, and after termination of the sale of capital, i.e. property contracts, are being transferred to the Share Fund portfolio.

In May 2010 the Law on Amendments and Supplements to the Law on the Right to Free Shares and Monetary Compensation Exercised by Citizens in the Privatisation Process was adopted ("Official Gazette" of the RS, no. 30/10);. The Share Fund was thereby established as well as the manner of selling of the shares and stakes which were transferred to the Fund. The regulation stipulating the deadline for the sale of shares and stakes registered by the Share Fund was erased.

This law provides for the exercise of the rights of the citizens to monetary compensation based on the sale of the shares or stakes registered by the Privatisation Register in the Share Fund, the free of charge transfer of the shares of the undertakings and companies as determined by this law, as well as the exercise of the rights of the employees and former employees to share transfer free of charge relating to respective undertakings and companies.

Regulation on the Rules and Procedure for the Sale of Shares and Stakes Owned by the Share Fund through Public Auction ("Official Gazette of the RS", no. 72/10) specifies the procedure and the manner of the sale of shares and stakes which were transferred to the Share Fund through public auction based on the decision adopted by the Share Fund Council.

3. As regards the socially owned undertakings with stopped privatisation procedure, whose founders were from former Yugoslav republics, and whose total number in the Auction Centre portfolio is 108, the continued privatisation is expected to be considered after the deadline defined by the Regulation on Protection of the Property of Companies that had Headquarters on the Territory of the Former SFRY, i.e. after 28/02/2011, for the purpose of the Agreement between the privatisation participants and the undertakings whose headquarters were on the territory of the former SFRY republics.

Significant activities are ahead of us following the introduction of the privatization model through strategic partner seeking, which would exclusively be applied for companies of special interest for the Republic of Serbia.

As regards the termination of the purchase and sale contracts, Article 41a of the Law on Privatisation, foresees that where obligations are not fulfilled under the contract, or within the additionally laid down period, the capital, i.e. property sale contract shall be deemed terminated.

Inclusive of 01/12/2010, the Privatisation Agency terminated the **total of 600 contracts** of capital, i.e. property sale with privatization entities, **mainly because of** the following: **non-payment of the instalments due as per the purchase and sale price, non-maintenance of the business continuity, non-respecting the social programme, non-submission of the bank guarantees, non-performance of the investment obligation, disposing of entity's property contrary to the contractual provisions.** Most cases generated several reasons for contract termination.

Article 41, of the Law on Privatisation, and relating to Article 12, of the Law on Amendments and Supplements to the Law on the Privatisation Agency, stipulates that after a contract for the sale of capital has been terminated with the buyer, privatisation entity's capital, which was the subject matter of the sale, shall be transferred to the Privatisation Agency, as well as the capital which was subject of the capital increase during buyer's contractual obligations. **There are 248 undertakings within the competence of the Privatisation Agency, as regards the transferred capital after contract termination.** Of this number 199 undertakings were inherited from the portfolio of the Share Fund of the RS, whereas 49 undertakings' capital was transferred directly to the Privatisation Agency, once the contract was terminated.

So far, for one undertaking the capital has been transferred from the Privatisation Agency to the Republic of Serbia, by concluding the agreement on the gifting of issuers shares, <<TK Prosveta>> ad, Čačak, as of 25/11/2010, on the basis of the Conclusion of the Government of the RS 05 Number: 023-8312/2010 of 11/11/2010.

In respect of activities needed to be implemented as to finalize the privatisation process, according to the Law on Privatisation, it is necessary to continue to promote privatisation, identify strategic partners and potential investors, as well as to prepare the undertakings for the sale in compliance with individual potential investor's requests, adhering to the legislation.

For big systems included in the restructuring procedure the following should be finalized:

status changes, legal form changes, changes in the internal organization and other organizational changes;

- financial restructuring of the undertaking;
- the resolving of social issues.
- For undertakings presently in the procedure of terminated privatisation the problems presently obstructing the sale of the capital i.e. the property, should be resolved, hence it is needed to:
- resolve the ownership and legal relations, or to finalize the procedure for the determination of the state-owned property in the assets used by the company, after which the privatization procedure shall be terminated or continued;
- for undertakings which are in line with the Regulation on Protection of the Property of Companies that had Headquarters on the Territory of the Former SFRY, it is needed to determine the share in the capital of the socially-owned company on the basis of the property entered and to prepare the draft Agreement to be signed by both participants, and delivered to the competent ministry, and referred to the Government of the RS for consent.

In respect of the present status and the portfolio of the Privatisation Agency, the portfolio of the Privatisation Centre contains 455 enterprises, of which:

255 are socially-owned companies and

200 have capital of the Share Fund, Privatisation Agency and/or the state-owned capital, i.e. capital of the Republic of Serbia, Pension and Disability Fund and/or Development Fund.

Of 455 undertakings:

for 31 undertakings, tender was specified as a method of sale

for 288 undertakings, auction was specified as a method of sale

whereas for 139 undertakings, restructuring procedure was introduced

(please note that the restructuring programme defined that for 3 undertakings, in the group of 139, tender was the method for the sale of the capital and property, hence these fell under both criteria, i.e. also in the group of 31 undertakings)

The Privatisation Centre portfolio includes 221 companies in the procedure of the stopped privatization process:

- 174 operate with majority socially-owned capital
- 47 with state-owned capital

The Law on Amendments and Supplements to the Law on the Privatisation Agency (<<OG of the RS>>, no. 30/10), extended the Privatization Agency activities, hence the Agency now also performs activities of selling the shares, i.e. stakes whose lawful holders are the Republic of Serbia, the Share Fund, the Fund for the Development of the Republic of Serbia, the shares which were transferred to the Republic Fund as the one charged with employees' pension and disability insurance, as well as the shares and stakes after termination of the contract of the sale of capital, i.e. property, concluded between the Agency and the buyer of the capital.

The Share Fund was established in line with the Law on Amendments and Supplements to the Law on the Right to Free Shares and Monetary Compensation Exercised by Citizens in the Privatisation Process (<<OG of the RS, No. 30/10), into whose ownership were transferred the shares and stakes as registered by the Privatization Register, as well as the shares and stakes transferred to the Shareholder Fund by the Share Fund, adhering to the law.

Since the beginning of December 2010, the Privatisation Agency has been charged with the sale of shares and stakes in more than 1,700 companies. The portfolio at the disposal of the Agency is as follows:

- 1) The Shareholder Fund – owned by the Share Fund contains shares in 1.517 open joint stock companies, shares in 24 closed joint stock companies, as well as stakes in 194 limited liability companies.
- 2) The Pension and Disability Fund – owned by the Pension and Disability Fund contains shares in 165 joint stock companies, and stakes in 10 limited liability companies.
- 3) The Fund for the Development - owned by the Fund for the Development contains shares in 23 joint stock companies.

b) Please quantify privatisation in terms of sales revenues and fees since 2000. How did the authorities use privatisation receipts? How will the future funds resulting from privatisation be used?

In respect of the use of privatisation receipts, that is defined under Article 61, of the Law on Privatisation, prescribing their distribution as follows:

- 1) 10% of the funds are paid to the Republic fund charged with pension and disability insurance;
- 2) 50% of the funds are allocated for the finance the restructuring and economy development on the territory of the Republic of Serbia.

Where the headquarters of the entities of privatization are located on the territory of the Autonomous Province of Vojvodina, 50% of the funds shall be allocated to finance the

restructuring and economy development on the territory of the Autonomous Province of Vojvodina.

- 3) 5% of the funds are allocated for remuneration to persons whose property was nationalized;
- 4) 5% of the funds are allocated to finance the infrastructure development and local self-government based on the headquarters of the entity of privatization.

c) Has corporate governance improved as a consequence of privatisation?

In the here above mentioned period corporate governance improved significantly as a consequence of privatisation. This can be observed in a number of successful undertakings, steered by new management, rationalization of employees, more efficient and effective operations.

Under its competencies, the Ministry of Economy and Regional Development shall continue with economic policy aimed at attracting green-field investments, and attracting foreign capital, new technologies and increased employment.

Arrival of the foreign capital into our country shall have multiplied effects on our economy, since big investor operations are linked to entire chains of small providers wherefrom small and medium-sized enterprises are developed.

Investments will be made in infrastructure, thus creating favourable conditions for investors and for balanced regional development.

Intensified creation of favourable conditions for the establishment of small and medium-sized enterprises through credits will reduce unemployment, increase competitiveness, stimulate balanced regional development and export.

The Ministry of Economy and Regional Development shall also continue with present activities aimed at attracting investors from information technologies, electronic industry, car industry etc.

17. Public sector: What is the public sector's share in the economy? What sectors are still controlled and/or owned by the state and to what extent? Please outline the government plans as regards the state-owned enterprises.

The Law on Public Enterprises and Activities of Public Interest specifies activities of public interest, consequently the fields where public undertakings may be established, as well as the manner of their establishment and the regulation of their status.

As to limit possible fiscal obligations, the state supervises and maintains financial discipline in public undertakings, especially as regards the salaries, employment policy, as well as other expenditures. With the same aim, the state also controls public undertakings established by the local self-government units, through the local self-government units.

State-owned enterprises on the republic level still exist in the following sectors: production and electric power transfer, coal, natural gas, railways, roads, postal services, air company, airports, forests and waters. The Republic of Serbia owns majority shares of 80% in the "Telekom Srbija" j.s.c. and a stake of 49% in the "Naftna industrija Srbije" j.s.c. In addition to the here above mentioned, the Republic of Serbia owns national parks.

Communal enterprises are under the competency of the local self-government, and several

public enterprises are under the competency of the Autonomous Province of Vojvodina.

Based on the previous analysis made for every public enterprise, the process of corporatization shall continue aiming to fully regulate ownership, organizational, management and other issues, basically targeted at raising the efficiency in performing the activities of public interest.

Public enterprises have been organizationally restructured on public level, secondary activities have been extracted from their structure, and in several cases of state-owned stake in public enterprises was sold with substantial investments with and without state guarantees. The program for restructuring the national transport undertaking is underway, with ambitious projects in other areas.

The Ministry of Economy and Regional Development has been preparing a strategy for transformation of local public enterprises and for defining the manner and modality for inclusion of private capital as to reduce losses and budget transfers, followed by the services quality improvement in this sector.

The Law on Privatisation has regulated the procedure and the requirements for the change of ownership of social, or state capital, i.e. privatisation. Besides the Ministry of Economy and Regional Development, which is competent for privatisation process, the corresponding ministries under its competence are competent for activities carried out by big public enterprises.

The initiated procedure for the adoption of the Law on Public Ownership will allow, inter alia, public enterprises to become owners of the property they use, being the precondition for successful corporatization. This is the very field that represents the main obstacle in the presentation of the real capital value. Inherited state ownership over enterprises and also ownership over property used by these enterprises, results in distorted business results, thus preventing data aggregation for this sector and decreasing the quality thereof, which is why it is productive to observe individual enterprise results.

To increase transparency, it was decided to announce information on the audited financial statements of state enterprises, as well as the reports on the management salaries structure therein.

Importance of the state-owned sector is reflected in the fact that of the 1,911 thousand people employed in Serbia, by the end of 2009, there were 94,1 thousand employed in public enterprises, whereas in the field of communal activities there were 65,2 thousand, employed in 595 enterprises.

18. Protected sectors (utilities, transport, housing...): Which sectors are subject to specific protection (market entry, price setting...). Please describe recent developments in this respect, such as specific measures of liberalisation or deregulation. Which sectors are to remain under special protection? Are there provisions of preferred treatment as regards former state-owned enterprises? (detailed information is required in *chapter 8 – Competition policy*)

Answer to this question is provided under answer number 15, of this Chapter, as well as under Chapter 8, “Competition Policy” – I part:” Antitrust Including Mergers” and III part “Liberalization” (questions/answers 42-49)

19. Enterprise restructuring: How many state-owned (or formerly state-owned) and socially owned enterprises have been restructured so far? How many enterprises are currently being restructured or envisaged to be restructured? Please identify the remaining sectors and state-owned enterprises in need of restructuring. (detailed information is required in *chapter 20 – Enterprise and industrial policy*) Please provide information about annual aggregate profits/loss of state-owned enterprises in the period 2000-2009. To the extent relevant, please describe briefly the privatisation strategy for the main state-owned and the remaining socially owned enterprises.

The process of socially-owned companies privatisation and restructuring is in the final phase. Ever since the Law on Privatisation was adopted many significant results have been accomplished in privatisation of social ownership. New ownership structure of the economy of Serbia contributed to the increase of the production and the efficiency of activities, the increase of investments in new production capacities and the technologies, export and accelerated development of the country.

Privatisation procedure through restructuring process has included 72 socially-owned companies, where the decision was also taken on the finalization of the restructuring procedure.

At present 139 enterprises are in the restructuring procedure:

- 51 with socially-owned capital,
- 88 with state-owned capital.

Most enterprises which have adopted the Restructuring Programme, started selling adhering to the program, where in majority of cases the concept of the sale for socially-owned companies under restructuring foresaw the sale of company's property. Finalization of their sale, and after that the finalization of the restructuring process shall depend on the market situation.

As regards the undertakings with state capital (socially-owned companies where purchase and sale agreement was terminated), of 88 undertakings, **51 were included in the restructuring after termination of the purchase and sale agreement**, which followed due to unfulfilled buyers' contractual obligations, and the capital was transferred to the Shareholder Fund and the Privatisation Agency. All these undertakings have been appointed temporary capital agents. Number of undertakings are in the procedure of public procurement of privatisation advisor, while others started restructuring program preparations, which will define the manner of the sale of capital and property. Their implementation will start after adoption of the program.

At the moment it is impossible to predict and give a precise answer as to how many remaining undertakings with state capital would need to have the restructuring procedure initiated.

In the coming period it is foreseen to initiate the adoption of restructuring strategy for local public communal companies, whose founders are local self-government authorities. The goal of Government of Republic of Serbia (RS) and other competent institutions is to apply an optimal transformation model to local public utilities companies, in order to preserve public interest and simultaneously ensure their efficient business, in line with the standards of the EU countries.

In the process of transformation of the entire public sector it is necessary to regard public communal companies as separate entities due to their complexity with a view to providing public-communal services, thus defining special models for each activity, which is especially important in cases when opting for a form of partnership with the private sector.

There are numerous problems in the functioning of public communal companies in the Republic of Serbia (in some parts of the RS they are the only operational companies, and therefore very important in the given region) which is a consequence of the inherited and newly created circumstances in the last 15 years: technical-technological obsolescence; oversized companies; tendency toward irrational spending; high indebtedness; high level of losses; strong budgetary dependency; inadequately resolved ownership issue; fragmentation of activities; decrease in volume and quality of services etc. Also, the main obstacle to a long-term public interest fulfilment regarding the quality of communal services is the lack of the means for modernisation and expansion of communal infrastructure, because most communal companies are not capable to finance participation in needed large scope investments with their own means.

In relation to the above and pursuant to the Conclusion of the Government of the Republic of Serbia, as of 6 November 2008, which suggested conducting an analysis of the situation of local public communal companies and proposing a strategy for their reconstruction, the Ministry of Economy and Regional Development formed a Working Group for communal companies, comprising representatives of the Ministry of Economy and Regional Development, the Cabinet of the President of the Government, other corresponding ministries, the Privatization Agency and the Standing Committee of Towns and Municipalities.

The first strategy draft has been finished so far, with participation of the representatives of the World Bank, “Programme of Support for Development of Infrastructure in Local Self-government”, the European Bank for Reconstruction and Development (EBRD), USAID’s “MEGA” project and the German Development Bank (KfW). This strategy is expected to be adopted in 2011.

It is foreseen that the strategy which should result in efficient and effective work of those companies (around 600 communal companies), will designate different models, such as PPP concept (Public-Private Partnership, i.e. the concept that implies interaction between private and public sector), concession and similar, in line with the positive experiences from the European practice.

20. Please describe the basic features of market entry in the corporate sector (business register, licensing procedures, number of separate administrative procedures, average amount of time for corporation) and of market exit (bankruptcy procedures)? How many companies declared bankruptcy over the last five/ten years? How many companies are currently under bankruptcy proceedings? (detailed information is required in chapter 20 – Enterprise and industrial policy)

The Business Registers Agency is a centralized institution for registrations on the territory of the Republic of Serbia.

It was established in 2004, under the Law on Business Registers Agency (OG of the RS, no 55/2004, and 111/2009), and it started on 1 January 2005, undertaking the implementation of reforms in the area of business registrations.

The Business Registers Agency operates in line with the regulations on public agencies, maintaining the unique, centralised, public, electronic register databases, as follows: Business Entities Register includes Companies Register, Register of Entrepreneurs, and, Register of Representative Office of Foreign Legal Entities, the Business Entities Register, Financial Leasing Register, the Register of Pledges on Movable Property and Rights, Register of Associations, Register of Foreign Associations, Register of Public Media, Register of

Regional Development Measures and Incentives, Register of Chambers of Commerce, Register of Tourism, Register of Bankruptcy Estate, Register of Financial Statements and Data on Solvency, which are managed by the Registrars, appointed by the Agency's Board of Directors, with the prior consent of the Government.

Competent ministries supervise and control the performance of the registers, subject to the type of the registration.

The reform which took place in the field of business entities data registration, and with established electronic register, as unique databases managed by the Business Registers Agency, and based on the the Law on Business Registers Agency, The law on Amendments and Supplements to the Law on Business Registers Agency, and the Business Registration Law, all contributed to the creation of a favourable environment for the development of the economy, as reflected in the results referring to the last 6 years of the operating of the Business Registers Agency (increased number of founded business entities, especially in the form of entrepreneurs and limited liability companies, which resulted from the simplified business entities founding procedure, shorter time limits, through one-stop-shop system which started on 06/05/2009, and reduced compulsory minimum initial capital for some forms of companies).

Registration procedure for companies is regulated by the Business Registration Law and is uniform for all companies, thus for the registration of the founding of a company, in most cases the following documents need to be provided: registration application, act of incorporation, proof of founder's identity, proof of paid financial contribution, decision on elected representatives, stamped signatures of representatives and proof of paid registration fee.

Some companies, as stipulated by special laws (the Law on Banks, the Law on Insurance, The Law on the Market of Securities and other Financial Instruments, etc.) need to have approval and consent by the competent authority as a precondition for their founding (e.g. to found a bank or an insurance company it is necessary to provide approval of the National Bank, to found a broker dealer company it is necessary to provide approval of the Securities Commission for the carrying out of the broker dealer activities).

Likewise, some entrepreneur activities (activities of natural persons engaged in all lawful activities for the purpose of gaining profit), are stipulated by the laws referring to the: health care activities, veterinarian activities, agricultural activities, taxi transportation, communal services, etc., which induce preconditions to be fulfilled prior to the registration, and the carrying out of the activities.

Prior consents are being issued in the form of decisions by the competent ministry for that field, whereas the party submits registration application when registering, as well as the decision ascertaining that requirements were met for the carrying out of the activities.

Registration procedure of the founding was successfully reformed introducing the "one stop shop" service as of May 2009, thus allowing business entities to submit a unique registration application for the founding, submitting the application to the Tax Administration and the Fund for Pension and Disability Insurance thus completing the registration of the business entity, and acquiring the following: the Decision on the founding of a business entity with the unique registration number of the business entity issued by the Statistical Office of the Republic of Serbia, tax identification number (TIN) issued by the Tax Administration, and insurance registration from competent health, pension and disability insurance funds.

Reform of the registration of the founding has reduced the whole procedure to two days, whereas registration shall take effect to third persons as of the next day after the registration of the change has been announced.

Bankruptcy

The Law on Bankruptcy ("Official Gazette of the Republic of Serbia", no. 104/2009) specifies business entities exit from the market. Bankruptcy procedure shall be initiated once:

- the proposal for initiation of the bankruptcy procedure has been submitted by the authorised proposer (creditor, or bankruptcy debtor), the court has reached its decision on the opening of the bankruptcy procedure having investigated the requirements thereof (existence of the reasons for bankruptcy), has adopted decision to open bankruptcy procedure;
- the notification by NBS – organization which is charged with the conducting of the forcible payment has been submitted to all commercial courts on the legal persons who stopped all payments in the continuous period of 3 years (in 2011 two years, and as of 2012 one year), or whose accounts were blocked, and the court has, ex officio, decided to initiate the preceding bankruptcy procedure, whereby ascertaining the existence of creditor's legal interest for the conducting of bankruptcy procedure.

There are several ways how enterprises may exit from the market through bankruptcy:

- 1) bankruptcy – selling the entire property of the bankruptcy debtor,
- 2) bankruptcy – selling the bankruptcy debtor as a legal person,
- 3) beforehand prepared reorganization plan
- 4) reorganization – in line with the adopted reorganization plan and redefined debtor-creditor relations, debtor status changes, or in any other way foreseen under the reorganization plan.

How many companies declared bankruptcy over the last five/ten years?

According to the data from the Agency for Licensing of the Bankruptcy Administrator³⁷ the total of 2417 bankruptcy procedures were opened in Serbia from 02/02/2005 until 01/12/2010, whereas it should be noted that in 2005, for 433 bankruptcy procedures, which had been conducted under the Law on Forced Settlement, Bankruptcy and Liquidation (LFSBL), the procedures were continued under the Law on the Bankruptcy Procedure (LBP) – in those procedures not more than 50% of the book value of the bankruptcy debtor was sold.

Table 1 – Listing of the bankruptcy procedures from 02/02 /2005 until 01/12/2010

³⁷ Law on the Agency for Licensing of the Bankruptcy Administrator has authorised the Agency for Licensing of the Bankruptcy Administrator ("Official Gazette of the RS" no. 84/04, 104/2009) to manage statistics for all bankruptcy procedures opened on the territory of the Republic of Serbia, and the data may be found on the website of the Agency w.w.w.alsu.gov.rs. The data are managed for:

- bankruptcy procedures which had been opened under the Law on Forced Settlement, Bankruptcy and Liquidation, and were continued as of 02/02/2005 under the Law on Bankruptcy Procedure;
- bankruptcy procedures which have been opened since 02/02/2005 under the Law on Bankruptcy Procedure;
- bankruptcy procedures which have been opened so far since 23.01.2010 under the Law on Bankruptcy;

| Year | Cases initiated under LFSBL and continued under LBP | Opened | Closed (stopped and concluded) | Active (end of year total number) |
|-------------------------|-----------------------------------------------------|--------|--------------------------------|-----------------------------------|
| 2005 | 433 | 158 | 17 | 579 |
| 2006 | | 267 | 184 | 662 |
| 2007 | | 201 | 241 | 622 |
| 2008 | | 148 | 220 | 550 |
| 2009 | | 328 | 167 | 711 |
| 2010 (до 01.12.2010) | | 877 | 137 | 1451 |
| Total | | 1979 | 966 | |

Statistics for 2010 indicate that number of opened bankruptcy procedures until 01/12/2010, was more than doubled compared to 2009, thus almost six times higher than the number of bankruptcy procedures in 2008. The main reason for the increased number of bankruptcy procedures is rooted in the norms of the Law on Bankruptcy, regulating the introduction of <<automatic bankruptcy>> for legal personalities who were blocked for more than 3 years (two, and as of 2012, one year).

Table 2 – Total number of bankruptcy-cases procedures registered by the Agency:

| Ordinal no. | Law | Number of procedures |
|--------------|------------------------------------------------------|----------------------|
| 1 | Law on Forced Settlement, Bankruptcy and Liquidation | 433 |
| 2 | Law on the Bankruptcy Procedure | 1115 |
| 3 | Law on Bankruptcy | 869 |
| Total | | 2417 |

The total number of procedures-cases conducted under the Law on Bankruptcy Procedure (hereinafter as: LBP): and the Law on Bankruptcy (hereinafter as: LB) is 2417, consisting of:

- 1451 active cases,
- 750 concluded cases, and
- 216 stopped cases.

How many companies are currently under bankruptcy proceedings?

Table 3 – Structure of active cases by type of bankruptcy administrator:

| Ordinal no. | Type of bankruptcy administrator | Case number: | Share |
|-------------|---------------------------------------------|--------------|--------------|
| 1 | Bankruptcy administrators (natural persons) | 930 | 64,1% |
| 2 | Privatisation Agency | 521 | 35,9% |

| | | |
|--------------|-------------|--------------|
| Total | 1451 | 100 % |
|--------------|-------------|--------------|

Table 4 - Bankruptcy procedures opened since 23/01/2010, under the Law on Bankruptcy;

| Bankruptcy procedures | Regular bankruptcy procedures | Automatic bankruptcy | Total |
|-----------------------|-------------------------------|----------------------|------------|
| ACTIVE | 207 | 629 | 836 |
| STOPPED | 1 | 0 | 1 |
| CONCLUDED | 6 | 26 | 32 |
| TOTAL | 214 | 655 | 869 |

According to the data available from the Business Register, 1385 business entities are presently in the bankruptcy procedure. As of 31/12/2008 there were 500 business entities registered under bankruptcy procedure by the Business Register, and as of 31/12/2009, there were 693.

The number of business entities with initiated and conducted bankruptcy procedure cannot be provided because the bankruptcy procedure is conducted in the court proceeding, and not before the Business Registers Agency, whereas the Business Register enters data on bankruptcy procedure based on the submitted registration application.

21. State aid: What is the legal framework for awarding state aid? What are the main features of this framework? How have subsidies and public guarantees developed over the past five years? According to what economic criteria is state aid granted? Please provide data on direct subsidies awarded since 2003. Please provide also information on the size and structure of all schemes for government guarantees on bank loans to the private sector. Is there a medium-term target on scaling down public guarantees? Please provide available annual reports on state aid. (*detailed information is required in chapter 8 – Competition policy*)

The basis for regulatory framework on state aid control is The Law on State Aid Control, which has been adopted in July 2009 (*Official Gazette* no. 51/09), and whose initial enforcement was envisaged for January 2010.

For the purpose of implementation of the Law, in March 2010, the Government adopted the Regulation on State Aid Granting (“Official Gazette”, no. 13/10) and the Regulation on Rules and Procedure for State Aid Notification (“Official Gazette of RS”, no. 13/10). These regulations came into effect on 10 March 2010, establishing a legislative framework for full law enforcement and implementation of the system for state aid control in compliance with the field related EU rules.

Given that direct enforcement of provisions of the law itself would have created a certain level of legal insecurity leading to arbitration in the performance of the Commission for State Aid Control, adoption of the two above regulations paved way for a functional framework of state aid control.

In December 2009 the Government adopted decision on formation of the Commission for State Aid Control ("Official Gazette of the RS", no. 112/2009). The Commission became operational in March 2010, when it held the first constitutional meeting.

The Commission for State Aid Control has adopted legal opinion to evaluate the alignment of only those individual aids and aid schemes passed after 20 March, while other acts could be taken account of under the Adjustment Program of Existing State Aids.

By the end of the year, the Ministry of Finance shall adopt the a Rulebook Underlying Methodology for Drawing up the Annual Report on State Aid in the Republic of Serbia, which inter alia, prescribes the time limit for submission of the data to the Ministry, and the time limit for annual report submission.

The Law on State Aid Control and by-law acts have transposed the rules and criteria from the *acquis (acquis communautaire)*, in the field of state aid, thus fulfilling the obligations contained in the SAA and Interim Trade Agreement thereof. Provision under Article 1, paragraph 2 of the Regulation on State Aid Granting foresees that in the course of state aid granting the state aid grantor, and the proposer of the regulations constituting the basis for state aid granting, while granting state aid, shall be bound to adhere also to the rules contained in concluded international contracts relating to state aid, and not included in the regulation.

The Government has been adopting annual reports on the granted state aid volume since 2003. The website of the Ministry of Finance contains annual reports on state aid since 2006, translated into English language. By the end of this year, the Ministry of Finance shall adopt the Rulebook Underlying Methodology for Preparation of Annual Reports, whereby the methodology for data collection and state aid classification shall fully be harmonized with the European.

The last annual report on granted state aid refers to 2009, and was officially adopted in June 2010. It was translated into English and published on the website of the Ministry of Finance, constituting an integral part of the answers to the EC Questionnaire.

22. Please indicate what you consider to be the main priorities of structural/microeconomic reform agenda.

Micro economic reforms in the coming midterm period will be focused on the improvement of business environment and on the fostering of the private sector role in economy.

Improvement of business environment will include completion of the project "regulatory guillotines" whose goal is to cancel the unnecessary laws and by-laws and to improve the existing laws, thus significantly reducing expenditures in economy, and simplifying the legislative framework pertinent for the economy, as well as the adoption of new legislation in the field of economy, primarily by adopting the new company law, aimed at the strengthening of corporate management and removing the impediments in the founding procedure and operations of companies.

While real sector has substantially been restructured and privatised in the transition period so far, the remaining reforms targeting further private sector development, will relate to:

- the completion of socially-owned undertakings privatisation and more efficient implementation of bankruptcy procedures for unsuccessful undertakings;

The remaining socially-owned undertakings, as prepared for privatisation by the Agency, are expected to be sold in the coming period, whereas in cases where the Agency can not find buyers, the undertakings will undergo bankruptcy or liquidation. To that effect, new Law on

Bankruptcy that has been passed, provides a higher level of the creditor settlement, reduced bankruptcy procedure period and lower bankruptcy procedure expenditures. Special consideration will be given to privatisation of the remaining big socially-owned enterprises under the restructuring procedure. Government will under a special program continue to restructure and privatise parts, or entities of enterprises in defence (military) industry and in military-income institutions.

- acceleration of the restructuring process for public undertakings and continuation of their preparation for privatisation (either majority or minority);

Restructuring process will continue in the coming midterm period for public enterprises, increasing private sector share and improving investment conditions, as follows: financial consolidation of public enterprise “Serbian Railways” and separation of railway infrastructure from the transportation of goods and passengers into separate enterprises, financial consolidation of public enterprise “Roads of Serbia”, restructuring of public enterprise “Underground Coal Exploitation – Resavica” under preparations for privatization, restructuring of public enterprise of PTT Communications “Serbia” after resolving ownership and contractual relations with “Telekom Serbia” j.s.c., restructuring of public enterprise “JAT Airways” j.s.c. under preparations for privatization, and reduction of the remaining redundant staff in all public enterprises.

Corporatization process will be accelerated for enterprises with state capital as to change the legal form and to accelerate the reforms of public enterprises, including restructuring and privatization where market conditions are fulfilled.

For ownership, organizational and business transformation of local communal enterprises the strategy for the restructuring and privatisation of public communal enterprises, the Law on Communal Activities, and Amendments to the Law on Concessions will be adopted. Local self-governments will decide on privatisation of public communal enterprises paying attention to the protection of public interest, and using positive experiences from the countries in transition. At the same time, natural monopolies on local level will not be privatized (electrical network, water distribution network, etc.).

- liberalization of infrastructure activities;

Privatisation of public and local public enterprises includes liberalization of infrastructure activities where it is possible to introduce competition, such as: production and distribution of electrical power, fixed telephony (with prior rebalance of the tariff system and technological modernization of the enterprise “Telekom Serbia” j.s.c.), passenger and goods railway transportation, certain postal services, air transportation, import of naphtha and certain communal activities.

New enterprises will be allowed to start carrying out the activities of infrastructure nature, thus introducing competition and improving the performance of the activities and quality of products and services thereof.

Public enterprises carrying out infrastructure activities will not be majority privatised if they have characteristics of a natural monopoly, such as: railway infrastructure; electrical power transfer; international gas and naphtha pipelines.

- better protection of competition;

Application of the new Law on Protection of Competition, harmonized with the EU legislation, will ensure the development of free competition in production and trade, price reduction, their free setting up on the market and improved products and services quality. Provisions of this law allow introduction of competition in infrastructure activities of general interest and demonopolization of public and local public enterprises. Particularly important for the implementation of the competition policy is the enforcement of the Law on State Aid Control, of 1 January 2010, and the enforcement of the Law Public Procurement.

- incentives for economy export capacities;

Export increase is a national economic priority. Increased export will be guided by faster export growth of higher processing level products, compared to growth of exported lower processing level products, and by export growth to the EU and CEFTA region. Special consideration will be given to the key export markets and to the accomplishment of high export growth rates based on the available raw material basis for groups of export products (basic metals, iron and steel, wood and food industry), the dynamic sector of small and medium-sized enterprises and the available human capital. To that effect, conditions will be created for the strengthening of the existing business systems, providing higher export rate, better international image of the country, increased investments in export sector, improved export structure, infrastructure development, human capital development, political stability, geographic export diversification by conquering new markets, incentives for influx of foreign direct investments which are export oriented, establishment of export support system corresponding to the accession dynamics to WTO and the EU. The key structure measures for export incentives are privatisation of enterprises with social and state capital increasing productivity and strengthening the competitive position in foreign markets, efficient services for exporters, improved cluster number, strengthening of economic diplomacy, reduction of administrative export impediments, and improvement of product standardization.

- support for development of small and medium-sized enterprises

Support for faster development of small and medium-sized enterprises and entrepreneurship will continue in the three next years, implementing the adopted Strategy for competitive and innovative small and medium-sized enterprises and the Operational Plan for its implementation. The goal is to develop a competitive sector of small and medium-sized enterprises based on knowledge and innovativeness providing growth in production, export and employment and a more balanced Serbia's regional development.

Special consideration will be given to the promotion and support to entrepreneurship and the founding of new small and medium-sized enterprises, as well as to their growth, with appropriate financial and tax incentives, and to the strengthening of competitive advantages for small and medium-sized enterprises on export markets through knowledge development, technological innovations, cluster development, linking with big business systems, introduction of the European standards and quality business operations.

23. How has the sectoral economic structure changed since 2000 (in terms of value added to GDP and employment)? What sectors have been the most dynamic in terms of growth and/or job creation?

Employment elasticity indicator allows to view the relation between the economic growth – measured in GDP – and two variables contributing to the growth of changes in employment

and productivity. In the period 2001-2008 Serbia had total negative employment elasticity of 0,12, thus indicating that 1 percent GDP growth point resulted in the drop of the total employment by 0,12 percent.

The main cause of negative employment elasticity in Serbia is the economy transition where, although GDP was growing until 2008, employment was dropping, due to privatisation and restructuring of enterprises. In 2009, the increasing number of the employed persons who became jobless was sustained by the world economic crisis, since the employers, due to economic difficulties, opted to reduce the number of employees, as well as state administration and employees in public sector. However, in developed countries the link between the economic growth and employment growth has been weakening in the last years (i.e. the growth of GDP was not automatically transferred to new businesses).

In the period 2001-2008 Serbia had total negative employment elasticity in agricultural sector of 0.45, thus indicating that 1 percent point of GDP additional growth in agricultural sector results in the drop in the employment in agriculture by 0.45 percent. The highest negative employment elasticity is in industrial sector (-2.26), thus indicating that 1 percent point of GDP additional growth in industrial sector results in the employment drop in industry by 2.26 percent.

