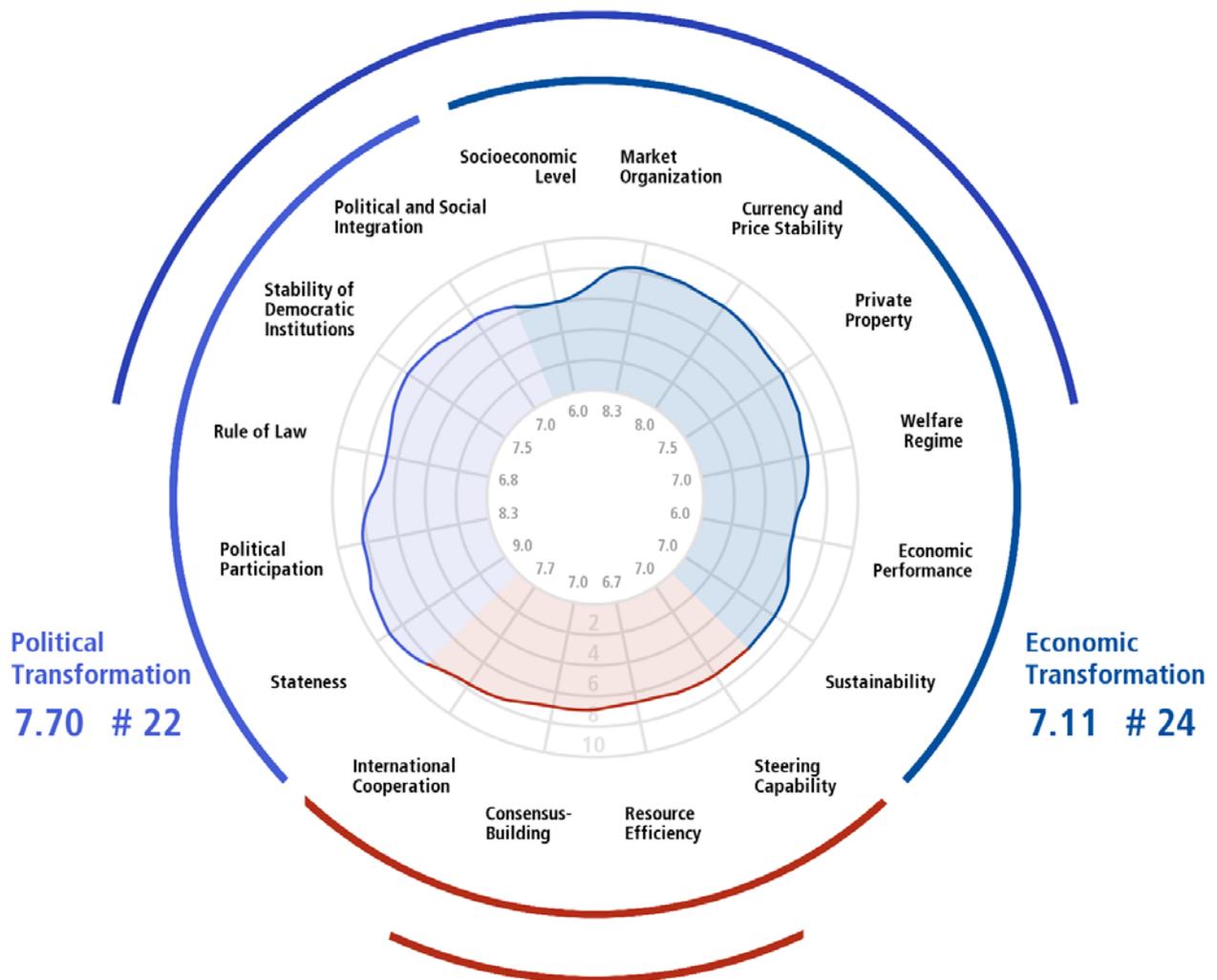


Serbia

Status Index

7.40 # 19

on 1-10 scale out of 129



Governance Index

6.06 # 22

on 1-10 scale out of 129

This report is part of the Bertelsmann Stiftung's Transformation Index (BTI) 2018. It covers the period from February 1, 2015 to January 31, 2017. The BTI assesses the transformation toward democracy and a market economy as well as the quality of political management in 129 countries. More on the BTI at <http://www.bti-project.org>.

Please cite as follows: Bertelsmann Stiftung, BTI 2018 Country Report – Serbia. Gütersloh: Bertelsmann Stiftung, 2018.

This work is licensed under a [Creative Commons Attribution 4.0 International License](https://creativecommons.org/licenses/by/4.0/).

Contact

Bertelsmann Stiftung
Carl-Bertelsmann-Strasse 256
33111 Gütersloh
Germany

Sabine Donner

Phone +49 5241 81 81501
sabine.donner@bertelsmann-stiftung.de

Hauke Hartmann

Phone +49 5241 81 81389
hauke.hartmann@bertelsmann-stiftung.de

Robert Schwarz

Phone +49 5241 81 81402
robert.schwarz@bertelsmann-stiftung.de

Sabine Steinkamp

Phone +49 5241 81 81507
sabine.steinkamp@bertelsmann-stiftung.de

Key Indicators

Population	M	7.1	HDI	0.776	GDP p.c., PPP \$	14512
Pop. growth ¹	% p.a.	-0.5	HDI rank of 188	66	Gini Index	29.1
Life expectancy	years	75.5	UN Education Index	0.779	Poverty ³	% 1.4
Urban population	%	55.7	Gender inequality ²	0.185	Aid per capita \$	44.0

Sources (as of October 2017): The World Bank, World Development Indicators 2017 | UNDP, Human Development Report 2016. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$3.20 a day at 2011 international prices.

Executive Summary

Serbia's current political system is characterized by the dominant rule of one political party at the national and provincial level, as well as most of the local government units. Parliamentary elections in April 2016 were evaluated as free and competitive, but characterized by biased media coverage and uneven advantages for incumbent governing elites relying on administrative resources. Civil society exerts only a weak impact on public policies, as governmental bodies do not regularly hold public discussions and consultations on draft legislation and policy proposals. The existing system of "checks and balances" is occasionally challenged. The, so-called, "fourth branch of power" – the Ombudsman and the Commissioner for Information of Public Importance and Personal Data – is often obstructed and its power is often limited to issuing non-binding recommendations and public appeals. Although most observers considered the 2016 parliamentary elections free and fair, opposition parties have complained about the quality of the election process.

The strategic priorities set by the government have been undermined by frequent parliamentary elections since 2012. Although the subjection of state power to the law exists, in recent practices it is undermined, particularly by passing laws on urgent procedures and infringements of independence of autonomous bodies such as the Ombudsman.

Minority rights are mostly respected and developed, as Serbia, according to its constitution, is defined as a multicultural state, rather than civic. The independence and pluralism of the mass media system has declined. The judiciary is not operating completely independently from political influence and is further plagued by inefficiency, nepotism and corruption. Anti-corruption policy is not consistent, since there are few judicial verdicts regarding high state officials, and envisaged activities and measures from the anti-corruption strategy and action plan are not fully implemented. The unemployment rate is still considerably high and informal employment is

widespread. The income inequality is especially pronounced in Serbia and a large percentage of people are at risk of poverty and social exclusion.

The government has introduced several important economic and fiscal reforms since 2014. The most important ones include streamlining the processes of obtaining a building permit, industrial relations and further inclusion of e-government services. The program of fiscal consolidation finally made the level of public debt stable, with an envisaged downward trajectory. However, public sector is still over employed, with little responsibility and efficiency. The current system of streamlining without functional analysis may be a significant burden on the future provision of public services. Fiscal rules (regarding public expenditures and public debt) are still disregarded. Reforms in management of public companies are yet to give any results (apart from the rail transport), and the process of privatization of state owned companies has been only partially carried out. Economic growth has finally rebounded, reaching 2.7% in 2016 and Serbian GDP surpassed its pre-crisis 2008 level, with moderately good economic prospects.

One of the most disputed issues Serbia is faced with relates to its border and the definition of territory, as the status of its formerly autonomous province Kosovo and Metohija (referred to as Kosovo in this report) has not been solved yet. Relations with neighboring Western Balkans countries have worsened in 2015 and 2016, primarily due to the political statements and actions of certain state officials. The main strategic goal of joining the European Union has not changed and the accession process has been continued.

History and Characteristics of Transformation

Serbia's transition to democracy and market economy has been fraught with statehood conflicts. The first democratic election took place in 1990, when Serbia was the largest constituent republic of the Socialist Federative Republic of Yugoslavia. The successor party of the former Communist party, led by Slobodan Milosevic, won the elections. Whereas Milosevic and his allies sought to preserve the common federal state in a centralized form, the newly elected political leaders of the Slovenian and Croatian republics wanted to decentralize and/or exit the federation. Irreconcilable objectives and nationalist mobilization led to the collapse of the federation, several wars and the emergence of Bosnia and Herzegovina, Croatia, Macedonia and Slovenia as independent states.

Facilitated by the wars, Serbia's President Milosevic established a semi-authoritarian regime in the remaining parts of Yugoslavia and remained in power until 2000. Clientelistic networks in the state apparatus and the state-dominated economy enabled him to control the electronic media, forge election results and effectively divide and isolate the political opposition. Responding to its deepening integration and legitimation crisis, the regime increased political repression in Serbia proper and violently repressed ethnic Albanians in Kosovo via military means. The country then slid into full-scale war. NATO air strikes forced the regime to abandon its control over Kosovo.