The main reason for the employment decrease in agriculture and industry is the over-employment in these sectors, or their not being competitive.³⁸

Employee structure in legal personalities (companies, enterprises, cooperatives, institutions and organizations)

| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
|--------------------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Total | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 |
| Agriculture, forestry and water management | 5.0 | 4.8 | 4.7 | 4.6 | 4.4 | 4.1 | 4.0 | 3.8 | 3.4 | 3.2 |
| Fisheries | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 |
| Ore and stone extraction | 2.2 | 2.1 | 2.0 | 2.0 | 2.0 | 2.0 | 1.9 | 1.6 | 1.6 | 1.6 |
| Processing industry | 35.9 | 35.3 | 33.8 | 32.6 | 30.6 | 29.7 | 28.6 | 27.4 | 25.9 | 24.3 |
| Production of el. energy, gas and water | 2.7 | 2.8 | 2.8 | 2.9 | 2.9 | 2.9 | 3.0 | 3.1 | 3.2 | 3.3 |
| Construction industry | 5.9 | 5.6 | 5.5 | 5.5 | 5.6 | 5.7 | 5.8 | 5.8 | 5.8 | 5.7 |
| Wholesale and retail trade | 12.0 | 11.8 | 12.1 | 12.5 | 13.2 | 13.2 | 13.4 | 13.7 | 14.0 | 13.8 |
| Hotels and restaurants | 2.1 | 2.2 | 2.1 | 1.9 | 1.8 | 1.7 | 1.7 | 1.7 | 1.7 | 1.6 |
| Transport, storage and communications | 7.3 | 7.2 | 7.4 | 7.4 | 7.5 | 7.5 | 7.5 | 7.6 | 7.6 | 7.6 |
| Financial mediation | 2.5 | 2.4 | 1.9 | 1.9 | 1.9 | 1.9 | 2.0 | 2.1 | 2.3 | 2.6 |
| Real estate and rental activities | 2.7 | 3.2 | 3.4 | 3.4 | 3.7 | 4.1 | 4.6 | 4.7 | 5.2 | 5.7 |

³⁸ Study "Serbia Development Report 2009", Republic Institute.

| | | | | | | | | | | |
|---------------------------------------------|-----|-----|-----|------|------|------|------|------|------|------|
| Public administration and social insurance | 3.4 | 3.6 | 3.9 | 4.2 | 4.5 | 4.6 | 4.7 | 4.8 | 4.9 | 5.1 |
| Education | 6.6 | 6.8 | 7.6 | 7.9 | 8.3 | 8.4 | 8.5 | 9.0 | 9.3 | 9.7 |
| Health care and social work | 8.9 | 9.3 | 9.7 | 10.1 | 10.4 | 10.7 | 10.7 | 11.0 | 11.2 | 11.6 |
| Other utility, social and personal services | 2.8 | 2.8 | 2.9 | 3.0 | 3.1 | 3.3 | 3.5 | 3.7 | 3.8 | 4.1 |

24. Please provide information on the number of companies grouped by size since 2000/2005. Please describe the main impediments to growth and job creation for local companies? (detailed information is required in chapter 20 – Enterprise and industrial policy)

REPUBLIC OF SERBIA

Number of enterprises

| year | total | micro: | small | medium | large |
|-------------------------------------------------------------|--------|-----------|-----------|-----------|--------------|
| | | 0 to 9 | 10 to 49 | 50 to 249 | 250 and more |
| | | employees | employees | employees | employees |
| | | | | | |
| 2000 | 62695 | 53322 | 5737 | 2605 | 1031 |
| 2001 | 65115 | 55455 | 6061 | 2616 | 983 |
| 2002 | 66878 | 56807 | 6583 | 2596 | 892 |
| 2003 | 73830 | 63298 | 7188 | 2540 | 804 |
| 2004 | 75477 | 64473 | 7742 | 2493 | 769 |
| 2005 | 75430 | 64254 | 8030 | 2452 | 694 |
| 2006 | 76234 | 64069 | 9027 | 2500 | 638 |
| 2007 | 84109 | 71065 | 9874 | 2572 | 598 |
| 2008 | 89198 | 75540 | 10415 | 2675 | 568 |
| 2009 | 89 115 | 76 243 | 9 873 | 2 470 | 529 |
| <i>Source: Statistical Office of the Republic of Serbia</i> | | | | | |

Available data indicate that during the past period there have been certain changes in the size of enterprises. Those changes are conditioned by the effects of several factors. Likewise, the following factors need to be considered: transitional processes which also include privatisation process, positive changes in business environment, especially as regards the simplified founding procedure for enterprises, government's supportive measures, in particular as regards the support for the founding of new enterprises, or for starting a business.

In the past period there has been a notable tendency of growth in the total number of enterprises within non-financial sector, except in 2009, when there was a slight drop in the total number of enterprises, resulting from the world economic crisis. In the structure of non-

financial sector, besides the registered entrepreneurs, dominant are micro enterprises, whose number has been constantly growing. On the other hand, number of big enterprises has been declining and in the preceding decade was reduced to almost half the number, primarily resulting from the privatisation process and large enterprises restructuring.

Besides the world economic crisis, as main reasons for the limited growth and job creation in local companies, other reasons can be the insufficient support of commercial banks, or lack of favourable sources of finance. This is followed by relatively undeveloped cooperation with big enterprises and inclusion in their supplier chains. This can be supplemented by the difficulties relating to not yet finished reform of the legal and administrative business framework, especially in the field of the issuance of construction permits and tax regulations and procedures. Faster development and growth was also jeopardised by the problem of disharmony between business operations and the quality standard requirements, and lack of information about the market and technologies, or low innovativeness level. Local companies have been developing more slowly also due to limited capacities of owners and managers, especially in the know-how and skills in business management. In certain cases the limiting factor was the lack of appropriately qualified and skilled employees, despite the high unemployment rate.

25. Please describe how the level (in % of GDP), structure (type per economic sector) and sources (public/private) of gross fixed capital formation has developed in the last five years. Please indicate the share related to infrastructure investment including changes in roads, rail and telephony lines. Please also make a particular reference to R&D expenditure. Please provide a synthetic assessment on the quality of major infrastructures (transport, telecommunication, energy), indicating areas where investment needs are important.

Data referring to investments reflect results of the research “Annual Report on Investments in fixed assets”, which has been partially amended and aligned with international statistic standards and methodologies, i.e. with the European System of Accounts 1995 (ESA95) and System of National Accounts 1993 (SNA93).

Investments in fixed assets of the Republic of Serbia

thou. RSD

| | 2006 | 2007 | 2008 | 2009 |
|-----------------------------------------------------|----------|---------------|---------------|---------------|
| Agriculture, hunting, forestry and water management | 16021164 | 15166335 | 24049717 | 14286443 |
| Fisheries | 199284 | 857387 | 476633 | 1075353 |
| Ore and stone extraction | 1119038 | 2067933 | 3038123 | 1487142 |
| Processing industry | 81885139 | 11743551 9 | 13825533 1 | 12013683 9 |
| Production of el. energy, gas and water | 32554301 | 39188091 | 55356647 | 48715146 |
| Construction industry | 32837116 | 46717678 | 54359052 | 72907463 |
| Wholesale and retail trade, vehicles repair | 59885045 | 98765231 | 81331872 | 69471398 |
| Hotels and restaurants | 7652011 | 3528530 | 4854665 | 3180759 |
| Transport, storage and communications | 48995579 | 69063715 | 74082118 | 58082198 |
| Financial mediation | 21069675 | 21203044 | 21999804 | 15048380 |

| | | | | |
|----------------------------------------------------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| Real estate and rental activities | 31332095 | 50665254 | 85462189 | 69742164 |
| Public administration and defence; compulsory social insurance | 23383561 | 38482233 | 41187335 | 32531496 |
| Education | 7547203 | 5493283 | 5510021 | 5400794 |
| Health care and social work | 9160785 | 12395240 | 17712584 | 11692881 |
| Other utility, social and personal services | 7031354 | 16112486 | 18199540 | 18445897 |
| | | | | |
| Activities - total | 38067335 0 | 53714196 1 | 62587562 9 | 54220435 4 |

During the observed period the level of investments in railways fixed assets, which are financed by the public budget, was low. Allocated funds were used mainly to cover the ongoing reproduction costs.

*Amount of allocated funds for infrastructure projects
from public budget in the period 2003-2009*

| Investment in railways | Real expenses (million €) | | | | | | |
|--------------------------------|---------------------------|-------|-------|-------|------|-------|-------|
| Type of works | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
| Modernization / rehabilitation | 41,27 | 21,41 | 20,54 | 16,17 | 8,41 | 10,81 | 30,20 |

Source: Serbian Railways Statistics -Finance and Accounting Department

In the last period in the field of railways there were some investment projects which were finished, or are underway, as financed by different private sources, such as credits, EIB, EBRD, EUROFIMA, by credits and donations from certain states, pre-accession funds (IPA) as well as by other EU support programs. Below is the listing of investment projects which have been finalised, or are underway:

- *Reconstruction of specially critical sections of Corridor X* – project is financed by EIB 1 credit worth EUR 70 million;
- *Reconstruction project for the railroad bridge between Bogojevo and Erdut*. Project financed by donations of the Government of the Kingdom of Belgium and the Kingdom of Norway (in total EUR 400,000), and by the budget of the Republic of Serbia, additional EUR 350,000;
- *Procurement and reconstruction of the means of transportation, mechanization for railroad maintenance and social program* – project financed by the credit EBRD 1 in the amount of EUR 57 million;

- *Reconstruction and modernization of railroad sections: Batajnica-Stara Pazova-Golubinci, Jovac (Gilje)-Čuprija and Čele Kula-Staničenje.* Project is underway and financed by the credit EIB 2 in the amount of EUR 80 million, continuation;
- *Procurement of 782 goods vehicles, subfloor lathe for finishing of the wheels with construction of the workshop for storage of the lathe and other equipment.* Project is in its final phase and financed by the credit EBRD 2, in the amount of EUR 60 million;
- *Reconstruction, rehabilitation and renovation of architectural and other premises of the common railway border station Dimitrovgrad - CARDS-EAR (2008-2009)* in the amount of EUR 3 million (donation by the EU was EUR 2,5 million).
- *Procurement of 12 new diesel-engine sets.* Project is underway and financed by the credit EUROFIMA in the amount of EUR 43 million Swiss Francs;
- *Procurement of about 25 new multi-section electromotor sets.* Project is underway and financed by the credit EBRD 3, in the amount of EUR 100 million;
- *Rehabilitation of backbone railways of Corridor X (sections of railroad Golubinci – Ruma, Sopot – Kovačevac, Vinarci – Đorđevo, Mala Krsna – Velika Plana, Bujanovac – Bukarevac, Vranjska Banja – Ristovac, value EUR 35 million) and procurement of multi-system electrical locomotives (value EUR 65 million).* Project is in its initial phase and financed by the credit EBRD 4, in the full amount of EUR 100 million;
- *Construction of a new bridge on the Danube in Novi Sad.* Project worth EUR 60 million is underway and financed partially by the credit IPA Fund (EUR 30 million) and by local sources.

A portion of investments in railway transportation was financed by the EU support funds, such as IPA Fund. Of all IPA funds allocated to the Republic of Serbia in the period 2007 – 2012, the following railway projects have been approved, or nominated to be financed:

Approved projects

- *System for analysis of railways condition.* Project approved within IPA 2008, value EUR 3 million.
- *Supervision over construction of the bridge on the Danube in Novi Sad,* at the location of the destroyed bridge “Zezeljev most”). Project approved within IPA 2008, value EUR 2.5 million.
- *Construction of a new bridge on the Danube in Novi Sad.* Project approved within IPA 2009, value EUR 30 million.

Nominated projects

- *Modernization of railways Pan-European Corridor X.* Project was nominated under IPA 2011, and is in the phase of programming. Value of IPA funds for the here above mentioned project is EUR 8,3 million and it includes two components:
 - Preparation of project documentation for the improvement and modernization of the railway Novi Sad-Subotica-border with Hungary (EUR 6,8 million), and
 - Construction of rail ring-road in Nis (EUR 1,5 million);
- *Modernization of the railways section Stara Pazova – Novi Sad.* Project is nominated under IPA 2012, and is in the phase of programming. Value of IPA funds for the here

above mentioned project is EUR 40 million and will be funded from component III – regional development.

- In the coming period investments in railroad transportation are expected to be intensified and funded both by local and private sources, as to meet the European standards in this field. Some of the most important future projects, whose implementation is in the initial phase are:
- *Modernization of section Stara Pazova-Noví Sad*, partially to be funded by EIB credit funds, in the amount of EUR 200 million;
- *Reconstruction and modernization of railway section Niš-Dimitrovgrad*, which will be funded by the credit of the Czech Export Bank, in the amount of EUR 120 million;
- Credit of the Government of the Russian Federation in the full amount of 800 million dollars is planned for funding of several projects, as follows:
 - *Construction and reconstruction of Belgrade railway junction*
 - *Repair and reconstruction of railway Resnik-Vrbnica;*
 - *Construction of railway Valjevo-Loznica*
- *Procurement of diesel-engine trains* by the credit of the Kingdom of Spain in the amount of EUR 37 million;
- *Modernization and electrification of railroad Pančevo-Vršac*, which will be funded by credit of the Government of the Federal Republic of Germany, in the amount of EUR 45 million;
- Projects which will be funded by the EBRD credit, of EUR 200 million, and by credit of the Government of the Republic of Poland, in the amount of EUR 70 million, are in the selection process.

For the realization of the here above mentioned projects, the needed project documentation should be prepared, whereas respective funds shall be obtained from the local, or other sources.

Public enterprise “Železnice Srbije” (“Serbian Railways”) exploits the network 3,809 km long. This network includes railways which are part of the Pan-European corridors, the railways of international importance connecting Serbia with the neighbouring countries and regional-local railways.

Performance of the railway infrastructure and quality of its means of transportation do not meet the requirements of modern transportation market.

Main problems in railway network relate to the lack of funds for the maintenance of infrastructure and means of transportation, thus significantly limiting the level of services as regards the speed, which is basically much lower than the projected speed. Consequently, railways’ share in transportation industry has been continuously dropping in the last years.

Infrastructure facilities in air transportation (terminal building and other logistic support facilities) are substantially aligned with the requirements of higher scope traffic and services quality, which will, along with the strengthened fleet, allow air transportation to have significant impact on opportunities for transportation connectivity in Serbia.

There are two international airports in Serbia qualified for passenger transportation (airport “Nikola Tesla” and airport “Niš”) and several smaller airports (Belgrade, Kraljevo, Vršac...)

which are not used for public transportation in air traffic, although with potentials to be used likewise, and there is also a number of sport airports.

Waterways condition varies from case to case. Fairway of the Danube is generally good, whereas investments are needed in some sectors. Fairway of the river Tisa is in good condition, whereas the fairway of the river Sava requires substantial investments in several sectors. Substantial investments are needed as regards the waterways in order to finalize the projects which refer to: extraction of unexploded lethal devices from the Danube, extraction of sunken fleet from the Second World War in the Prahov sector, renovation of switch point Đerdap 1 and Đerdap 2, and implementation of regulatory and dredger works in critical sectors along the Danube and the Sava. Substantial funds are needed to be invested as to allow technical and exploitation waterway parameters in the Republic of Serbia to meet the requirements laid down by the European Agreement on Main Inland Waterways of International Importance (AGN).

As regards the ports, adoption of the Law on Navigation and Ports on Inland Waters ("Official Gazette of the RS", no 73/10) has created legal preconditions, by denoting ports and quaysides as goods of common interest, as well as the forthcoming establishment of the Port Governance Agency, thus enabling to enter into substantial investments process in the port infrastructure (bank revetments, coast walls, port roads (roads, lanes, railway tracks with supporting railway devices), waterworks, sewage, energy and communication systems, lighting, fences and other facilities and devices which are intended for safe access and vessels fastening), whose current condition is not in line with actual requirements for the port services users, whereas investments in port suprastructure (facilities constructed in port area (main offices, warehouses, silos, reservoirs), as well as special equipment (container lifts, cranes, docks for passenger boarding and disembarking and similar) shall be provided by private sector.

Given that infrastructure, i.e. waterways and ports development, will facilitate further development of the fleet, as well as of the port hinterlands, it is necessary to enter the process of the securing of investments for this development in the coming period.

Telecommunications share in GDP for the period 2005-2009;

| Year | Share in GDP (%) |
|-------------|-------------------------|
| 2009 | 4,76 |
| 2008 | 4,87 |
| 2007 | 4,7 |
| 2006 | 5,6 |
| 2005 | 7,2 |

Source: Republic Agency for Electronic Communications (RATEL)

Investments in fixed and mobile telephony for the period 2005-2009, billion RSD

| year | in fixed telephony | in mobile telephony |
|-------------|---------------------------|----------------------------|
| 2009 | 9,3 | 13,9 |
| 2008 | 5,3 | 21,3 |
| 2007 | 13,3 | 50,1 |

| | | |
|------|------|-----|
| 2006 | 17,4 | 8,3 |
|------|------|-----|

Source: Republic Agency for Electronic Communications (RATEL)

Service quality in fixed network

| Parameter | Measure | Unit | Jan - June 2008 | July - Dec 2008 | Jan - June 2009 | Jan - Dec 2009 |
|---------------------------------------|------------------------------------------------------------------|---------------------------------------------------------------------------|--------------------------------------------------------------------------|----------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------|
| 1.1. Time of service implementation | for 95% new connections in one year (average time by connection) | (day) | 186 | 28 | 14 | 21 |
| | % of services implemented by the contracted deadline | % | 100 | 0,7466 | 87,93 | 82,63 |
| | time of application receipt | from ..to...weekdays from....to....Saturdays from....to.... Sundays | Weekdays from 08:00 to 19:00 Saturdays from 08:00 to 14:00 Sundays | Weekdays from 08:00 to 19:00 Saturdays from 08:00 to 15:00 Sundays from 09:00 to 21:00 | Weekdays from 08:00 to 19:00 Saturdays from 08:00 to 15:00 Sundays from 09:00 to 21:00 | Weekdays from 08:00 to 19:00 Saturdays from 08:00 to 15:00 Sundays from 09:00 to 21:00 |
| 1.2. Number of faults per access line | 100 lines per year | (number) | 17 | 41,2 | 12,21 | 34,87 |
| 1.3. Average fault repair time | 80% fastest repaired access line faults in one year | (hours) | 50 | - | 48 | 48 |
| | 95% fastest repaired access line faults in one year | (hours) | 73 | - | 8 | 192 |
| | 80% fastest repaired other faults | (hours) | 26 | - | 24 | 24 |
| | 95% fastest repaired other faults | (hours) | 40 | - | 48 | 48 |
| | %repaired faults within 24 hours from malfunction report | % | 28,57 | 61 | 76 | 65 |
| | malfunction report time | from ..to...weekdays from....to....Saturdays from....to.... Sundays | Weekdays from 07:00 to | Weekdays from 07:00 to | Weekdays from 00:00 to | Weekdays from 00:00 to |

| | | | | | | |
|--|--|--|-----------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------|
| | | | 21:00 Saturdays from 08:00 to 15:30 Sundays from 08:00 to 15:30 | 21:00 Saturdays from 08:00 to 15:30 Sundays from 08:00 to 15:30 | 24:00 Saturdays from 00:00 to 24:00 Sundays from 00:00 to 24:00 | 24:00 Saturdays from 00:00 to 24:00 Sundays from 00:00 to 24:00 |
|--|--|--|-----------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------|

Service quality in fixed network (continued)

| Parameter | Measure | Unit | Jan - June 2008 | July - Dec 2008 | Jan - June 2009 | Jan - Dec 2009 |
|------------------------------------------|---------------------------------------------------------------------|-----------|--------------------|--------------------|--------------------|-------------------|
| 1.4. Unsuccessful calls percentage | all calls | % | <1% | 0,0057 | 0,0037 | 0,78 |
| | national calls in fixed network within LC | % | <0.2% | 0 | 0 | 0 |
| | national calls in fixed network outside LC | % | <0.2% | 0,0071 | 0,0038 | 0,71 |
| | national calls from fixed network to mobile operators | % | <1% | 0,0034 | 0,0042 | 0,62 |
| | national calls from fixed network to other fix operators | % | - | - | - | - |
| | international calls | % | <1% | 0,0016 | 0,0063 | 0,67 |
| Successful calls percentage | all calls | % | 56 | 55 | 57 | 58,84 |
| | national calls in fixed network within LC | % | 56 | 50 | 55 | 54,55 |
| | national calls in fixed network outside LC | % | 55 | 54 | 60 | 59,14 |
| | national calls from fixed network to mobile operators | % | 60 | 61 | 59 | 59,03 |
| | national calls from fixed network to other fix operators | % | - | - | - | - |
| | international calls | % | 55 | 55 | 42 | 56,36 |
| 1.6. Time for call establishment | average time for national calls | (seconds) | | 22.59s | 19.80s | 16,36 |
| | average time for national calls in fixed network | (seconds) | <1s | 19.34s | 13.70s | 22,75 |
| | time for establishment of 95% national calls in fixed network | (seconds) | <1.5s. | <1.5s. | - | |

| | | | | | | |
|--|-----------------------------------------------------------------------|-----------|----|---------|--------|------|
| | average time for national calls from fixed network to mobile networks | (seconds) | 5s | 20.28s. | 20.12s | 15,5 |
|--|-----------------------------------------------------------------------|-----------|----|---------|--------|------|

Service quality in fixed network (continued)

| Parameter | Measure | Unit | Jan - June 2008 | July - Dec 2008 | Jan - June 2009 | Jan - Dec 2009 |
|---------------------------------------------------------------------------------|----------------------------------------------------------------------------|-----------|-----------------|-----------------|-----------------|----------------|
| 1.6. Time of call establishment (continued) | time for establishment of 95% national calls from fixed to mobile networks | (seconds) | 5.5s. | - | - | |
| | average time for international calls | (seconds) | 1.2s | 21.9s. | 17.37s. | 19,02 |
| | time for establishment of 95% international calls | (seconds) | 1.5s. | - | - | |
| 1.7. Operator services response time (9813,977) | average response time in one year | (seconds) | 115s, 35s | 122s | 170s, 89s | 125 |
| | % answered calls in the period of 20 seconds | % | 18.25%, 64.89% | - | - | 11 |
| 1.8. Response time for access to inventory of public voice service users (988) | average response time in one year | (seconds) | 33.95s. | 0.56s | 1,73 | 1,73 |
| | % answered calls in the period of 20 seconds | % | 91 | - | 81 | 81 |
| 1.9. Percentage of public telephone booths in full working order | % in one year | % | 90 | 96 | 99 | 90,42 |
| 1.10. Percentage of complaints on bill irregularity compared to number of users | % in one year | % | 0,00085 | 0,0008 | 0,0012 | 0,88 |
| 1.11. Number of unresolved requests for new telephone lines | | (број) | | | 314628 | 249486 |

- Time of service establishment is the time period from the moment of request receipt until the moment of service activation
- Number of faults per access line is the total number of faults in a year divided by the number of active lines and multiplied by 100
- Average fault repair time is the total time of duration of all faults (period from reporting until repair) divided by the number of faults
- Unsuccessful calls percentage is the percentage of calls to existing user not successfully forwarded due to system malfunction, or incorrectly dimensioned beams. Case B subscriber busy and B subscriber did not answer are not an unsuccessful calls.
- ACP is percentage of calls ended by answering of subscriber B
- Time of call establishment is the time period from the moment of dialling the last digit of subscriber's number until the call control
- Response time is the time from call control until operator's response
- Percentage of public telephone booths in full working order is the mean value of the percent of booths in full working order
- Percentage of complaints on bill irregularity is the mean value of complaint percent on annual level

Service quality in mobile network

| Name | 2009 | | | 2008 | | |
|-----------------------------------------------------------------------------------------------------|---------|---------|-------|---------|---------|-------|
| | Telekom | Telenor | VIP | Telekom | Telenor | VIP |
| Percentage of territorial signal coverage in GSM mobile network | 83,17 | 85,2 | 74,56 | 82,72 | 78,25 | 56,63 |
| Percentage of territorial signal coverage in UMTS mobile network | 46,66 | 17,77 | 2,42 | 29,50 | 8,79 | 2,42 |
| Percentage of population signal coverage in GSM mobile network | 88,70 | 93,66 | 79,16 | 88,25 | 93,23 | 73,9 |
| Percentage of population signal coverage in UMTS mobile network | 63,15 | 53,14 | 25,83 | 55,85 | 34,88 | 25,83 |
| Percentage of successfully established voice calls in GSM network (CSSR) | 98,88 | 99,79 | 98,78 | 98,5 | 99,37 | 98,02 |
| Percentage of successfully established voice calls in UMTS network | 97,89 | 99,64 | 99,07 | 98,13 | 99,86 | 98,21 |
| Percentage of successfully established video calls in UMTS network | 93,36 | 99,65 | 100 | 95,8 | 99,68 | 100 |
| Percentage of successfully established data transfer sessions in UMTS network | 82,5 | 99,57 | 98,98 | 96,2 | 100 | 98,85 |
| Percentage of irregularly ended voice calls in GSM network (hereinafter as: <i>Call Drop Rate</i>) | 0,74 | 0,6 | 0,71 | 0,69 | 0,52 | 1,33 |
| Percentage of call drop rate in voice calls in UMTS network | 0,83 | 0,25 | 0,55 | 0,43 | 0,23 | |
| Percentage of call drop rate in video calls in UMTS | 0,83 | 0,22 | 0 | 0,25 | 0,31 | |

| | | | | | | |
|---------------------------------------------------------------------------|--------|--------|-----------|-------|-------|------|
| network | | | | | | |
| Percentage of drop rate in data transfer sessions in UMTS network | 5,31 | 2,54 | 1,26 | 3,62 | 0,6 | |
| UL BLER for voice service | 0,64 | 0,45 | 0,9 | 0,61 | 0,49 | 0,89 |
| Average data transfer rate towards user for <i>r99 packet interactive</i> | 145,47 | 89,2 | 8,71 | 103 | 158 | |
| Average data transfer rate towards user for <i>HS interactive</i> | 610,75 | 1736,6 | 17,2 6 | 495 | 1478 | |
| Percentage of successful handovers in GSM network | 97,95 | 98,51 | | 96,94 | 98,62 | |
| Percentage of successful Inter-RAT handovers UTRAN->GSM | 94,95 | 95,03 | 96,5 5 | 94,81 | 96,9 | |

Infrastructure quality of broadband access and networks for digital broadcasting of radio and television programs

With significant transportation capacities of electronic communication networks, the access networks are still underdeveloped compared to the European Union countries, one year after adoption of the Strategy for the Development of Broadband Access ("Official Gazette" No 84/09), which laid down 4 Mb/s as the minimum flow of broadband access, proposing several regulatory measures for the improvement of the development of alternative networks, and for the opening of the last kilometre for alternative operators access, thus providing a wider selection of services to end users and assisting the development of economy on regional level through development of small and medium-sized enterprises, on the territory of the Republic of Serbia.

Global competitiveness index for the Republic of Serbia is 3,77, whereas global availability index of electronic communications networks is 3,5, positioning the Republic of Serbia among the countries with undeveloped electronic communications infrastructure and significantly lower number of internet users as opposed to the European Union countries.

Although the number of broadband access users has been growing considerably, conditioning the drop in *dial-up* connection users, most users still use *ADSL* technology for internet access, which basically applies copper cables. However, noteworthy is the growing number of users who utilize infrastructure of cable television operators for internet access. There are 42.6 % of households in the Republic of Serbia with cable television connections. With basic program scheme, or digital program packages, cable network operators offer up to 40% cheaper internet access compared to the same flow connection, offered by *ADSL* technology. The outcome is that there are 24,6 % households in the Republic of Serbia using this infrastructure for internet access.

As to assist large capacity networks development, based on technologies *FTTx*, the Government of the Republic of Serbia adopted the Strategy for the Development of Electronic Communications from 2010 until 2020, (Official Gazette, no. 86/10), foreseeing introduction of the latest technologies in broadband access to high speed internet. Besides a number of regulatory measures, the Strategy proposes accomplishment of a pilot project on the level of local self-governments, aimed at the improvement of public institution networks, user infrastructure and development of public administration service. Substantial investments in this field should provide for modern infrastructure development of electronic communications, as long-term solution for access to services which would then possibly be offered to end users at more affordable prices, assisting further economy and GDP growth.

Strategy for the Transition from Analogue to Digital Broadcasting of Radio and Television Programs in the Republic of Serbia ("Official Gazette of the RS", no. 52/09) specifies the framework for transition to digital program broadcast, founded on modern accomplishments in digital radio-diffusion, and in fields influencing it, or resulting thereof, targeting the most efficient and the highest quality delivery of television, radio, multimedia and other significant contents, to end users. Strategy lays down the standards for data compression - *MPEG-4* and the standard for digital TV signal broadcast - *DVB-T2*, which will be utilized in Serbia. In our country there are seven national programs, and 129 television stations in total, which must in digital technology be put in multiplexes, thus providing their seamless broadcast. Investments in the process of television digitalization in the Republic of Serbia include major funds.

Given that distribution network of television transmitter was totally destroyed during the bombing of Serbia in 1999, an indispensable precondition to implementation of transition from analogue to digital broadcast of television signals, is to build up new television transmitters distribution network.

Serbia has undertook to align its legislation with the EU *acquis* as well as to implement it in practice. Aimed at assisting Serbia to successfully implement the digitalization process, the EU offered support through pre-accession aid funds for 2010 (IPA funds). This fund will be used for consulting services and preparation of legal framework, as well as for implementation of media promotion of the transition to digital television program broadcast (€ 2.5 million). The rest of the funds will provide for procurement of equipment and its placement to corresponding locations (€ 8 million). Primary distribution network, forwarding the signal to the transmitter, will be *IP* oriented, with one national and several regional *headends*. IPA project includes purchase of equipment for 3 *headends*, 30 transmitters, equipment for signal testing and measurement, 38 microwave links and antenna systems. Consequently, that will enable the formation of the first multiplex. The first multiplex will give space for programs with national coverage and programs with regional coverage. Next phase will induce provision of additional equipment for the formation of the second multiplex, which will be receiving all local programs. In addition, extra investments are needed as to accomplish the reconstruction and recovery of the main transmitter and repetitor locations, whereon broadcast equipment for digital broadcast should be placed.

SHARE CONCERNING INVESTMENTS AND INFRASTRUCTURE, INCLUDING CHANGES IN ROADS, RAILWAYS AND TELEPHONIC LINES

Answer to this question is contained in:

- Annual reports on the implementation of the Program of Works for the Maintenance, Protection, Construction and Reconstruction of Main and Regional Roads on the Territory of the Republic of Serbia for 2005, 2006, 2007, 2008 and 2009.
- Rebalanced Business Program of the Public Enterprise "Roads of Serbia" for 2010 (Official Gazette No 73/10)
- Rebalanced Program of Works for the Maintenance, Protection, Construction and Reconstruction of Main and Regional Roads on the Territory of the Republic of Serbia for 2010 (Government's consent announced in OG of the RS No 100/10),

as summarized in the table below:

INVESTMENTS IN FIXED ASSETS OF PUBLIC ENTERPRISE "ROADS OF SERBIA" FOR THE PERIOD 2005 - 2009

| Value of realized investments in fixed assets in 2005 (in thou. RSD) | | | | |
|----------------------------------------------------------------------|----------------------------------------------------|-----------------------------------|-----------------------------------|-------------------------|
| Total | Construction works | Domestic equipment and assemblage | Imported equipment and assemblage | Land |
| 11,679,972 | 10,575,232 | | 209,409 | 895,331 |
| Payments made for investments in fixed assets in 2005 | | | | |
| Total | From public enterprise "Roads of Serbia" own funds | From joint funds | Used domestic and foreign credits | From state bodies funds |
| 10,805,839 | 4,493,315 | | 4,809,893 | 1,502,631 |

| Value of realized investments in fixed assets in 2006 (in thou. RSD) | | | | |
|----------------------------------------------------------------------|----------------------------------------------------|-----------------------------------|-----------------------------------|----------------------------|
| Total | Construction works | Domestic equipment and assemblage | Imported equipment and assemblage | Land |
| 12,350,007 | 11,836,420 | | 152,422 | 361,165 |
| Payments made for investments in fixed assets in 2006 | | | | |
| Total | From public enterprise "Roads of Serbia" own funds | From joint funds | domestic and foreign credits | From state authority funds |
| 9,824,443 | 3,928,000 | | 4,184,588 | 1,711,855 |

| Value of realized investments in fixed assets in 2007 (in thou. RSD) | | | | |
|----------------------------------------------------------------------|----------------------------------------------------|-----------------------------------|-----------------------------------|----------------------------|
| Total | Construction works | Domestic equipment and assemblage | Imported equipment and assemblage | Land |
| 10,199,117 | 9,270,453 | | 388,221 | 540,443 |
| Payments made for investments in fixed assets in 2007 | | | | |
| Total | From public enterprise "Roads of Serbia" own funds | From joint funds | domestic and foreign credits | From state authority funds |
| 11,445,412 | 3,611,324 | | 3,551,325 | 4,282,763 |

| Value of realized investments in fixed assets in 2008 (in thou. RSD) | | | | |
|----------------------------------------------------------------------|--------------------|-----------------------------------|-----------------------------------|---------|
| Total | Construction works | Domestic equipment and assemblage | Imported equipment and assemblage | Land |
| 11,268,732 | 10,193,002 | 3,130 | 204,962 | 867,638 |

| Payments made for investments in fixed assets in 2008 | | | | |
|-------------------------------------------------------|----------------------------------------------------|------------------|------------------------------|----------------------------|
| Total | From public enterprise "Roads of Serbia" own funds | From joint funds | domestic and foreign credits | From state authority funds |
| 13,990,240 | 3,349,990 | | 4,634,851 | 6,005,399 |

| Value of realized investments in fixed assets in 2009 (in thou. RSD) | | | | |
|----------------------------------------------------------------------|----------------------------------------------------|-----------------------------------|-----------------------------------|----------------------------|
| Total | Construction works | Domestic equipment and assemblage | Imported equipment and assemblage | Land |
| 8,895,837 | 7,449,715 | 3,977 | 92,657 | 1,349,488 |
| Payments made for investments in fixed assets in 2009 | | | | |
| Total | From public enterprise "Roads of Serbia" own funds | From joint funds | domestic and foreign credits | From state authority funds |
| 10,650,458 | 4,523,502 | | 2,899,430 | 3,227,631 |

SOURCES OF FINANCE

The legal grounds are provided under the Law on Public Roads (*OG of the RS No 101/05 and 123/07*), Chapter III Public Roads Funding, Articles 16 and 17.

Article 16 specifies 6 funding sources for construction and reconstruction, maintenance and protection of public roads, as follows:

- 1) fee for using public roads
- 2) fee for maintenance of state roads from excise on naphtha derivatives and fluid naphtha gas in the amount:
 - in the period 1 January 2008 – 31 December 2008 15,0%
 - **in the period 1 January 2009 - 20,0%**
- 3) financial credits
- 4) investments by domestic and foreign persons
- 5) budget of the Republic of Serbia
- 6) other sources complying with the law.

Article 17 further elaborates the fees for using public roads – there are 13 types of the fees, as follows:

- 1) annual fee for motor vehicles, tractors and accessory vehicles
- 2) annual fee for motor driven vehicles not included under item 1, of this Article
- 3) fee for extraordinary transportation
- 4) fee for placement of billboards, devices for graphic or sound information or advertising on public roads, or on other land sites used by the public road manager, complying with legal regulations
- 5) special fee for using public roads, or their parts, or road facilities (road toll)
- 6) fee for over-use of public roads, their parts, or road facilities
- 7) rental fee for parts of public road land zone
- 8) rental fee for other land used by the public road manager
- 9) fee for connections of access roads to public roads

- 10) fee for placement of pipelines, sewage, electrical, telephonic and telegraphic lines and similar, on public roads
- 11) fee for construction of commercial facilities with access available from public roads
- 12) annual fee for using commercial facilities with access available from public roads, and
- 13) fee for using public roads for vehicles registered abroad.

Income of the public enterprise “Roads of Serbia” is based on the fees charged for using public roads, Article 17, items 3 to 13.

INVESTMENTS IN ROADS IN THE PERIOD 2000 – 2009

Despite the world economic crisis, 2009 was the year of big road investments, which can be seen observing the period since 2000.

INVESTMENTS IN ROADS IN PREVIOUS DECADE

INVESTMENTS

| Year | Investments (in millions of RSD) | EUR exchange rate | Investments ((in millions of EUR) | Index (basis: 2000) | | Index (basis: previous year) | |
|-------------|----------------------------------|-------------------|-----------------------------------|---------------------|-------------------------------|------------------------------|-------------------------------|
| | | | | expressed in RSD | expressed in foreign currency | expressed in RSD | expressed in foreign currency |
| 2000 | 2.660,6 | 51,5800 | 51,6 | 100 | 100 | 263 | 139 |
| 2001 | 6.690,2 | 60,0000 | 111,5 | 251 | 216 | 251 | 216 |
| 2002 | 14.486,7 | 60,6413 | 238,9 | 544 | 463 | 217 | 214 |
| 2003 | 18.319,9 | 64,2679 | 285,1 | 689 | 553 | 126 | 119 |
| 2004 | 26.233,8 | 72,1759 | 363,5 | 986 | 705 | 143 | 128 |
| 2005 | 39.961,9 | 82,7750 | 482,8 | 1.502 | 936 | 152 | 133 |
| 2006 | 49.443,7 | 86,0000 | 574,9 | 1.858 | 1.115 | 124 | 119 |
| 2007 | 53.844,8 | 79,0254 | 681,4 | 2.024 | 1.321 | 109 | 119 |
| 2008 | 60.413,9 | 78,9784 | 764,9 | 2.271 | 1.483 | 112 | 112 |
| 2009 | 57.052,6 | 93,4415 | 610,6 | 2.144 | 1.184 | 94 | 80 |

Note:

Exchange rate EUR:

- In the period 2002 – 2009: middle exchange rate, EUR, as on 30/06 for the year
- (information source: NBS, Exchange Rate Lists)
- For 2000 and 2001 derived exchange rate for EUR (assumption: 1 EUR = 2 DM)
 - in 2001, DM 1 = RSD 30
 - in 2000, DM 1 = RSD 25.79 (average annual commercial exchange rate, calculated based on monthly averages in 2000)

Investments in 2009, amounted RSD 57,1 billion, or EUR 610.6 million.

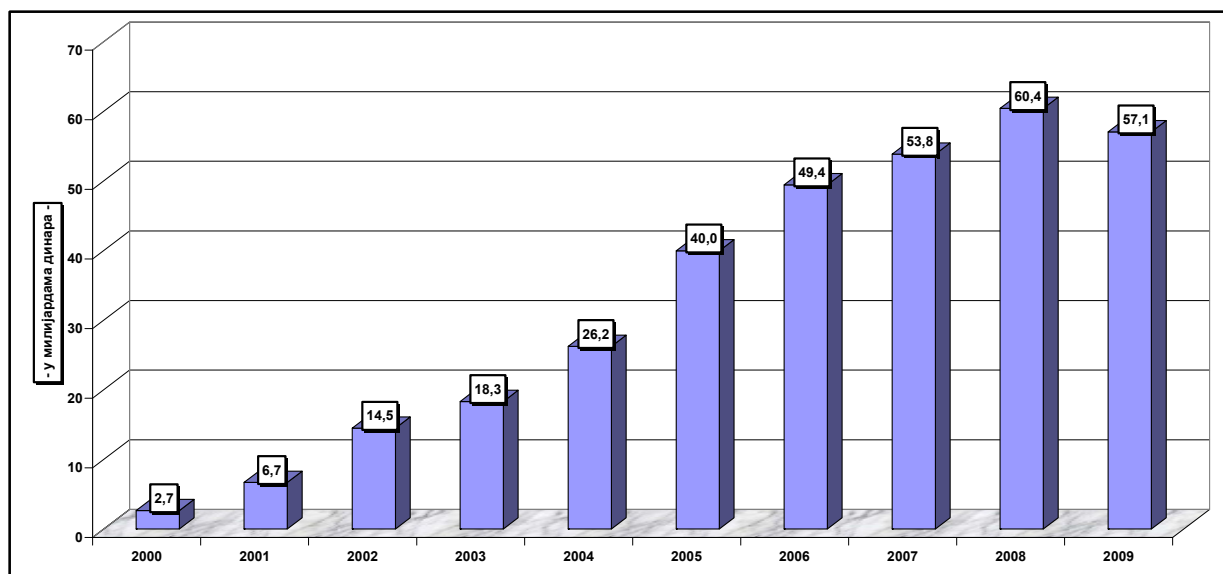
Compared to previous, 2008, (RSD 60,4 billion, or EUR 764,9 million), investments were lower by 6%, expressed in RSD, or by 20%, expressed in EUR.

Compared to 2000, (RSD 2.7 billion, or EUR 51.6 million), investments were 21,4 times higher, or 11,8 times expressed in EUR.

For clearer illustration, the data are also graphically presented.

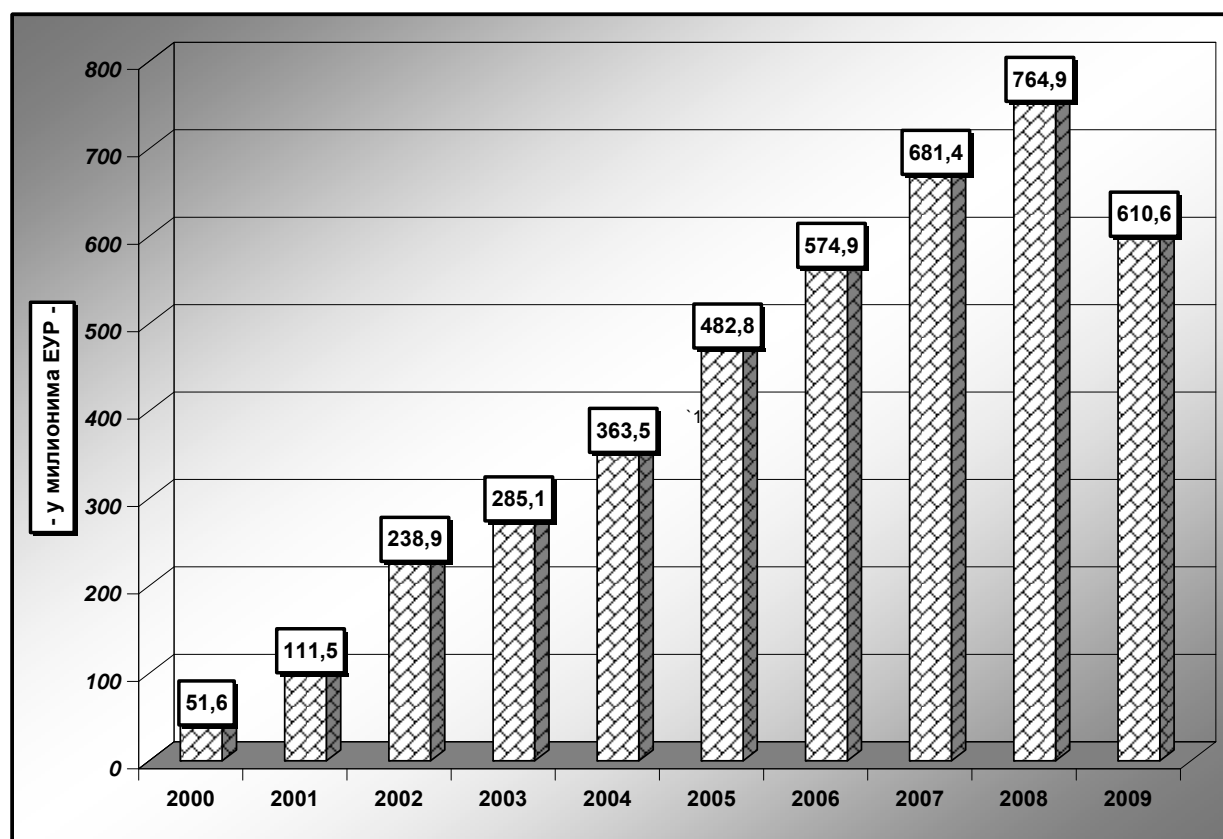
GRAPHICAL PRESENTATION FOR THE PERIOD 2000 – -2009

AMOUNT OF INVESTMENT (expressed in RSD)



In billions of RSD

AMOUNT OF INVESTMENT (expressed in foreign currency)



In millions of EUR

In the previous 5 years “Roads of Serbia” invested finance in transportation infrastructure – roads, which were funded as follows:

- partially by the state budget, or remunerations for the main roads maintenance from the excise on naphtha and fluid naphtha gas in the amount of (%), as determined by the Law on Public Roads (OG of the RS No 101/05 и 123/07)
- by commercial banks credits
- by international financial institutions: EIB (European Investment Bank), EBRD (European Bank for Reconstruction and Development), World Bank (IDA – International Development Association and IBRD – International Bank for Reconstruction and Development)
- as well as by EAR (European Agency for reconstruction) funds and donations, donations by governments: by The Kingdom of Sweden / Twinning Program with Sweden Road Administration, Czech Republic and the Kingdom of Holland (Program G2G).

We underline that funding of roads was also implemented through the Ministry of National Investment Plan, Corridor 10, as well as partially by budgets of the cities.

In the previous five-year period the key investment projects implemented through public enterprise “Roads of Serbia”, were funded by international credits.

Below is presentation of international credits which were agreed in the preceding decade.

CREDITS FROM EIB, EBRD AND WORLD BANK (IDA AND IBRD)

| Creditor | Credit | Time of agreement conclusion | Project | Agreed credit amount | Currency |
|-------------------------------------------------------------------|--------------------|------------------------------|---------------------------------------------|-----------------------|------------|
| EBRD (European Bank for Reconstruction and Development) | EBRD - 22705 | 31/07/2002 | Upgrading of Corridor X | 76,000,000,00 | EUR |
| | EBRD - 32190 | 20/05/2005 | Highway Belgrade-Novi Sad and Beška Bridge | 72,000,000,00 | EUR |
| | EBRD - 36651 | 15/11/2007 | Highway trespassing Belgrade ring-road | 80,000,000,00 | EUR |
| | Total EBRD: | | | 228.000.000,00 | EUR |
| EIB (European Investment Bank) | EIB- 21631 | 16/07/2002 | Existing roads rehabilitation | 95,000,000,00 | EUR |
| | EIB-21386 | 13/12/2001 | Urgent transportation recovery | 37,000,000,00 | EUR |
| | EIB - 22550 | 17/05/2004 | European Roads Project B | 120,000,000,00 | EUR |
| | EIB - 24037 | 16/7/2007 | Roads and bridges rehabilitation project B2 | 33,000,000,00 | EUR |

| | | | | | |
|------------|-------------------------------------------------------------------------------|------------|----------------------------------------------------------------|----------------|-----|
| | E1B - 24036 | 16/07/2007 | Gazela Bridge Recovery Project | 33,000,000,00 | EUR |
| | Total EIB: | | | 318,000,000,00 | EUR |
| WORLD BANK | IBRD YF-7463 (International Bank for Reconstruction and Development) | 27/07/2007 | Additional funds for transport reconstruction project | 36,800,000,00 | EUR |
| | IDA-3909 (International Development Association) | 09/06/2004 | Transport reconstruction project in Serbia | 55,000,000,00 | USD |
| | Total World Bank: | | | 55.000.000,00 | USD |
| | | | | 36.800.000,00 | EUR |
| TOTAL EUR | | | | 582.800.000,00 | EUR |
| TOTAL USD | | | | 55.000.000,00 | USD |

INTERNATIONAL CREDITS AGREED IN THE PERIOD 2001-2009

INTERNATIONAL DEVELOPMENT ASSOCIATION (IDA)

Credit of USD 55 million was endorsed as of 09/06/2004, for rehabilitation project intended for transportation sector in Serbia, including three components:

- rehabilitation of 7 road directions, 240,24 km long
- pilot project for road maintenance in the Mačva and Kolubara regions, 1.200 km long
- institutional fostering of public enterprise "Roads of Serbia".

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (IBRD)

Credit of USD 50 million was endorsed as of 27/07/07 for improvement of transportation infrastructure in Serbia, and improvement of the regular and winter roads maintenance. It included the following sections:

- pilot project for regular and winter road maintenance in the Mačva (660 km) and Kolubara (517 km) regions
- rehabilitation of 7 road directions
- provision of technical assistance for road maintenance supervision and road rehabilitation, including monitoring of environmental effects
- increase of road safety (elimination of high-risk points in road network).

EUROPEAN INVESTMENT BANK (EIB)

Credit of EUR 120 million (Belgrade – Novi Sad)

Credit Agreement (EIB 3) was endorsed as of 18/07/2004 for construction of the second highway lane Belgrade – Novi Sad (E-75) and recovery of the existing bridge "Beška".

Credit of EUR 33 million ("Gazela" Bridge)

Credit Agreement was endorsed as of 16/07/2007 for recovery of the "Gazela" Bridge.

Credit of EUR 33 million (bridges on main and regional roads)

- Credit Agreement was endorsed as of 16/07/2007 for rehabilitation and recovery of 100 bridges on main and regional roads (**mainly in direction E-761/M-5/ Zaječar – Paraćin – Pojate – Kruševac – Kraljevo – Čačak - Užice**)

Credit for Belgrade ring-road, Sector A

Credit Agreement in the amount of EUR 60 million was endorsed as of 19/10/2007 for construction of Belgrade ring-road, Sector A (Sector 0) Batajnica – Dobanovci.

Credit for Belgrade ring-road, Sector B

Purpose: construction of Belgrade ring-road, Sector B.

EUROPEAN BANK FOR RECONSTRUCTION AND DEVELOPMENT (EBRD)

Credit of EUR 72 million

Credit Agreement (EBRD 2) was endorsed as of 20/05/2005 for construction of the new bridge Beška and rehabilitation of the existing highway lane Belgrade – Novi Sad.

Credit for rehabilitation of highway E-70, section

Airport – “Bubanj Potpok” and circular road P-251

Credit Agreement was endorsed as of 15/11/2007, in the amount of EUR 25 million. Purpose: highway E-70, rehabilitation of roadway on section Airport Nikola Tesla - Bubanj Potok and circular road P-251 (as Belgrade ring-road).

Some key investments during the observed period were as follows:

Highway E-75 (Belgrade – Novi Sad):

- Improvement of the existing road Belgrade – Novi Sad and construction of a new highway section 108 km – 117 km, construction of left lane, 117 km – 136 km, construction of new section and delevelled crossroad 120 km – 178 km
- Construction of bridge on the Danube, near Beška, at 137,365 km - 139,623 km and construction of north and south bridge accesses
- Reconstruction of existing bridge on the Danube, near Beška
- Rehabilitation of existing roadway and existing bridges 108 km – 178 km,
- as well as closed system for toll pay.

Highway E-75 (Novi Sad-Subotica):

- In 2009 full highway profile was finished in sections: E-75 Novi Sad - Subotica 28 km - 38 km and 98 km – 108 km

Highway Bujanovac – Preševo:

- In 2009 highway section Bujanovac – Preševo was finished.

Belgrade ring-road:

- Implementation of EIB credit 24134, of EUR 60 million and EBRD credit 36651, of EUR 80 million, started for the construction of full highway profile of Belgrade ring-road, sections Batajnica – Dobanovci, and construction of new arm at the loop Batajnica 184 km, rehabilitation of the highway trespassing Belgrade E-70/E-75, 564,582 km - 594,300 km, from Airport Nikola Tesla to Bujanj Potok, as well as rehabilitation of circular road P-251.
- EIB credit 25748, of EUR 40 million, purpose: Belgrade ring-road, section Orlovača – Avala, L=5, 4 km, full profile

Gazela Bridge:

- EIB credit 24036 is under implementation, EUR 33 million, purpose: reconstruction of the Bridge on the Sava (Gazela), 579+223 km - 580+954 km

Main road M-25:

- European Agency for reconstruction has financed the rehabilitation of the roadway in sections M-25 Kladovo – Negotin – Zaječar – Svrnjig.
- International Development Association (IDA), credit value USD 55 million, Project for Transport Rehabilitation
- Update of the existing road databases was funded as well as procurement of new traffic counter devices and rehabilitation of the following road directions 240 km long: M-4 Loznica - Valjevo – Čelije, M-21 Šabac – Koceljeva – Valjevo, M-19 Šabac-Zminjak, Prnjavor - Loznica, M-23.1 Ravni Gaj - Kraljevo and M-23 Kragujevac – Ravni Gaj, as well as implementation of the pilot project with 2 contracts of regular road maintenance in the areas of Mačva and Kolubara, 1,200 km long. Realization of this project resulted in introduction and implementation of RWIS application on those territories – road weather information system for meteorological monitoring and forecast on micro level in a road area, whose goal is to increase efficiency and reduce winter maintenance costs. Special vehicle was procured for thermal mapping and thermal mapping has been completed for first order state roads.
- World Bank Project has been rounded by special Arrangement with Swedish Road Administration, financed by the Swedish International Development Agency. The Arrangement included implementation of regular maintenance activities funded by the World Bank credit in the areas of Mačva and Kolubara, traffic safety improvement and environment protection in the road corridor, as well as improvement in planning and road network management.
- International Bank for Reconstruction and development (IBRD), agreed amount USD 50 million. Additional funding of the project for transportation reconstruction. The credit included rehabilitation of certain road sections, fostering of institutional capacities of the public enterprise “Roads of Serbia” and traffic safety raising in critical points.
- In line with the previously defined aims of the Dutch-Serbian Business World, intensified cooperation initiated in 2008, resulted in implementation of the project No: G2G09/SB/5/2. This part of the project has been finalized: Assistance to Serbia in Road Structure Planning and Programming. Project goal was to prepare and adopt the Cost Benefit Analysis Manual for Serbia.

- Implementation of the project G2G08/SB/5/5, Reduction of Traffic Noise in Serbia, is underway
- Implementation of the Project G2G09/SB/5/4, Utilization of Secondary Raw Materials, Electric-filter Ashes and Dross for the Needs of Road Construction Industry, is underway
- In 2008, within the EBRD technical assistance, the program for Technical Assistance to public enterprise "Roads of Serbia" – Support System in Decision Making, was implemented being the outcome of the Project Corporate Plan for Public Enterprise "Roads of Serbia"
- Project EuroRAP-Serbia
- Public Enterprise Roads of Serbia, together with Auto-Moto Association of Serbia actively participated in the Project EuroRAP-Serbia contemplated to assist the Government of Serbia and the World Bank in identifying those positions where application of rational design counter-measures would reduce road accident victims, as well as in national goals as regards traffic road safety. EuroRAP – European Program for Road Evaluation started in 2000 being a radical supportive initiative for the accomplishment of the objective of reduced victims in car accidents on roads, by 50%. The program included 3,000 km of roads in Serbia. This Report was completed in 2009, and has been used as the basis in decision making for funding of projects relating to the traffic safety raising.

EXPENDITURE FOR RESEARCH AND DEVELOPMENT

- Studies and Projects: Response to this question is contained in the investment position of PE "Roads of Serbia: **Studies and Projects** (investment amounts per years are laid down in Annex No 1, Study and Project Positions).

| Investments in Studies and Projects in the Period 2005-2010 | | | | | | |
|-------------------------------------------------------------|-------------|-----------|-----------|-----------|-----------|-----------|
| in RSD millions | | | | | | |
| Description | Realization | | | | | |
| | 2005 | 2006 | 2007 | 2008 | 2009 | Revision |
| Studies and Projects | 1,187 | 1,064.50 | 602.7 | 1,041/9 | 1,678.30 | 4,570.20 |
| Total Investments of PE Roads of Serbia | 38,961.90 | 49,443.70 | 53,844.80 | 60,413.90 | 57,052.60 | 51,760.70 |
| % of total investments | 3.00% | 2.20% | 1.10% | 1.70% | 2.90% | 8.80% |

Source of data: Annual reports on realization of Work Programmes for 2005, 2006, 2007, 2008 and 2009. Revision of the Business Plan of PE "Roads of Serbia" for 2010.

- **Sector for Strategy, Designing and Development** within the PE “Roads of Serbia” conducts activities of technical preparation, strategic planning, studies, development, research, designing, planning documentation, traffic safety, environment protection etc. In addition, the Sector also participates in realization of the projects financed by the international financial Institutions and European Funds.

The following projects have been realized: general, preliminary, main designs for construction, reconstruction, recovery and rehabilitation of public roads of I and II category and structures, necessary pre-feasibility studies, feasibility studies, projects for road management and improvement, traffic studies, traffic regulation projects, necessary planning documents, environment impact assessment studies, research and development projects.

The following departments are part of the abovementioned Sector:

- 1) Department for Technical Preparation
 - 2) Department for Strategic Planning, Studies and Development
 - 3) Department for Designing and Planning Documentation
 - 4) Department for Traffic Safety
 - 5) Department for Environmental Protection.
- **Collection of toll** is conducted on all sections through automated technical collection system. 120
 - The collection has been modernized through introduction of TAGs (electronic cards) – electronic toll payment, without stopping a vehicle. Toll amount is deducted from the amount prepaid by the user. Toll collection system enables interoperability with modern toll systems in Europe.
 - Electronic toll collection was introduced for the first time in the section Belgrade – Sid, and the system was also established in the section Niš – Leskovac (toll booth Doljevac) and Belgrade – Subotica, as well as in the individual toll booths along the Belgrade – Niš motorway (Belgrade, Mali Požarevac, Vodanj, Ražanj, Aleksinački Rudnici, Aleksinac, Niš).

There is at least one exit lane with electronic toll collection at the main and side toll booths.

This type of cashless toll payment in the Serbian motorways (toll pre-payment) provides:

- Toll collection without stopping, which prevents possible traffic jams
- Simplicity of toll collection
- Shorter transaction time and larger number of transactions in a shorter time period

Electronic toll collection without stopping a vehicle is in line with modernization trend of toll collection, which makes PE “Roads of Serbia” closer to global trends.

Toll can be paid via domestic and international payment cards (VISA, VISA Electron, MASTERCARD, MAESTRO, POSTCARD, DINACARD, AMERICAN EXPRESS), as well as via coupons and cheques.

- **Website of PE “Roads of Serbia, information provided to users**

PE “Roads of Serbia” maintains contact with all road users on a daily basis, in order to constantly provide users with information on a timely basis. Quality and speed of information

provided to the public have been improved with the development of the website, www.putevi-srbije.rs, which has been on that address following the introduction of the new .rs domain.

Website of the enterprise has been developed in order to inform the domestic and international public, as well as specialized institutions, organizations in the field of traffic and transport engineering. The website provides basic data on the condition and future development of road network, organization and activities of PE “Roads of Serbia”, presentations etc. Information of particular importance pertains to road works, as well as current toll prices.

Public road management is a very responsible task, which, due to its specificity and public significance, has to be constantly monitored by the public through numerous print and electronic media

Regular daily website updating resulted in continuous notification of the public of all activities of PE “Roads of Serbia”; thus, the enterprise moved its service closer to the road users by providing adequate and precise information. In addition to the website, the information is transmitted via other portals, such as Automobile and Motorcycle Association of Serbia, which provides for timely information of users on the condition of the road network and quality of services rendered.

All these activities are conducted within the Law on Public Roads, as well as the Law on Public Administration, which govern cooperation with other state and local authorities, citizens, undertakings and other organizations.

- Modern technologies are used in operations, technological processes are developed and other solutions are implemented.
- Possibility for development and improvement of operations are defined within the feasibility study and development strategy.
- Automatic toll counters in the road network provide acquisition of information on average annual daily traffic (PGDS) on the public roads of I and II category in the Republic of Serbia. PE “Roads of Serbia’s” website contains information on road traffic burden in the Republic of Serbia in the period 2005-2010 – as well as the map and table broken down per directions.

QUALITY ASSESSMENT OF MAIN INFRASTRUCTURE TYPES (TRANSPORT, TELECOMMUNICATION, ENERGETIC), EMPHASIZING AREAS IN WHICH THERE IS A NEED FOR SIGNIFICANT INVESTMENTS

ROAD NETWORK (length and condition)

Republic of Serbia has a public road network of categories I and II, value of which is estimated at 13 billion US Dollars.

Serbia is a European country with median population density and well developed road network.

Road network of the Republic of Serbia, 40,845 km long, consists of:

- 5,525 km of category I public roads
- 11,540 km of category II public roads and
- 23,780 km of local roads.

Road network contains:

- 498 km of motorways subject to toll collection

- 136 km of semi-motorways subject to toll collection.

(Source of data: PE "Roads of Serbia" website).

European E-Road Network covers 2,150 km of main road network in Serbia.

The Map of Main Road Network in Serbia is laid out in the following text.

Corridor X runs through Serbian territory, in the length of 792 km along the main route: Croatian border – Belgrade – Niš – Macedonian border, and with two branches:

- Branch B: Section Hungarian border - Novi Sad - Belgrade
- Branch C: Section Niš - Dimitrovgrad – Bulgarian border.

Corridor X is the most important route in the Serbian territory, part of the South-Eastern Transport Axis and main regional transport network. It connects Austria, Hungary, Slovenia, Croatia, Republic of Serbia, Bulgaria, Macedonia and Greece.

Road network in the Republic of Serbia stretches along various altitudes, starting from 30 meters (Negotin) up to 1,700 meters above sea level (Golija). It is estimated that 40% of road network is situated at altitudes over 600 meters above sea level.

Asphalt roads of category I and II state roads were built between 1963 and 1985, and many of the routes kept the elements of the old routes, so that asphalt was placed over the existing gravel roads. In the same period, the most important routes were built pursuant to projects; hence, such sections were equipped with newer, better elements of longitudinal and transverse profile.

At the level of the entire road network, 2/5 of sections have gravel roads and dirt roads.

In the Republic of Serbia, 32% of category I and II roads are more than 20 years old, and only around 14% up to 10 years.

Bridges and Tunnels

Tunnels:

There are 2,638 **bridges** along the roads in the Republic of Serbia (excluding data from the territory of the Autonomous Province of Kosovo and Metohija), with total area of around 800,000 square meters. Out of which:

- 215 bridges on the motorways
- 996 bridges on category I state roads and
- 1,427 bridges on category II state roads.
- Undepreciated value of all bridges is estimated at 1 billion US dollars.

The bridges were built at different times, of different shapes and construction designs, made of woods, stone, concrete, reinforced concrete, steel and various static systems. Length of bridges varies between 5 and 2,212 meters (bridge over the Danube at Beška).

Republic of Serbia possesses 12 large bridges, 7 over the Danube and 5 over Sava.

Tunnels:

There are 78 **tunnels** that have been constructed along the Serbian roads, with total length of 10,053 meters. Out of that number, 1 tunnel is located along the motorway, 71 tunnels along category I state roads and 6 tunnels along category II state roads.

Tunnels have been built at different times, with different construction technologies employed in various geological environments. The total of 32 tunnels is longer than 100 meters, and the longest tunnel is the Sargan Tunnel, along the route from Kremna to Višegrad, 775 meters long. The largest concentration of these objects is along the Đerdap rout, with 25 tunnels in total.

Due to long-term lack of investments in road maintenance and reconstruction, the current condition of the road network is not satisfactory.

LACK OF INVESTMENTS IN MAINTENANCE OF THE SERBIAN ROAD NETWORK

Maintenance of existing road network is the priority for PE “Roads of Serbia”.

Road maintenance via contracts has been entrusted to road undertakings which are obliged to secure permanent and constant high-quality maintenance and protection of roads and ensure safe and unhindered traffic on such roads.

Maintenance problems are the following:

- Insufficient funds for maintenance
- Poor condition of roads and objects on roads
- Large number of landslides from the past, large number of orders issued by the Inspectorate for Road Traffic of the Ministry of Infrastructure and Ministry of Interior.
- Problems with obsolete road equipment (protective fence on motorways, wired fence, traffic signs, urgent need for replacement of inadequate traffic signs – obsolete, faded, stolen traffic signs in the past).
- Deformation of asphalt road surface, as a result of high temperatures
- Modernization of road network maintenance, traffic control and control of toll collection system.

Due to insufficient funds and the need to balance between planned investments and funds, the Work Programme is adopted based on the available (and unacceptably) small funds, so that planned investments are upfront limited and inadequate compared to the needs.

In financial terms, on-going, constant and high-quality maintenance and protection of roads could not have be realized within the Work Programme for many years, since the Programme is adopted with insufficient funds, resulting in excess of investments in road maintenance relative to planned funds.

Lack of financial funds may cause inability to maintain category I and I roads, as well as safe and secure traffic, in compliance with the Law on Public Roads and Law on Road Transport Safety, as well as the Strategy adopted by the Government of the Republic of Serbia.

Road investments are long-term capital investments and require stable long-term financing sources.

The obligation of securing funds necessary for maintaining main and regional road network in the Republic of Serbia was also assumed when the contract was signed for reconstruction of roads with the European Bank for Reconstruction and Development, which stated:

- That the Republic of Serbia will ensure that all annual costs for road maintenance be covered according to priorities, defined in the Road Reconstruction Plan agreed with the Bank, and which, for the fiscal year, will not be less than:

| Year | Amount (in EUR million) |
|-------|-------------------------|
| 2003. | 116,0 |
| 2004. | 186,0 |
| 2005. | 195,0 |

AREAS IN WHICH THERE IS A SIGNIFICANT NEED FOR INVESTMENTS

- **National Construction Plan for Road and Railway Infrastructure in the Republic of Serbia 2008-2012 identifies the following priorities:**
 1. Completion of Corridor 10 through Serbia, with ring road sections around Belgrade / finalized financial agreement for 2008-2011 stipulates EUR 1,585 million.
 2. Construction of motorway Belgrade - Southern Adriatic / 2009-2015 stipulates EUR 600 million / funds for entire section have not been secured.
- * Planned Section Kragujevac – Batočina was not completed in the period 2008-2010.
- **General Master Plan for Transport in Serbia (2007-2027)**, adopted in 2009 stipulated 13 priority projects for which close to EUR 5 billion need to be invested in the road infrastructure in the mentioned period.

NETWORK DEVELOPMENT

Long-term objectives for road network development include:

- Construction of a new transport corridor Belgrade – Vršac - Romanian border (Route 4)
- Construction of a new transport corridor Belgrade – Southern Adriatic (link between Corridor IV and Corridor X with the Adriatic)
- Transversal link between Corridor IV in Bulgaria and Corridor X (the extension route Zaječar – Paraćin is in the process of rehabilitation using World Bank loan (through Pojate – Kruševac – Kraljevo – Čačak / link to Corridor Belgrade – Southern Adriatic)
- Route 7 within the main network for the Western Balkans, Niš – Prokuplje – Kuršumlja – Priština, and transverse link of Corridor Xc with Priština (Routes 6 and 7 within the main network), from Pirot to Leskovac and on towards the Kosovo border (and further on Priština – Peć – Montenegro - Murino – Berane) should be observed in the same context.
- **MOTORWAYS** – elementary indicators of road network analyses result in defining so called MAIN TRIANGLE (BELGRADE – POJATE – CACAK – POZEGA – BELGRADE), with significant indirect effects along the existing two-lane roads. Expansion of the main motorway network in Serbia towards outer areas is based upon the MAIN TRIANGLE and should be implemented in phases.

Short-Term / Medium-Term Objectives for Road Network Development

Through its High Level Group Document, the European Transport Policy limited its priority projects until 2010, by observing Serbian road infrastructure in the following manner:

List 1:

Short-term / medium-term Projects

- a) Improving the road quality on sections Hungarian border - Belgrade - Niš - Macedonian border (rehabilitation finished)
- b) Ring road around Belgrade, Section Batajnica – Bubanj Potok (in the process of finalization, work in progress)

List 2:

Long-Term Significant Projects on Multimodal Axes and Projects of Regional and National Importance

- a. **The Gazela Bridge in Belgrade (work in progress)**
- b. **Intermodal Logistical Platform in Belgrade**

The same document defines high-priority reconstructions/rehabilitations of the following routes:

- Corridor X – with ring road around Belgrade (work in progress)
- Corridor X/E-70/M-1 Croatian border - Batrovci - Belgrade - E-75/M-1 Belgrade - Niš - Leskovac - Bujanovac - Macedonian border (rehabilitation of existing sections completed)
- Xc, E-80 Niš – Bulgarian border (work in progress)
- Xb Belgrade – Hungarian border (work in progress)
- Routes 3/M-5 border with Republic of Srpska - Užice
- Routes 4/E-70 Romanian border – Belgrade – Čačak – Užice – Montenegrin border (rehabilitation completed)
- Route 5/E-761 Bulgarian border – Vrska Cuka - Zaječar – Paraćin – Pojate – link between Corridor X and Corridor IV (rehabilitation in progress)
- Route 6/M-2 Montenegrin border – Ribarici – Kosovo - Priština
- Route 7/ R-245 (Doljevac – Žitorađa – Prokuplje), M-25 Nis – Prokuplje – Merdare - Kosovo border) and transverse link Pojate – Kruševac – Kraljevo – Čačak and Pirot – Leskovac – Lebane – Kosovo and Metohija.

It is necessary to pay attention at:

Removal of bottle necks - dominant problem of the main road network in Serbia are roads through and around Belgrade, bridges on the Danube and Sava Rivers in Belgrade and its vicinity, ring road around Belgrade, road Belgrade – Novi Sad, bridge at Beska, temporary road-rail bridge in Novi Sad, Ibarska Magistrala road.