Military defeat, the deepening socioeconomic crisis, a student protest movement and a broad alliance of opposition parties contributed to Milosevic's ouster in October 2000. The opposition coalition won the federal parliamentary and presidential elections as well as the Serbian local and parliamentary elections in 2000. The opposition leaders Vojislav Kostunica and Zoran Djindjic became federal president and Serbian prime minister. The heterogeneity of the coalition and the assassination of Djindjic in 2003 limited the government's capacity to sustain its initially dynamic policy of economic and political reform. However, successive parliamentary and presidential elections in 2003, 2004, 2007 and 2008 generated majorities for political parties and candidates who were committed to liberal democracy and European integration. In 2006, Serbia adopted a new constitution, and in 2008 a Stabilization and Association Agreement was signed with the EU.

In 2008, a group of politicians led by Tomislav Nikolic and Aleksandar Vučić left the anti-EU Serbian Radical Party and created the pro-EU Serbian Progressive Party (SNS). Together with the Socialist Party of Serbia, the SNS won the 2012 elections, and Nikolic became state president in 2012. The 2014 parliamentary election confirmed a governing coalition of political actors who had once supported the Milosevic regime.

Serbia's state framework has changed several times since the dissolution of communist Yugoslavia. Between 1992 and 2003, Serbia and Montenegro, the two still united republics of the former Yugoslavia, constituted the Federal Republic of Yugoslavia. In 2003, Serbia and Montenegro replaced this state with an EU-facilitated state union possessing only limited powers. The main aims of this union were EU accession and the creation of an internal market in accordance with EU principles and standards. Following a referendum in 2006, Montenegro became an independent state and the state union was dissolved.

As a consequence of its military defeat in the Kosovo war, Serbia had to accept a U.N.-led interim administration in Kosovo. This administration has exercised political authority over the territory since 1999, based upon U.N. Security Council Resolution No. 1244/1999. Serbia's government and major political actors interpret this resolution as the legal basis according to which Kosovo continues to belong to Serbia. Following violent interethnic clashes in Kosovo, the international community in 2005 initiated negotiations between Serbia's government and the Kosovo Albanian representatives on the final status of Kosovo. The failure of these talks led the United States and major Western states to back internationally supervised independence for Kosovo. In 2008, the government in Pristina declared Kosovo's independence, subsequently recognized by major Western states but fervently opposed by Serbia, Russia, China and, among others, five EU member states.

In 2013, Belgrade and Pristina agreed to integrate the municipalities of Northern Kosovo, where the majority of residents are ethnic Serbs, into Kosovo's legal framework in exchange for guaranteed representation and veto rights. This so-called Brussels Agreement as well as the arrest and extradition of several indicted war criminals by Serbia's government paved the way for the opening of EU accession negotiations in 2014.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

Transformation Status

I. Political Transformation

1 | Stateness

The Republic of Serbia has the monopoly on the use of force over its territory with the exception of its formerly autonomous province of Kosovo and Metohija (in Kosovo), the status of which is disputed. Serbia opposed the Kosovar parliament's declaration of independence in 2008 and continues to consider Kosovo as part of its state territory. Its legal argument is that U.N. Security Council Resolution 1244/1999 guarantees the territorial integrity of the Federal Republic of Yugoslavia (FRY) and Kosovo's autonomy "within" FRY. As the undisputed successor state of FRY, Serbia is also considered to be the inheritor of these guarantees.

In 2016, Kosovo was recognized as an independent state by more than 100 countries, including 23 of 28 European Union member states. Yet, Kosovo is still not a member of the United Nations. The multinational peace force, NATO-led Kosovo Force (KFOR), and the United Nations' mission, established by Resolution 1244 as an international security presence and an interim administration for Kosovo, continue their presence in Kosovo but operate on a much lower level than before 2008.

Improvements in the organization and capacities of police, security and intelligence agencies have significantly reduced the threats posed by organized crime to public security and order in Serbia. In 2016, the government adopted a first thorough threat assessment of serious and organized crimes. However, the authorities failed to arrest and convict major criminal groups in the period under review.

However, in October 2016, there was a serious incident characterized as an assassination attempt nearby the home of Aleksandar Vučić when a van filled with guns and ammunition was found. This clearly shows that the state monopoly on the use of force is still challenged.

Question
Score

Monopoly on the
use of force

9



1

The constitution defines Serbia as the state of the Serbian people and all citizens who live in Serbia. According to the 2011 census, the population is composed largely of ethnic Serbs (83.3%). In addition to Serbs, there are also Hungarians (3.5%), Roma (2.1%), Muslims (0.3%), Bosniaks (2%), Croats (0.8%), Slovaks (0.7%), Albanians (0.1%), Montenegrins (0.5%) etc.

Although the first article of the constitution clearly supports the Serbian majority, it also sets out a multicultural model of state and its society, rather than a civic one. Therefore, national minority rights are highly developed and national minority councils are established for 19 minorities. Furthermore, the official use of minority languages in public issues and even education is allowed in certain local self-government. In the Autonomous Province of Vojvodina, there are six official languages (Serbian, Hungarian, Croatian, Romanian, Slovakian and Ruthenian). Ethnic Serbian citizens residing in neighboring countries are entitled to hold dual citizenship, with the exception of Montenegro as Montenegrin citizens are expected to renounce other citizenships.

Serbia is defined by its constitution as a secular state. It is also, for the most part, socially secular. Serbia is one of the most religiously diverse European countries. Its population is composed of 84.5% Serbian Orthodox, 5% Roman Catholic, 3% Islamic, 1% Protestant, 1.1% atheistic or agnostic, 0.1% other and 4.4% unspecified. Religious dogmas have some impact on the state policies.

However, the Serbian Orthodox Church often tries to exert political and moral influence. For example, the Serbian Orthodox Church strongly objected to Kosovo independence, opposed same-sex marriage, opposed abortion and idealized the royalist Chetnik resistance movement of World War II. Many citizens attribute moral authority to the Serbian Orthodox Church and its statements. Furthermore, in most recent cases the Serbian Orthodox Church has clearly put itself above the laws of the state, by confirming ongoing tax immunity. The same case is present with other religious communities in Serbia.

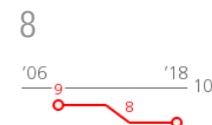
In some regions in Serbia with religion majority other than the Serbian Orthodox one, there is a presence of clergy dogmas within the certain religion community. This was particularly the case in the Muslim communities' conflict in Novi Pazar with neighboring local self-government units. Later on, this was also present in the political engagement of former mufti, Muamer Zukorlic, and in establishing immunity from the state laws, such as in cases of illegal construction.

State identity



1

No interference of religious dogmas



1

Serbia has a differentiated administration that extracts and allocates state resources throughout the country, albeit with limited efficiency and effectiveness. 99% of the population has access to an improved drinking water source, and 96% of the population has access to improved sanitation facilities (World Bank data).

Basic
administration

10



2 | Political Participation

In the period from 2012 to 2016, three parliamentary elections and one presidential election took place. The 2014 and 2016 parliamentary elections were extraordinary elections linking subnational elections with national elections, called for by the governing coalition to capitalize on the weakness of the major opposition party and to benefit from the relatively high popular support for Prime Minister Vučić. The parliamentary election of April 24, 2016, was held according to a proportional electoral system with a 5% threshold, party lists and a single nationwide constituency. The turnout was 56%. The Venice Commission of legal experts attached to the Council of Europe and the European Parliament have criticized that after the elections political parties are able to freely choose which candidates from their lists become members of parliament.

Free and fair
elections

8



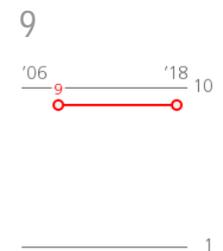
The international observers sent by the Organization of Security and Cooperation in Europe (OSCE) stated that the 2016 parliamentary election respected the fundamental freedoms of voting and offered voters a choice between different political parties. However, their report also noted a “biased media coverage, undue advantage of incumbency and a blurring of distinction between state and party activities...Key shortcomings include unclear rules on candidate registration,...the misuse of administrative resources for campaigning, inadequate regulation of campaign finance, deficiencies and loopholes in dispute resolution.” Moreover, the report observed, “ruling parties exerting pressure on voters, particularly those employed in the public sector, and enticing voters through welfare initiatives.”

By January 2017, the state institutions had not fully investigated several complaints submitted by opposition parties and movements on the elections.

The access to media favors the ruling Serbian Progressive Party (SNS). According to one report, around 51.4% of all print and electronic media content is dedicated to the SNS and its leader, Prime Minister Vučić. The opposition parties have tried to address this imbalance by using social networks to communicate its positions.

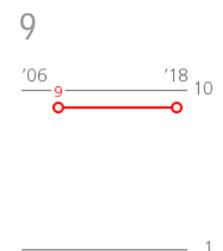
Serbia's democratically elected government has the effective power to govern. Parliament has democratic and civil oversight of the army and the secret service through its parliamentary defense and security committee. However, these committees have rarely exerted genuine control over the government. In particular, these committees have little influence over the security sector actors. The executive clearly dominates the legislature, and executive power is clearly dominated by the prime minister and his decisions. Although the government claimed to have banned domestic and foreign business tycoons from interfering in the policy-making process, they continue to influence political decision-making through informal channels, particularly in the cases of great capital investments. In 2015 to 2016, courts have launched proceedings against some tycoons (for example, Miroslav Bogićević from Šabac, the owner of the company Farmakom), while trials against other tycoons have been pending as of January 2017.

Effective power to govern



The freedoms of association and assembly are constitutionally guaranteed and the government generally respects these rights in practice.

Association / assembly rights

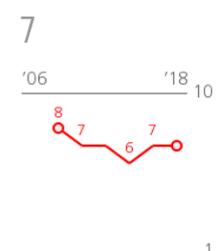


Parliament adopted a new law on public gatherings in February 2016, introducing some improvements (legal remedies) and aiming to align with the Serbian constitution. However, NGOs criticized that the new restrictions would prevent medical workers and teachers from protesting in front of their work places. Activists of the LGBT community were able to hold the Pride Parade in Belgrade in 2015 and in 2016.