Work on rehabilitation of the motorway through Belgrade is in progress, as well as reconstruction of the Gazela Bridge over Sava, circular road around Belgrade P-251 is

rehabilitated, negotiations are underway for road P-267, existing sections on Belgrade – Novi Sad route are rehabilitated, completion of the second lane is in progress along with renovation of existing and construction of the new bridge, Ibarska Magistrala Road is rehabilitated, while work is in progress on the road-rail bridge.

- Bridge reconstruction in the road network – for the purposes of reinforcement of construction, stability and load capacity, bridge reconstructions are necessary. Due to inadequate maintenance during the year and increased traffic density on certain sections of the network, bridges have become a significant bottle necks. Special analysis must be conducted, in order to define priorities for reconstruction on the main network (bridge reconstructions in progress).
- Implementation of higher safety level, introduction of official methodology for defining and repairing black spots. Dangerous spots must be reconstructed and roundabouts should be introduced wherever necessary and possible. Preparation of a study on general priority safety transport measures on international roads.

List of high-priority dangerous spots has been defined, and accordingly the technical documents for resolving such spots are developed, as well as technical documents for large number of roundabouts.

Landslide stabilization should be a priority activity on sections which, due to landslide activities, experience interruptions and slowdown of traffic (regular procedure).

Construction of the second motorway road lane at the branch of Corridor Xb, Section Horgos – Belgrade (work in progress).

Construction of the remaining sections of motorway at Corridor X, Leskovac – Macedonian border, and at branch of Corridor Xc Niš – Bulgarian border (work is being contracted).

Reconstruction of the bottle neck in Ovčar Banja (Ovčar Banja ring road constructed, along with the tunnel).

Rehabilitation of the road Subotica – Bačka Palanka.

OVERVIEW OF THE KEY TRANSPORT INFRASTRUCTURE PROJECTS PLANNED FOR THE NEXT PERIOD OF 8 YEARS

Strategic Objectives of PE “Roads of Serbia” are the following:

| | |
|------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Road network | Prevention of road deterioration, maintaining road network value and its improvement |
| Road development | In addition to road maintenance, there are plans for investments in construction, rehabilitation, reconstruction and drafting studies and projects. These investments are in compliance with the strategic commitments of the Republic of Serbia in the sector of road transport - to be operationally integrated into European Road Network |
| Traffic safety | Increasing safety, removing dangerous spots |

| | |
|--------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Environmental Protection | Reduction of harmful effects of roads and traffic to the environment |
| Improvement of transport links | <p>High-quality and efficient links between economic areas, as well as between counties and provinces within the Republic</p> <p>Efficient links between the Republic of Serbia and the region, neighbouring countries in particular</p> <p>Transport and economic valuation of geographic, international and transport position of the Republic of Serbia in the region</p> <p>Active participation in integration process in the Western Balkans</p> <p>Inclusion into the fast roads system of European importance, intended for transit and tourist transport, primarily at Corridor 10</p> |
| Services | Improving the quality of services rendered to road users through improvement of quality management and quality control |
| Employment | <p>Employing capacities of roads undertakings and construction undertakings</p> <p>Providing stimulus to overall economic trends</p> |
| Financial objectives | <p>Reduction of debt level</p> <p>Reduction of spending on all levels</p> <p>Cooperation with international financial institutions</p> <p>Increase of own revenues</p> |
| Institutional strengthening | <p>Improving capacity for strategic planning, management of public roads and assets of "Roads of Serbia", in compliance with the national regulations and international standards</p> <p>Harmonization with the EU standards and procedures</p> <p>Establishment of quality management system ISO 9001: 2008</p> <p>Improvement of information system</p> <p>On-going training and development of employees</p> |

Strategic objectives of PE "Roads of Serbia" will be realized primarily through implementation of the following:

- Development Strategy for Rail, Road, Water, Air and Intermodal Transport in the Republic of Serbia, 2008-2015.
- National Construction Plan for Road and Railway Infrastructure in the Republic of Serbia 2008-2012.
- General Master Plan for Transport in the Republic of Serbia.

Strategy for the Development of Railway, Road, Water, Air and Intermodal Transport in the Republic of Serbia from 2008 until 2015

This strategy, adopted by the Government of the Republic of Serbia on 27 December 2007 (*O. Gazette of RS*, No. 4/08), determines the conditions in all areas of transport, establishes a

concept of infrastructure and transport development, defines objectives of transport system development and action plan for their realisation, taking into account the need for a sustainable development of transport in the Republic of Serbia. Guidelines for such development are based on the principles of safety, intermodality, application of modern technologies, complementary use of all modes of transport and rational use of available capacities and resources in the country.

Main objectives of the Strategy are:

- Integration of the transport network of the Republic of Serbia into the Trans-European Transport Network
- Efficient use of comparative advantages of every mode of transport
- Increasing the quality of transport system services
- Increasing the level of safety and security of the transport system
- Strengthening the transport market and its gradual deregulation
- Reduction of the negative environmental impact of transport, in compliance with principles of sustainable development
- Establishing a stable source of financing of transport system development.

National Plan for the Construction of Road and Railway Infrastructure in the Republic of Serbia in the period between 2008 and 2012

The Government of Serbia has adopted the National Plan for the Construction of Road and Railway Infrastructure until 2012, which envisages investments in road infrastructure in the amount of EUR 2.9 billion.

According to the plan, these funds shall be used for the construction of Corridor X highway, Belgrade – South Adriatic Region highway, as well as the following sections: Kragujevac – Batocina (highway), Kikinda – Ada – Novi Sad – Sremska Mitrovica – Sabac – Loznica (semi-highway), Pozarevac – Kucevo – Majdanpek – Neogtin (M-25) (semi-highway) and Pancevo – Vrsac (highway).

General structure of financing: (a) necessary borrowings EUR 1.39 billion, (b) donations EUR 100 million, (c) remaining EUR 1.41 million from the budget.

General Master Plan for Transport in the Republic of Serbia

In May 2010, General Master Plan for Transport in Serbia, which envisages investments in the amount of EUR 13.5 billion in road transport until 2027, including maintenance of road network, was presented in the Ministry of Infrastructure.

The most important projects to be realised in the area of road transport are projects related to Corridor X, including those realised on the north section of this Corridor from Novi Sad to Subotica (Y section), as well as on the section from Nis to Dimitrovgrad and from Nis to Presevo.

A more detailed explanation of certain objectives and strategies for their realisation

Maintenance of roads

The objective of road maintenance in the Republic of Serbia is to ensure an optimum level of service alongside with securing an acceptable level of safety of participants and minimising negative impact on the environment.

The policy of road maintenance is aimed at maintaining existing roads and achieving a safe and efficient transport of goods and services.

Development of roads

In addition to road maintenance, investments in their construction, reconstruction and rehabilitation are necessary, as well as investments in designing studies and projects as prerequisites for these works.

Traffic safety

The objective of improving road traffic safety in the Republic of Serbia is to reduce the number of persons killed in traffic accidents in 2010 to the level of the majority of European countries from 2005.

Environmental protection

Environmental protection policy is aimed at reducing the impact of traffic sector on air, water and soil pollution, noise pollution, global warming, as well as at reducing risk in transportation of dangerous goods.

The objective is to establish an infrastructure that is in harmony with natural and cultural environment, in such a manner so as to preserve natural resources and make the impact of traffic tolerable/acceptable in terms of people's health and well-being.

Institutional strengthening

Institutional strengthening includes establishing quality management system, as well as development of structures and capacities for: corporative planning, strategic planning and programming of road infrastructure, management of PEPS (Public Enterprise "Putevi Srbije" ("Roads of Serbia")) assets, information system with databases, project management, etc.

Establishing quality management system in compliance with the international standard ISO 9001: 2008 means showing and proving (in the process of certification) that PE "Putevi Srbije" is capable of consistently providing services which fulfil requirements of users and relevant regulations.

The aim is to increase user satisfaction by effective application of the system, including processes for its constant improvement, as well as to prove compliance with users' requirements and regulatory requirements.

New technologies

The aim of introducing new technologies is the improvement of the quality of service to road users, reduction of social expenditure and financial savings, through reduction of traffic jams, increase in safety and reduction of environmental impact.

This aim is realised by substituting old, defective material with new material, its recycling and re-use, applying road weather information system (RWIS) in winter maintenance and applying telematics (intelligent transport systems - ITS) in traffic management.

Strategy

The set objectives shall be achieved through:

- Harmonisation and enhancement of legal regulations and technical standards;

- Efficient and rational planning of construction works, in accordance with secured financial resources;
- Procurement of goods, construction works and services according to market principles, disabling of monopolies and ensuring the equality of bidders (application of the Law on Public Procurement);
- Enforcement of severe sanctions for rendering contractual services of poor quality:
- application of contractual penalties, termination of contract, filing of damage compensation claims, making a list of unsuitable bidders for a period of time;
- Enhancement of management and planning of roads and roadworks:
 - enhancement of organisation, information system, communication, collection and processing of data on road conditions, climate, traffic density, application of new - more rational and more efficient - technologies in works, modernisation of traffic signalisation and road equipment;
- Cooperation with all competent institutions, authorities and participants in traffic:
 - a special form of cooperation with institutions that have legal competences related to roads – the Ministry of Infrastructure and MoI, as well as with public enterprises whose infrastructure facilities lie within the road corridor or intertwine with it;
- Reducing harmful impact of roads and roadworks on the environment:
 - by: inducing a quicker pace of traffic by good roads, which indirectly lowers harmful gas emission; planning, projecting and constructing roads according to plans and technical solutions which are in compliance with regulations related to environmental protection; locating and constructing roads, bridges and other facilities in harmony with the surroundings; preserving cultural and natural landmarks of special value; applying materials and technologies which do not degrade the environment, constructing and maintaining road drainage system, applying strict penalty policy for leaving waste within the road strip;
- Improvement of traffic safety on national roads
 - application of official methodology for defining and securing high-risk sections and their repair. Checking road traffic safety requirements in all phases of road projects; introduction of managing dangerous road spots through monitoring road traffic accidents, including identifying, analysing and repairing dangerous spots; introduction of a database on traffic accidents in the PE with entry statistical information from police reports;
- Improving protection of road users (access roads, facilities, billboards, etc.) within the road strip in line with the Law on Public Roads;
- Enhancement of the application of transparency principle in work;
- Efficient management, monitoring and comparison of achieved results;
- Permanent education and training of human resources for quality and specialist areas.

Quality management system according to ISO 9001: 2008

PE “Putevi Srbije” is obliged to secure a consistent performance of services, which fulfil requirements of users, international institutions and relevant regulations, in terms of road management process (including toll collection system).

PE has to identify processes and apply them in the whole organisation, specify schedule and interaction of these processes, specify criteria and methods required for effective performance and management thereof; secure availability of resources and information necessary for supporting performance and monitoring of these processes; monitor processes, measure and analyse their performances and apply measures required for achieving planned results and constant improvement of these processes.

Demonstrating and proving (during certification process) abilities for quality management, securing quality and quality control is a necessary strategic goal in the situation in which the chosen direction leans towards market-oriented business operations and in which more than 60% of companies – contractors already have a quality system certificate in line with international standards.

Quality control and laboratory tests

In the area of quality management, quality control is a permanent obligation of PE “Putevi Srbije”. In the area of laboratory tests, based on technical documentation, conditions required for testing are being prescribed and the following takes place:

- control of the management of documents related to the quality of the input raw materials and materials;
- reporting on controls carried out;
- verification of the application of written procedures for conducting laboratory tests;
- Activities mentioned here are permanent activities related to investments, maintenance of level I and II roads, as well as reconstruction and rehabilitation of carriageway constructions. These activities are performed through cooperation between Quality Division, Investments Department and Department for Maintenance of Level I and II Public Roads. The amount of funds for laboratory tests has to be increased every year, following the increase in the investments in road infrastructure.

Strategic planning and programming of road infrastructure

This activity is related mainly to the realisation of the Strategy for the Development of Transport in the Republic of Serbia, 2008-2015, and the National Plan for Road Infrastructure. The most important activities from these two documents for PEPS in 2010 are the following:

- completing and putting into function the full road infrastructure on the international route Corridor 10, the Bypass around Belgrade (section Orlovaca – Bujanj Potok) and other bypasses around bigger towns
- further elaboration of the construction of highway from Krusevac, Cacak, Kraljevo and Uzice towards Bosnia and Herzegovina (Republika Srpska) - a section of Corridor 10
- initiative for adopting and continuation of elaboration of a new Corridor 11 proposed as a part of the network of European corridors, which should connect Timisoara with Italy

via Belgrade and Podgorica (a phase in the construction of the highway from Belgrade to Cacak) and

- planning of repair and rehabilitation of national roads in terms of traffic safety, by applying IRAP Serbia programme (designing technical documentation and applying engineer solutions for the first phase of the construction of circular intersections, widening of road shoulders, construction of road crossings with signalisation, overtaking lanes, and improving road surface).

PE "Putevi Srbije" shall respect provisions of the new **Spatial Plan of Serbia** and apply guidelines from the **General (Master) Plan** for the development of transport and plans of road infrastructure. The road network shall be incorporated to the maximum into the multimodal transport network of Serbia, Trans-European Networks TEN and TEM and the so-called "Core Network" of SEETO;

The following two projects shall begin: Creation of a Strategic Study including the proposal for a **Medium-Term Plan and Programme** for Construction and Reconstruction, Maintenance and Protection of National Roads, **2010-2015**, and the project of Development and Application of a System for PEPS Asset Management (RAMS), in line with the new Law on Planning and Construction, preformed assessment of fixed assets of PE "Putevi Srbije" and with the use of the new road-related database.

Creation of a strategic framework and guidelines for the application of the PPP model for financing road infrastructure and optimisation of the charge for the use of roads (toll) shall be initiated.

Traffic safety

PE "Putevi Srbije" places special attention to the **enhancement of road traffic safety**.

The main medium-term objective specified in the Policy for Traffic Safety of PE "Putevi Srbije" is to reduce the number of persons killed in traffic accidents in 2010 in Serbia to the level of the majority of European countries from 2005 (approximately by 1/3). This is quite an ambitious objective and its realisation depends on the success of legal regulations and cooperation between departments. The consequence of this vision for PE "Putevi Srbije" shall be an increased responsibility for the "road" factor in creating a safe road traffic system.

In 2008, 897 persons were killed in traffic accidents on Serbian roads, which amounts to 2-3 persons on average per day. The death rate on Serbian roads is more than two times higher (per 100,000 inhabitants) and over 5 times higher (per 10,000 vehicles) when compared with the best result in Europe. It is necessary to invest great efforts and resources in order to prevent or at least mitigate forecasts of the World Bank on the further increase in the number of persons killed in road traffic accidents (by more than 80% in the period 2000 - 2020).

In 2009, 798 persons were killed in traffic accidents on Serbian roads, which amounts to 2 persons on average per day.

The following table contains the number of traffic accidents and the number of persons injured and killed in them, in the period 2001 – 2009 (according to MoI data):

| Year | Total number of traffic accidents | Total number of persons injured or killed | Number of persons killed | Number of persons injured |
|------|-----------------------------------|-------------------------------------------|--------------------------|---------------------------|
| 2001 | 61,711 | 21,181 | 1,275 | 19,906 |
| 2002 | 52,177 | 15,614 | 854 | 14,760 |

| | | | | |
|------|--------|--------|-----|--------|
| 2003 | 55,660 | 16,821 | 868 | 15,953 |
| 2004 | 62,356 | 18,511 | 954 | 17,557 |
| 2005 | 61,958 | 17,713 | 841 | 16,872 |
| 2006 | 63,913 | 19,305 | 900 | 18,405 |
| 2007 | 70,789 | 23,177 | 968 | 22,209 |
| 2008 | 67,708 | 23,172 | 897 | 22,275 |
| 2009 | 64,800 | 22,298 | 798 | 21,500 |

** the data refer to the area without Kosovo and Metohia*

The new Law on Road Traffic Safety specifies several new obligations for PE “Putevi Srbije”:

- Strategic comparative analysis of the impact of a new or reconstructed road on the traffic safety in the road network,
- Review of traffic safety and control of road traffic safety,
- Monitoring of traffic safety conditions and analysis of high-risk sections. Monitoring of traffic safety conditions includes: managing black spots, risk mapping etc,
- Analysis of how much the road factor contributes to traffic accidents resulting in deaths,
- Conditions which have to be fulfilled by road facilities and other road elements from the aspect of safety.

Besides PE, the main participants in the implementation of this programme are the Ministry of Infrastructure, the Ministry of Interior, the Faculty of Transport and Traffic Engineering and institutes.

According to the “Report of the World Bank on Capacity Management in the Area of Traffic Safety in Serbia” (from 2007), it is necessary to adopt a Strategy for Traffic Safety Management and, on account of it, to “within a 10-year period, establish a system of traffic safety management which shall offer high-quality results on manageable and sustainable bases”. At the same time, “securing sustainable annual financing of traffic safety and transparent distribution of funds remain the priority”.

Obligations of PE “Putevi Srbije” are:

- 1) to identify sections with the highest risk in the road network;
- 2) to create guidelines for the activities with the best results in terms of cost-effectiveness and update traffic safety standards with harmonisation requirements by applying good practice of road traffic safety reviews (RSA);
- 3) to prepare technical documentation related to traffic safety enhancement;
- 4) to design programmes for repair works in terms of traffic safety according to priorities based on the estimated cost-effectiveness;
- 5) to set up vertical signalisation, horizontal signs, protective fences and perform minor works (widening of road shoulders in high-risks curves, roadsides, islands, etc.) related to traffic safety enhancement;
- 6) to develop and apply knowledge on “sustainable safety” approach and gear management in the roads.

In the area of the direct realisation of measures, the extension of the Transport Rehabilitation Project (World Bank) has provided conditions for the implementation of the review of traffic safety requirements (RSA) and the implementation of measures.

Environmental protection

In the Republic of Serbia, laws related to environmental protection clearly specify rules and procedures to be observed by all legal and natural persons whose actions have negative impact on the environment. Accordingly, PE “Putevi Srbije” has recognised its obligations and in the course of planning, projecting, construction and exploitation of roads it tries to secure quality road infrastructure while at the same time observing all requirements related to environmental protection.

The programme for environmental protection in the area of transport has to include and specify responsibilities of every relevant function on all levels within PE for achieving ecological goals. New laws related to environmental protection clearly specify the responsibility of the project manager in all phases of planning, projecting and performing of works. Environmental impact of a road is huge and it relates to water, air and soil pollution, noise pollution, impact on protected areas. In 2010, the accent shall be placed on resolving noise pollution issue; therefore, the completion of the Feasibility Study of Technical Measures Aimed at Reducing Road Traffic Noise Pollution is in its final phase. Based on this Study, and pursuant to bylaws which shall enter into force in the middle of 2010, the creation of strategic noise maps and action plans for noise protection on national roads shall begin.

Basic components of this programme are:

- planning, projecting and construction of roads on the basis of plans and technical solutions compliant with regulations related to environmental protection
- management of studies on the assessment of road projects' impact on the environment (three phases of impact assessment, assessment of the impact of current condition on the basis of the project for a facility, etc.)
- evaluation of transport-related projects with regard to their compliance with the Law and rulebooks on strategic assessment of environmental impact
- preservation of cultural and natural landmarks of special value (protected areas)
- reducing negative environmental impacts of construction, maintenance and exploitation of the roads by defining guidelines (instructions) for project designers and rules (plans, technical instructions) for contractors
- implementation of the Plan for Environmental Protection Management related to construction works on national roads
- monitoring of the realisation of works and condition of the environment
- examination of skills and knowledge of PE staff.

Necessary investments in the implementation of the environmental protection programme are estimated to be 1.5% GDP per year.

PE holds the opinion that the measures envisaged by this programme can be implemented in the period until 2011 on condition that necessary resources have been secured. Financing environmental protection on the current level would mean that ecological objectives within transportation sector shall not be fulfilled.

New technologies

On the basis of the "Programme for the Development and Application of Intelligent Transport Systems on the Roads in the Republic of Serbia", the following has been envisaged: introduction of ITS, enhancement of telematics and application of new technologies on highways, bypass around Belgrade and the sections of level I and II roads with the highest traffic density (software-based determining of an integrated surrounding, introduction of modern systems, recording, counting and monitoring relevant parameters).

On the system management level, it is necessary to establish a traffic information (management) system for collecting, processing and distribution of relevant data and application of IT services (telematics, system for winter maintenance RWIS, GIS, etc.) in the whole territory of Serbia.

The complete system consists of adaptable sub-systems for traffic management, detection of incident situations, SOS, RWIS, automatic collection of toll, video surveillance, control of highway access, management of traffic by traffic lanes, changing signalisation, etc.

On the hardware level, it consists of facilities, devices, stations, sensors, detectors, video cameras, communication links and signalisation elements, whose functioning is supported by different operation and telecommunication technologies.

The implementation consists of studies, projects, software and hardware. Hardware consists of technical systems and components, the basic ones being:

a) System for measuring and collecting data, that includes:

- System for collecting data on traffic – automatic system for data collection (sensors, detectors, vehicle counters) and information (police reports, etc.) and
- System for collecting data on environment – weather parameters, RWIS, roadworks, network video surveillance, etc. (detectors for precipitations, temperature, wind, visibility and degree of slipperiness of road surfaces on the traditionally most dangerous sections of road network, where potentially critical meteorological conditions are expected).

b) Communication system: Communication links for data transfer to and from the management centre (cable links along the road strips, optical cables along the length of 500 km of national roads, including periphery equipment, installation of SOS telephones on main highway routes).

c) Management centre: Control unit with components necessary for appropriate data storage and procession, control and surveillance of the network, as well as bringing management decisions.

d) System for dissemination of information to users: Traditional or special light signals or several complex systems of changing traffic signalisation. Its purposes are: gear management (within the system for the management of incident situations and traffic jams, and access control), management of free lanes, disseminating information to users and management of customers per network.

26. Please describe the initiatives taken to enhance the business environment and the results achieved so far. Please provide focussed information on the main obstacles for doing business.

Government of the Republic of Serbia adopted as of 9 October 2008, the Regulatory Reform Strategy of the Republic of Serbia for the period 2008 – 2011 (hereinafter: the Strategy), in order to improve the business environment, reduce legal insecurity and increase competitiveness of local economy. The Strategy foresees a number of measures which need to be taken as to accomplish several goals, primarily the reduction of administrative operational expenses by 25% until 2011, and the simplification of administrative procedures, thus significantly improving the international rating of the Republic of Serbia as regards the business environment quality. The measures primarily relate to improvement of the existing Regulatory Impact Analysis (RIA) and single repeal or amendment of inefficient regulations - Comprehensive Regulatory Reform (CRR).

Regulatory Impact Analysis (RIA))

Serbia has been carrying out the Regulatory Impact Analysis (RIA) since 2004, with the aim to assess the impact new laws have on business environment. According to *ex-ante* principle, RIA represents compulsory annex to draft laws, prepared by the competent regulatory body, while adoption and implementation of regulations is followed by *ex-post* analysis, which has not been fully developed. RIA should include the *cost-benefit* and *standard cost model* analysis of the impact new laws have on business environment. Competent regulatory body submits RIA statements to the Council for opinion. The Secretariat of the Council makes detailed checks on RIA statements and then issues opinion on submitted RIA as publicly available on website: www.ria.merr.gov.rs. There have been 350 opinions so far on RIA (111 opinions issued solely during 2009) thus indicating the highly dynamic regulatory activity in Serbia in this period.

Comprehensive Regulatory Reform (CRR)

For implementation of the Comprehensive Regulatory Reform, the Government adopted the Decision on Establishing the CRR Implementation Unit. Action plan for implementation of the Strategy foresaw several phases of CRR implementation.

In the first phase all general regulations on the national level were listed (laws, regulations, rulebooks and all other by-law acts relating to third persons – both to the business sector and to the citizens) which itself improved legal security and transparency. This phase included around 200 participants among those employed in regulatory bodies, who had previously been trained and who entered into CRR database about 5,540 regulations through *online* forms. In the second phase 2,024 rules and regulations referring to the business were analysed as to decrease administrative operational expenses. During this phase business entities (and institutions and associations representing them, such as chambers of commerce, Council of Foreign Investors, and others), were directly included in the reform, giving their concrete suggestions for the legislation which needed to be cancelled, or amended as to improve business environment. Focus was on cancellation and amendments to redundant or inefficient administrative procedures.

Cooperating with regulatory bodies, CRR Implementation Unit made a list of 196 rules and regulations which were proposed to be cancelled. Government passed the Regulation on Cancellation of Certain Regulations, abolishing 15 regulations, as well as the Decision on

Cancellation of Certain Regulations abolishing 11 decisions. By the Conclusion of the Government, as of 03/12/2009, regulatory bodies were charged with cancelling the total of 170 rules and regulations. Of 170 rules and regulations which were to be cancelled, 166 have, and 4 have not been cancelled yet.

In line with submitted initiatives from the business sector and the citizens, CRR Implementation Unit made 340 recommendations for amendments to inefficient rules and regulations and was submitting them in October and November 2009 to regulatory bodies for opinion.

Of 340 recommendations submitted by the CRR Implementation Unit, after agreement with regulatory bodies, 216 recommendations were submitted for Government's consideration and were adopted in the session on 29 December 2009. Government's Conclusion on Adoption of the Programme for Strategy Implementation ordered competent regulatory bodies to implement the recommendations. So far implemented recommendations, or those under implementation, have been generating for the economy of the Republic of Serbia annual savings of about EUR 142,4 million, as well as significant positive unquantifiable effects. Of the recommendations adopted by the Government, implementation, i.e. application of 70 has started in practice, as well as of 9 additionally aligned recommendations. In the implementation procedure there are still 122 adopted and 14 additionally harmonized recommendations, whose text was incorporated in the draft law and by-law acts, or where other activities for their implementation have been undertaken, although they have not yet taken effect in practice. Percentage-wise, 192 recommendations, that is 88,8%, have been, or are in the process of implementation, out of the 216 adopted by the Government. Having had adopted 216 recommendations in 2009, at its session as of 26/11/2010, the Government also adopted the second package with 66 recommendations.

Where it was possible, CRR recommendations included quantification of the savings (using the *standard cost model*) to be accomplished once recommendations have been implemented in practice, and where that was not possible, positive effects of proposed recommendations were indicated. Total savings accomplished on the basis of the implemented recommendations were EUR 50,8 million, while on the basis of recommendations whose implementation is underway, expected additional savings amount to EUR 91,5 million, so that totally accomplished savings will amount to EUR 142,4 million per year. Estimated amount of savings from recommendations not yet implemented is EUR 46,358,862 per year, hence total savings, in case all recommendations by the CRR Implementation Unit were implemented, would amount to EUR 188,775,821 per year.

A number of initiatives addressed system problems, so the CRR Implementation Unit prepared general recommendations – guidelines for overcoming those problems (e.g. reform of inspections, maintenance of electronic registers and their availability, availability of the acts operationally applied by the public authorities as regards third persons and alike).

Having finalized the above mentioned processes, anticipated results will improve competitiveness of Serbia, resulting from more secure and transparent regulatory environment, whereas administrative operational costs in business sector will be reduced by at least 25%. We also expect that one of the results will be the improved rating of Serbia in international studies, such as the one made by the World Bank, „*Doing Business*“, and „*Global Competitiveness Index*“ by the World Economic Forum, by at least 20 positions.

It should also be noted that under this reform, since 2007, more than 200 civil servants have gone through a five day training for regulatory impact analysis (RIA).

This reform was supported by the donation of the Government of the Kingdom of Sweden, administered by the World Bank, and by the Ministry of Economy and Regional Development of the Republic of Serbia.

The tasks carried out by the *Secretariat of the Council for Regulatory Reform* and the CRR Implementation Unit, as interim bodies, will in future be performed under the scope of activities of the Office for Regulatory Reform and Regulatory Impact Analysis, as standing Government's service, established by the Regulation on the Office for Regulatory Reform and Regulatory Impact Analysis, as adopted in the Government's session as of 18/11/2010. This Regulation stipulates that the Office shall carry out professional tasks required by the Government and relating to the implementation of the regulatory reform and regulatory impact analysis, as proposed by the ministries and special organizations, including: giving a prior opinion at the request of the proposer of regulations on the need for implementation of impact analysis and on the regulatory impact analysis intended for public debate and on the completeness of the content of the enclosed impact analysis; assistance to proposers of regulations when establishing mechanisms for monitoring and regulatory impact analysis during its application; collection and processing of business entities' initiatives, as well as by other legal persons and citizens for replacement of inefficient regulations on the national level; submission to competent proposers the initiative for amendment of inefficient regulations; participation in organizing trainings for civil servants engaged in activities related to the regulatory impact analysis; performing tasks related to monitoring and analysis of institutional and staff capacities for regulatory reform implementation; establishment and maintenance of internet site for full information availability on the performance of the Office and for enabling active participation by business entities and citizens in regulatory reform; promotion activities for regulatory reform implementation on national and local levels and other activities prescribed by laws and acts of the Government.

Here below are **examples** of well implemented reforms:

Social insurance registration

As to simplify the procedure for employers, there has been established one-stop shop for social insurance registration/change/deregistration for all three organizations involved in compulsory insurance: the Institute for Health Insurance, the Pension and Disability Insurance Fund and the National Employment Service, through a single insurance registration.

Since 1 October 2010, registration and deregistration of employees for health insurance, insurance in case of unemployment and pension and disability insurance has been carried out as one-stop shop. Employers may select whether to carry out registration/deregistration of employees in the Institute for Health Insurance, or the Pension and Disability Insurance Fund. A new form, Form M, is provided for single registration, change and deregistration of compulsory insurance.

Introduction of the one-stop-shop was significantly time-saving for employers, and it meant simplified activities as regards registration and deregistration of social insurance, incomparably fewer documents, thus eventually alleviating the work of the Institute for Health Insurance, the Pension and Disability Insurance Fund, the National Employment Service offices, and expecting three times fewer documents to be received, as opposed to the respective average so far.

Pursuant to the Law on Central Registry of Compulsory Social Insurance ("Official Gazette of the RS" No 30/10), an institution receiving a single registration shall be legally bound, the same day, to forward the required data to other organizations for compulsory social insurance. This system will function until the formation of a single Central Register base.

Registration of business entities

The Business Registers Agency is a centralized institution for registrations on the territory of the Republic of Serbia. It was founded in 2004, upon adoption of the Law on Agency for Business Registers ("OG of the RS" No 55/2004, and 111/2009), and it started on 1 January 2005, undertaking the implementation of reforms in the area of business registrations.

The Business Registers Agency operates in line with the regulations on public agencies, maintaining the registers as unique, centralised, public, electronic databases as follows: Business Entities Register (within which the following registers are managed: Companies Register, Register of Entrepreneurs, and Register of Representative Office of Foreign Legal Entities), Financial Leasing Register, the Register of Pledges on Movable Property and Rights, Register of Associations, Register of Foreign Associations, Register of Public Media, Registrar of Regional Development Measures and Incentives, Register of Chambers of Commerce, Register of Tourism, Register of Bankruptcy Estate, Register of Financial Statements and Data on Solvency, which are managed by the Registrars, appointed by the Agency's Board of Directors, with the prior consent of the Government. Competent ministries supervise and control the performance of the registers, subject to the type of the registration.

The reform which took place in the field of business entities data registration, and with established electronic register, as unique databases managed by the Business Registers Agency, and based on the the Law on Business Registers Agency, The law on Amendments and Supplements to the Law on Business Registers Agency, and the Business Registration Law contributed to the creation of a favourable environment for the development of the economy, as reflected in the results referring to the last 6 years of the operations of the Business Registers Agency: increased number of founded business entities, especially in the form of entrepreneurs and limited liability companies, resulting from the simplified business entities founding procedure, shorter time limits, through one-stop-shop system which started on 06/05/2009, and reduced compulsory minimum initial capital for some forms of companies.

Registration procedure for companies is regulated by the Business Registration Law and is uniform for all companies, thus for the registration of the founding of a company, in most cases the following documents need to be provided: registration application, act of incorporation, proof of founder's identity, proof of paid financial contribution, decision on elected representatives, stamped signatures of representatives and proof of paid registration fee.

For some companies, registration requirements are stipulated by special laws, as follows: the Law on Banks, the Law on Insurance, the Law on the Market of Securities and other Financial Instruments, etc. In case companies are subject to these laws, than as compulsory precondition for their founding, they will have to provide approval and consent by the competent authority (e.g. to found a bank or an insurance company it is necessary to provide approval of the National Bank, to found a broker dealer company it is necessary to provide approval of the Securities Commission for the carrying out of the broker dealer activities).

Likewise, some entrepreneur activities (natural persons engaged in all lawful activities for the purpose of gaining profit) are stipulated by the laws, referring to the: health care activities, veterinarian activities, agricultural activities, taxi transportation, communal services, etc. Prior consents are being issued in the form of decisions taken by the competent ministry for that field, whereas the party submits registration application when registering, as well as the decision ascertaining that requirements were met for the carrying out of the activity.

Registration of the founding has been successfully reformed with introduction of the “*one stop shop*” service, as of 06/05/2009, thus allowing business entities to submit a single registration application for the founding, thus also submitting the application to the Tax Administration and the Fund for Pension and Disability Insurance and completing the registration of the business entity, and acquiring: the Decision on the founding of a business entity including the unique registration number of the business entity issued by the Statistical Office of the Republic of Serbia, tax identification number (TIN) issued by the Tax Administration, and insurance registration from competent health, pension and disability insurance funds.

Reform of the registration of the founding has reduced the whole procedure to two days, whereas registration shall take effect to third persons as of the next day after registration of the change has been announced.

Serbia Investment and Export Promotion Agency (SIEPA) implements the following project:

1) Development of local supplier chains:

By using success stories deriving from practice of similar programs from the EU countries, aligned with business requirements in Serbia, with the provision of consulting and technical assistance to enterprises, and in partnership with them, initiatives will be taken as to raise the competitiveness level and promote export activities. At the same time, enterprises will be given an opportunity to work with local and foreign consultants in order to increase business efficiency and improve competitiveness. Multinational companies such as SIEMENS, HP, FIAT, Intel, GSK, West pharma, U.S.Steel, Oracle, IBM, Microsoft and many others which operate on the territory of Serbia will also participate as strategic partners.

During the entire time of the project duration, enterprises will be enabled to get in direct contact with multinational companies and special attention will be devoted to organize “Meet the Buyers” where multinational companies from Serbia and the region will appear as buyers, while enterprises, participants of the program, will act as potential sellers.

Development of local supplier chains is aiming at the development of a competitive local supplier chain capable of fulfilling the criteria of multinational companies operating in Serbia and the region. By improving their managerial and production capacities, the program will also enhance the opportunities for local enterprises to do business with multinational companies and thereof become part of the global supplier chain.

The task of the program is to provide technical and consulting assistance to selected enterprises in order to establish an efficient system for the improvement of business activities and increase of sales in international markets.

The program will support the activities as in the following manner :

- free of charge assessment of enterprise performance, based on the method applied by the EFQM and other methods determining the field of business for the development, as well as specific activities which will generate guidelines for the expansion of the enterprise capacities. EFQM model, inter alia, enables enterprises to complete self-assessment with regard to the required standards and to develop a plan of action for improved business.

- the best 50 enterprises, out of the selected 80 from the beginning of the program, will be included in the intensive program phase, where direct technical assistance will be provided in line with the needs expressed by the enterprises, so that they will be allocated international experts for the recognized fields of business improvement.

- enterprises will participate in specialized sale fairs – “Meet the Buyers” where they will have an opportunity to directly talk to representatives of buyers, multinational companies.
- enterprises will be given a chance to participate in specialized trainings organized with the intention to enable them to directly satisfy the needs of the enterprise.

2 . Award “Exporter of the Year”:

The distinguished award, Exporter of the Year, promotes successes of domestic companies in exporting goods and services to foreign markets. This ceremony was first held in 2004. The winner announcement ceremony is attended by the Government of the Republic of Serbia, representatives of the diplomatic core, international financial institutions, as well as domestic and foreign companies. Since 2010, the award has been given in five categories: Exporter of the Year, the Best Export Product, Conquering the New Market, the SME Exporter of the Year and the Best Exporter in the Category of Corporate Social Responsibility. Criteria based on which the prizes are awarded include quality of the product, export markets and exported quantities, i.e. the value of goods and services within a year. The committee for application evaluation has 6 members, representatives of the highest state institutions. Award winners receive not only media affirmation, but also the right to use the logo of the Exporter of the Year in promotional campaigns.

3.Project “Redesign – Creating New Brands”:

Based on SIEPA’s activities, in the domain of export promotion of small and medium-sized enterprises, and improvement of business environment, the project “Redesign – Creating New Brands” has been implemented since 2009, with the aim to create new Serbian brands and connect the economic and educational institutions. The purpose of the Project is to improve visual identity of exported products as well as to offer professional training to the higher education staff, based on examples from practice. Besides the visual modification of products of those companies participating in the project, the goal is also to raise public awareness toward the importance of packaging, as well as to encourage direct cooperation of the economic and educational institutions. This Project allows interested companies to receive quality product packaging, while design students accomplish their creative ideas. Creating packaging in line with international trends surely is one of the major conditions for a product to be distinguished, particularly in a situation where domestic market is opening and a growing number of products are seeking their chance in foreign markets. In view of the fact that Serbia has many young designers, this Project will enable the economy to use their potential to some extent. When selecting products, the expert commission is guided by balanced geographic distribution, business results of an enterprise, the level of the required product packaging design and brand recognisability, giving priority to consumer goods.

4.Preparing local self-governments to attract foreign direct investments

Since five years ago SIEPA recognized the weaknesses and potentials of Serbian local self-governments, as well as their importance in the creating the business and investment climate in Serbia. i.e. investment conditions in the Republic of Serbia. Through the specific on sight work with investors, as well as direct work with local self-government units, it was clearly indicated that there were weaknesses in doing business with investors, especially in the part related to the location preparedness for Greenfield investments, presentation of local self-governments potentials, etc. To that effect, in 2005, in cooperation with the Standing

Conference of Towns, SIEPA initiated the Project “*FDI Investment Outreach*”, supported by UNDP. Work on the Project was founded on concrete activities with local self-government representatives, i.e. one-day seminars where they had an opportunity to learn about the important aspects of attracting foreign direct investments, the manner of dealing with investors, recognizing and representing the local self-government potentials. The Goal of the Project was to prepare local self-government representatives and make them aware of their potentials, as well as weaknesses, as to be able to attract potential investors in an appropriate manner. The Project included the complete territory of Serbia proper, with seminars taking place in bigger centres to which representatives of smaller local self-government units were coming. Results of the work with local self-government representatives were excellent, given that majority of the representatives for the first time had a chance to learn about the work of SIEPA, as well as about the term of foreign direct investments. For those seminars SIEPA prepared special publications which were handed out free of charge to local self-governments, focusing on foreign direct investments, and general and the most important information on investment conditions in the Republic of Serbia, and generally about opportunities for local investment conditions improvement. Results of this work were soon visible since local self-governments then knew where and who to address regarding foreign direct investments, preparation of promotional and educational publications, as well as gaining the basic knowledge about foreign direct investments, the manner of dealing with investors and generally about comprehensive preparedness for the arrival of new investments.

SIEPA continued dealing with local self-governments and assisting them in preparations for the communication with potential investors. Likewise, SIEPA and representatives of the World Bank jointly worked under the World Bank Project “*Serbia Investment Promotion Program*” SIEPA, worked on the Project “*Local Investment Promotion Consultant*” with the aim to establish a network of employees in local self-governments, specialized for dealing with foreign investors. The program was a continuation of the previous project “*FDI Investment Outreach*” which was used as a model. Work was organized through seminars for local self-government representatives, related to the improvement of business and investment conditions in local self-governments. Goal of the Project was actually to create a network of consultants and specialists with adequate know how and required skills educated and certified by the World Bank and SIEPA to work with foreign and domestic investors alike. The Project included all local self-government units in Serbia proper, and was excellently accepted by the participants. It is important to mention that majority of seminar participants were the ones from the previous Project “*FDI Investment Outreach*”, thus accomplishing a continuity and creating a network of economy specialists for foreign direct investments. This certification program, at the end of the seminar, was combined with the project *MEGA - USAID*, i.e. NALED, and the certification process was carried out together with this project. The project has been successful given that it additionally strengthened the offices for economic development located in a number of local self-governments, at the same time empowering the local self-government capacities, so that they have become readier and more organized to await for investors, they have learned the basics about promotion, and generally have a clearer picture about the manner how economy and investment conditions in this environment can be improved, and primarily have become aware that the outcome of their work, knowledge and efforts could be economic development.

5. Promotion of the Republic of Serbia as an investment destination

One of SIEPA’s priority tasks is the promotion of the Republic of Serbia as an investment location. To that effect SIEPA has been creating and implementing many activities aimed at presenting the economic, geographic and other values of Serbia, as an investment location. Those activities include organization of different promotion seminars and conferences,

participation in investment conferences and investment fairs, cooperation with corresponding institutions in other countries and information exchange as to assist the interested businessman take business decisions, preparation and development of different informative leaflets and monthly publications, organization and maintenance of databases on investment locations and potential suppliers. In order to accomplish its goals SIEPA cooperates with different domestic and international organizations such as the World Bank, through the program for the promotion of West Balkan countries, *“Invest in the Western Balkans”*, *OECD* and *UNDP*, jointly organizing seminars and promotion conferences. In cooperation with similar organizations abroad, SIEPA strives to organize promotion seminars where business opportunities in Serbia are presented to interested parties. . SIEPA has organized such events in almost all EU countries so far. Consequently, the image of Serbia, as an investment location, has significantly improved, resulting in corresponding increase of questionnaires coming to SIEPA, in connection with country’s investment potentials.

Main impediments in doing business

Here are only some of the impediments indicated in the course of implementation of Comprehensive Regulatory Reform: bureaucratized procedures, poor payment for the receivables, unresolved ownership and legal issues, unqualified staff, obsolete technology and insufficient innovation implementation in practice.

Summing up the remarks SIEPA has been receiving from investors and in reference to the “White Book”, annually published by the Foreign Investors Council, we point at the following impediments in doing business in the Republic of Serbia: unpredictable state policy negatively affecting business conditions, heavy bureaucracy, unclear ownership regulations and extensive procedure for the establishment, as well presence of the monopoly and oligopoly in some economy sectors: New Law on Protection of Competition, which has been implemented since 1 November 2009, undoubtedly resulted in certain improvement in the protection of competition in the Republic of Serbia. However, expected progress in the implementation of regulations on protection of competition has not yet been satisfactory.

27. Trade:

a) Please provide information on the main trading partners (for both merchandise imports and exports) and the overall structure of trade by sector.

Tables presenting trade flows of the Republic of Serbia, by countries and economic groups, and by trade structure, for the period 2007-2010/10m, are given under Chapter 30 – External Relations, under answer to the question number 3, Annex 30.

Since 2001 Serbia has been consistently recording growth of the total trade. The highest growth rate of 41.4% was accomplished in 2006. Due to the influence of the global economic crisis, a drop in exports of 19.8% was recorded in 2009. Overall exports in this period reported increase by more than three times.

The highest import growth rate of 31.9% was accomplished in 2001, while drop in imports of 2.1% and 30.2% was recorded in 2005 and 2009. Since 2001, imports increased 2.5 times. Coverage rate of imports by exports has been increased from less than 40% to 50%, as of 2009. In the observed period the Republic of Serbia recorded continuous deficit in foreign trade, with the highest deficit amount of EUR 8 billion, in 2008.

Foreign trade in goods in the Republic of Serbia in the period 2001 – 2010/10 months

in millions of EUR²¹

| Year | Export | Export index | Import | Import index | Balance | Coverage of imports by exports % |
|----------------|--------|--------------|--------|--------------|---------|----------------------------------|
| 2001 | 1,896 | 112.9 | 4,758 | 131.9 | -2,862 | 39.85 |
| 2002 | 2,192 | 115.6 | 5,919 | 124.4 | -3,727 | 37.04 |
| 2003 | 2,442 | 111.4 | 6,589 | 111.3 | -4,147 | 37.07 |
| 2004 | 2,832 | 115.9 | 8,623 | 130.9 | -5,792 | 32.84 |
| 2005 | 3,608 | 127.4 | 8,439 | 97.9 | -4,831 | 42.76 |
| 2006 | 5,102 | 141.4 | 10,463 | 124 | -5,361 | 48.76 |
| 2007 | 6,432 | - | 13,507 | - | -7,075 | 47.62 |
| 2008 | 7,428 | 115.5 | 15,494 | 114.7 | -8,066 | 47.94 |
| 2009 | 5,961 | 80.2 | 11,505 | 69.8 | -5,544 | 51.81 |
| 2010/10 months | 5,958 | 121 | 10,230 | 108.2 | -4,272 | 58.24 |

Source: Statistical Office of the Republic of Serbia

Drop in total trade in 2009 was caused by the world economic crisis, primarily by the drop in primary products prices in the world market, constituting a substantial part of the export structure of the Republic of Serbia, as well as by decrease of domestic industrial production.

On the other hand, in the first ten months 2010, resulting from a slight recovery of the international and domestic economy, there was a growth of exports by 21%, and imports by 8.2%, compared to the same period 2009. The import export coverage increased to 58.2% in this period. Prediction is that this recovery trend will continue in the coming period.

Trade exchange structure

Ten CT chapters with the highest share in exports of the Republic of Serbia (about 49%) in 2009 are in table 1:

Table 1

| Chapter s | Description | Exports in EUR 000 | Share |
|-----------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------|-------|
| 72 | Iron and steel: | 479,341 | 8.04 |
| 85 | Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and accessories of such articles | 456,583 | 7.66 |
| 84 | Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof | 376,549 | 6.32 |

²¹ Statistics based on the new methodology have been available only since 2007, whereas data on the preceding years were derived based on the methodology of “moderated definition” (this is the reason why the data on the growth index in 2007 are not available). Chapter 30 –External Economic Relations, answer to the question number 3, include statistics on trade flows, both based on the old and new methodology.

| | | | |
|----|------------------------------------------------------------------------------------------------------|---------|------|
| 27 | Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes | 277,683 | 4.66 |
| 39 | Plastics and articles thereof | 271,036 | 4.55 |
| 10 | Cereals | 233,401 | 3.92 |
| 8 | Edible fruit and nuts; peel of citrus fruit or melons | 229,247 | 3.85 |
| 74 | Copper and articles thereof | 222,524 | 3.73 |
| 62 | Articles of apparel and clothing accessories, not knitted or crocheted | 192,357 | 3.23 |
| 61 | Articles of apparel and clothing accessories, knitted or crocheted | 189,463 | 3.18 |

Major exporting products of the Republic of Serbia in 2009 were: corn (3.1% of the total world export), raspberries (2.5%), electrical power (2.4%), tinplate (1.8%), new pneumatic tires for passenger car (1.8%), sugar (1.6%), other men clothes, parts for electric motors and electric iron and steel generators, tights, medicines, paper and carton and floor covers.

Top ten CT chapters with the highest share in imports of the Republic of Serbia (about 50%) in 2009 are in table 2:

Table 2

| Chapter s | Description | Imports in EUR 000 | Share |
|------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------|--------------|
| 27 | Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes | 1,711,789 | 14.88 |
| 84 | Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof | 987,214 | 8.58 |
| 85 | Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and accessories of such articles | 727,730 | 6.33 |
| 87 | Vehicles other than railway or tramway rolling stock, and parts and accessories thereof | 533,653 | 4.64 |
| 39 | Plastics and articles thereof | 476,420 | 4.14 |
| 48 | Paper and paperboard; articles of paper pulp, of paper or of paperboard | 303,038 | 2.63 |
| 72 | Iron and steel: | 299,404 | 2.60 |
| 30 | Pharmaceutical products | 253,813 | 2.21 |
| 73 | Articles of iron or steel | 221,362 | 1.92 |
| 90 | Optical, photographic, cinematographic, measuring, checking, precision, medical or surgical instruments and apparatus; parts and accessories thereof | 198,184 | 1.72 |

Major importing products of the Republic of Serbia in 2009 were oil (7.1% of the total world import of the Republic of Serbia), natural gas (4 %), passenger vehicles (2.3%), medicines (1.3%), coke (1.2%), electrical power, mobile phones, cathodes, TV sets and coffee.

In the first ten months 2010, import and export structure remained relatively unchanged.

Trade partners:

On the export side,, the EU members have been the main trading partner of the Republic of Serbia. The EU's share in the total exports of the Republic of Serbia was 54% in 2009. Besides the EU, the Republic of Serbia has been realizing the most of its export to CEFTA members – B&H, Montenegro, Macedonia and the Russian Federation.

On the import side, besides the EU members, which again are the main trading partners of the Republic of Serbia with 57% of the imports from the world in 2009, the biggest trading partners are the Russian Federation, China, B&H, Croatia and the USA.

In the overall trade, by economic groups, the share of the EU in 2009 was 55.7%, followed by the CEFTA (16%) and the CIS – former Soviet Union countries (12%). This trend was the same in the first ten months of 2010.

b) How has the trade integration with the EU developed over time? What are the main EU trading partners and products? How has the export structure changed? Are there indications of a shift from resource- or labour-intensive to capital- or technology-intensive products?

How has the trade integration with the EU developed over time?

The Republic of Serbia has enjoyed the preferential status for export of goods to EU since 2001, due to the Autonomous Trading Measures (ATM), approved by the EU by the Council's Regulation no. 2007/2000, thus allowing free export of goods originating from the Republic of Serbia to the EU market (except wine, some fish products, beef and sugar).

Those measures were extended in 2005, and intended to have effect until 31 December 2010, but when the Interim Trade Agreement took effect (ITA), they were replaced by the provisions of the Agreement.

The Republic of Serbia and the EU signed on 31 March 2005 the Textile Agreement ("Official Gazette of the RS", number 45/05), which took effect on 1 July 2005. This Agreement is of multiple importance and economic significance as its application established free trade in textile products. Agreement abolished all restrictions in trading textile products with all EU members, whereby textile products of Serbian origin were given duty free status. The term of diagonal cumulation of goods origin is introduced (textile products made of basic materials and accessories provided from any of the EU countries have duty free status when exported to the EU). On the other hand, the Agreement foresees gradual reduction of customs rates for textile products imported in the Republic of Serbia and originating from the EU. Since 1 January 2008, adhering to the predicted dynamics, textile products originating from the EU have duty free status on the market of the Republic of Serbia.

Negotiations on the Stabilisation and Association Agreement (SAA) started on 10 October 2005. The first round of technical negotiations took place in November 2005, and the final round ended on 10 September 2007. The Agreement was endorsed on 7 November the same year.

Stabilization and Association Agreement and the ITA were signed on 29 April 2008, in Brussels.

On 9 September 2008, the Parliament of the Republic of Serbia ratified the SAA. On 16 October Serbian Government unilaterally adopted the decision on implementation of the Interim Agreement with the EU and started its full implementation as of 1 January 2009.

In December 2009, the EU Council adopted the decision to immediately start implementation of the Interim Trade Agreement, which officially took effect on 1 February 2010.

Government of the Republic of Serbia adopted the Decision to establish the bodies as foreseen by the Agreement, and on 5 February 5 sub-committees were established charged with the implementation of the Interim Agreement with the EU, as follows: Sub-committee for trade, industry, customs, taxes and cooperation with candidate countries, Sub-committee for agriculture and fishery, Sub-committee for internal market and protection of competition, Sub-committee for economic and financial issues and statistics and Sub-committee for transportation.

The first meeting of the Sub-committee for trade, industry, customs, taxes and cooperation with candidate countries was held on 22 June 2010, where it was acknowledged that there existed a satisfactory level of the ITA implementation, as well as a positive trend in the trade relations between the Republic of Serbia and the EU.

What are the main EU trading partners and products?

Tables presenting detailed exchange between the Republic of Serbia and the EU, by state members, as well as the exchange by trade structure, for the period from 2007 until 2010 (first ten months) are included under Chapter 30 – External Relations, answer to the question number 3, Annex 30.

As here above mentioned, the EU is the major trade partner of the Republic of Serbia. In the period from 2001 until 2010, there has been a continued growth in the scope of the trade in goods. The highest export growth rate of 39% was recorded in 2006, while the highest import growth rate of 30% was recorded in 2004. In the observed period the Republic of Serbia recorded continuous deficit in trade with the EU, with the highest deficit amount of EUR 5 billion, in 2008.

In the period 2001 – 2010/10 months the EU had continuously high share in the overall trade with the Republic of Serbia, with average share of about 50%. Export to the EU in 2009 amounted 54% of the total exports of the Republic of Serbia, while share of imports was 57%.

Trade in goods between the Republic of Serbia and the EU in the period 2001 – 2010/10 months(in millions of EUR²²)

| Year | Export | Export index | Import | Import index | Balance | Coverage of imports by exports % |
|------|--------|--------------|--------|--------------|---------|----------------------------------|
| 2001 | 1,104 | 121 | 2,740 | 123 | -1,636 | 40.29 |
| 2002 | 1,305 | 118 | 3,530 | 129 | -2,225 | 36.97 |
| 2003 | 1,316 | 100 | 3,842 | 109 | -2,526 | 34.25 |
| 2004 | 1,604 | 122 | 5,000 | 130 | -3,396 | 32.08 |
| 2005 | 2,116 | 132 | 4,577 | 92 | -2,461 | 46.23 |
| 2006 | 2,962 | 139 | 5,696 | 125 | -2,734 | 52.00 |
| 2007 | 3,603 | - | 7,687 | - | -4,084 | 46.87 |

²² Statistics based on the new methodology have been available only since 2007, whereas data on the preceding years were derived based on the methodology of “moderated definition” (this is the reason why the data on the growth index in 2007 are not available). Chapter 30 – External Relations, answer to the question number 3, include statistics on trade flows, both based on the old and new methodology.

| | | | | | | |
|-----------------------|--------------|--------------|--------------|--------------|---------------|--------------|
| 2008 | 4,029 | 112 | 9,073 | 118 | -5,044 | 44.41 |
| 2009 | 3,196 | 79.3 | 6,533 | 72 | -3,337 | 48.92 |
| 2010/10 months | 3,411 | 130.8 | 5,764 | 106.6 | -2,353 | 59.18 |

Source: Statistical Office of the Republic of Serbia

As a result of the world economic crisis, drop in exports to the EU by 20.7% was recorded in 2009, as well as drop in import by 28%. However, in the first ten months of 2010, resulting from the reviving of the world and domestic economy, and from mutual implementation of the ITA, export from the Republic of Serbia to the EU increased by 30.8%, and import by 6.6%, compared to the same period 2009. The effect of this was the coverage of imports by exports of 59.2%, being the highest value since 2001.

According to distribution within the EU member states in 2009, the biggest export partners of the Republic of Serbia were Germany (19,5% from overall export to the EU and 10,5% from the world export) and Italy (18,3% from the overall export to the EU and 9,8% from the overall world export), then Romania (10,7%), Slovenia (7,7%), Austria (6,5%), Hungary (5,7%) and France (5,6%).

In the first ten months of 2010, this order was almost the same, whereas Italy was in the lead with even 20.1 % in the overall export from the Republic of Serbia to the EU and 11.5% in world export, instead of Germany which was second, with 18,4% in the overall export to the EU.

Regarding imports, the first ranking trade partner of the Republic of Serbia from the EU was again Germany (21.6% in the overall import from the EU, that is 12.2% in the overall world import), followed by Italy (17% in the overall import from the EU, that is 9.7% in the overall world import), Hungary (7.1% in the import from the EU), Austria (5.9%), Slovenia (5,8%), and Romania (5,8%).

In the first ten months of 2010, Germany remained to be the first with 19% in the overall import from the EU, that is 10.7% in the overall world import, whereas second was Italy (15.2% in the overall import from the EU), followed by Hungary (8.8%), Romania (6.2%), Bulgaria (6.1%) and Slovenia (5.4%).

In 2009, the Republic of Serbia recorded trade exchange deficit with all EU members, except Cyprus, Portugal, Malta, Latvia and Lithuania, where low scope surplus was realised.

Trade exchange structure

The Republic of Serbia in 2009, exported mostly corn to the EU (5% in the total export to the EU), raspberries (4.5%), new pneumatic tyres for passenger cars (2.9%), parts for electro motors and electric generators of iron and steel (2,8%), sugar (2.8%), tights (2.6%), tinplate (2.4%), electrical power, other products of iron and steel, and other fruits.

In 2009 the Republic of Serbia imported from the EU mostly passenger cars (3,4% in the overall import from the EU), medicines (1.7%), cathodes (1.2%), oil from oil and bituminous minerals (1.2%), intermediary goods of iron (1.1%), wash and clean preparations (0.7%), mobile phones and TV sets.

As here above mentioned, major trade partners of the Republic of Serbia are Germany and Italy. As regards the export structure, the products we export to Germany are mostly spare parts for machines, raspberries, tights, pneumatics and medicines, and to Italy tights, conductor sets for ignition, plates, sheet plates, coil tapes and parts for shoe covers. On the other hand, products we import for the most part from Germany are passenger cars and medicines, and from Italy tights and nylon fibre. Exported for the most part to Romania are corn, sugar and propylene, and imported are fuels and electric power. The most imported from Austria are spare parts for machines and medicines.

Trade in textile products

Overall trade in textile products in 2008 reached EUR 628 million, which is the highest amount recorded in the last years. However, due to the world economic crisis, exports of textile products from the Republic of Serbia to the EU 27 in 2009 decreased by 10.6%, and imports decreased by 12.3%.

In the first ten months of 2010, there was growth in export compared to the same period last year, by 5.5%, while import drop in the same period was less than 2%.

Considering the share of textile products in overall trade with the EU, growth in export share from 7.9% (2008) to 8.9% (2009) may be noted, followed by share growth of imported textile products from the EU in the overall import from the EU from 3.4% (in 2008) to 4.2 % (in 2009).

In the observed period, the Republic of Serbia recorded continuous positive balance in textile products trade with the EU, except in the period 2004-2006. The highest surplus was realised in the first ten months of 2010, of EUR 25 million.

Trade in textile products Serbia EU 27, in the period 2007 – 2010/10months in millions of EUR²³

| Year | Export | Export index | Export share in overall export to the EU | Import | Import index | Import share in overall import from the EU | Overall trade: | Balance | Coverage of imports by % |
|-------------|---------------|---------------------|-------------------------------------------------|---------------|---------------------|---------------------------------------------------|-----------------------|----------------|---------------------------------|
| 2001 | 194 | 141.61 | 17.57 | 136 | 140.21 | 4.95 | 330 | 58 | 142.65 |
| 2002 | 161 | 82.99 | 12.38 | 151 | 111.03 | 4.28 | 312 | 10 | 106.62 |
| 2003 | 156 | 96.89 | 11.84 | 143 | 94.7 | 3.72 | 299 | 13 | 109.09 |
| 2004 | 124 | 79.49 | 7.74 | 237 | 165.73 | 4.74 | 361 | -113 | 52.32 |
| 2005 | 193 | 155.64 | 9.11 | 248 | 104.64 | 5.42 | 441 | -55 | 77.82 |
| 2006 | 250 | 129.53 | 8.54 | 296 | 119.35 | 5.19 | 546 | -46 | 84.46 |
| 2007 | 315 | - | 8.74 | 301 | - | 3.92 | 616 | 14 | 104.6 |

²³ Statistics based on the new methodology have been available only since 2007, whereas data on the preceding years were derived based on the methodology of “moderated definition” (which is why we do not have available the data on the growth index in 2007). Chapter 30 – Foreign Economic Relations, answer to the question number 3, include statistics on trade flows, both based on the old and new methodology.

| | | | | | | | | | |
|-----------------------|------------|---------------|-------------|------------|---------------|-------------|------------|-----------|--------------|
| 2008 | 318 | 100.95 | 7.89 | 310 | 102.99 | 3.42 | 628 | 8 | 102.6 |
| 2009 | 286 | 89.94 | 8.95 | 272 | 87.74 | 4.16 | 558 | 14 | 105.1 |
| 2010/10 months | 246 | 105.5 | 7.22 | 221 | 98.05 | 3.83 | 467 | 25 | 111.3 |

Source: Statistical Office of the Republic of Serbia

How has the export structure changed? Are there indications of a shift from resource- or labour-intensive to capital- or technology-intensive products?

Comparing export of the Republic of Serbia to the EU in 2001 and 2009 it is notable that change took place in export structure. Mainly, the products with the highest share in export in 2001 were textile products, fruit, footwear and rubber products, whereas in 2009, leading products were iron, steel, electric machines and mechanical devices and medicines. Here above mentioned data indicate that there has been shift in export structure from labour-intensive to capital- intensive products. This change resulted from foreign and domestic investments since 2001 in the sectors with presently highest share in export.

| Top 10 chapters for export to the EU - 2001 | | | | Top 10 chapters for export to the EU - 2009 | | | |
|---------------------------------------------|-------------------------------------------------------------------------------|---------|-----------|---------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------|---------|-----------|
| Ch apt er | Description | Exports | Shar e | Ch apt er | Description | Exports | Sha re |
| 62 | Articles of apparel and clothing accessories, not knitted or crocheted | 126,677 | 11.5 | 72 | Iron and steel: | 347,893 | 10.9 |
| 8 | Edible fruit and nuts; peel of citrus fruit or melons | 88,911 | 8.1 | 85 | Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders | 323,828 | 10.1 |
| 64 | Footwear, gaiters and the like; parts of such articles | 71,728 | 6.5 | 84 | Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof | 188,319 | 5.9 |
| 40 | Rubber and articles thereof | 70,360 | 6.4 | 8 | Edible fruit and nuts; peel of citrus fruit or melons | 185,666 | 5.8 |
| 72 | Iron and steel: | 63,228 | 5.7 | 10 | Cereals | 170,665 | 5.3 |
| 74 | Copper and articles thereof | 54,402 | 4.9 | 61 | Articles of apparel and clothing accessories, knitted or crocheted | 169,151 | 5.3 |
| 44 | Wood and articles of wood; wood charcoal | 47,140 | 4.3 | 74 | Copper and articles thereof | 150,856 | 4.7 |
| 17 | Sugars and sugar confectionery | 43,349 | 3.9 | 40 | Rubber and articles thereof | 147,348 | 4.6 |
| 84 | Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof | 42,646 | 3.9 | 76 | Aluminium and articles thereof | 129,772 | 4.1 |
| 39 | Plastics and articles thereof | 41,694 | 3.8 | 39 | Plastics and articles thereof | 112,011 | 3.5 |

Source: Statistical Office of the Republic of Serbia

Data on trade with the EU by the SITC classification also indicate that in the period 2007-2009 Serbian export of capital-intensive was greater than of labour-intensive products.

**Chart presenting export and import of capital-intensive and labour-intensive products
to and from the EU according to the SITC**

| in EUR 000 | | 2007 | | 2008 | | 2009 | | 2010/10 months | |
|------------------------------------------|--------------------------------------------------------------------------------------------------|-----------|-----------|-----------|-----------|---------|-----------|----------------|-----------|
| SIT C | Capital-intensive products | Export | Import | Export | Import | Export | Import | Export | Import |
| 11 | Beverages | 4,282 | 11,489 | 7,010 | 15,525 | 12,044 | 16,225 | 9,982 | 10,450 |
| 12 | Tobacco and tobacco manufactures | 5,868 | 9,283 | 6,968 | 14,007 | 17,185 | 18,531 | 13,443 | 12,294 |
| 35 | Electric current | 10,354 | 85,635 | 8,007 | 85,910 | 52,676 | 34,935 | 68,502 | 37,447 |
| 53 | Dyeing, tanning and colouring materials | 8,084 | 95,090 | 5,464 | 98,073 | 3,612 | 80,640 | 2,519 | 72,547 |
| 55 | Essential oils and resinoids and perfume materials; toilet, polishing and cleansing preparations | 22,859 | 186,013 | 25,061 | 202,935 | 24,189 | 185,429 | 21,161 | 157,512 |
| 62 | Rubber manufactures, n.e.s. | 164,761 | 65,534 | 161,415 | 81,124 | 135,793 | 59,455 | 140,971 | 63,440 |
| 67 | Iron and steel | 628,141 | 270,644 | 758,401 | 272,031 | 349,710 | 220,085 | 484,913 | 234,695 |
| 68 | Non-ferrous metals | 404,382 | 263,662 | 354,664 | 273,129 | 227,883 | 188,407 | 333,138 | 236,569 |
| 78 | Road vehicles | 39,582 | 531,768 | 54,177 | 608,079 | 65,342 | 436,964 | 73,999 | 280,212 |
| TOTAL: | | 1,288,313 | 1,519,118 | 1,381,167 | 1,650,813 | 888,434 | 1,240,671 | 1,148,628 | 1,105,166 |
| Share in overall export/import to the EU | | 35.76 | 19.76 | 34.28 | 18.19 | 27.80 | 18.99 | 33.68 | 19.17 |

Source: Statistical Office of the Republic of Serbia

| in EUR 000 | | 2007 | | 2008 | | 2009 | | 2010/10 months | |
|------------|---------------------------------------------------------------------------------------------------------------------|---------|---------|---------|---------|---------|---------|----------------|---------|
| SIT C | Labour-intensive products | Export | Import | Export | Import | Export | Import | Export | Import |
| 26 | Textile fibres (other than wool tops and other combed wool) and their wastes (not manufactured into yarn or fabric) | 876 | 10,324 | 759 | 8,403 | 683 | 6,149 | 1777 | 5,897 |
| 61 | Leather, leather manufactures, n.e.s., and dressed furskins | 6,290 | 67,373 | 6,290 | 70,079 | 7,329 | 54,269 | 7,430 | 50,807 |
| 63 | Cork and wood manufactures (excluding furniture) | 41,723 | 109,052 | 40,384 | 116,698 | 26,830 | 86,783 | 26,190 | 66,899 |
| 64 | Paper, paperboard and articles of paper pulp, of paper or of paperboard | 44,139 | 245,855 | 48,201 | 268,064 | 59,085 | 228,048 | 63,769 | 203,181 |
| 65 | Textile yarn, fabrics, made-up articles, n.e.s., and related products | 29,028 | 186,720 | 29,493 | 179,714 | 30,571 | 164,186 | 27,484 | 142,168 |
| 66 | Non-metallic mineral manufactures, n.e.s. | 59,683 | 144,977 | 65,132 | 152,432 | 32,228 | 106,817 | 29,766 | 94,120 |
| 69 | Manufactures of metals, n.e.s. | 165,304 | 245,637 | 150,941 | 285,168 | 117,634 | 190,927 | 111,201 | 164,779 |
| 81 | Prefabricated buildings; sanitary, plumbing, heating and lighting fixtures and fittings, n.e.s. | 6,137 | 47,832 | 8,486 | 49,991 | 8,441 | 28,946 | 6,782 | 19,030 |
| 82 | Furniture, and parts thereof; bedding, mattresses, mattress supports, cushions and similar stuffed furnishings | 57,165 | 57,316 | 53,840 | 59,356 | 52,521 | 47,027 | 53,475 | 34,995 |
| 83 | Travel goods, handbags and similar containers | 861 | 5,586 | 870 | 4,666 | 722 | 2,477 | 555 | 1,887 |
| 84 | Articles of apparel and clothing accessories | 285,612 | 109,687 | 288,147 | 127,712 | 252,326 | 106,238 | 217,699 | 76,298 |
| 85 | Footwear | 122,289 | 41,565 | 126,858 | 43,966 | 99,414 | 31,264 | 93,544 | 27,490 |
| 89 | Miscellaneous manufactured | 57,877 | 175,552 | 76,162 | 186,381 | 67,858 | 158,472 | 56,488 | 123,395 |

| | | | | | | | | | |
|------------------------------------------|------------------|---------|-----------|---------|-----------|---------|-----------|---------|-----------|
| | articles, n.e.s. | | | | | | | | |
| TOTAL: | | 876,984 | 1,447,476 | 895,563 | 1,552,630 | 755,642 | 1,211,603 | 696,160 | 1,010,946 |
| Share in overall export/import to the EU | | 24.34 | 18.83 | 22.23 | 17.11 | 23.64 | 18.55 | 20.41 | 17.54 |

Source: Statistical Office of the Republic of Serbia

Characteristics of foreign trade exchange of goods are presented in Annex.

VI Financial markets

A. General

28. Please indicate how interest rates are determined? Are any rates administratively set? If so, which ones?

Executive Board of the National Bank of Serbia determines the level of key interest rate. The key interest rate is the highest, i.e. the lowest interest rate applied by the National Bank of Serbia in repo transactions, i.e. purchase of securities with the two-week maturity term. Interest rates corridor is determined according to the key interest rate, i.e. the highest and the lowest interest rate of the National Bank of Serbia applied in money market operations (lending facility interest rate and deposit facility interest rate).

Commercial banks determine interest rates level according to the business policy of the bank, based on the market principles. The only exception are the state subsidized loans approved within the scope of the Government Program aimed at mitigating the effects of the global economic crisis, which has been implemented in cooperation with the business banks. The Program provides for the state to finance a portion of expenses arising from the newly approved corporate and retail loans. An ultimate beneficiary does not pay the entire market interest rate for the funds disbursed, but only a portion of market rate, while the rest is financed by the state. This program has been implemented since 2009, with the annual realization. The state has continued to implement the program of subsidized loans in 2010, but with decrease in level of interest rate limitations.

29. Do quantitative ceilings exist on credit expansion? What instruments are available to prevent excessive credit growth and potential exchange rate volatility from eroding the quality of lenders' portfolios?