The police and public prosecutors tried to intimidate activists of the “Let’s Not Give/Drown Belgrade” movement, a civic initiative that organized protests in 2016 to oppose a major commercial and real-estate development project promoted by Belgrade city and national authorities. In 2015, the authorities prohibited roughly six rallies. One of the banned demonstrations was the Seven Thousand event planned to be organized for remembering the victims of the Srebrenica massacre in 1995. This event was canceled due to an estimated high security risk.

The constitution guarantees freedom of expression and freedom of press. However, the independence and political pluralism of the media system has declined in recent years. This has been due to a dramatic reduction in purchasing power, predominance of certain political groups, falling living standards, opaque media ownership and funding, weak financial base of many private media outlets, and a corresponding dependence on business and political interest groups.

Freedom of expression



In August 2014, parliament adopted a Law on Public Information and Media envisaging the privatization of almost all publicly owned media in order to create fair competition for all media. The only exceptions from mandatory privatization were the main public service broadcasters, which target the population of Kosovo, and minority media publishers established by National Minority Councils. The privatization of several media groups has been highly disputed and impacts the

quality of information. On the local level, this was the case in Belgrade, Kragujevac, Krusevac, news agency “Tanjug,” dailies “Politika” and “Vecernje novosti.” Moreover, the privatization of state media outlets did not lead to greater transparency of ownership or funding sources, including state funding.

Political actors exert influence over the editorial policies of print and electronic media. Financial and editorial pressures are placed on the media. Those that are most critical of the government are attacked publicly. For example, the investigative media group Balkan Investigative Reporting Network, cable TV “N1” and certain on-line portals are often targeted as hostile.

There are threats, violence and intimidation against journalists. Very often, information leaks to media outlets (e.g., about ongoing investigations) threaten the personal safety of journalists and are an invasion of personal privacy. According to the EC Serbia Report 2016, investigations and prosecution of reported intimidation and attacks on journalists are rare.

However, journalists tend to self-censor, particularly when interviewing members of the establishment.

3 | Rule of Law

The separation of powers is in place and functioning. Checks and balances are occasionally subject to interference, but a restoration of balance is sought. The separation of powers is secured through the constitution of the Republic of Serbia and numerous laws defining the status and relations of the executive, legislature and judicial system.

Although the subjection of state power to the law exists, in recent practice it is undermined by several negative tendencies. According to research from Open Parliament in 2016, 88 laws were passed, from which 51 (59.00%) followed the urgent procedure that constrains the parliament’s influence on legislation. According to the same research, 98% of passed laws were proposed by the government. According to the Ombudsman Report, the government used a law on maximum staff sizes in the public sector to undermine the independence of the Ombudsman Office. According to the European Commission’s 2016 report on Serbia, the legislative and constitutional framework leave some room for undue political influence over the judiciary.

The judiciary in Serbia is not independent, but it is fairly influenced by political pressures from the executive power. Even the constitution, although prescribing judicial independence as a principle and rule, also stipulates that the three branches of power are to control each other, leaving some room for influence on the judiciary.

Separation of powers



1

Independent judiciary

6

However, the biggest problem lies in judicial appointments, where the national parliament appoints new holders of judicial offices, who are then reelected after three years by the Judicial Council. Prevailing political culture and the election system concentrate political power at a small group of political oligarchy instead of dispersing it over the whole political party, which leaves the executive power holding the prevailing influence over the legislative, instead the other way around. This situation is further aggravated by the existing practice of judicial appointments.

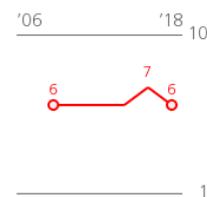
International sources describe the country's judiciary as very prone to political influences. World Economic Forum ranks Serbia as 122 out of 138 countries in its Global Competitiveness Report 2016-2017. World Justice Project depicts Serbia in its Rule of Law Index as a country with a very weak rule of law, especially in the area of Improper government influence. Furthermore, courts are slow and inefficient with an average length of a court case standing at 635 days (World Bank, Doing Business 2017) and there is a significant backlog of old unresolved cases, which augments delays.

Corruption is also one weak point of the judiciary. The existing strategic documents on judicial reform are not strictly followed and implementation is lagging. The new minister of justice (after the 2016 elections) promised new deep reforms of the judiciary, but this is yet to be seen. High ranking politicians continue to influence courts by even publicly criticizing court dealings and calling for what should be or not be done.

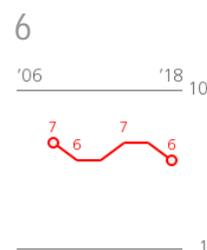
The current situation is illustrated by the Savamala affair in May 2016 in which a group of armed masked men razed to the ground a city quarter in downtown Belgrade and restrained movement of the people in vicinity while the police were ordered by high officials not to intervene. Furthermore, this was done with the help of city utility services. Still no one has been prosecuted and the investigation is still ongoing. A constant problem regarding division of power in Serbia is the dominance of executive power over the judicial and legislative powers.

Serbia has created an existing legal framework to fight corruption, abuse of power and other corrupt practices. The regulation continues to be upgraded, most recently by introducing the law on protection of whistle-blowers, which began implementation in 2015. However, cases of public officials in senior positions being found guilty of corruption or similar felonies are very rare. Allegations of corruption among politicians are often used as a political weapon against other parties and their leaders, and these allegations seldom initiate court proceedings.

The trial settled in 2016 found one of the most prominent tycoons in the county, Miroslav Miskovic, an accomplice in a tax evasion scheme conducted by his son's company. However, an appeal of this verdict is expected.



Prosecution of office abuse



The public procurement process is envisaged as a focal point of corruption, leading to a new law to tackle this question adopted in 2013. However, a significant amount of public procurements still evade the law through loopholes in legislation. Furthermore, the most important infrastructure projects are not implemented along the guidelines set by the law on public procurement, since they are usually set up as a part of international agreements, which take precedence over national law (some of these agreements were concluded with the Russian Federation, Azerbaijan and the United Arab Emirates).

Implementation of the National Anti-Corruption Strategy 2013-2018 is very slow and inefficient, and completely lacking in some areas, most prominently in the field of public company management, which is prone to political appointments regarding the level of expertise. By January 2017, parliament had not adopted the new law on the anti-corruption agency and amendments to the criminal code in the economic crimes sections. Amendments to the law on free access to information of public importance and the law on ombudsman, which were envisaged to strengthen their capacities and were compiled in 2011, were still not enacted.

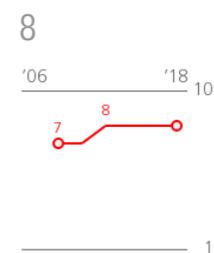
In January 2017, the government continued to ignore the recommendations of its Anti-Corruption Council, and the Anti-Corruption Agency was not fully staffed.

For parliamentary elections held in 2016, the supervisory board of the national parliament was not created, although prescribed by law on the election of members of parliament, since the government and majority of members of parliament did not appoint their representatives to this entity, whose main tasks would be to supervise the campaign process.

Serbia has established a strong system for guaranteeing and protecting civil rights, and for protecting citizens from discrimination. However, persons belonging to the Roma and LGBT communities continue to face prejudices and discrimination in society. Prison conditions remain difficult. Still there is no centralized official data record on the number of crimes motivated by homophobia and transphobia. Gender inequality is still present, both regarding labor issues and presence within public institutions. Serbia has no procedures for legal gender recognition in place, even in cases of gender reassignment.

The most illustrative case of breaching individual civil rights and freedoms are those related to property rights and freedom of movement in case of demolishing private construction projects on the night of the parliamentary elections April 24, 2016. Namely, buildings in the Belgrade neighborhood of Savamala were demolished by an unidentified group, while the citizens present at the crime scene were held captive by the unauthorized group. The executive power, police and courts have not undertaken steps in this case until this day.

Civil rights



Serbia still hosts one of the largest populations of displaced people in Europe. Beside this, Serbia has been one of the countries on the so-called Balkan Migration Route of refugees coming from Middle East countries. In 2015 alone, there were more than 330,000 asylum seekers in Serbia, an increase of more than 300,000 persons since 2014.

Equal rights of men and women are guaranteed by the legal system and official state policies. The new national strategy for gender equality 2016-2020 and an action plan for 2016-2018 were adopted in January 2016. In recent years, there have been more reports on family violence and domestic violence. According to research in 2013, the gender payment gap amounts to around 17.5%. Discrimination is present when it comes to transgender persons engaged in public sector work. Sexual minorities do not have equal rights guaranteed. Disabled persons face discrimination with regard to access to public services.

Report on implementation of the law on free access to information of public importance and the law on personal data protection issued in 2016 showed that the number of cases in this regard continued to increase in comparison to previous years (in 2015, the number of cases increased by 3.2% compared to 2014).

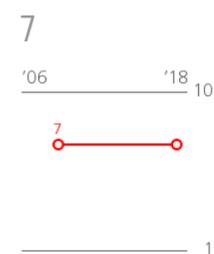
4 | Stability of Democratic Institutions

Currently in Serbia, dominance by the executive power at national level over legislative, judicial, as well as provincial and most local self-government units is highly present. In 2016, only two legislative proposals came outside of the government of Serbia and those proposals came from members of parliament (research by Open Parliament Initiative in 2016). This is mainly because of the space created by the ruling Serbian Progressive Party, which effectively controls other branches of power. This weakens the constitutional system of check and balances.

In 2016, the work of the Ombudsman and the Commissioner for Information of Public Importance and Personal Data Protection was undermined. For example, the government ignored the ombudsman's report on illegal data collection by the Military Intelligence Agency on political parties' activities. Moreover, these two watchdog institutions are often stigmatized in public and provided neither the latitude nor the tools required to exercise control. Their power is limited to issuing recommendations and public appeals.

In 2015, the government adopted 75 laws out of a planned 284. Parliament has adopted 196 laws and 119 acts. This data indicates a decrease in comparison with previous years. Public participation is rather scarce, as the practice of public discussions and consultations is still not properly regulated and practiced. Furthermore, the role of members of parliament is degraded, primarily due to the

Performance of democratic institutions



government's relationship with parliament and a frequent practice of urgent procedures which leaves almost no time for impact.

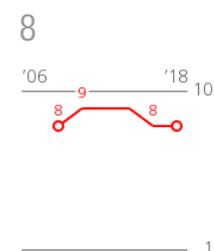
The number of parliamentarians who broke away from the parties on whose lists they entered parliament in 2016 increased to 14, indicating weak cohesion of some political parties but also informal influences.

Currently, the place of Ombudsman has been vacant since former Ombudsman Saša Janković decided to run in the presidential elections in spring 2017.

Public administration is in the process of restructuring. However, the number of complaints on transparency and work of public institutions remains high.

Most democratic institutions are accepted as legitimate by most relevant actors. However, the governing coalition has weakened the resources of the Ombudsman's and ignored reports about violations by the military intelligence agency of political parties' rights. While the governing parties generally accept the principle of free and fair elections, government officials have also misused administrative resources and their control over the state media to ensure electoral support for the governing parties.

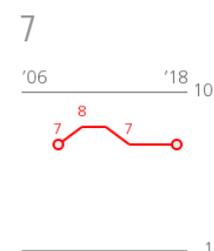
Commitment to democratic institutions



5 | Political and Social Integration

The Serbian party system is highly fragmented, moderately polarized and mostly dominated by individual personalities, many of whom have been active on Serbia's political scene for more than two decades. For the last four years, the party system has been dominated by Prime Minister Vučić's Serbian Progressive Party (SNS). Other political parties can neither separately, nor jointly, make a significant impact. In January 2017, parliament's majority consisted of SNS, Socialist Party of Serbia and their associates. The opposition consists of pro-European Union parties, such as the Democratic Party, Social Democratic Party, Liberal Democratic Party, League of Social Democrats of Vojvodina, undeclared "Enough is Enough," and anti-European Union parties, Serbian Radical Party, "Dveri" and Democratic Party of Serbia.

Party system



Political parties across the political spectrum participated in parliamentary elections held in April 2016. Serbian Progressive Party maintained a majority, with 131 seats out of 250, and the list of its main coalition partner, the coalition gathered around Socialist Party of Serbia obtained 29 seats. The Democratic Party has 16 seats. "Enough is Enough" party won 16 seats. The coalition of the Social Democratic Party, the Liberal Democratic Party and the League of Social Democrats of Vojvodina obtained 13 seats. Parties opposing Serbia's European Union integration re-entered parliament: the Serbian Radical Party won 22 seats, and the Democratic

Party of Serbia in coalition with the “Dveri” movement took 13 seats. Five parties representing national minorities, which are exempt from the 5% threshold, obtained 10 seats. Women continue to comprise one-third of all members of parliament.

Around 1.5 million people in Serbia are members of political parties. As the public sector in Serbia is rather large compared to EU member states, political parties are perceived as channels to become employed. Although the restriction on employment in public sector is still in power, this restriction is regularly detoured by concluding contracts for work which are not registered as official employment.

Currently, there are around 22,000 civil society organizations (registered as foundations, associations) in Serbia. This number is constantly rising, and the spectrum of interest groups is relatively broad. The number of labor unions in Serbia is around 26,000. Having in mind this data, Serbia is ranked as a country with the highest number of such organizations in Europe. However, there is an existing discrepancy between the number of associations which should represent citizens' interests and the advocacy of those interests and their implementation.

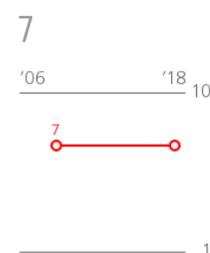
Civil society organizations participate in public discussions both nationally and locally, but this practice is rather rare. Official government agencies do not regularly hold discussions because the provisions for such fora are subject to interpretation. When held, such discussions are rarely commensurate with legal standards. Even when public discussions are held, the interest of civil society organizations are not highly regarded. Civil society organizations mostly impact public policies through their individual or joint coalition initiatives in areas such as European Union accession process, youth or security issues.

Cooperation between labor unions exists to some extent, although there is no present regular tripartite social dialogue process.

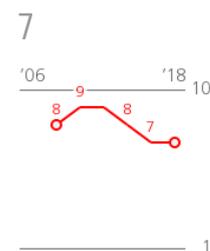
Business interests are organized in a network of local, regional and national economic chambers that function as interest associations. In 2016, chambers of commerce have been in the process of restructuring in order to set more centralized activities for the Serbian Chamber of Commerce.

Citizens generally approve democratic norms and procedures, and accept the constitutional framework. However, in research conducted by the Centre for Free Elections and Democracy, the share of respondents who believe that democracy is better than all other forms of government declined from 39% in 2007 to 30% in 2014. Research done by the Belgrade Centre for Security Policy in 2016 shows trust of citizens in Serbia varies from institution to institution. Parliament is least trusted by citizens (around 40%).

Interest groups



Approval of democracy

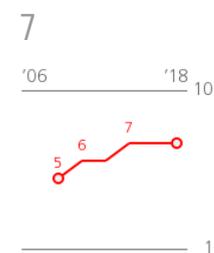


According to a survey conducted for the European Bank for Reconstruction and Development in 2016, 35% of Serbian citizens declared that most people can be trusted. This level of interpersonal trust has been slightly higher than in other Southeast European countries, but lower than in Poland or Estonia. The survey also showed that 16% of respondents were active members of civil society organizations (including churches and religious organizations).

Currently, in Serbia there are around 22,000 civil society organizations (registered as foundations, associations) in Serbia. This number is constantly rising. There is no exact number, nor database, of civil society organizations engaged in certain areas, as well as the number of networks and coalitions between them. While many organizations are inactive or lack clout, there are some respectable examples, such as the Coalition 27 established for monitoring the European Union accession process in terms of accession chapter 27: Environment. Also, some of the civil society organizations actively offer their services in certain social problems, such as domestic violence, trafficking, consumer protection or free legal aid. These organizations cannot “survive” as voluntary, but rather need financial support coming from the domestic (in most of the cases, these are the governmental bodies) or foreign donors.

Currently, social aid in Serbia has decreased a lot, due to the high, and in some cases unjustified, scrutiny measures. On the other hand, in Serbia there are 26,000 labor unions which should represent and protect interests of their member. Nonetheless, this does not guarantee that these interests will be protected. For example, the institution of social dialogue between the state, labor unions and employers is not active and not producing concrete results.

Social capital



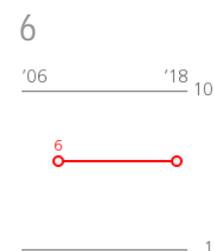
II. Economic Transformation

6 | Level of Socioeconomic Development

Estimated gross domestic product per capita of Serbia in 2016 (International Monetary Fund, World Economic Outlook) stands at EMU 4,940 in current prices or EMU 13,280 in PPP. This puts Serbia among upper middle-income country, according to the World Bank economy classification. Serbia is among the poorest countries in Europe, surpassing only Bosnia and Herzegovina and Albania. In terms of Human Development Index (HDI) Serbia ranked 66th in 2014, with the score of 0.771 – higher than Bosnia, Macedonia, Albania, Ukraine or Moldova, but lower than all other European countries. In 2015, 41.3% of the population was at risk of poverty or social exclusion, considerably higher than the average value of EU-28 countries which stood at 23.7% (Eurostat). The level of absolute poverty stands at 8.9% of population, and is significantly higher in rural areas. The risk of relative poverty was

Question Score

Socioeconomic barriers



25.4%, with the threshold of 60% of median income (National Statistical Office). Groups at higher risk of poverty and social exclusion are children and the young people under the age of 24, the unemployed, households with three or more children and single-parent households.

The income inequality in Serbia is among the highest in Europe as indicated by the values of the Gini coefficient and the S80/S20 income quintile share ratio which are significantly higher than values for all other EU countries. The S80/S20 income quintile share ratio was 9 – meaning that the total income received by the top earning 20% of the population was nine times higher than the income received by the 20% of the population with the lowest income. The Gini coefficient for Serbia was 38.2 in 2015 and thus remained almost unchanged since 2012. Gender Inequality Index was 0.176 in 2014 which assigns Serbia a rank of 38 (UNDP).

According to the findings of the MIMIC method applied to Serbia, the informal economy was estimated at 30.1% of GDP in 2010 (FREN, 2013). Informal employment is widespread, consisting of 19.7% of the total employment (or approximately 493,000 people) in 2015, and the overall unemployment rate stood at 19.9% in 2015 and continued to decrease (National Statistical Office, Labor Survey).

Economic indicators		2013	2014	2015	2016
GDP	\$ M	45519.7	44210.8	37160.3	37745.1
GDP growth	%	2.6	-1.8	0.8	2.8
Inflation (CPI)	%	7.7	2.1	1.4	1.1
Unemployment	%	22.1	18.9	17.7	16.5
Foreign direct investment	% of GDP	4.5	4.5	6.3	6.1
Export growth	%	21.3	5.7	10.2	11.9
Import growth	%	5.0	5.6	9.3	6.8
Current account balance	\$ M	-2794.6	-2634.6	-1751.1	-
Public debt	% of GDP	61.1	71.9	76.0	74.1
External debt	\$ M	36397.4	33078.6	31364.2	29599.4
Total debt service	\$ M	8455.2	8319.5	4268.4	5958.7

Economic indicators		2013	2014	2015	2016
Net lending/borrowing	% of GDP	-	-	-	-
Tax revenue	% of GDP	-	-	-	-
Government consumption	% of GDP	17.8	17.7	16.2	16.2
Public education spending	% of GDP	-	4.2	-	-
Public health spending	% of GDP	6.0	6.4	-	-
R&D expenditure	% of GDP	0.7	0.8	0.9	-
Military expenditure	% of GDP	2.0	2.1	1.9	1.9

Sources (as of October 2017): The World Bank, World Development Indicators | International Monetary Fund (IMF), World Economic Outlook | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database.