Currently there are no quantitative limitations in relation to the loan activity. There are still certain limitations with respect to retail financing: the amount of monthly installment cannot exceed 30% of the personal monthly income, and the last installment of a mortgage loan must be repaid before reaching 63 years of age. Limitations that were previously in place (total approved retail loans could not exceed 200% of the bank's capital, and prescribed maximum maturity terms for cash and consumer loans), have been suspended in the scope of measures aimed at mitigating the adverse effects of global economic crisis.

In order to prevent the portfolio erosion due to exchange rate volatility, the banks approve FX currency hedged loans (cca. 80% of the total loan portfolio consists of foreign currency hedged loans). The banks are also protecting by calculating due loan installments according

to the official middle rate of the NBS applied on the repayment due date, and if the rate in question is lower than the rate per which the loan has been initially approved, the basis for calculation shall be the rate valid on the loan approval date (though presents it is still not widely accepted practice among banks).

Because of a considerable slackening in the loan activity of banks, resulted from the adverse effects of global financial crisis, the decision was made to suspend one of the key ratios of the credit activity limitation. Namely, it is a gross retail loans / core capital ratio (Tier 1). Initially, this ratio was establish at the level not exceeding 200%, but reduced to the level of 150% in the time of a distinct loan growth. At the moment, having in mid the consequences of economic crisis and unfavorable macro-economic trends, the decision was made for the ratio referred to above to be suspended (as at June 2009). On the other hand, large exposure limit ratio totaling to maximum 400% of the total regulatory capital is still in effect. A brief overview of all regulatory limitations is given in the following chart:

| Exposure Type | Limit | Note |
|--------------------------------------------------------------------------------------------------|------------------------|------------------------|
| Gross retail loans / Core capital | $\leq 200\%$ (150%) | Suspended in June 2009 |
| Sum of large exposures / Regulatory capital | $\leq 400\%$ | In effect |
| Exposure to one person (or group of related persons) / Regulatory capital | $\leq 25\%$ | In effect |
| Exposure to one person related to the bank / Regulatory capital | $\leq 5\%$ | In effect |
| Total exposure to persons related to the bank / Regulatory capital | $\leq 20\%$ | In effect |
| Investment in entities outside the financial sector / Regulatory capital | $\leq 10\%$ | In effect |
| Investments in entities outside the financial sector and non-current assets / Regulatory capital | $\leq 60\%$ | In effect |

In addition, one of the key instruments of the monetary policy, used very often as an instrument of regulation, i.e. limitation of excessive credit activity, is the required reserve of the National Bank of Serbia. In times of a strong loan growth, the required reserve was at the level of up to 45% on all FX funding sources (deposits from customers and borrowings). The most recent amendment to the decision on banks' required reserves held with the NBS, the percentage of set-aside was reduced to 25% on all FX and 5% on all Dinar funds (Dinar required reserve was reduced from the level of 10%).

High level of eurization of the Serbian economy makes it exposed to a higher risk from significant volatilities in the FX rate. The key after-effect of such situation has been the most obvious in the domain of the level and trends prevailing in banking sector NPLs. Due to a higher risk inherent to FX loans and advances (including the currency hedged loans), and considering that the majority of customers are not insured in terms of their net monthly income in the national currency, more rigorous criteria of classification and higher risk-weights have been structured for these banking loans from the very beginning. Though the explicit numeric limits for such loans have not been considered (until now), it is clear that due to more rigorous regulatory criteria with respect to FX and FX hedged loans, the loans in question are more expensive for the banks. In addition, more restrictive level of the ratio of customers' monthly liabilities and their monthly income makes it more difficult for retail customers to become exceedingly indebted. Established regulatory limits of a maximum 30%

of net monthly liabilities in relation to a net monthly income for each category of loans, except the mortgage loans, and the limit of maximum 50% should a mortgage loan be added to the total indebtedness of a customer, can be considered purposeful, considering precisely the high level of eurization and a high loan demand thus far. These limits, and particularly the effects of potential FX rate fluctuations on the ratio referred to above, must be taken into consideration by the banks when approving retail loans in foreign currency. The following table contains more details:

| Exposure Type | Risk weight |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------|
| Unsecured mortgage loans | Risk weight 75% instead of 50% |
| Unsecured loans | Risk weight 125% instead of 100% |
| <p><i>Note:</i> The banks must apply the Guidelines to Assess Effects of the FX Rate Changes to Customers' Credit Risk</p> <p>The bank that has no such document shall be under obligation to classify its customers into higher-risk categories and set aside higher amounts on the basis of</p> <p>loan loss provision. Also, the meaning of <i>(un)secured</i> in this context relates to a (non)existence of a customer's inflow in the same currency as</p> <p>the loan currency.</p> | |

30. Provide an assessment of access to the international financial markets by the state and by the private sector. On what financial terms? Please give examples.

During the preceding period, the Republic of Serbia financed its requirements in terms of the budgetary deficit funding, repayment of principal debt amount and project financing, through non-returnable international assistance, loans granted by the international financial institutions (World Bank, International Monetary Fund, European Bank for Reconstruction and Development, European Investment Bank, Council of Europe Development Bank, KfW etc.), bilateral loans, loans granted by non-state financial institutions – domestic and foreign banks, and issues of short-term securities on the national financial market.

Serbia's credit rating is BB- (according to the credit rating agencies Fitch and Standard&Poor's). Foreign investment banks did participate in tendering procedures to procure loans of the Republic of Serbia in the previous period. However, the state has not come out on the international debt covering market until now, although the interest of international investment banks, as brokers/dealers for such an operation, is very high. We estimate that Serbia could achieve a successful issue of EUR or USD hedged securities in the future.

The only bond of the Republic of Serbia currently traded on the international capital markets is the so called London Club bond, which is quoted on the Luxemburg stock market (ISIN XC0214240482), as a result of restructuring of debt of the Republic of Serbia arising from the obligations to the London Club creditors.

We could come to the conclusion that the Republic of Serbia, even though still almost unexposed to the international financial markets, has access to them, but so far it has mainly relied on favourable loans of multi-lateral institutions and issue of securities on national financial markets.

Private sector access to the international financial markets is reflected in significant growth of total external debt of the private sector (bank and corporate sector debt under cross-border loans) in the period from 2003 until the end of 2009.

From the outbreak of the global economic crisis in 2008 until present-day, total external corporate debt has been decreasing constantly, while the total bank sector debt constantly increased as a result of increase in long-term bank financing sources and decrease of short-term deposits taken by banks. Decrease of mandatory reserves on new bank borrowings affected the increase of bank sector debt.

Domestic banks have largely borrowed from parent banks or members of the same banking group. Out of total disbursements under corporate sector loans in 2010, approximately one half pertains to loans approved by foreign banks with subsidiaries operating in Serbia, the other half is divided evenly among inter-company loans and loans approved by other creditors respectively (suppliers, strategic partners as well as international financial organizations that mostly finance small and medium enterprises).

31. If relevant, what are the legal arrangements concerning central bank credit to the private sector? If so, please quantify.

There is no legal framework concerning central bank (NBS) credit to private sector.

32. What are the main characteristics of the interbank clearing and settlement system? Please assess the functioning of these systems. Are there changes envisaged in the payments' system?

The National Bank of Serbia operates the interbank RTGS and Clearing System. RTGS system is a system of funds transferring in real time, by gross settlement principle. It avails with the standard functionalities, such as: waiting queue according to FIFO rule, assignment and change of priorities of transactions, real-time monitoring of accounts by the participants etc. Participants in the RTGS are all banks holding the operating licence of the National Bank of Serbia, the Ministry of Finance via consolidated treasury account, Central Securities Depository and Clearing House (operator of the system for securities settlement) and ancillary systems. Clearing system of the National Bank of Serbia is processing payments of up to 250,000 RSD, settling multilateral net positions in the RTGS system. RTGS has been appraised as fully compliant with the CPSIPS, in the scope of FSAP for Serbia.

There are clearing system for cheques and direct debits in the Republic of Serbia – operated by the Association of Serbian Banks, and the clearing system for DinaCard, national payment card, operated by the National Bank of Serbia. These systems are settled in RTGS. Net positions for RSD payments by international brand payment cards issued in Serbia are calculated in the companies in question, and such payments are settled in Dinars in RTGS of the National Bank of Serbia. Both RTGS and the NBS clearing system are highly reliable and efficient, which is demonstrated by the level of their availability ranged from 98,87% to 100% during the last 8 years.

The National Bank of Serbia oversees all systems referred to above in line with the Law on the National Bank of Serbia and the Decision on Oversight of Payment, Clearing and

Settlement Systems (*Official Gazette of RS* No 46/2009). In addition, the National Bank of Serbia defined the Payment System Oversight Policy, Guidelines for the Application of Principles for Effective Functioning of Payment Systems, and the Methodology for the Assessment of Payment System Compliance. All the systems referred to above have been established in line with the Law on Payment Transactions (*Official Journal of SRY* No 3/2002, *Official Journal of FRY* No 5/2003, and *Official Gazette of RS* No 43/2004 and No 62/2006) and regulations adopted on the basis of the Law in question. Systemically important payment system is the RTGS system of the National Bank of Serbia, appraised in the FSAP, while other systems have been classified as important systems.

The Ministry of Finance – Treasury Administration participates in the interbank clearing system and settlement based on the **Decision on the Settlement and Clearing and on Functioning of Clearing Accounts with the National Bank of Serbia** (*Official Gazette of RS* No 57/2004) and the relating Operating Rules based on the Decision in question. Operating Rules for Clearing (Net Settlement) Services and Operating Rules for Real Time Gross Settlement.

The Ministry of Finance – Treasury Administration, participates in the interbank clearing and settlement through consolidated treasury account kept with the NBS.

The consolidated treasury account is a joint treasury account of the Republic of Serbia and treasuries of the local authorities, through which payments are effected between beneficiaries of budgetary funds, mandatory social insurance funds and other beneficiaries of public funds, on one hand, and entities included in the banking system, on the other.

Messages exchanged within the system must meet the following main conditions:

- 1) SWIFT formatted;
- 2) Sent and received under terms and conditions established by the decision regulating electronic payments;
- 3) Sent in accordance with the Real Time Gross Settlement.
- 4) The system, operated by the NBS, is very stable, based on clear rules and procedures that follow occasional changes in terms of operating hardware and software update.

Complying of the national legislation with regulations of the European Union referring to the payment systems and services is underway.

B. The banking sector

(Detailed information is required in chapter 3 – Right of establishment and freedom to provide services)

33. Please describe the evolution of the banking sector (size, share in the economy) in the past five years.

A key phase in the process of Serbian banking sector restructuring and stabilization ended in the period 2000 – 2005. The number of banks was halved, from 81 in year 2000 to 40 banks at the end of 2005, through the procedures of consolidation, merger and acquisition, and particularly by takeover of majority shareholding in domestic private and “state” banks (privatization), and by revoking operating licenses to insolvent and illiquid banks. Ownership structure of the banking sector has been considerably changed by continuing the processes of consolidation after 2005. As of the end of October 2010, the banking sector consists of 33 banks – the majority holdings in 4 banks have been acquired by domestic legal entities and

natural persons, 8 “state” banks with the Republic of Serbia being directly or indirectly the controlling shareholder, while the controlling shares in 21 banks are held by foreign legal entities and natural persons. Foreign banks have 73,7% share in the balance sheet sum, 74,6% share in loans to customers, and 68,8% in deposits from customers of the banking sector. In addition, concentration in the sector is not significant, since the values of NNI in the most important segments of the banking activities do not exceed 724 units.

In the last five-year term (2006 – 2010), it is possible to identify intensive growth phase (during 2006 and 2007) and slower growth phase (as of 2008 onwards). In the first phase, balance growth was financed by an increase of deposit potential (in average 40,8%) and continually intensive capital increases (in average 62,0%), with somewhat smaller-scale relying on the loans from abroad (in average 22,1%). During the two years period referred to above the balance sheet assets doubled. Growth in banking sources of funds served as the basis for an intensive growth of the banks’ credit activity, with an average annual rate of 37,1%. The banks offered new types of products, with particularly intensive growth in payment card operations. At that, the banking sector remained highly liquid, solvent and profitable.

The beginning of 2008 was marked by a certain slowdown. First effects of the global economic crisis in Serbia, in the last quarter of 2008 occurred in a highly capitalized (CAR – 23,3%) and liquid sector of domestic banks (share of liquid assets in total 35%). Banks’ profitability recorded the highest rates in the last few years – with two-figure return on equity rate (ROE) and with the return on assets (ROA) coming to cca.3%²⁴

Reputation risk of foreign parent banks operating in Serbia instigated to a large extent spreading of the crises to the Serbian banking sector, in the form of mass withdrawal of (FOREX) retail deposits – only in October 2008, there was an outflow of cca. EUR 800 mil., and during the last quarter the total amount of EUR 971 mil. was withdrawn. However, so early as November, the outflowing trend slowed down, and by the end of December there was an increasing upturn. Deposit withdrawal induced significant depreciation pressures²⁵ and represented strong impact to FX liquidity of the banks. In addition, high FX exposure of banks particularly to the customers with no adjusted FX position meant a considerable growth of currency induced credit risk. These were the most important channels of manifestation of the crisis in the banking sector.

Nevertheless, the banks in Serbia managed to overcome the critical 2008 and 2009 with no major upheaval, owing to the previously formed significant liquidity and solvency reserves (largely conditioned by the strict prudential requirements), and partly due to support of their parent banks and timely regulatory response of the NBS (including the Vienna initiative).

| Amounts in million RSD | 31.12.06. | 31.12.07. | 31.12.08. | 31.12.09. | 31.10.10. |
|-------------------------------|------------------|------------------|------------------|------------------|------------------|
| | | | | | |
| Number of banks | 37 | 35 | 34 | 34 | 33 |
| Number of employees | 28,092 | 30,246 | 32,342 | 31,182 | 30,336 |
| | | | | | |
| Balance sheet sum | 1,169,271 | 1,563,746 | 1,776,955 | 2,160,411 | 2,473,952 |

²⁴ Data referring to the Q3 2008

²⁵ During the last quarter of 2008, Dinar depreciated by 15,7% in the nominal amount.

| | | | | | |
|--------------------------------|------------------|------------------|------------------|------------------|------------------|
| Off balance sheet items | 1,163,308 | 1,579,674 | 2,156,621 | 2,304,527 | 2,722,960 |
| | | | | | |
| Total loans | 577,474 | 857,829 | 1,068,597 | 1,201,274 | 1,533,901 |
| Companies | 315,929 | 431,169 | 534,128 | 622,200 | 747,245 |
| Retail | 195,222 | 301,328 | 393,684 | 419,904 | 517,591 |
| | | | | | |
| Deposits | 666,290 | 960,161 | 1,024,708 | 1,301,235 | 1,445,223 |
| Companies | 177,833 | 290,700 | 267,999 | 293,114 | 295,822 |
| Retail | 294,269 | 428,220 | 466,956 | 627,544 | 750,822 |
| | | | | | |
| Foreign loans | 186,246 | 133,953 | 151,697 | 210,522 | 295,306 |
| | | | | | |
| Capital | 216,288 | 328,493 | 420,011 | 447,487 | 491,735 |
| Capital stock and other | 182,562 | 272,846 | 332,849 | 340,740 | 361,015 |
| | | | | | |
| Financial result | 16,531 | 23,268 | 34,739 | 20,025 | 24,608 |
| ROE | 9.67% | 8.54% | 9.28% | 4.62% | 6.29% |
| ROA | 1.70% | 1.70% | 2.08% | 1.02% | 1.27% |
| | | | | | |
| CAR | 24.7% | 27.9% | 21.9% | 21.4% | 20.1% |

From the very beginning, the NBS reacted by numerous prudential and monetary measures – the required reserve policy was relaxed, exposure to FX risk limit was reduced, requirement related to calculation and setting aside the reserve for general banking risks in the conditions of intensive loan growth was suspended. At the same time, daily monitoring of the banks' liquidity was initiated.

In the beginning of 2009, the National Bank of Serbia, in the context of arrangements with the IMF, prepared the Program in Support of the Country's Financial Stability ("the Vienna Initiative"), with the aim of upholding public confidence in the banking sector and preserving financial and macro-economic stability. Special facilities of support were made available to those banks which, together with their majority shareholders, agreed to take certain measures (maintaining of exposure to the Republic of Serbia until the end of 2010 at the level from December 2008²⁶, maintaining of capital adequacy and banks' liquidity ratios at the prescribed level, enabling debtors to convert their FX loans and loans with FX clause into Dinar loans and to change terms of repayment in accordance with the defined frame. In the

²⁶ Namely, at the level of 80% of the said amount, in line with the subsequent changes to the arrangement, introduced in the spring of 2010.

period to follow, the prudential measures of the National Bank of Serbia were focused on supporting the liquidity i.e. solvency of banks and encouragement of credit growth.²⁷

With depreciation rate of 8,2% in 2009, total loan growth came to 12,4% in nominal amount, while retail loan growth rate came to only 6,7% and corporate loan growth rate to 16,5%. Growth of the loan activity was to a large extent conditioned by the incentives of the Government of the Republic of Serbia, which primarily subsidized liquidity and consumer loans. Slowing down of the credit growth has been one of the factors for NPL ratio set-back. Gross NPL ratio has increased from 11,28% to 15,69% in one year.

Rising tendency of retail FX savings was only interrupted in March 2009, thus resulting in reaching the pre-crisis level of EUR 5,7 billion²⁸ in November 2009. During 2009, total deposits increased by 27%. At the same time, the volume of foreign borrowings increased 38,8%, and own funding sources by 6,5%.

Recovery of the loan activity followed in 2010 - with total nominal growth rate in the first ten months coming to 27,7%, corporate loan growth rate 20,1% and retail loan growth rate 23,3%. In addition, the banks' loan portfolio quality deteriorated, measured by the NPL ratio, which at the end of October came to 17,69% gross. Continuing of deterioration was expected in the conditions of slackened economic activity, Dinar depreciation, rising prices and unemployment. Growth ratio still remains considerably slower in the retail than in the corporate sector.²⁹

Although still functioning at the low leverage level, the banking sector continued to decrease level of own sources used to finance business activities in 2010 - at the end of October 2010, capital amounted to 19,9% of total banks' funding sources. Total banks' deposits increased 11,1%, owing to the continuing tendency of retail deposits growth referred to above. FX savings amounted to EUR 6,6 billion at the end of October. The banks are largely relying on borrowed sources of financing – banks' loans amount to RSD 346,3 billion.

In addition to the loan growth funding sources referred to above, the banks re-directed significant available liquid funds to placements, but kept a satisfactory level of liquidity. Share of liquid assets in total assets comes to 24%. Despite the reduction in the scope of capital increases, banking sector remained solvent with an average adequacy ratio considerably above the prescribed minimum - 20,12% at the end of October 2010.

Because of growing aversion to risk, in 2009 and 2010 the banks are increasingly turning to investments in public sector. In 2010, said investments amounted to more than RSD 200 billion, with the banks increasingly orienting to investments in Dinar state securities, owing to the higher yield, at the expense of decrease in repo transactions with the NBS.

A drop in sector's profitability was recorded in 2009, mostly resulting from increasing loan losses. Profitability grew in 2010, not only because of relatively high net interest and fees and commission income, but because of decrease in some categories of expenses, in particular the expenses from impairment of loans and provisions. Net profit before tax for the first 10

²⁷ For the regulatory purposes, the banks were also able to include in capital the subordinated liabilities up to 75% of their core capital, to raise FX risk ratio from 10% to 20% of their core capital, the limit of 150% i.e. 200% gross loans to core capital ratio was suspended, classification rules were mitigated, including the suspension of the requirement set before the banks to calculate special loan loss provision with respect to the receivables classified as A.

²⁸ From September 2008.

²⁹ Gross corporate NPL was at 23,4%, and gross retail NPL was at 8,1% at the end of October 2010.

months of 2010 amounted to RSD 24,6 billion, which was 38% higher than the result achieved in the same period of 2009.

Despite the continuing banking sector growth, the scope of financial intermediation still remains relatively low. The banking sector's assets share in GDP amounted to 80,55% at the end of September 2010.

| | 31.12.06. | 31.12.07. | 31.12.08. | 31.12.09. | 31.10.10. |
|-----------------------|-----------|-----------|-----------|-----------|-----------|
| Banking sector assets | 59,59% | 67,92 | 65,27% | 76,75% | 80,55% |

34. What is the number of banks and other credit institutions operating in your country (if possible, by type of credit institution – banks, savings banks, mortgage credit institutions, etc.)? Please provide the following information:

a) total number;

b) domestic;

c) non-domestic- EU, of which:

i) subsidiaries and

ii) branches.

d) non-domestic non-EU, of which:

i) subsidiaries and

ii) branches.

Changes in (a) to (d) since 2003.

Enclosed Excel table containing the answer to question 34. (*See Annex)

35. Assets of the banking system (if possible, by type of credit institution – banks, savings banks, mortgage credit institutions, other):

a) total assets of the banking system;

b) assets owned by domestic credit institutions (in volume and share of total);

c) assets owned by non-domestic EU credit institutions (in volume and share of total), of which:

i) by subsidiaries of non-domestic EU credit institutions (in volume and share of total);

ii) by branches of non-domestic EU credit institutions (in volume and share of total).

d) total assets owned by non-domestic non-EU credit institutions (in volume and share of total), of which:

i) by subsidiaries of non-domestic non-EU credit institutions (in volume and share of total);

ii) by branches of non-domestic non-EU credit institutions (in volume and share of total).

Changes in (a) to (d) since 2003.

Enclosed Excel table containing the answer to question 35. (*See Annex)

36. Total deposits (if possible, by type of credit institution – banks, savings banks, mortgage credit institutions, other):

a) total deposits;

b) deposits held by domestic credit institutions (in volume and share of total);

c) deposits held by non-domestic EU credit institutions (in volume and share of total), of which:

i) by subsidiaries of such credit institutions (in volume and share of total);

ii) by branches of such credit institutions (in volume and share of total);

d) total deposits held by non-domestic non-EU credit institutions (in volume and share of total), of which:

i) by subsidiaries of such credit institutions (in volume and share of total);

ii) by branches of such credit institutions (in volume and share of total).

Changes in (a) to (d) since 2003.

Enclosed Excel table containing the answer to question 36. (*See Annex)

37. Concentration of the market (respectively as a share of total assets, of loans and of total deposits held by the largest institutions), indicating whether they are:

a) domestic;

b) non-domestic EU;

c) non-domestic non-EU.

Changes in (a) to (c) since 2003.

Enclosed Excel table containing the answer to question 37. (*See Annex)

38. Importance of the public sector in the banking industry:

a) Number of banks owned by public institutions and the amount of their assets and deposits;

The Republic of Serbia is the owner of shares in 8 banks- it is a majority shareholder in 2 banks, it is also a majority shareholder jointly with the European Bank for Reconstruction and Development in 2 banks, whereas it is a minority shareholder in 4 banks.

| | Total assets (30 September 2010) | | | Deposits (30. (30 September 2010) | | |
|--------------------------------------------------|-------------------------------------|--------------------------|-----------------------|--------------------------------------|--------------------------|---------------|
| Banks having the state as a majority shareholder | in millions of RSD | in millions of EUR | % of total banking | in millions of RSD | in millions of EUR | % of total |

| | | | | | | |
|----------------------------------------------------------------------------------------------------------------------------------|-----------|----------|--------|-----------|----------|----------------|
| | | | system | | | banking system |
| 1. Banka Postanska Stedionica a.d. Beograd | 32.891 | 309,78 | 1,36% | 21.557 | 203,3 | 1,56% |
| 2. Srpska Banka a.d. Beograd | 13.618 | 128,26 | 0,57% | 10.439 | 98,32 | 0,75% |
| Banks having the state as a majority shareholder jointly with the European bank for Reconstruction and Development (EBRD) | | | | | | |
| 3. Komercijalna Banka a.d. Beograd | 253.926 | 2.391,59 | 10,54% | 198.268 | 1.867,38 | 14,31% |
| 4. Cacanska Banka a.d. Cacak | 28.385 | 267,34 | 1,18% | 14.114 | 132,94 | 1,02% |
| Banks having the state as a minority shareholder | | | | | | |
| 5. JUBMES Banka a.d. Beograd | 8.097 | 76,26 | 0,34% | 2.557 | 24,09 | 0,18% |
| 6. PB Agrobanka a.d. Beograd | 67.442 | 635,20 | 2,80% | 47.270 | 445,21 | 3,41% |
| 7. Privredna Banka Beograd a.d. Beograd | 32.049 | 301,85 | 1,33% | 21.214 | 199,80 | 1,53% |
| 8. Credy Banka a.d. Kragujevac | 9.705 | 91,41 | 0,40% | 7.499 | 70,63 | 0,54% |
| Total number of banks with the RS as a shareholder | 446.114 | 4.202 | 18,51% | 322.919 | 3.041,39 | 23,30% |
| Total banking system | 2.409.986 | 22.698 | | 1.385.900 | 13.053 | |

| | Total assets | | % of total banking system | Deposits | | % of total banking system |
|--------------------------------------|--------------------|--------------------|---------------------------|--------------------|--------------------|---------------------------|
| | in millions of RSD | in millions of EUR | | in millions of RSD | in millions of EUR | |
| Razvojna Banka Vojvodine | 36,583 | 344.6 | 1.52% | 28,005 | 263.8 | 2.02% |
| Jugobanka Jubanka Kosovska Mitrovica | 8,826 | 83.1 | 0.37% | 145 | 1.4 | 0.01% |
| Dunav Banka Zvecan | 1,827 | 17.2 | 0.08% | 693 | 6.5 | 0.05% |

b) Timetable, objectives and scope of the privatisation;

The Government of the Republic of Serbia adopted the Strategy on Managing the Shares of the Banks owned by the Republic of Serbia for the period 2009-2012 in May 2009. During

the first phase of the implementation of the Strategy, the continuation of the following activities is planned: preparation and implementation of institutional building plans, analysis of economic justification of the merger of certain banks and recapitalization. Sale of state participation in banks will be conducted in the following period, upon the fulfilment of favourable conditions on the market. The Government of the Republic of Serbia is highly dedicated to the continuation and the finalization of the restructuring of the financial sector through the implementation of necessary reforms and privatization.

Definition of the timeframe and the manner for handling the shares of banks in which the Republic of Serbia is a shareholder will differ from bank to bank. The deadline for the completion of the sale of shares depends on general economic environment and further development of the financial and real sectors. In addition to this, concrete deadline for the sale of shares of every bank will depend on the interest expressed by prospective investors and on the result of the analysis to be conducted by privatization advisors.

Two banks were recapitalized in 2009 and 2010, whereas the recapitalization of one bank is planned for the beginning of 2011. Recapitalizations were performed by international financial institutions and a professional investor with whom the Republic of Serbia signed the Shareholders Agreement defining, *inter alia*, the process of selling of the banks, as well as international obligations and responsibilities with regard to the planned sales. Komercijalna Banka a.d. Beograd and Credy Banka a.d. Kragujevac were recapitalized, whereas the completion of the process with regard to Cacanska Banka a.d. Cacak is planned for the beginning of 2011.

- Komercijalna Banka a.d. Beograd

Shareholders Agreement was signed between the Republic of Serbia and professional investors during the recapitalization of Komercijalna Banka and transaction closed on 19 January 2010. The said agreement defines in detail the following: the deadline for the engagement of the joint financial advisor until 31 October 2012 (in order to analyze market conditions in terms of privatization, assess the value of the bank and the give the proposal of the model of sale (competitive bidding to the strategic investor or initial public offer on an internationally recognized Stock Exchange or on the Belgrade Stock Exchange)); the deadline for submission of Joint Privatization Plan- 31 December 2013; the deadline for completion of Joint Privatization Plan- 31 December 2015 (the said deadline may be extended by 12 months, under the special circumstances defined by the Agreement and having the consent of all contracting parties).

- Credy Banka a.d. Kragujevac

Following the initial recapitalization of Credy Banka performed in March 2010, Nova Kreditna Banka Maribor (NKBM) became a majority shareholder holding 55% of the share in the bank's capital. The NKBM performed two more recapitalizations in 2010 increasing its share to 72.38%. The Shareholders Agreement signed between the Republic of Serbia and the NKMB regulates the right to buy (a call option) relating to the shares of the RS upon the expiration of the first year following the completion of recapitalization, as well as the right of the RS to sell (put option) upon the expiration of the third year following the completion of recapitalization.

- Cacanska Banka a.d. Cacak

The recapitalization of Cacanska Banka is underway. It is to be performed by two financial institutions: IFC and EBRD. Based on the negotiated agreements, the signing of which is planned for December 2010, the following time schedule for the realization of activities related to the sale of this bank is defined: the Republic of Serbia and international financial

institutions will engage a joint financial advisor until 31 December 2011 in order to perform the analysis of market conditions for privatization and assessment of the value of the bank. A hired privatization advisor is going to submit the proposal of a Joint Privatization Plan related to the sale of the capital of the bank by the means of international tender to a strategic investor until 30 April 2012. The deadline for privatization is 3 years upon the completion of recapitalization (the said deadline may be extended by 12 months under special circumstances stipulated by the agreement and having the consent of all contacting parties).

- JUBMES Banka a.d Beograd, PB Agrobanka a.d. Beograd and Privredna Banka Beograd a.d. Beograd

The Republic of Serbia is a minority shareholder in JUBMES Banka a.d Beograd, PB Agrobanka a.d Beograd and Privredna Banka Beograd a.d. Beograd. With regard to these banks, the Strategy defines the sale of minority share until the end of 2011, either through the sale of shares on the Stock Exchange, take-over, joint sale of state-owned shares and shares owned by private shareholders or through competitive bidding.

c) Do public banks benefit from special treatment? Do banks directed by public or political party officials benefit from special treatment and how? Do public utilities/companies keep their accounts with commercial banks?

In the period 2002-2006 the Republic of Serbia became a majority shareholder of a number of domestic banks based on the conversion of debts vis-à-vis the Paris and London Clubs of Creditors and frozen foreign currency bonds into share capital of the banks. Following the performed restructuring and the privatization of a number of banks, the market share of the banks in the state ownership decreased from 45% to up to 18.5%. On 30 September 2010, the Republic of Serbia was a shareholder in 8 banks on the banking market, with majority ownership in two banks, joint ownership with EBRD in two banks and minority ownership in four banks. The banks having the RS as a shareholder do not have a special treatment in any event, and they operate as other banks, in accordance with the Law on Banks and the regulations of the National Bank of Serbia, which is uniformly applied to all the banks operating on the market of the Republic of Serbia, without any exceptions.

During the appointment of persons to be the representatives of the Republic of Serbia in the management bodies of the banks in which the Republic of Serbia is a shareholder, the National Bank of Serbia determines the competency and suitability of proposed persons and only upon obtaining the consent of the National Bank of Serbia, the proposed persons are appointed. In accordance with the Law on Banks (Article 72) and the Decision on the Implementing the Provisions of the Law on Banks relating to Granting of a Provisional Permit to Set up a Bank and Subsequent Issuing of a Full Operating License, as well as individual provisions relating to the consent obtained by the National Bank of Serbia (point 28), proposed persons have to meet the following conditions: have at least three years of experience in management position in a financial sector, or six years of experience in the field of finance and banking, and that they have distinguished themselves as experts or scientists in such fields, have references on the competence, abilities and moral integrity, good business reputation and appropriate qualifications, criminal proceedings have not been instituted against them, i.e. they have not been convicted of a criminal offence. In accordance with the Law on the Deposit Insurance Agency (Article 7), one of the priorities of the Agency is to participate in the management of banks in which the Republic of Serbia is a shareholder by

monitoring operations of those banks and their bodies, consequently ensuring the professional management of the said banks.

Public utilities/companies keep their accounts with commercial banks, in accordance with the positive legislation of the Republic of Serbia.

d) Is there policy in place/envisaged to recapitalize them?

- Komercijalna Banka a.d. Beograd

Komercijalna Banka was recapitalized on 19 January 2010 through a closed issuance of convertible preferred shares amounting to EUR 120 million, by professional investors-European Bank for Reconstruction and Development (EBRD), IFC Capitalization Fund, established by IFC and Japan Bank for International Cooperation, L.P. , Deutsche Investitions - und Entwicklungsgesellschaft mbH, (DEG) and Swedfund International AB. In accordance with the Shareholders' Agreement signed between the RS and professional investors, the RS might invest in convertible preferred shares of the bank in the following three years.

- Credy Banka a.d. Kragujevac

According to the Shareholders' Agreement signed between the Republic of Serbia and new majority shareholder of Credy Banka-the NKBM, the NKBM is going to invest the additional EUR 30 million within 5 years following the completion of recapitalization, following the initial recapitalization amounting to EUR 10 million. In accordance with that, the NKBM invested EUR 15 million in the bank, by the means of recapitalization and subordinated loan in the middle of 2010.

- Cacanska Banka a.d. Cacak

The recapitalization of Cacanska Banka is underway and it is performed by the IFC and EBRD amounting to EUR 8 million. Owing to this, the share of IFC will amount to 19.9%, whereas the EBRD will maintain its share of 24.9% of the bank's capital. In accordance with the harmonized Shareholders' Agreement, the RS might perform the recapitalization of the bank in order to maintain its share of 38.84% in the period of two years following the investment of these two investors.

- Banka Postanska Stedionica a.d Beograd and Privredna Banka a.d. Pancevo

The Government adopted a decision on 21 January 2010 on the launching of an initiative relating to the commencement of the merger between the **Banka Postanska Stedionica a.d Beograd** and Privredna Banka a.d. Pancevo, ordering the Deposit Insurance Agency to perform all necessary activities in order to conduct the merger. The merger was completed on 1 September 2010.

According to the strategy, professional investors may perform recapitalization as of 2010.

- JUBMES Banka a.d Beograd, PB Agrobanka a.d. Beograd and Privredna Banka Beograd a.d Beograd

If necessary, the RS may consider the possibility of recapitalization of these banks. In case the shareholders express their interest, the Republic of Serbia may sign with them an Act on the Assuming of Obligations defining their relations prior to the sale and/or the joint sale of shares.

e) Indicate the percentage of bank capital held by public entities on a bank by bank basis.

| The state of affairs on 30 November 2010 | The name of the bank | The share of RS (%) | DIA-bankruptcy (%) | Total share (%) |
|---------------------------------------------------------------------------------------------------------------------------|-----------------------------------------|---------------------|--------------------|-----------------|
| Banks having the state as a majority shareholder | Banka Postanska Stedionica a.d. Beograd | 96.30% | 0.59% | 96.90% |
| | Srpska Banka a.d. Beograd | 96.52% | | 96.52% |
| Banks having the state as a majority shareholder jointly with the European bank for Reconstruction and Development (EBRD) | Komercijalna Banka a.d. Beograd | 42.60% | 6.55% | 49.15% |
| | Cacanska Banka a.d. Cacak | 38.84% | 4.46% | 43.30% |
| Banks having the state as a minority shareholder | JUBMES Banka a.d. Beograd | 21.20% | 8.33% | 29.53% |
| | PB Agrobanka a.d. Beograd | 20.07% | 0.55% | 20.62% |
| | Komercijalna Banka a.d. Beograd | 19.41% | | 19.41% |
| | Credy Banka a.d. Kragujevac | 15.24% | 2.97% | 18.21% |

Note: With regard to the Banka Postanska Stedionica a.d. Beograd, the share of the Republic of Serbia is 69.56%, the share of P.E. of PTT Communications "Srbija" is 24.27%, and that of the Pension and Disability Insurance Fund 2.48 %.

f) Is the Government considering or engaged in any bank re-nationalisation? If yes, please explain the objectives and scope of such operation.