7 | Organization of the Market and Competition

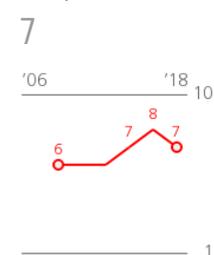
Institutional framework for market competition has been established and mostly upheld in Serbia. The private sector is a major factor in the economy and has the highest share in the GDP generation and employment. However, the state still has a pronounced role in many economic fields, controlling many strategic sectors, and is also a very significant employer. The state sector is usually inefficient, with elevated wage bill (both through increased number of employees and higher wages) and many companies rely on some kind of state support, via direct or indirect subsidies (toleration for arrears, not paying taxes, etc.). A current IMF-backed fiscal consolidation program brought lower subsidies and canceled state guarantees for state company loans other than for investments.

Setting up a new company is an easy and inexpensive task, lasting seven days with only five procedures consuming 6.5% of per capita income (World Bank, Doing Business 2017). However, business regulation once the company starts working is not considered to be business friendly. There are many burdensome procedures and overlapping authorities, as well as a high incidence of corruption among state officials and bureaucrats. The legal framework is not consistent and is prone to unexpected and significant changes, which is detrimental to entrepreneurial calculation.

There is legally no discrimination based on type of ownership. The new law on investment adopted in 2015 finally lifted all restrictions between domestic and foreign companies, but foreign natural persons still cannot possess agricultural land, and domestic companies are still privileged in public procurements with a 5% price premium.

Shadow economy in the country is very widespread, and was estimated to reach 30.1% of GDP in 2013, which is the second highest in Europe after Bulgaria. Shadow

Market-based competition



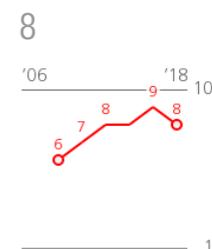
economy measured as tax gap is almost equal in the field of product consumption and production, with VAT gap and income tax (and social contributions) gap above 20%. Shadow employment according to the Labor Force Survey in 2015 stood at 20% of the total labor force. Main drivers for this level of shadow economy are high taxes, which are necessary to fund the welfare state, low productivity within the economy and burdensome business regulations which are costly to implement.

Legal framework in the field of competition is mostly in line with existing EU regulations. The law on competition that was adopted in 2009 and last amended in 2013 established the Commission for Protection of Competition as the public institution to uphold antimonopoly rules. The commission is an independent state body, and its dealing is mostly consistent with the legal framework. It is charged with preventing restrictive practices, such as collusion agreements and authorizing concentration. However, some of its ruling are not considered to be of high quality, which could be due to low capacity of expertise, or the low number of employees – the commission in 2015 had only 39 people employed out of 54 envisaged. In several cases, the commission failed to act according to their authority. For example, the commission has yet to give a negative opinion on concentration, although it did give four conditional positive opinions. Bigger problems in competition policy lie in the field of state aid – the legal framework is also mostly consistent with the EU regulation, but is scarcely implemented due to strong political pressures for financial assistance going mostly to state owned enterprises (SOE). Although there are no commercial monopolies per se, and liberalization of several markets has been introduced – the most important were railroad freight transportation, electricity and gas distribution – competition to SOEs in these sector is restricted either by price regulation policy (with prices that do not account for full cost recovery) or other soft means of protection.

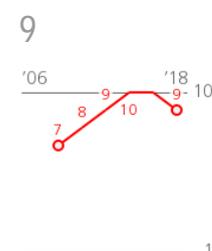
Foreign trade is mostly liberalized. However, Serbia is still not a member of the World Trade Organization (WTO). The majority of Serbian foreign trade is conducted via bilateral free trade agreements – most important of which are the Stabilization and Association Agreement (SAA) with the European Union, Central European Free Trade Agreement (CEFTA) or agreements with the Russian Federation and Turkey. Main trade partners are the EU and CEFTA countries (all of which have EU candidate country status or strong intentions to join) comprising almost 80% of total trade. Other important trade partners are Russia and China. WTO accession has not been in progress for several years (last meeting of the working group was held in 2013), the main issue being genetically modified organism (GMO) treatment. Serbia banned not only production of GMO products but also its trade which is against WTO rules.

Although international trade procedures are well evaluated by the World Bank (Serbia ranks 24th in Doing Business' Trade Across Borders), customs office is not well organized and badly equipped, using electronic systems from 1996. The recent

Anti-monopoly policy



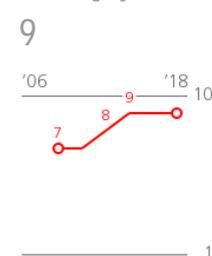
Liberalization of foreign trade



introduction of the New Computerized Transit System (NCTS) has made transit of goods in international trade across Serbia more expeditious. Import tariffs are low, with mean applied tariff rate standing at 7.4% but agricultural products receive more protectionist measures, such as high variable tariffs on milk and dairy products introduced in 2015, but finally abolished at the end of 2016. Non-tariff trade barriers are considered to be present, according to the Global Competitiveness Report.

Banking system in Serbia is considered to be solid and efficient, and it historically dominates the financial system. There are 30 banks operating in the country in total, the majority being foreign private ownership dominating the market with a 75% share in assets, but there are still six state owned banks (four small and two more significant ones). In previous years several state banks (Development bank of Vojvodina, Serbian bank, Agrobank, Privredna banka Beograd) and a private bank (Universal bank) went bankrupt and were bailed out by the government, and all assets were transferred to another bank. Their closure was due to political decisions that influenced bank loan policy, leading to a very high non-performing loan ratio (NPL). Since then, supervisory activities of the central bank substantially increased in quality. State owned Commercial Bank, in which significant shares hold IFC and EBRD, is selected for privatization in 2017. Serbia has been fully implementing Basel III standards since 2015. Capital requirements are in line with international practice, and average bank capital adequacy ratio is 21.5%, much higher than nationally stipulated 12%, or Basel III 8%. Bank capital stood at 649 billion dinars, and assets at 3,172 billion (ratio of 20%). NPL share which significantly rose since 2012, started to decrease from 21.5% of loans in 2014 to 19.5% in III quarter 2016 partially due to implementation of the Strategy for NPL reduction which was composed in collaboration with the IMF.

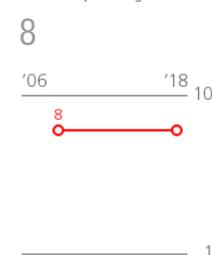
Banking system



8 | Currency and Price Stability

The Serbian central bank is using the monetary policy of inflation targeting. However, since Serbian economy and its financial system is faced with a high level of euroization (which is a consequence of a long history of inflation since the 1990s) current monetary policy framework is not effective. Foreign exchange is in a managed or dirty float regime, with a big influence on domestic prices due to significant pass-through effects. Inflation rate has been relatively high in recent years, with a peak in 2012 (12.2%) which subsided, standing at 1% in 3rd quarter of 2016. Current low inflation rate is attributed to low and stable capital inflows, so its sustainability in the long run is questioned. The inflation targeting has been inefficiently implemented in Serbia – in 93 months since 2009, inflation rate measured by CPI has been outside the envisaged band during 66 months, or 70% of the time. Inflation rate has been relatively unstable, with the standard deviation standing at 4.9 in the period 2005 to 2015. National currency, the dinar, has been relatively stable, with a 1.8% depreciation in 2014 to 2016 period, with the rate of

Anti-inflation / forex policy



123.2 dinars per euro. Foreign reserves are high above the IMF minimum standards. The central bank has recently been conservative, very slowly lowering the key interest rate to 4% in late 2016, from its 2014 levels of 9.5%.

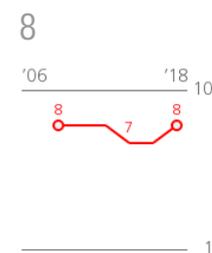
Current governor of the central bank, Jorgovanka Tabakovic, although an economist by education, is not perceived as an economic and monetary policy expert, but as a close political appointee due to her close connections with the Serbian Progressive Party. Her appointment in 2012 after Serbian Progressive Party took power was amidst changes of the law on central bank which curbed the bank's independence by enabling the governor to be discharged from his post only by the parliamentary majority, instead of relying on board of governors' recommendations. Her PhD thesis from a private university was recently found to be plagiarized (approximately 20% of the text) by independent investigative journalists.

Public finance has been a matter of growing concern due to high public deficits and the high accumulated public debt. Several early attempts to curb the deficit since 2012 proved unsuccessful. However, reform steps under the auspices of the IMF, which backed the current fiscal austerity program, produced good results, lowering budget deficits in 2016 to under 2% of GDP (from 6.6% in 2014). The most important features of the fiscal program are wage and pension bill containment through a general reduction, decreasing the number of civil servants through lower number of persons employed than retired (ratio 1:5), decreasing subsidies to state owned enterprises, decreasing the scope of shadow economy, and increasing public revenues from undeclared economic activities, mostly from excise duties for tobacco and oil derivatives and VAT. Recovering economic growth of 2.7% in 2016, although below regional average, coupled with the fiscal measure led for the first time since 2008 to a reduction in public debt, from 74.7% of GDP to 72.4% in relative terms, and even in the absolute one, from 24.8 to 24.7 billion euros. However, this level is well above the one stipulated by the fiscal rule of 45%.

Export has been recording strong growth rates – 9.3% for the first three quarters of 2016 compared to the previous year (National Statistical Office). Although the trade deficit shrank, the export-import gap is still significant: exports in 2015 reached 15.6 billion euros (46.5% of GDP) while imports stood at 18.9 billion (56.4% of GDP). Imports were 80% covered by exports. The trade account deficit was offset by the surplus of the financial account which financed the trade deficit.

Public expenditures are in line with most European countries, with general government expenses reaching 43.6% of GDP in 2016. However, when compared to other economies in transition, Serbia (alongside Montenegro, Bosnia and Croatia) has significantly higher public consumption. Serbia recorded primary budget balance in 2016, but public expenses on interest payments remain high at approximately 3.6% of GDP and in 2017 the state needed a further seven billion in new loans to repay the maturing public debt. At the end of 2016, Serbia's credit rating was marked by

Macrostability

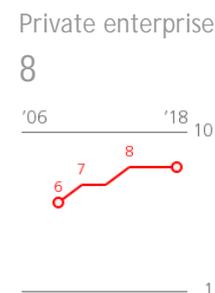
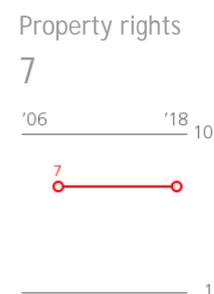


Moody's Investors Service as B1 with positive outlooks, thus considered to be relatively secure and marked by positive trends.

9 | Private Property

The legal framework defining and protecting property rights in Serbia is mostly well defined. However, the main problems lie in the field of actual implementation. Courts are slow and inefficient, leading to long legal procedures which on average last 635 days with high costs averaging 40% of the claim (World Bank, Doing Business). First level commercial courts often lack expertise and knowledge, so the majority of cases would continue toward appeal courts. Resolving insolvency is also inefficient, with case lasting two years on average and with very low recovery rate of 32.5% (World Bank, Doing Business). Furthermore, there are strong out-of-court influences on the judiciary and the Prosecution Office, mostly by the political elite from the executive branch, which can have substantial impact on court proceedings and private property rights protection, clearly evident in the Savamala case. Registering property has been recently streamlined and Serbia ranks 56th by this parameter in Doing Business Report 2017. However, the cadastral registry does not cover significant parts of the territory outside major cities, and there is an important question of undeclared real estate, in operation but not legally, estimated to stand at 700,000 homes. Corrupt practices in courts and cadastral offices also pose a significant problem. Property rights of agriculture land which was formerly collective owned cooperatives are not clear – in many cases it was seized from current owners who privatized the land and given to newly established cooperatives. The new law on investments lifted all the remaining restrictions on possession of property by foreigners, and in September 2017 natural persons from the EU will under the SAA finally have the right to own agricultural land. The process of restitution of private property that was seized after World War II is not yet finished, although it did proceed – in total, 176 square km of agriculture land, 42 square kilometers of forests and 5,572 objects were returned to their rightful owners (data from Serbian Restitution Agency). Companies in restructuring finally stopped being exempted from litigation and legal enforcement of contracts in 2016, which largely undermined property rights due to very long restructuring processes which in some cases lasted almost a decade.

Serbian economy relies mostly on private enterprises. The private sector comprises a dominant share of GDP generation and employment. However, state owned enterprises (SOEs) remain very present in the economy, even in cases where there is hardly any justification at all such as in competitive markets. Most important SOEs are present in electricity generating and distribution, telecommunications, transport, public utilities, mining, and so forth. Many of these companies either receive substantial subsidies (amounting to more than 3% of GDP) or continue to enjoy privileged status in the market, and sometimes even outright monopoly. The total number of public enterprises reached 587 in 2016 with approximately 150,000



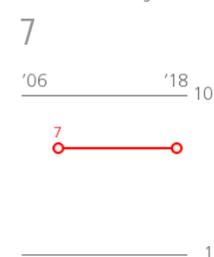
employees (data from the Ministry of Economy). Companies in restructuring are, under the agreement with the IMF, in the process of either privatization or liquidation but this process is very slow – although a majority of the 502 companies has been resolved since 2014, the remaining companies still employ 45,000 employees, and many of these companies, although bureaucratically put back on the market are highly likely to remain dependent on state aid and subsidies. Privatization process is not regarded as transparent, with many contracts hidden from the public, even in cases where the Public Commissioner on Information of Public Importance stipulated them be presented to the public.

10 | Welfare Regime

Demographic changes, most notably the low fertility rate (TFR standing at 1.32 children per woman in 2012) and high emigration rate lead to an annual decrease of 38,000 inhabitants. This trend puts more pressure on an already stretched national welfare system, increasing expenditures for health care system and pensions. Although total health care expenditures are high, reaching 10.4% of GDP in 2014 (World Development Indicators), the system is very inefficient and in Europe bests only those of Romania, Bulgaria, Albania and Poland (European Health Care Consumer Index 2015). The state pay-as-you-go pension system has been unsustainable for decades, and only although average pensions are low, only 60% of them are financed through the social security contributions while the remaining 40% are direct transfers from the state budget. A fiscal austerity package implemented in 2015 lowered the total pension bill for 5%, by curbing progressively pensions above the average one, standing at 200 euros per month, with a flat increase in 2017 of 1.5%. Still, the pension bill in Serbia is among the highest in Europe, comprising approximately 30% of all public expenditures, standing at 12% of GDP in 2016, which is still above the legal level of 11% prescribed by fiscal rules. With all its shortcomings, the pension system in Serbia protects income in old age, with the minimum pension slightly above the poverty threshold, enabling very low poverty rates among the elderly.

Social programs in Serbia lack internal coherency. There are many special programs, aimed at certain segments of population (students, disabled, veterans), with different goals (population growth, poverty alleviation, social objectives, etc.). A social assistance network is not well designed – there are many bureaucratic procedures associated with it, and the majority of programs are not means tested, which leads to the situation in which many citizens entitled to different social assistance programs cannot exercise their rights, while a significant proportion of resources are allocated to those who are not in need of it. For example, 80% of resources for social assistance to women on maternity leave go to women from the upper 40% of income distribution (World Bank, Republic of Serbia Public Finance Review, 2015). On the other hand, a means-tested financial social assistance program is well designed, reaching mostly

Social safety nets



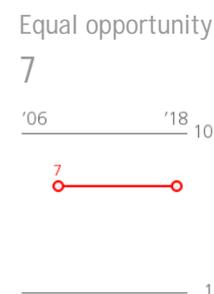
households from the lowest quintile, but with somewhat limited coverage. Since 2017, social allowance for households with infant children will be increased, in order to offset costs of lifting a VAT waiver on baby products.

The protection against discrimination is ensured by the legal and institutional framework, including a comprehensive anti-discrimination law in place since 2009. The government adopted the Strategy for the Prevention and Protection from Discrimination (2013-2018), the National Strategy for Gender Equality (2016-2020) and Strategy for the Social Inclusion of Roma in the Republic of Serbia (2016-2025) with accompanying action plans. However, as in other instances, implementation of strategic documents and legislation is somewhat dubious.

In 2015, the majority of registered complaints pertain to discrimination suffered in the job recruitment process or workplace-related discrimination (Commissioner for the Protection of Equality, annual report). The largest number of complaints alleged gender based discrimination (22.1%), closely followed by alleged discrimination based on national affiliation (18.4%) and complaints claiming discrimination on the grounds of disability (11.3%).

The overall score on the Gender Equality Index in 2014 ranked Serbia 22nd compared with EU Member States with a score of 40.6 points out of 100 (the EU average being 52.9). Comparative index values for Serbia and the EU indicate that the largest gaps are in the domains of work and money, whereas in the domain of power, Serbia shows even slightly better scores. Gaps are particularly pronounced in participation, segregation and quality of work. Adjusted wage gap is 14%, meaning that women earn 86% of the wages of their male co-workers, after one controls for differences in educational and job characteristics. On the other hand, an unadjusted wage gap stands at only 4.5% – but women in employment on average tend to have higher education qualifications than men (Social Inclusion and Poverty Reduction Unit and World Bank, 2016). Female labor participation is significantly lower than men, 59.4 compared to 73.9%, and unemployment is slightly higher, 15.8 compared to 13.3% (Labor Force Survey III quarter 2016). However, in the field of education the gender gap is in-existent - primary gross enrollment ratio for both sexes is high, reaching 100% and the literacy rate is very high, apart from elderly generations where illiteracy can still be encountered.

However, Roma face a high level of discrimination in society, most importantly in education and employment. Almost one-third of Roma (34.2%) did not complete even compulsory primary education, and the share of Roma with a secondary school diploma or a college and university degree is 11.5% and only 0.7%. The share of illiterate Roma in the total population aged over 10 is 15.1% and as such remains well above the national average of 2% (National statistics office, Census data 2011).



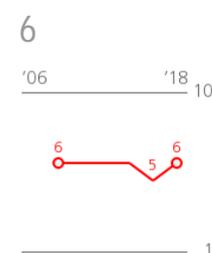
11 | Economic Performance

The Serbian economy recorded growth in 2016 of 2.7% of GDP, which is a strong acceleration compared to previous years (in 2014 it recorded a negative growth of 1.7% and in 2015 a modest growth of 0.8% which was more a consequence of a low statistical base). Growth is widespread among industries, but is most visible in construction, manufacturing and agriculture. This strong performance is even more positive bearing in mind it happened in the midst of a fiscal austerity reform package during which usually production shrinks due to a decrease in public expenditures. However, household consumption rose insignificantly. Prices are stable, with the increase in CPI of approximately only 1% in 2016. Serbia remains one of the poorest countries in Europe in terms of GDP, which reached only €5,000 in current prices in 2016, or slightly above €13,400 in PPP, leading only Albania and Bosnia and Herzegovina. Investments in the country are low compared to other countries in transition, reaching 18.3% of GDP in 2016 (up from 17.7% from the previous year); this rise has been recorded due to more efficient public infrastructure investments as well as due to marginally higher FDI, which still remain low, with FDI stock in June 2016 reaching 27.5 billion euros (National Bank of Serbia) or below €3,900 per capita. Low national savings (standing at only 14% of GDP) pronounce the great importance FDI and foreign banks have in promoting investments and economic growth in Serbia.