Based on the analyses performed by the National Bank of Serbia, the banking system may be considered extremely liquid and satisfactorily capitalized- therefore the country currently does not take into consideration and does not participate in the nationalization of any banks.

Having in mind the world financial crisis affecting the national economies all over the world as of 2008, as well as the fact that the crisis contributed to the attitude that the existing regulations are not sufficient for the prevention or alleviation of effects of the occurrence of critical situations, all relevant institutions in the Republic of Serbia have been working on the creation of legal basis for the improvement of existing and defining new measures to preserve financial stability of the Republic of Serbia, protecting the interest of depositors, as well as on the maintenance and strengthening of the credibility of the banking sector in Serbia.

39. Please describe the current situation concerning access of private companies to bank credit and the trend compared to previous years. To what extent have issues relating to property registration and bankruptcy hindered access to credit?

Available data on bank credit activities regarding private companies show that the access of companies to banking loans was not jeopardized in the previous period. Namely, in 2009, which was the year when bank credit activity slowed down considerably, the total loan growth is the result of primarily growth of loans disbursed to companies. According to the data of the Banking Supervision Sector of the National Bank of Serbia, these loans were increased by 16.5%, while the growth of total credit activity of the banking sector was 12.4%. Even during

2010, loans disbursed to companies significantly contributed to the growth of total credit portfolio of banks – during the 11 months in 2010, corporate loan portfolio was increased by 22.5%, while total bank loans were increased by 33.2%. As of the end of November 2010, loans disbursed to companies amounted to 762 billion dinars.

Data from the Credit Bureau within the Association of Serbian Banks also reflect the unhindered access to bank loans, according to which number of legal persons who took loans was increased by 11% in the two-year period (2008-2010).

To what extent have issues relating to property registration and bankruptcy hindered access to credit?

In order to be able to take a mortgage loan, a person must have the real estate registered in appropriate registries. The mortgage may be imposed only upon registered real estate, in order to secure the claim of the creditor.

Property registration also plays a role in assessment of solvency of the loan beneficiary, because the owner of the real estate is considered to be only person whose real estate is entered into appropriate registry.

In Serbia, implementation of the project is in its final stage according to which all real estates in Serbia will be kept in the Real Estate Cadastre of the Republic Geodetic Authority. The Real Estate Cadastre, which covers more than 80% of the Serbian territory, is a modern, uniform, efficient, high-quality and public register in an electronic form.

Legal person in respect of whom bankruptcy proceedings have been instituted may not be a loan beneficiary. The reason for that is the fact that the bankruptcy proceedings are instituted because of long-term insolvency (when such person may not meet its financial obligations within 45 days following the due date or completely terminated all payments for 30 days continuously), as well as because of overly large debts.

If the reorganization plan is adopted during the bankruptcy proceedings, through redefining debt-creditor's relations, status changes of the debtor and through any other way stipulated by the reorganization plan, the bankruptcy proceedings are terminated and legal person may be a loan beneficiary.

40. Please evaluate the degree of competition in the banking system (price competition, new products, changes in market share, and other indicators). Are there any particular concerns about the market share of the largest banks?

There are 33 banks operating in the banking sector of Serbia, which is a relatively high number compared to the market size. Namely, the banking sector is significantly fragmented, bearing in mind that a large number of banks have a low market share in the crucial segments of operating. The calculated HHI concentration ratio (whose value of up to 1.000 indicates the absence of concentration in the sector, the value between 1000 and 1800 indicates the presence of medium concentration, whereas the value exceeding 1.800 indicates the presence of high concentration) speaks in favour of it, amounting to 625 with regard to the balance sheet, 649 with regard to loans, and 699 with regard to deposits³⁰ In addition to this, index values have been on the decrease in the last two years. The largest bank in the system has the market share of 13.7%, 5 leading banks of 45%, and 10 largest banks of 69.3%.

³⁰ At the end of November 2010.

In the last couple of years several banks in Serbia have offered versatile products, aiming at the attracting additional sources of funds and placing them on the market. Card business and electronic banking services are increasing rapidly. Recently the banks have concluded an increasing number of agreements with clients dealing with financial derivatives, thus managing their exposures, mostly dealing with the credit risk and currency risk. The banks also provide the possibility to clients related to the conversion, refinancing and rescheduling of their debts. With regard to the liabilities, various forms of savings products are offered. Due to the fact that banks provide stimulating interest rates with regard to the collected deposits, in addition to the expenses they incur based on the insurance premiums, expenses related to mandatory reserves and risk premiums, banks also form relatively high active interest rates. However, even though interest rates and spreads are still high, they show a steady decrease. The latest survey relating to the trends of interest rates on household loans done by the National bank of Serbia in the second quarter this year supports that. Interest rates are formed freely, based on the bank business policy and pricing strategy.

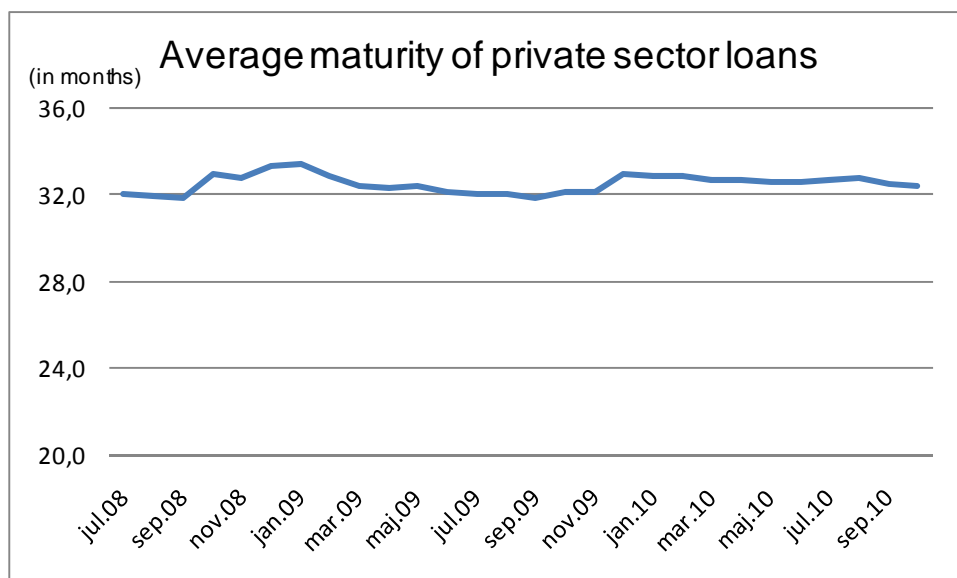
41. What is the average interest rate spread (lending/deposit rates in domestic and foreign currency respectively) in banking over the past five years? Please supply data on the profitability of banks during recent years and comment on developments.

The interest rate statistics deals solely with the dinar loans and deposits. There are data solely regarding newly approved loans. However, there are not any data on average interest rates with regard to outstanding amounts of loans and deposits. A new methodology which is completely harmonized with the requirements of the European Central Bank came into force in September 2010. The publishing of the first data is expected for the beginning of 2011. In October 2010 the spread relating to total activities of the banks amounted to 7.75 percentage points.

Excel table with indicators relating to question 41. (**See Annex*)

42. What is the average maturity of bank loans to the private sector over the past five years? What is the share of loans with maturity of up to one year?

Average maturity of loans to the private sector amounted to 32.4 months at the end of October 2010, whilst the simultaneous participation of short-term loans amounted to 40.8%. The tables containing the data relating to the participation of loans with different maturity in the total amount of loans approved to the non-monetary and private sectors are provided in the Annex. The private sector encompasses: corporate sector, household sector and non-profit institution sector. The non-monetary sector includes the private sector expanded by public enterprises, other financial institutions and local self-government.



In order to calculate the average maturity of loans, the average of time categories of remaining maturity was used as an indicator with regard to this category (e.g. for the category from 3 to 5 years, 4 years were used as an indicator). Weights were calculated as participation of loans of certain maturity category in the total of approved loans. The approximation of 61 months was used for the maturity exceeding 5 years. In the middle of 2008 a new Chart of Accounts for banks was introduced, so that the data relating to earlier period are not available.

(*See Annex)

43. Please provide data on foreign currency denominated and foreign currency indexed deposits and loans.

Excel tables enclosed with the statistics regarding question No. 43. (*See Annex)

Overview of the currency structure of loans and deposits (assets and liabilities).

| | September 2010 | |
|----------------------------|----------------|--------------------|
| | Assets | Liabilities |
| <i>Loans</i> | 100,0% | 100,0% |
| RSD | 27,6% | 4,1% |
| FX | 8,2% | 95,3% |
| FX clause | 63,5% | 0,6% |
| Other security instruments | 0,7% | 0,0% |
| <i>Deposits</i> | 100,0% | 100,0% |
| RSD | 14,2% | 23,0% |
| FX | 80,8% | 73,9% |
| FX clause | 5,0% | 3,0% |
| Other security instruments | 0,0% | 0,0% |

44. How do you assess the stability of the banking sector? What is the current situation and trend concerning capitalisation, structure of capital, regulatory capital, risk weighted assets? How has the banking sector been influenced by the global financial crisis?

Capital, risk-weighted assets and capital adequacy ratio

| | |
|----------------------------------------------------------------------|----------------|
| in billions of RSD | 30.09.2010. |
| Tier I capital | 434,0 |
| Tier II capital | 94,4 |
| Tier III capital | - |
| Regulatory deductions | 136,9 |
| TOTAL regulatory capital | 391,5 |
| TOTAL risk-weighted assets | 1.945,4 |
| Credit risk exposure | 1.924,1 |
| Market risk exposure | 21,3 |
| <i>To foreign –exchange risk</i> | 17,6 |
| <i>To other market risks</i> | 3,7 |
| Settlement/delivery risk and counterparty risk | 0,2 |
| Price risk (as well as the exposure to risk on position in options) | 3,5 |
| Capital adequacy ratio (%) | 20,12 |

Overall stability of the banking sector was achieved and capital adequacy ratio did not drop below 20% during 2010 as well as during the critical 2009. Overall capital adequacy ratio has been decreasing as of the commencement of the financial crisis reaching 20.12% at the moment. The total regulatory capital amounted to RSD 391.5 billion- Tier 1 capital amounting to RSD 434 billion presenting the key element of the capital at the end of September this year. Tier II capital amounts to RSD 94 billion, whereas the total amount of regulatory deductions from capital amounts to RSD 136.9 billion. Deductions are mostly the shortfall amount of special loan loss provisions amounting to RSD 128.5 billion. The key banking sector exposure is credit risk exposure since it comprises 98.9% of total exposures to all risks.

The world financial crisis had the largest impact relating to the decrease in aggregate demand, increased non-liquidity of economy and certain number of citizens, significant decrease in the value of domestic currency as well as consequential increase in the level and absolute amount of problematic loans of the banking sector followed by the decrease in the profitability of banks and the increase in the number of banks operating with losses. The beginning of the crisis at the beginning of October 2008 was officially marked by considerable outflow of citizens' savings amounting to up to EUR 1 billion. The outflow presented the decrease in the deposits by 15%. At the same time, the domestic currency has lost (nominally) approximately 29% of its value from the beginning of the crisis to date. The profitability of the sector recovered in 2010 as compared to the previous year (September 2010/2009, profit before tax increased by 34%), even though it is still significantly below the level of 2008 (September 2010/2008, profit before tax lower by 39%). At the same time, the number of employees in the banking sector, as well as the number of organizational units (branches, subsidiaries etc.)

significantly decreased with beginning of the crisis. Namely, after five subsequent years marked with the growth in the number of employees, the banking sector for the first time decreased the number of employees in 2009. At the end of September 2010 the number of employees decreased by 4.7%, i.e. by 1.515 persons as compared to the end of 2008. The number of organizational units also decreased by 7.5%(by 205 branches, subsidiaries and other organizational units). Currently the key problem of the banking sector are extremely high and problematic loans i.e. loans with arrears exceeding 90 days. At the end of September this year they amounted to RSD 277 billion comprising 17.8% of the total number of approved loans (gross) whereas they were at the level of 10.2% prior to the crisis. Bearing in mind the amounts of problem loans at the time when the collecting of the data commenced (September 2008: RSD 101 billion) the current level presents an increase of 175%.

45. Please provide an analysis and an estimate (as an absolute amount, as a % of total assets) of non-performing loans (NPLs) in banks.

Overview of non-performing loans of the banking sector

| In Dinars | September 2010 |
|---------------------------------------------|-----------------|
| Total gross assets | 2.620,2 billion |
| <i>Gross assets valuation adjustment</i> | 210,2 billion |
| Total gross loans | 1.554,6 billion |
| <i>Gross loans valuation adjustment</i> | 150,7 billion |
| NPL | 277,1 billion |
| <i>NPL % of assets</i> | 10,6% |
| <i>NPL % of loans</i> | 17,8% |
| Coverage of NPLs | |
| <i>By total valuation adjustment (IFRS)</i> | 54,4% |
| <i>By total loan loss provision (NBS)</i> | 127,9% |

As of end of September this year, total NPLs make 10,6% of total gross assets and 17,8% of total gross loans of the Serbian banking sector. At the same time, in spite of distinctly high level of the total sum and the NPL ratio by itself, NPL coverage ratios can be considered satisfactory, having in mind the NPL coverage by total calculated loan loss provision (according to the NBS methodology) of 127,9%. Despite the decrease in presented ratio in Q3 of this year, we consider the achieved rate of loan loss provision to be adequate and on the level that enables minimizing adverse effects of potential asset quality deterioration on the banking sector capital adequacy.

Overview of the non-performing loans of the banking sector (structure)

| | | | 30.9.2010. |
|-----------------------------------------------|-------------|-------|------------|
| | RSD billion | Share | Gross NPL |
| Financial sector | 4,6 | 1,7% | 17,5% |
| Corporate sector (public and other companies) | 199,9 | 72,2% | 22,0% |

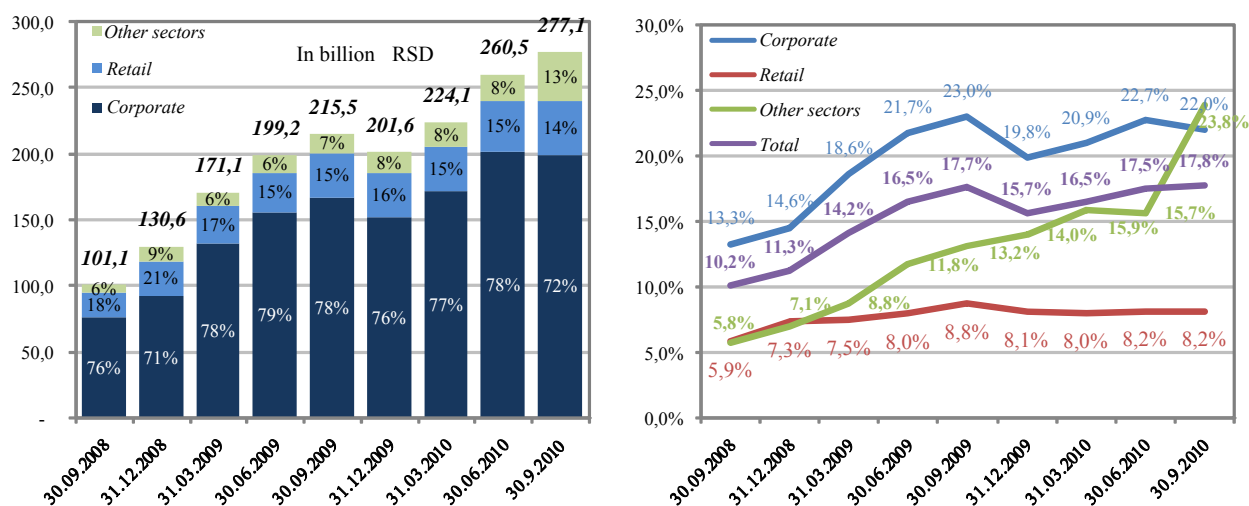
| | | | |
|----------------------------|-------|--------|-------|
| Retail | 40,2 | 14,5% | 8,2% |
| Entrepreneurs | 9,2 | 3,3% | 20,6% |
| Other sectors | 23,2 | 8,4% | 27,5% |
| TOTAL non-performing loans | 277,1 | 100,0% | 17,8% |

The key driver of a total level of non-performing loans is the corporate sector (public and other companies) with the level of 199,9 billion Dinars, i.e. share of 72,2% in total non-performing loans. In practice, every fifth loan, i.e. 22% of loans in corporate sector is over 90-day in default. Retail sector, which takes the second place by concern, having 14,5% share in total non-performing loans, is the least over 90 day defaulting sector of all observed, with the amount of 40,2 billion Dinars. In retail, 8,2% of all loans are 90 days overdue. High NPL ratio level also appears in the entrepreneur sector, with the value of 20,6%, although their share in total non-performing loans is not crucial, considering that with the level of 9,2 billion Dinars they make 3,3% of all non-performing loans. Entities such as broker-dealer companies and other entities in the financial sector (excluding banks, insurance and leasing companies and pension funds), primarily take the highest share in total over 90 day default of the financial sector, with the level as high as 17,5%.

46. What has been the NPLs development over the past five years? Has the past rapid credit growth in any way affected the average quality of the loan portfolio?

Overview of non-performing loans of the banking sector by quarters

(Absolute and relative amounts, tendency and structure)



Considering the limited availability of data on non-performing loans, primarily conditioned by the beginning of reporting on the loans in question as of September 2008, data on non-performing loans covering previous five years are not available for the purpose of more detailed analysis of this phenomenon. At the same time, a very rapid credit growth remains the fact, along with the high loan growth rates in the last few years. Due to unavailability of data on non-performing loans, the link between these two phenomena has not been explored; consequently, it has neither been explicitly confirmed.

47. Please provide an analysis of the historical data on the asset and liability structure of the banking sector .

Analysis of the banking sector's balance sheet can be done by observing three periods – pre-crisis (2008), during the crisis (2009) and the period of recovery, i.e. overcoming the crisis (first nine months of 2010).

Loans to customers definitely represent a key category in total assets. Namely, as of the end of September this year, loans to customers (net) make 58,3% of total assets, which is an indicator of reactivation of sector's credit activity, bearing in mind that the same position was at 52,7% at the end of 2009. In practice, before the crisis occurred, loans to customers totalled to 57,1% of the total assets (end of 2008) in the Serbian banking sector. At the same time, instead of highly risk-involving loans to corporate customers, a fair investment alternative of the banking sector during 2009 were the investments in the Republic and the National Bank of Serbia. More specifically, with the emergence of short-term securities of the Republic of Serbia (Treasury bills of the Republic of Serbia) at the beginning of 2009, the banking sector considerably re-directed its available liquid funds, and the share of securities referred to above suddenly increased in the banks' balance sheets. Having regard to the fact that in 2008 T-bills were not available, in 2009 amounted to 3,3% of the total assets, and at the end of Q3 this year T-bills made 5,2% of the total sector assets. Together with the investments into T-bills of the Republic of Serbia, the banks made considerable investments into repo operations with the National Bank of Serbia, which particularly came into focus during critical 2009, when repo operations came to 7% of the total assets. With the recovery of credit activity in this year, repo operations with NBS totalled only 2,7% of total assets, and one can also perceive slowing down of banks' investments into T-bills of the Republic of Serbia. Considerable “escape” into the most liquid and the least risk-involving investment alternatives the financial market of Serbia could offer, was a key feature of the balance sheet structure of the banking sector during 2009 – the most liquid positions (cash and cash equivalents, RS T-bills and NBS repo transactions) made 21,0% of total assets (September 2010: 14,2%).

Serbian banking sector balance sheet

| | 2008 | | 2009 | | 30/09/2010 | |
|-------------------------------------|-------------|------|-------------|------|-------------|------|
| | RSD billion | % | RSD billion | % | RSD billion | % |
| Cash and cash equivalents | 266,7 | 15,0 | 244,3 | 11,3 | 151,5 | 6,3 |
| Callable deposits and loans | 267,2 | 15,5 | 439,6 | 20,3 | 413,9 | 17,2 |
| Out of which: | | | | | | |
| <i>Repo transactions with NBS</i> | 77,8 | 4,4 | 151,7 | 7,0 | 64,5 | 2,7 |
| <i>Required FX reserve with NBS</i> | 193,4 | 10,9 | 278,8 | 12,9 | 344,9 | 14,3 |
| Funds deposited | 54,4 | 3,1 | 60,7 | 2,8 | 91,7 | 3,8 |
| Loans to customers (gross amount) | 1.094,9 | 61,6 | 1,241,4 | 57,5 | 1.530,2 | 63,5 |
| Out of which | | | | | | |
| <i>Investment loans</i> | 165,6 | 9,3 | 212,7 | 9,8 | 280,5 | 11,6 |

| | | | | | | |
|------------------------------------------|----------------|--------------|----------------|--------------|----------------|--------------|
| <i>Export loans</i> | 4,1 | 0,2 | 9,5 | 0,4 | 17,2 | 0,7 |
| Working capital loans | 201,4 | 11,3 | 265,6 | 12,3 | 347,7 | 14,4 |
| <i>Consumer loans</i> | 28,0 | 1,6 | 39,5 | 1,8 | 44,3 | 1,8 |
| <i>Mortgage loans</i> | 163,8 | 9,2 | 192,5 | 8,9 | 245,2 | 10,2 |
| <i>Transaction account overdrafts</i> | 42,3 | 2,4 | 38,9 | 1,8 | 46,8 | 1,9 |
| <i>Impairment of loans</i> | 80,8 | 4,5 | 103,0 | 4,8 | 125,8 | 5,2 |
| Loans to customers (net amount) | 1.014,2 | 57,1 | 1.138,4 | 52,7 | 1.404,4 | 58,3 |
| Securities (shares, stakes) | 25,1 | 1,4 | 112,2 | 5,2 | 174,4 | 7,2 |
| Out of which | | | | | | |
| <i>T-Bills of the Republic of Serbia</i> | 0,0 | - | 72,0 | 3,3 | 126,4 | 5,2 |
| Fixed assets and investment property | 66,2 | 3,7 | 67,2 | 3,1 | 65,8 | 2,7 |
| Other assets | 74,3 | 4,2 | 97,9 | 4,5 | 108,3 | 4,5 |
| TOTAL Assets | 1.777,0 | 100,0 | 2.160,4 | 100,0 | 2.410,0 | 100,0 |
| | | | | | | |
| | 2008 | | 2009 | | 30/09/2010 | |
| | RSD billion | % | RSD billion | % | RSD billion | % |
| TOTAL Liabilities | 1.356,9 | 76,4 | 1.712,9 | 79,3 | 1.922,8 | 79,8 |
| Total deposits | 1.024,7 | 57,7 | 1.301,2 | 60,2 | 1.385,7 | 57,7 |
| Out of which | | | | | | |
| <i>Transaction deposits</i> | 217,3 | 15,3 | 302,0 | 14,0 | 319,8 | 13,3 |
| <i>Other deposits</i> | 753,4 | 42,4 | 999,2 | 46,3 | 1.065,9 | 44,2 |
| <i>Retail savings</i> | 350,5 | 19,7 | 491,0 | 22,7 | 597,9 | 24,8 |
| Borrowings | 189,5 | 10,7 | 247,4 | 11,5 | 353,0 | 14,6 |
| <i>From foreign persons</i> | 152,6 | 8,6 | 211,1 | 9,8 | 311,4 | 12,9 |
| Subordinated liabilities | 83,3 | 4,7 | 99,9 | 4,6 | 111,5 | 4,6 |
| <i>EUR</i> | 80,1 | 4,5 | 96,4 | 4,5 | 105,1 | 4,4 |
| <i>CHF</i> | 3,2 | 0,2 | 3,5 | 0,2 | 6,5 | 0,3 |
| Other liabilities | 59,4 | 3,3 | 64,3 | 3,0 | 72,5 | 3,0 |
| TOTAL Capital | 420,0 | 23,6 | 447,5 | 20,7 | 487,2 | 20,2 |
| Nominal and other capital | 332,8 | 18,7 | 340,7 | 15,8 | 361,0 | 15,0 |
| Reserves | 74,2 | 4,2 | 104,5 | 4,8 | 127,8 | 5,3 |
| <i>For estimated losses</i> | 52,0 | 2,9 | 81,4 | 3,8 | 105,7 | 4,4 |
| <i>Accumulated profit/loss</i> | 13,0 | 0,7 | 2,3 | 0,1 | (1,6) | (0,1) |
| TOTAL Liabilities | 1.777,0 | 100,0 | 2.160,4 | 100,0 | 2.410,0 | 100,0 |

On the other hand, key source of funds of the banking sector are the deposits. Deposits make 57,5% of total liabilities, with retail savings amounting to 43,1% of total deposits (i.e. 24,8% of total liabilities). The value of retail savings deposits has amounted to 597,9 billion Dinars as of the end of September this year.

Significant source of funding of the banking sector's assets are the banks' borrowings, primarily from foreign entities (borrowings from parent banking groups), which continuously make a growing portion of total liabilities – currently at 14,6%, while at the end of 2009 and 2008 amounted to 11,5% and 10,7% respectively.

In addition, subordinated liabilities remained at stable 4,6% of total liabilities in virtually all observed periods.

Having regard to the nature of banking business, and expected structure of the balance sheet, one can say that Serbian banking sector is not excessively indebted, thus the leverage effect remains at a very low level. More specifically, share of total capital in total liabilities of the sector came to 20,2% at the end of Q3 of this year, whereat nominal and other capital amounted to 15,0% of total assets. Crisis effects, reflected in deterioration of loans and advances quality, are highly visible in the increased amount and share of the loan loss provision by banking sector loans to customers, making 4,4% of the total assets in this year, as well as 3,8% and 2,9% at the end of 2009 and 2008 respectively, and the increased share of loans impairment in total assets - 5,2% at the end of Q3 of this year, 4,8% and 4,5% at the end of 2009 and 2008 respectively.

48. Have there been changes to the bankruptcy legislation? Are any (further) adjustments envisaged? Please comment on the practice as well as the legal framework. How easily can banks mobilise their claims through such proceedings?

Reforms of the bankruptcy legislation in Serbia have begun in 2001, by identification of the causes of inefficiency of the existing bankruptcy legal framework and adoption of the new legal solutions. Previous Law on Compulsory Settlement, Bankruptcy and Liquidation (*Official Journal of SFRY* No 84/89 and *Official Journal of SRY* No 37/93 and 28/96) – **ceased to be in force on 02/02/2005**, but still applies on the bankruptcy proceeding that involve selling of more than 50% of the book value of property until 02/02/2005. All bankruptcy proceedings initiated according to the Law referred to above, which do not involve selling more than 50% of a bankruptcy debtor's book value of property continued to have conduct according to the Law on Bankruptcy Proceedings.

The Law on Bankruptcy Proceedings (*Official Gazette of the Republic of Serbia* No 84/04) influenced by the UNICITRAL Model Law on Cross-Border Insolvency (General Assembly resolution 52/158 of December 15, 1997), and sub-legal acts passed pursuant to this Law: **the Code of Ethics for Bankruptcy Administrators** (*Official Gazette of RS*, No 43/05) and the **National Standards for Administering the Bankruptcy Estate** (*Official Gazette of RS* No 43/05), have been in force since February 2005. The Law referred to above regulates the procedure of liquidation of an insolvent company by initiating the bankruptcy proceeding, which may be conducted in two directions: as the bankruptcy proceeding that involves settlement of creditors by sale of an entire bankruptcy debtor's estate, and reorganisation, which involves settlement of creditors under the terms and conditions established by the plan of reorganisation. This Law, and the **Law on Bankruptcy Supervision Agency** (*Official Gazette of RS* No 84/04) established the Bankruptcy Supervision Agency as an authorised institution to issue, renew and cancel licences to bankruptcy administrators, and to the effect

of providing higher level of expertise and control of the bankruptcy administrators and persons who implement bankruptcy proceeding.

In 2008 and 2009, based on the detailed analysis of collected data regarding the implementation of the Law in effect, consideration of opinions of the persons directly involved in bankruptcy proceedings, primarily the bankruptcy administrators, bankruptcy judges and competent agencies, but also having regard to comparative and legal analysis, draft of the new **Law on Bankruptcy** was prepared and adopted in December 2009. The main reason for drafting the new Law on Bankruptcy lies in the fact that its implementation in the preceding four years indicated that current solutions can be made more efficient with regards to numerous details, and that there was a need to implement new, modern institutes.

The Law is primarily supposed to facilitate the initiation of bankruptcy, step up the proceeding itself, but also to cut its costs. New solutions do not change the existing concept; they are rather based on the problems identified in practice and focus on improving the existing solutions, legal and technical specification, and providing adequate answers to the growing after effects of the global financial crisis, not only to make the bankruptcy proceeding more efficient per se, but also to make use of their own flexibility to, whenever possible, assist the Serbian economy to preserve business of a company more easily. The new Law aims to improve three key efficiency indicators of the Serbian bankruptcy proceeding: duration, creditors' settlement rate and costs..

The Law on Bankruptcy Proceedings (*Official Gazette of RS* No 84/2004 and 85/2005), **ceased to be in effect on 23/01/2010**, but still applies on the bankruptcy proceedings initiated until 23 January 2010.

The Law on Bankruptcy (*Official Gazette of RS* No 104/2009), which has been in application since **23 January 2010**, is currently effective legal instrument applicable to all bankruptcy proceedings initiated as of 23 January 2010.

The key innovations in comparison to the Law on Bankruptcy Proceedings reflect in the following: introduction of the bankruptcy proceeding principles and objectives, specification and introduction of the new reasons for bankruptcy initiation; suspension of the panel of bankruptcy judges, lowering advance payment for initiation of the proceeding and reduction of proceeding expenses; clarification of the role of the Bankruptcy Supervision Agency in supervision of the bankruptcy administrators' activity, introduction of the claim preclusive deadline, introduction of set off possibility, introduction of an "automatic bankruptcy" for legal entities which accounts are blocked for more than 3 (two as of 2011, and one as of 2012) year period; introduction of a pre-packaged reorganisation plan, changes with respect to the legal consequence of a confirmation of plan of reorganization, removal of the entrepreneurs bankruptcy the law and changes to the minor value bankruptcy cases.

The Law on Bankruptcy, which largely strengthened authorisation of the Bankruptcy Supervision Agency and clearly prescribed disciplinary measures that include warning, public warning, fine and removal of licence, also provided the basis to prescribe disciplinary procedure through a sub-legal act passed by the Ministry of Economy, whereby enabling achievement of the main role of the Bankruptcy Supervision Agency, which is to monitor the development of bankruptcy administrator profession and provide regulatory frame to perform this duty, imposing sanctions for each unprofessional or fraudulent activity by prohibiting further performance of duty, i.e. removal of licence. The **Law on Amendments of the Law on the Bankruptcy Supervision Agency** (*Official Gazette of RS* No 104/2009) was prepared and adopted in December 2009. Main objective of the proposed amendments to the Law on Bankruptcy Supervision Agency was to solve the problems arising in practice by defining the

position, rights and obligations of the Agency, and by specifying its powers and scope of activity as a regulatory authority, particularly in the field of professional supervision. These amendments provided an efficient system of professional supervision over the performance of bankruptcy administrators, in terms of unique implementation of bankruptcy administrators' performance appraisal, standardized performance and higher level of expertise, as well as the quality of the very profession of bankruptcy administrator, in order to strengthen its role in the market economy that implies confidence in the system of protection of property, thereby protection of a bankruptcy estate as well, transparency and consistency in application of the adopted rules of behaviour for all participants in the bankruptcy proceedings.

One of significant innovations is the establishment of the so called pre-packaged reorganisation. This institute provides flexible and quick procedure of recovery for the company facing business problems. A company in difficulties shall have the opportunity to reach an agreement with its creditors on business reorganisation and redefinition of debtor-creditor relations before mobilizing the claim, i.e. before instituting the bankruptcy proceedings, and the agreement thereof shall turn into proposal to initiate bankruptcy with pre-packaged reorganisation plan.

In terms of establishing effective mechanisms in the bankruptcy proceedings, which enable closing down of non-viable companies, we indicate the provisions of Article 150 - 154 of the Law on Bankruptcy (*Official Gazette of RS*, No 104/2009), and the provision of Article 208 of the same Law (so called automatic bankruptcy of companies in long-term blockade), which in our opinion, if applied consistently, shall lead to closing down of non-viable companies, i.e. companies suffering long-term insolvency, to the aim of creating a sound economic environment.

All relating sub-legal instrument were adopted in 2010: Rulebook on Random Selection of Bankruptcy Administrators; Code of Ethics for Bankruptcy Administrators, Rulebook on Establishing the National Standards for Administering the Bankruptcy Estate, Rulebook n on Supervisors' Official ID; Regulation on Content, Method of Registration and Keeping the Register of Bankruptcy Estates; Regulation on the Type and Amount of Fees for Registration and Other Services Provided by the Agency for Business Registers in the Process of Keeping the Register of Bankruptcy Estates; Rulebook on the Manner of Issuance and Renewal of Licences for Bankruptcy administrators; Rulebook on the Conditions, Curriculum and Manner of Taking the Bankruptcy Administrator Licensing Examination, Rulebook on Methods of Professional Supervision of the Performance of Licensed Bankruptcy Administrators, Rulebook on Enforcement of Pre-packaged Reorganisation Plan and its Contents; Rulebook on the Basis and Criteria for Determining Performance Bonuses and Compensation of Costs for Bankruptcy Administrators; Tariff on Determining Costs of Services Provided by the Bankruptcy Supervision Agency.

The Law on Bankruptcy has specified neither the bankruptcy proceeding for a private entrepreneur nor bankruptcy of a physical person, which is planed to be done as additional compliance with the regulations of the European Union.