Unemployment in Serbia has been high since the beginning of transition. However, recently there have been some positive trends in the labor market, and the unemployment rate among the working age population (15-64 years-old) stood at 14.4% in the third quarter of 2016. At the same time, youth unemployment (15-24 years-old) stood at double the national level at 28.8% (National Statistical Office, Workforce Survey). However, the sharp decline in unemployment levels is partially attributed to methodological changes applied since 2014. Female participation rate and employment rates are lower than for males, with approximately 10 percentage point gap. Active labor market programs are limited, and its funding received 3.35 billion dinars or approximately 0.8% of GDP in 2016. A separate Transition Fund has been active since 2014 for severance payments for employees of state companies in restructuring that will be made redundant due to privatization of liquidation process. However, these funds have been put to limited use due to a slow finalization of these processes. People not in education, employment or training (NEET) stood at 27% in 2014.

Export has been recording strong growth rates – 9.3% for the first three quarters of 2016 when compared to the previous year (National Statistical Office). Although trade deficit shrank, the export-import gap is still significant: exports in 2015 reached €15.6 billion (46.5% of GDP) while imports stood at €18.9 billion (56.4% of GDP). Imports were 80% covered by exports. The trade account deficit was offset by the surplus of the financial account which financed the trade deficit.

Output strength



12 | Sustainability

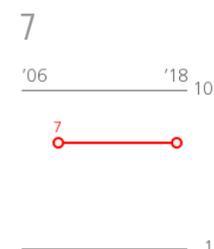
The National Economic Reforms Plan (2016-2018) tackles environmental concerns at the level of specific projects' but environmental protection and sustainable development are not recognized as objectives of economic reforms. Development of Climate Change Strategy is in its initial phase. According to Intentionally Nationally Determined Contributions (INDCs) (submitted in June 2015 to UNFCCC), Serbia's greenhouse gas (GHG) emission target is set up as 9.8% of GHG emission reduction in 2030 comparing to 1990. Independent estimations showed it means increasing GHG emission 15% compared to 2013.

According to the European Commission 2016 Progress, Serbia has largely aligned its domestic environmental protection legislation with EU rules. There continue to be significant gaps in implementing the EU acquis, for example, with regard to waste management, air quality monitoring and river basin management.

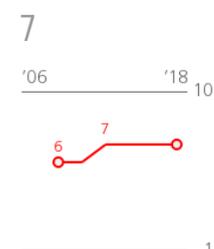
The Serbian economy is highly energy intensive. Coal is the main energy source. According to Serbian energy 2016 balance sheet coal represents 74% of total electricity generation. Hydropower dominates among renewable energy sources with 24% of total electricity generation. Wind and solar are less than 1%. As an Energy Community member, Serbia has adopted a goal to reach 27% of renewables in final energy consumption until 2020. In 2014, Serbia achieved a 23.1% share of energy from renewable sources, mainly due to a decrease of energy consumption rather than investments in new renewable energy capacities. When it comes to energy efficiency it should be noted that envisaged share of final energy consumption in households in 2016 is 52% total final energy consumption. The Energy Efficiency Fund was established in 2013 but with limited financial resources. In 2016, the Green Fund has been re-established but it is not aligned with the "polluter pays" principle.

Primary and secondary net enrollment rate are high, approximately 96% and 92% in 2014 (World Bank). Tertiary education enrollment is much lower, standing at 24% in 2012, but the strategy for education stipulates a set of measure to increase it to 40% of the population. Currently, only 10.6% of the general population have a university degree (National Statistics Office, census data 2011). Serbia did not participate in the Program for International Student Assessment (PISA) 2015, due to political changes within the Ministry of Education which led to a late signing of participation documentation. Nevertheless, the existing data from previous PISA cycles (2003, 2006 and 2012) indicate that a large share of Serbia's 15-year-olds fail to demonstrate an adequate level of achievement in reading, mathematical and scientific literacy – over one-third of pupils are considered to be functionally illiterate, although they completed primary school. However, public education expenses are high in comparison to other countries from the region, reaching 4.2% of GDP in 2014 (UNESCO statistics). The vast majority of the funds are allocated to salaries of the inefficiently high number of teaching staff, although their salaries are lower than average in the economy.

Environmental
policy



Education policy /
R&D



There are eight universities and 47 colleges in the public sector and 10 universities and 21 colleges in the private sector. In 2014, there were 241,054 students enrolled in higher education institutions, of which 87% were enrolled in universities and colleges in the public sector and 13% were enrolled in universities and colleges in the private sector. Only Belgrade University is ranked in international university rankings, such as the Shanghai list, with the rank of 200-300 best universities in the world. There were several high cases of corruption or plagiarism of PhD thesis in Serbia among both private and public universities, for which there were no institutional response. For example, more than 40 university professors were apprehended at the University in Kragujevac for selling exams or diplomas, and the legal procedures has been pending since 2007. And, several high officials, among others: mayor of Belgrade, minister of the interior, governor of central bank and mayor of the largest municipality in Belgrade, were accused with strong evidence for PhD thesis plagiarism and still none were revoked. Expenditures on R&D stood at 0.77% of GDP in 2014, of which only 7.5% came from private funds. Not only low resources, but also problems in their allocation plague public funded research, due to existence of clientelistic networks and lack of good objective indicators for funding decisions. In 2016, the strategy for development of science and technological development was adopted, which envisages doubling research resources. The total number of patent applications was 191 in 2015 (World Intellectual Property Organization), and Serbia is ranked 50th in this field (World Economic Forum, Global Competitiveness Report 2016-2017).

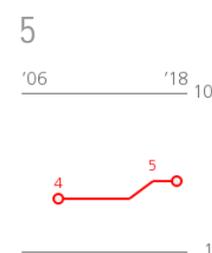
Governance

I. Level of Difficulty

Structural constraints on governance in Serbia have increased. The impact of economic crisis that spilled over to Serbia in 2008 can still be felt; Serbia has, unlike most other transition countries, experienced a prolonged recession with several waves (in 2008, 2012 and 2014), and only in 2016 did the GDP reach its pre-crisis level. Low economic prospects in the country, mostly low wages and high unemployment encourage high emigration rates, especially among the young and educated people, mostly to advanced EU countries. Serbia was ranked 137th in the world by its ability to attract or retain talent, out of 138 countries in the rankings (World Economic Forum, Global Competitiveness Report 2016-2017). The economic situation still poses significant concerns, since economic growth has not yet been able to provide quality workplaces in a scope sufficient to significantly alleviate conditions of living. The workforce is relatively well educated when compared to the existing level of GDP per capita (EMU 5,000 in nominal terms or EMU 14,200 in PPP), with majority of the workforce having a secondary education degree. Therefore, economic issues, alongside corruption, remain among the most important topics in public opinion polls. Parts of the Serbian society are deeply conservative, inhibiting the process of modernization. The dissolution of Yugoslavia, and especially the situation with Kosovo, still are a traumatic experience for a significant proportion of the population, which is torn between cooperation with the East (embodied in the Russian Federation) and the West (the EU and the United States). Infrastructure deficiency is high, due to very low investments since the 1990s; with overall quality of infrastructure ranked 107 out 138 countries (World Economic Forum, Global Competitiveness Report 2016-2017). Although recent investment in public transport infrastructure may somewhat alleviate this situation, public infrastructure in other important areas (most notably, public communal services and health care system) yet to gain attention.

Serbia has a moderately strong tradition of civil society, rooted in the dissident movements against the communist regime, and afterwards, as opposition to Slobodan Milosevic regime. Compared to civil society in Western countries where it was established in order to protect and advocate particular interests of certain larger self-funded groups, civil society in Serbia was based mostly on political issues and funded in most of cases by donation. This tendency “exploded” in the years following

Structural
constraints



Civil society
traditions

4

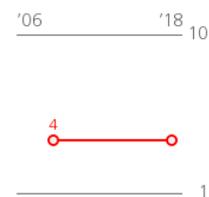
democratic changes in 2000, as the donor community was primarily dealing with state and peace building and reconciliation. Although the number of associations is large, in recent years the number of donors is constantly decreasing. This resulted in the decrease of donor-funded civil society organizations and media, as well as slow establishment of self-funded civil society organizations. For now, civil society organizations are dealing with issues such as rule of law, human rights, democratization, European Union accession process, environment, consumer protection, domestic violence and migration.

Keeping in mind a short history of civil society in Serbia, trust of citizens toward civil society is rather low. This is also caused by the stigmatization of civil society started in the 1990s and revived in the last couple years. Civil society organizations are often described as the “foreign mercenaries” and “domestic betrayers,” not only by some political parties, far-right extremist groups and certain tabloid media, but also by the official government.

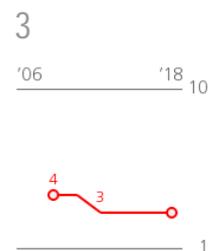
Serbian society and the country’s political elite continue to be polarized along ethnic issues, such as Kosovo and relation with neighboring countries. Issues which were predominant a couple of years ago have largely diminished in importance, such as the status of Autonomous Province of Vojvodina, tensions in Novi Pazar and neighboring local self-government units and very south east of Serbia. Polarization is rising on the other side, such as economic and social status. Currently, there are around 40 local self-government units classified as underdeveloped in Serbia. The interesting fact is that these units are based in the south west and south east of Serbia and that in the last ten years around 700,000 people have abandoned these areas.