The banks secure their claims by pledge of debtors' movable and immovable assets, and generally appear in the bankruptcy proceedings as the secured creditors. The Law on Bankruptcy Proceedings clearly defines the types of creditors (excluding creditors, secured creditors and bankruptcy creditors), together with their position and rights in the bankruptcy proceedings. This concept has not been changed in the Law on Bankruptcy, on the contrary, it has been further specified, strengthening the position and rights of the secured creditors (mainly banks), their priority settlement from the amount received by sale of property pledged as collateral, and their position as bankruptcy creditors, if pledged property was sold for less

than owed on the secured claim. Many protective mechanisms have been incorporated, providing an easy initiation of foreclosure proceedings by banks, which enabled banks to easily mobilize their claims, with higher access to information and transparency of data on bankruptcy proceedings (court docket, websites of Business Supervision Agency and Agency for Business Registers)

C. Capital market

(see also chapter 4- Free movement of capital)

49. What is the structure of the capital market? Is the stock exchange operational? How many companies are listed on the stock exchange? Please describe the evolution of the turnover on the stock exchange in the past five years? What percentage of transactions is carried outside the stock exchange? What are plans for the future? In practice, does capital market provide an alternative source of finance for enterprises? Please quantify?

What is the structure of the capital market?

Institutional structure of the capital market is regulated by the Law on the Market of Securities and other Financial Instruments (*Official Gazette of RS No. 47/06*) defining: conditions and procedures for issuing securities, trade of securities on the regulated securities market, the organization, structure and manner of functioning of the regulated market in the

Republic of Serbia, the definition of the term and activities of the market operator, the founding and activities of the participants on the regulated market, the organization and competences of the Securities Commission, as well as the organization and competences of the Central Registry, Depository and Clearing of Securities.

Securities Commission of the Republic of Serbia is an independent, regulatory and supervisory authority on the securities market. It is a regular member of the International Organization of Securities Commissions (IOSCO). The Commission is independent and autonomous, having the status of legal entity and performing regulatory and supervisory functions on the regulated securities and other financial instruments market. It is accountable to the National Assembly of the Republic of Serbia for its activities. The Commission has 5 members inclusive of the President of the Commission presenting and acting on behalf of the Commission. The President and the members of the Commission are elected and released from duty by the National Assembly of the Republic of Serbia, at the proposal of the relevant working body of the National Assembly responsible for finance. The legislation of the Republic of Serbia presents the legal framework for the activities of the Securities Commission. The activities of the Securities Commission in the field of the takeover of companies are regulated by the Law on Takeover of Joint-Stock Companies (*Official Gazette of RS, No. 46/2006 and 107/2009*) whereas the competencies of the Commission in the field of investment funds are defined by the Law on Investment Funds (*Official Gazette of RS, No. 46/09 and 51/09*).

The Central Securities Depository and Clearing House is a joint-stock company that keeps records of lawful possessors of securities and other financial instruments and of the rights arising from such securities and/or instruments, as well as of the third party rights to securities and other financial instruments and of such persons, and activities related to clearing and settlement of securities and clearing and settlement of financial liabilities and receivables arising on the grounds of activities involving securities, and performs other activities in accordance with the Law on the Market of Securities and other Financial Instruments.

The Belgrade Stock Exchange operates as a market operator presenting the institutional frame of the capital market in Serbia jointly with the Central Securities Depository and Clearing House and the Securities Commission. These institutions jointly with the Ministry of Finance of the Republic of Serbia, National Bank of Serbia, broker-dealer companies, commercial banks, investment and pension funds and other domestic and foreign buyers and sellers of securities present regulators, intermediaries and direct participants on the capital market of Serbia.

The securities market currently operates with the following securities: shares and bonds.

Is the stock exchange operational?

The Belgrade Stock Exchange functions as an operator of a regulated market (consisted of Official and Unofficial market segments). It is organized as a joint-stock company performing the activities related to the organization of securities trading and other financial instruments in accordance with the Law on the Market of Securities and other Financial Instruments and by-laws of the Securities Commission.

The Belgrade Stock Exchange was established in 1894. However, following the termination of its activities in 1941, it continued its activities as late as in 1989. It obtained its real function of the operator on the capital market as late as in 2001 with the introduction of the first shares in trade and the commencement of electronic bond trading of the Republic of Serbia.

The Belgrade Stock Exchange is organized as an order driven market, whereas trading is performed by the means of two standard stock exchange methods pertaining to this type of the market (single price auction and continuous trading). It is divided in two market segments:

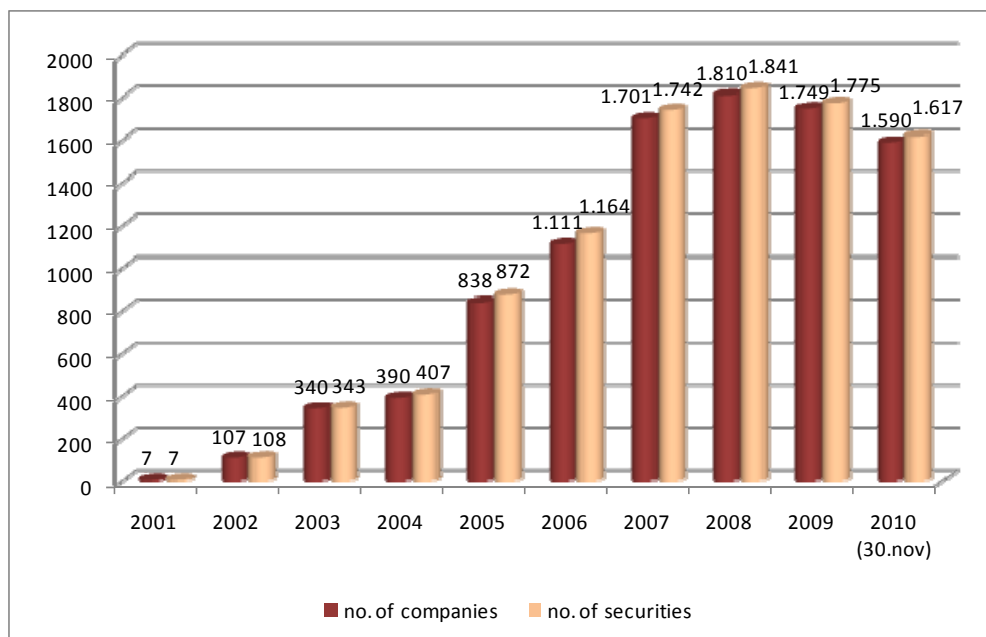
- *Official market* (official listing market segment), trading in shares of companies and debt securities obligating, in addition to legal obligations, to additional obligations (mostly referring to the higher level of corporate reporting). Apart from the additional obligations, companies have to fulfil certain conditions in terms of market capitalization and liquidity measured by average daily number of transactions and average daily turnover, but also have to perform bilingual reporting (in English and Serbian). Depending on the fulfilment of these conditions, but also on the decision of the company, the shares may be introduced into the highest market segment-Prime market or the lower segment-Standard market. In both of the segments the trading is organized using the continuous trading method.

- *Unofficial market* (traded but not listed segment) –all the shares not admitted to the official listing are on this market mostly presenting a non-liquid segment of the market, i.e. the shares of the companies that were obliged to enable a transparent secondary trade of shares of minority shareholders by introducing their shares on the Stock Exchange following the privatization process. Therefore, the companies had to observe regulations, they were not driven by market or business needs of majority shareholders. The trade of more liquid shares on the unofficial market, 33 of them, is performed using the continuous trading method, whilst the trade of other shares is performed using the single price auction on a daily basis.

How many companies are listed on the stock exchange?

According to the official listing of the Belgrade Stock Exchange, it is traded with the shares of 7 companies and with 6 bonds of the Republic of Serbia. As for the unofficial market (traded but not listed segment) 1.600 shares of the companies are quoted. The legal obligation relating to the admittance of shares on the Belgrade Stock Exchange led to the continuous increase in the quoted companies in the last ten years. The trend is changing this year, as a result of the

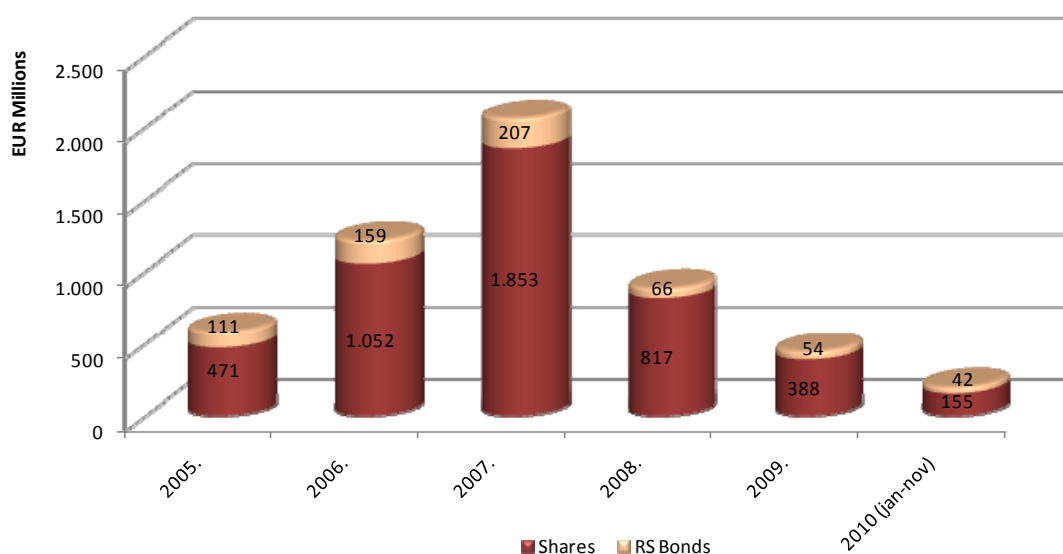
completion of the privatization process and the amendments of regulations with regard to admitted companies. This trend is expected to accelerate in the future.



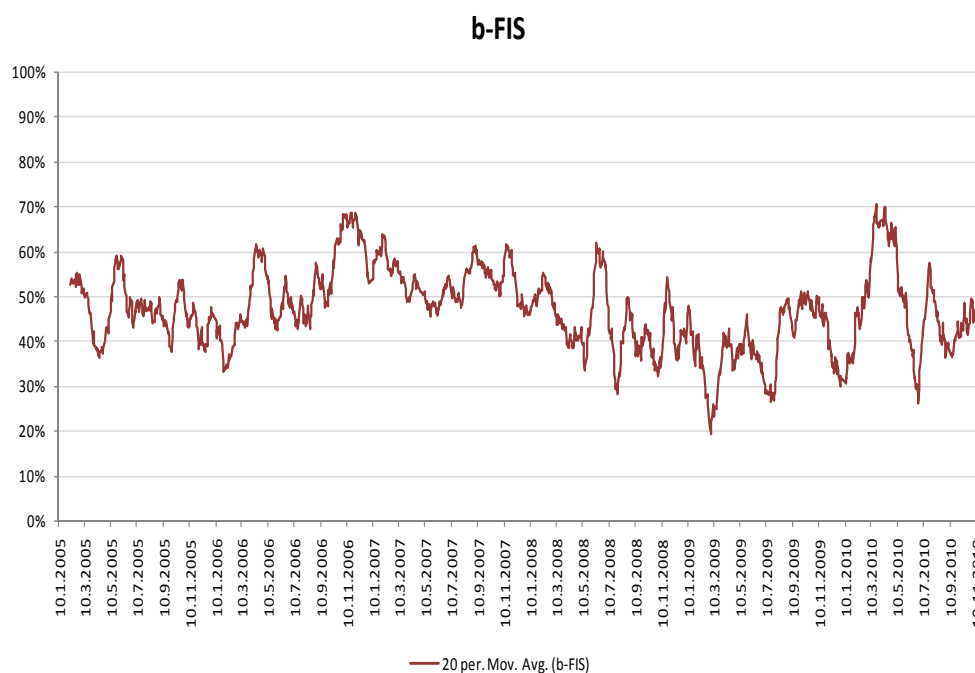
Note: the number of securities admitted to the market is higher than the number of companies as some companies issued and admitted to the market securities of different types or different characteristics.

Please describe the evolution of the turnover on the stock exchange in the past five years?

The Belgrade Stock Exchange had an increasing turnover starting with the commencement of trading in shares, which grew parallel with the continuous technological development of trading system, inclusion of new clients in trading as well as with the growth of the stock exchange indices. Following the year 2007 and the effects of the world economic crisis, turnovers and values of indices restored to the level attained at the beginning of development. The recovery is expected following the establishment of stability on developed world markets and adopting of the strategy on capital market development in Serbia. The highest growth was recorded in the period following 2004 and the commencement of electronic share trading of the Stock Exchange members from remote locations. The highest value of total turnover was recorded in 2007 amounting to over EUR 2 billion, out of which 90% was realized through trading in shares. The main characteristic of the Serbian capital market is dominant participation of shares as compared to bonds in the total turnover, owing to the unused potential of the debt market.



The basic characteristics of the trading on the Belgrade Stock Exchange are determined to a large extent by the activity of foreign investors. In the period prior to the world economic crisis foreign investors were dominant participants in trading on the capital market of Serbia. A special category of investors influencing the fluctuation of prices and turnover were foreign institutional investors holding dominant positions in the capital of domestic companies. The participation of foreign investors was primarily related to buying at the beginning, but following the escalation of crisis this relation became more balanced so that the participation of foreign investors is equally distributed on buying and selling. The graph presents the activities of foreign investors on the buy side in the last five years.



What percentage of transactions is carried outside the stock exchange?

The Central Securities Depository and Clearing House based on the data existing in the data base drew up a table containing the data on the transactions performed outside the Stock Exchange:

| Overview of trading in shares performed outside the Stock Exchange | | | | | | |
|--------------------------------------------------------------------|-------------------------------|------------------|--------------------------|----------------------------------------------------------------------------------------------------|-----------------------|-------------------------|
| Year | No. of performed transactions | Number of shares | Market value (in dinars) | Participation of trading in shares performed outside the Stock Exchange in total trading in shares | | |
| | | | | % of transactions performed outside the Stock Exchange | % of number of shares | % of total market value |
| 2004 | 19.707 | 4.595.745 | 13.912.850.592 | 22,73 | 20,98 | 36,26 |
| 2005 | 43.406 | 17.185.685 | 65.149.932.516 | 25,44 | 43,25 | 62,04 |
| 2006 | 24.106 | 13.666.774 | 121.658.433.493 | 17,26 | 35,40 | 58,28 |
| 2007 | 27.138 | 7.017.838 | 35.440.367.124 | 8,69 | 14,94 | 19,34 |
| 2008 | 41.299 | 16.186.236 | 47.929.195.355 | 26,95 | 42,48 | 41,62 |
| 2009 | 18.172 | 8.431.578 | 53.346.105.689 | 20,93 | 32,12 | 59,04 |

The data shown in the table relate to the period 2004-2009, due to the fact that the Central Securities Depository and Clearing House took over the data base relating to shares and shareholders from the Privatization Agency on 12 January 2004 showing the state of affairs on 31 December 2003, i.e. entry of shares into the Central Securities Depository and Clearing House, as well as the transactions based on trading in shares are performed as of 1 January 2004.

What are plans for the future?

Plans for the future are divided into two levels:

- 1) Strategic development and
- 2) Operational development plans.

Within the strategic development level the following activities are planned:

- the development and adjustment of the organization of the capital market of Serbia in accordance with the new Law on Securities Market, announcing the migration to MIFID regulations;
- harmonization of regulations amongst the countries in the region, as well as
- connecting with a strategic partner.

- Within the operational development level the plans are focused on:
- **Externally-** local, regional and international environment in order to maintain the position of the domestic capital market jeopardized by the effects of economic crisis influencing badly the capital market of Serbia. Within these activities it is planned to:
 - promote the concept of initial public offers to the private sector;
 - promote the introduction (issuing and trading) of debt financial instruments and financial derivatives;
 - promote alternative forms of savings and the growth of funds industry;
 - maintain the existing level and intensity of regional cooperation;
 - implement BELEXFIX system on other markets etc.
- **Internally-** increasing the quality of the services of the Belgrade Stock Exchange. Within these activities it is planned to:
 - implement the new fluctuation zone concept (dynamic volatility bands);
 - implement a new segmentation of market adjusted to critical conditions of operating based on the liquidity of market relating to individual securities and analysis of effects of certain methods of trading;
 - conversion of calculation of BELEXline index from *end-of-day* regime to *real-time* regime, as well as the development of new indices and indicators;
 - analysis of qualitative and quantitative corporate components and liquidity characteristics of the issuers of shares aimed at the increase in the corporate culture of issuers;
 - further development of the value added concept to the listed companies, implying: organization of investors' conferences, stimulation of frequent and timely reporting of the companies, new technical models of distribution of corporate reports including the development of the concept of remote-access of the issuer to the Stock Exchange; stimulation of development of better relations with investors etc;
 - improvement of the function of market maker;
 - redesigning of business policy with regard to the distributors of the Stock Exchange data;
 - monitoring new technical, technological and business achievements in industry and their implementation in the trading system of the Belgrade Stock Exchange etc.

In practice, does capital market provide an alternative source of finance for enterprises?

The basic function of the capital market relating to the financing of the development of companies through the issuing of capital market instruments in the last ten years is not developed. Investing availability of shares on the capital market is not the result of the process of incorporating of companies or the process of initial public offerings, but the privatization process.

Banking loans present the basic way to raise capital in Serbia, whereas the issuing of shares (and/or bonds) as a means for the raising of additional capital has just begun. Except for several examples of secondary public offerings of shares, primarily by banks, capital increases were mostly performed in cases when the investing of majority shareholder was

prescribed (due to contractual obligations arising from privatization agreements or owing to the requirements of certain regulatory/supervisory authorities). In the majority of cases, the whole process of capital raising was implemented through private placements, presenting a more dominant form of capital raising.

So far there have not been any initial public offerings on the domestic market, even though in the period prior to the crisis, some domestic and even foreign companies (2007) were quite interested in this form of financing.

50. To what extent did choices on the early methods of privatisation of state-owned companies affect the development of the stock market? Do limitations on certain investment in real estate and prudential rules on investment in securities of one issuer, etc. mean that the assets of institutional investors are channelled into government bonds?

To what extent did choices on the early methods of privatisation of state-owned companies affect the development of the stock market?

Bearing in mind the fact that companies have not raised capital through the initial public offer (IPO), i.e. all public companies with shares available to the investors, became open companies in the privatization process, one can say that the selection of methods of privatization had a key role regarding the development of the Stock exchange. Even though there were several legal solutions in the nineties offering different methods of privatization, two legal solutions had a crucial influence on the development of the Stock Exchange. The Law on Ownership Transformation (*Official Gazette of RS, No. 32/97*) offered the model presenting a form of insider privatization, generally leading to the wide dispersion of ownership over underlying assets, without emphasizing a dominant owner. Companies privatized in accordance with this Law had a significant potential for trading, bearing in mind that there were up to 60% of shares in the ownership of retail shareholders, and all of these shares are in “free float”, while the remaining shares remained in the ownership of the state i.e. different state institutions and agencies. In accordance with the Law on Privatization (*Official Gazette of RS 38/2001*), the basic characteristics of the privatization process, regardless of the method of the sale of capital, was the identification of dominant owner of the subject of privatization. Having this framework, all the companies which were admitted to the Stock Exchange following the sale process, had a significantly lower potential for trading, owing to the lower “free float” and consolidated ownership. Out of the two methods used during the privatization in accordance with the said law, competitive bidding was used for largest companies, leaving only up to 15% of outstanding shares to stock exchange trading. However, this trading was subject to time limits and it aimed solely at the consolidation of ownership and final takeover of the whole company. According to the second method that was used-auction sale, the property of the company (medium or small prospective capitalization) are sold in the amount of 70% of the assets, whereas 30% was allocated to the employees, presenting the maximum potential of the available free float. That situation generated a large number of open (public) companies which do not present, in terms of their size, a means for the stock exchange transactions, do not have interest to improve corporate governance and which are on the market exclusively due to mandatory regulations. The end consequence of the stated legal solutions is low liquidity (even an absolute non-liquidity) of such shares, i.e. it is impossible to valorise the value of the assets which individuals (employees-citizens) possess and it was given to them as a gift from the state.

51. How developed is the equity market? Does it provide, in practice, an alternative source of finance for enterprises? How much was raised on the market in recent years?

How developed is the equity market?

Equity market presents one of the segments of the financial market having the most dynamic and high-quality growth in recent years. Assets traded on the equity market in recent years were the shares of the companies issued in accordance with different laws, but exclusively during the privatization process. In accordance with this, the basic processes taking place on the equity market were directly related to the mechanisms of reallocation of property rights, i.e. acquiring of corporate control over companies participating on the market.

As for the secondary market microstructure, it is rather developed. The procedures implemented on the market are at the quality level existing on developed equity markets. Domestic market is recognized as such by a large number of foreign institutional investors trading daily on the Belgrade Stock Exchange.

Standard Stock Exchange trading methods (call auction or single price auction and continuous trading method) are used for the revealing of price on the order driven market, where clients have a direct market access, with infrastructure enabling members' trading from different locations as well as online (FIX 4.4. protocol). Clearing and settlement of transactions are within the competence of the Central Securities Depository and Clearing House (CSDCH). All the transactions concluded on the Belgrade Stock Exchange are binding and with the settlement period T+3 which can be even shorter (according to the acts of the CSDCH), in accordance with the system DVP (Delivery vs Payment), whereas the RTGS system is used for settlement with regard to the interbank communication. Used protection mechanisms are the guarantee fund registered with the CSDCH, as well as special procedures to protect settlement (buy-in, sell-out).

All securities are classified by CFI code and identified by ISIN numbers.

Serbian market is identified as a frontier market in international investment circles.

Corporate management, presenting the criterion for the development of equity market in Serbia, is one of the fields making significant improvements in the former period. All the companies having their shares traded, are obliged to publish the basic information on their business activities in accordance with the Law using the basic prospect and register on the Stock Exchange.

Companies officially listed on the Belgrade Stock Exchange are obliged to accept and implement the codes of corporate governance harmonized to the full extent with the good business practise in the European Union. Except for the minimum defined by the Law, companies officially listed on the Belgrade Stock Exchange are obliged to perform the prompt bilingual reporting, as well as to publish quarterly business and financial reports.

Generally speaking, the reporting of the companies has been made transparent. The company is obliged to publish (in at least one daily newspaper) information on the outcome of public offer, report relating to important events, excerpt from annual financial reports, as well as other reports significant for the business activities of the companies. Unauthorized usage of privileged (inside) information is defined as a basic misuse and manipulation on the financial market.

Does it provide, in practice, an alternative source of finance for enterprises?

It has already been answered in question 49.

How much was raised on the market in recent years?

The Central Securities Depository and Clearing House based on the data existing in its data base drew up a table containing the data on the total money turnover of shares with regard to transactions performed on the Stock Exchange and outside the Stock Exchange.

| Total money turnover of shares realized on the Stock Exchange and outside the Stock Exchange (in dinars) | |
|-------------------------------------------------------------------------------------------------------------|--------------------|
| Year | Amount |
| 2004 | 38.382.223.968,81 |
| 2005 | 107.999.501.647,70 |
| 2006 | 208.742.073.362,50 |
| 2007 | 185.572.209.079,01 |
| 2008 | 117.439.928.937,78 |
| 2009 | 90.618.134.949,65 |
| Total: | 748.754.071.945,45 |

The data shown in the table relate to the period 2004-2009, due to the fact that the Central Securities Depository and Clearing House took over the data base relating to shares and shareholders from the Privatization Agency on 12 January 2004 showing the state of affairs on 31 December 2003, i.e. entry of shares into the Central Securities Depository and Clearing House, as well as the transactions based on trading in shares are performed as of 1 January 2004.

52. How developed is the bond market? Who are the main participants in the market and which are the main financial instruments used? Are there private issues? Is there a secondary market? Please supply detailed information on the size, activity and structure of the bond market, including average maturity of the most important securities.

The most important securities on the bond market are long term treasury securities issued by the Republic of Serbia in 2002 in order to repay debts in accordance with the Law on the Settlement of the Public Debt of the Federal Republic of Yugoslavia arising from the Citizens' Foreign Exchange Savings (*Official Journal of the FRY, No. 36/2002*). In accordance with the said Law, public debt stock, i.e. the volume of issued securities amounted to EUR 4.2 billion. The bonds mature on each 31 May, in the period 2002-2016 containing a pre-calculated annual interest rate of 2%, until maturity date. Bonds were issued as non-material securities, individually for each year, registered in the name of the holder and being transferable, registered in proprietary accounts with the Central Securities Depository and Clearing House, and paid in euros or dinars, at the owner's request.

The bonds of the Republic of Serbia are traded on the Stock Exchange-using foreign currency and on the OTC market -using dinars. Bondholders may be domestic and foreign legal entities and individuals.

The trade in bonds of the Republic of Serbia is unlimited and tax-free, payment operations commission-free, capital gains tax-free, financial transactions tax-free and free from other

taxes. Foreign legal entities and individuals may freely transfer abroad the foreign exchange funds acquired through the sale of bonds.

Foreign legal entities and individuals may freely transfer abroad the foreign currency realised through the sale of bonds.

As of September 2002 until 30 November 2010, the total volume of trading in bonds of the Republic of Serbia on the Belgrade Stock Exchange and on the OTC market amounted to EUR 5.138,0 million. Out of this amount, the turnover of EUR 987.7 million was realized on the Belgrade Stock Exchange, whereas the turnover of EUR 4.150,3 million was realized on the OTC market i.e. the trading outside the Stock Exchange exceeds the OTC trading by four times.

According to the data of the Central Securities Depository and Clearing House, the participation of foreign investors related to the trading in these bonds, amounted to 22.6%.

On 30 November 2010, the market value of the block of bonds (series A2011 - A2016) amounted to 86.9% of the nominal value- the highest market value referred to the bonds maturing on 31 May 2011- 97.9%, whereas the lowest referred to the bonds maturing on 31 May 2016- 78.9%.

Currently it is traded on the stock exchange market with the 6 remaining series of sovereign bonds denominated in euros and having maturity dates until 2016. Corporate bonds were sporadically admitted to the trading on the unofficial market in recent years. However, their joint characteristic was total, or almost total absence of trading. The fact that there is only one corporate bond currently traded ~~outside~~ on the Belgrade Stock exchange speaks in favour of the underdevelopment of bond market which still does not present the way to raise capital. Private placements of corporate bonds are presented to some extent; however they remain in the sphere outside the secondary trading.

D. Money market

53. How developed is the market for short-term financial instruments? Who are the main participants in the market and which are the main financial instruments used? Is there a secondary market? Please supply detailed information on the size, activity and structure of the money market.

The most important financial instruments on the money market are bills issued by the National Bank of Serbia and treasury bills issued by the Republic of Serbia.

The National Bank of Serbia issues bills in order to regulate the liquidity of banks, primarily related to the withdrawal of excess liquidity from the banking system. As of January 2009, the National Bank of Serbia has issued bills with maturity of up to one year which are sold at repo auctions, having transaction due date of two weeks and using the fixed, key policy rate of the NBS. Banks may trade amongst themselves with bills on the OTC market, having the obligation to sell the same bills to the National Bank of Serbia on the repurchase date. Auctions are organized once a week (every Wednesday).

The buyers of bills on the primary and secondary markets may only be domestic banks, having in mind the secondary market is underdeveloped.

On 15 November 2010 in the portfolio of the banks there were bills in the amount of RSD 39.9 billion.

One of the most important segments of the domestic money market is interbank money market. The participants on the said market are domestic banks. Taken out loans have maturity from overnight loans to loans with a 12-month repayment period

As of January 2008, the National Bank of Serbia has calculated and published data on overnight loans on domestic interbank money market. In the period as of 1 January 2009 until 15 November 2010, the average daily volume of these loans exceeded RSD 8.1 billion. 33 banks participated on the market in the said period. In the period as of 1 April until 15 November 2010, the average daily volume of these loans amounted to RSD 8.2 billion. The weighted average interest rate of 8.5% was realized in the said period.

Primary market of short-term financial instruments functions through the emission of treasury bills in domestic currency having the maturity of: 3, 6 and 12 months (it has been functioning as of 2003), 18 months (as of May 2010) and 24 months (as of July 2010). The auctions take place twice a week. The participants are the banking sector and professional investors, with low presence of individuals. Secondary market is not organized. However, certain transactions are performed "over the counter" following the primary trading.

54. What changes are considered necessary in order to improve market organisation and efficiency?

In order to improve money market, the following activities of relevant institutions should be directed to the organization of information support for collecting and distribution of relevant data needed for secondary trading with short-term financial instruments, i.e. the treasury bills of the RS and bills of the NBS. The National Bank of Serbia is also ready to provide necessary assistance and support to market participants related to the establishment of legal framework for the efficient performance of secondary trade of these securities. It is also planned to establish the cooperation with market participants in order to collect, exchange and analyze market trends (Market Intelligence).

E. Non-bank financial institutions

(see also chapter 3- Right of establishment and freedom to provide services)

55. What is the number of insurance institutions operating in Serbia?

a) total number;

b) domestic;

c) non-domestic- EU, of which:

i) subsidiaries and

ii) branches

d) non-domestic non-EU, of which:

i) subsidiaries and

ii) branches.

Changes in (a) to (d) since 2003.

Enclosed Excel table containing the answer to question 55. (*See Annex)

56. Concentration of respectively the life and non-life markets (in terms of gross premiums held by the largest undertakings), indicating whether they are:

a) domestic;

b) non-domestic EU;

c) non-domestic non-EU.

Changes in (a) to (c) since 2003.

Enclosed Excel table containing the answer to question 56. (*See Annex)

57. Please assess the degree of competition in the sector.

In accordance with the Law on Insurance adopted in 2004, insurance companies which performed unlawful business activities and contrary to the insurance profession rules were excluded from the insurance market. Owing to the adoption of this Law, normative preconditions for high-quality development of the insurance market and better protection of the beneficiaries of insurance services were created.

At the same time, there was an increase in foreign investments into the insurance activities and the strengthening of competition, i.e. the establishment of new insurance companies, whose founders are primarily foreign insurance companies having done business on their home state market for a longer time. Owing to this, better selection and quality of insurance products is provided.

In the period starting with 2004, with 40 insurance companies doing business until the third quarter of 2010, with 26 companies doing business, 18 operating licences were revoked, 5 insurance companies conducted voluntary liquidation, one transformation into a voluntary pension fund was performed, one merger took place, and as many as 11 green field licences were issued. Twenty two companies are engaged solely in the insurance activities whereas 4 are engaged in the reinsurance activities. As for the companies engaged in insurance activities, 7 companies deal solely with life insurance, 9 companies with non-life insurance, and 6 companies deal with both life and non-life insurance.

Share of insurance companies in the total premium according to peer groups ¹⁾

| Group | | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 3Q2010 |
|-------|-------------------------------|------|------|------|------|------|------|--------|
| I | Share in % | 74.2 | 64.9 | 63.4 | 59.0 | 69.6 | 65.8 | 64.9 |
| | Number of insurance companies | | | | | | | |
| II | Share in % | 11.8 | 21.5 | 21.6 | 22.1 | 19.0 | 23.2 | 22.8 |
| | Number of insurance companies | | | | | | | |
| III | Share in % | 14.0 | 13.6 | 15.1 | 18.8 | 11.4 | 11.0 | 12.3 |

| | | | | | | | | |
|--|-------------------------------|--|--|--|--|--|--|--|
| | Number of insurance companies | | | | | | | |
|--|-------------------------------|--|--|--|--|--|--|--|

1)The companies dealing with reinsurance are not included.

Source: National Bank of Serbia

Two largest companies (DDOR and DUNAV) had majority share (74.2%) on the insurance market in 2004, with a decreasing trend until 2007, according to the data shown in the Table. Following this period, another insurance company joined the said group.

However, insurance market in Serbia, measured by Herfindahl Hirschman's index still has the characteristics of a concentrated market, with decrease in 2007 **from high to moderate level**, which is the result of joining new companies and maintaining this trend following 2007 (index value of 1523 in 2007 drops to 1182 in the third quarter of 2010.)

58. What is the situation regarding new financial markets and instruments, for example venture capital companies, factoring, leasing, etc.? Is the legal framework in place for such operations? Please provide any available information on market developments.

Financial leasing is regulated by the Law on Financial Leasing (*Official Gazette of RS, No. 55/2003 and 61/2005*).

The said Law does not present an adequate legal framework for defining needed conditions for business operations based on good financial foundations of financial lessors with regard to the relevant EU regulations, owing to which the initiation for the amendment of the Law was launched. The leaders of activities relating to the drafting of a new Law are the Ministry of Finance and the National Bank of Serbia.

Taking into account the development of financial leasing market, the following data is provided:

| No. | Description | December 2007 | December 2008 | 31 December 2009 |
|-----|------------------------|---------------|---------------|------------------|
| 1 | Assets | 95.265.098 | 122.550.536 | 111.313.931 |
| 2 | Capital | 5.901.680 | 6.224.605 | 8.956.313 |
| 3 | Long-term liabilities | 85.630.081 | 111.582.929 | 100.397.529 |
| 4 | Short-term liabilities | 3.733.337 | 4.743.002 | 1.960.089 |

59. Please provide information on the establishment of a capitalised pension system. What are the main challenges for its development? What are the planned steps?

Voluntary pension funds in the Republic of Serbia present the result of the pension system reform initiated by the adoption of the **Law on Voluntary Pension Funds and Pension Schemes** (*Official Gazette of RS, No. 85/2005*, adopted on 6 October 2005). The Law is implemented as of 1 April 2006. Owing to the adoption of the said law, system of voluntary

pension funds was introduced, so that the pension system of the Republic of Serbia now includes the First and the Third pension insurance pillars. The First Pillar is the State Pension and Disability Fund, obligatory for all employees and functioning according to the system pay-as-you-go. The Third Pillar includes voluntary private pension funds functioning according to the system of accumulation and capitalization of assets and defined contributions, where the amount of the pension is not guaranteed, but depends on the amount of the realised returns.

Currently there are 8 voluntary pension funds management companies jointly with 9 voluntary pension funds on the Serbian market (one management company governs two pension funds). Total amount of net assets of all pension funds at the end of October 2010 amounted to EUR 88.3 million (RSD 9.49 billion). There are 168.992 beneficiaries in the system of voluntary pension funds having 222.581 concluded contracts (one beneficiary may be a member of several funds).

According to the above-mentioned data, the industry of voluntary pension funds is still insufficiently developed, which is not unusual, bearing in mind that it has existed for only four years. At the same time, the data show the room for its further development. The fact that the capital market in Serbia is underdeveloped, i.e. there is an insufficient number of high-quality securities and therefore the dispersion of investments is narrow, presents a significant impediment for the development of the system of voluntary pension funds. One should bear in mind that the world economic crisis influenced both domestic economy and standard of living of the citizens of Serbia, therefore those events contributed to somewhat slower growth of the said industry. Financial education of citizens should also influence in a positive way the development of the system of voluntary pension funds.