Polarization also exist across the political spectrum on several issues, such as accession to the European Union, relation with Russia, neighboring relations, as well as internal policy issues, such as capital projects, rule of law, crime and scrutiny measures. In this moment, this polarization can be in tensions within the National Assembly. These polarizations which gain traction daily may serve in the near future as a solid base for mobilizing large groups of the population and even increasing radicalism.

Unfortunately, violence is still present to a certain extent and in some cases, as the “Savamala” case, the culprits were not processed. Violence is present also in the actions of the quasi-political far-right groups and especially groups of sport hooligans, although to a lower degree than in previous years.



Conflict intensity



II. Governance Performance

14 | Steering Capability

The government of Serbia set strategic priorities after election in April 2016. Those were the third parliamentary elections since 2012 so this trend seriously undermines any long-term perspectives in strategic planning when it comes to government priorities. This situation is further complicated by the possibility of a new round of parliamentary elections which could accompany presidential elections in 2017.

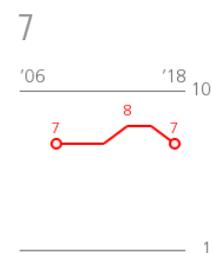
Although the government of Serbia formed in August 2016, by January 2017 the government program was not available on the official government website and the only document which could serve as a framework for prioritization is the prime minister's Expose. The Expose lacks clear prioritization of the policies which will be the focus of the government as well as the major policy goals in long-term perspectives (e.g., in environment and energy, no policy priority has been presented even though these two policies were highly rated on the government agenda). European integration process remains the main long-term strategic perspective. Key priorities are the depoliticization of public administration and the judiciary, as well as the effective prosecution of corruption and organized crime. However, the second revised national program for the Adoption of the EU Acquis (NPAA) was adopted in November 2016 while the first revised version of NPAA expired in December 2015, meaning almost all of 2016 lacked a strategic framework on prioritization in harmonization with EU policies and Acquis.

Elections held in April 2016 resulted with the new composition of parliament and government of the Republic of Serbia. Although Serbian Progressive Party and Social Party of Serbia regained the majority in parliament (with smaller changes among their smaller coalition partners) and formed the government, it is hard to evaluate whether the continuity with the government priority from 2014 is maintained. This is due to the fact that government program is not available – the only available document that presents the policy priorities is the prime minister's Expose which in many policy areas lacks clear policy goals and focuses more on past achievements than future priorities in policy implementation.

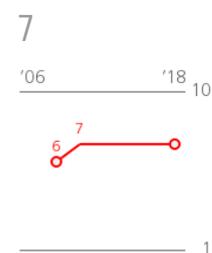
Although fiscal consolidation has been achieved this has been done predominantly by savings on the expenditure side (by decreasing pensions and salaries in public sector) while the achievements in the reform of the public administration remained rather modest (Balkan Investigative Research Network Report on the work of government in period 2014-2016). The government remained committed to creating a functioning market economy, addressing issues such as budget deficit, growth

Question
Score

Prioritization



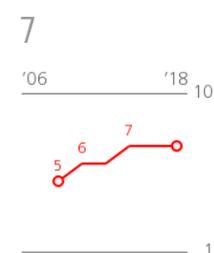
Implementation



perspectives domestic and external imbalances. Price stability has been preserved. However, government debt is still very high. Unemployment is very high, particularly among youth. The private sector is underdeveloped and hampered by weaknesses in the rule of law. Corruption remains prevalent in many areas and continues to be a serious problem. Serbia has still not adopted the new law on the anti-corruption agency nor the amendments to the criminal code in the economic crimes sections. The government still does not take the recommendations of its own advisory body, the Anti-Corruption Council, into account. No progress was made on improving Serbia's track record of convictions or stepping up the implementation of the national anti-corruption strategy and action plan (Serbia Progress Report 2015).

The current government led by the Serbian Progressive Party, which has been in power since 2012 in different shapes, has announced deep reforms in many areas of society. While these reforms represent learning from international best practices and transfer of foreign experience, the expected impacts are yet to fully materialize or the reforms were put aside for the time being. Key reform procedures that are backed by international financial institutions, such as the IMF and the World Bank, or by other international donors, have the most chance of being successfully implemented, due to political backing. However, even in these areas, there are policy solutions that are not fully implemented or that are very slow to materialize. The government employed several non-political persons as policy experts in certain areas as ministers, but some of them have been widely criticized for lack of policy measures or left the government due to a falling out with the political majority regarding reform implementation. Advice from independent state bodies, such as the Fiscal Council, State Audit Institution or Anti-Corruption Council, are not seriously taken into account or are disregarded. Civil society is also not embraced as a partner in policy planning and implementation. However, a more coherent policy coordination framework has been put to place, and policy documents are of increasing quality, with numerical target values, specification of sources of validation and resource allocation planning. Monitoring and evaluation still require more improvements. The overwhelming influence of the prime minister and members of his personal cabinet pose a significant limit to independent action of individual ministries, which often await permission.

Policy learning



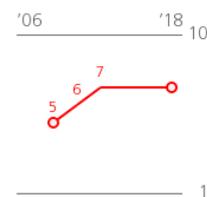
15 | Resource Efficiency

The present organizational, social and economic situation limits efficient use of existing resources by the government. Public sector in Serbia is very inefficient, with large numbers of employees and low quality of services provided. Government e-services are still limited. Low level of public administration quality is one of the main reasons for this situation – higher public officials are not recruited according to meritocracy but often due to other important traits (political affiliation or clientelistic network), which is sometimes present even at low levels of administration. Very

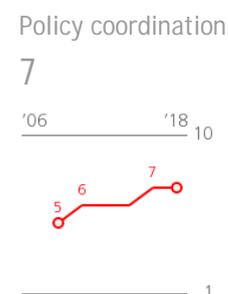
Efficient use of assets

7

often public resources that are in current use are not even accounted for, with the example of real estate in public property. A new strategy on regulatory reform and improvement of public policy management was adopted in 2014, with a thorough action plan, with the aim of increased public administration efficiency. Although some progress has been made, most notably in increase in availability of government e-services and the introduction of a more rigorous public policy planning system, further breakthrough is necessary. The public wage bill is very high, standing at more than 11% of GDP (higher than the estimated level of 8% as stipulated by the fiscal rule), with wage premium for employees with lower qualifications and wage negative premiums for those with tertiary education, which is most prominent in fields of tax administration and ICT. Current restriction on new employment (one new employee per five who retire) is putting increased pressure on some public administration segments and can lower the current level of public services in the near future. Public enterprises are very inefficient, relying mostly on public subsidies which are higher than the EU average, standing at 3% of GDP on consolidated level. The level of public debt is very high, especially for a country on Serbian development level, standing at 72% of GDP in 2016, but has finally been put on the downward spiral, although on a very slow pace. Public budget records moderate deficit levels in 2016, and when interest rates expenses are not taken into account, it even records primary surplus, but fiscal risks emanating from inefficient management of public enterprises and negative economic prospects in Europe can lead to higher than envisaged deficits.



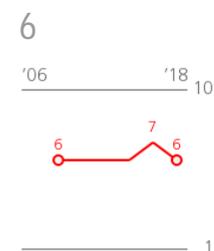
The government tries to coordinate conflicting objectives, but friction, redundancies and gaps in task assignment are significant. Although the majority of the political parties represented in the National Parliament (including those forming the majority) declared EU integration a top priority, in practice, different policy streams of prioritization can be observed. Serbia failed to coordinate with the EU during the launching of bilateral agreements with the non-EU countries, such as Ukraine. Serbia also needs to address, as a matter of priority, other issues of noncompliance with the SAA, in particular safeguarding measures on some agricultural products, state aid control, and fiscal discrimination (European Commission Country Report 2016). Here we can also mention the case of Serbia failing to establish a legally separate subsidiary in charge of network operation within Srbijagas which could result in sanctions by Energy Community (Energy Community Country Report 2016).



the National Secretariat for Public Policies prepared a draft law on the planning system of the Republic Serbia accompanied with the bylaw on the methodology for public policies management, public policy analysis and policy document content, as well as bylaw on the methodology for development of mid-term plans. Aforementioned documents are designed to provide horizontal coordination and introduce a clear division of roles in policy planning and development following the policy priorities of the government of Serbia. However, these documents did not enter the legislative process in 2016.

An institutional and legal framework for fight against corruption in Serbia has been established; and significant proportion of it is of good quality even by international standards (for example, the law on free access to information of public importance). However, as in other areas, actual implementation of this regulatory framework is a far cry from being satisfying. Two of the biggest problems lie in the field of political will to actually eradicate corruption, since it will close many opportunities for personal gains of officials, on one hand, and very bad situation in the judiciary, on the other. Even when there is some political will to implement some changes, the initiative is often stopped at courts: for example, the law on protection of whistle-blowers was adopted in 2015, but in reality, the process of receiving protection for whistle-blowers is coupled with many obstacles, some of which arise from primary courts interpretation of events. Independent public bodies in the field of anti-corruption are committed to their work, but their prerogatives are limited, and they often work with limited resources, understaffed and under-financed. A national strategy for fight against corruption for 2013 to 2018 is under implementation, but progress is slow, uneven and seldom successful. For example, during 2015 out of 422 monitored activities from the action plan for strategy implementation, only 82 or 19% were implemented, out of which only 29 or 6.9% fully in accordance with the manner and envisaged timetable of the Strategy (Anti-Corruption Agency of Serbia, Annual Report 2015). State Audit Institution provides oversight over public expenditures, but lack resources to increase the scope of its audits. Even when cases of embezzlement or unlawful public spending are found, seldom does it end in criminal charges against public officials, and few of them are charged, and even a smaller fraction are convicted. A financial audit of political parties remains ineffective, although efforts have been made in order to strengthen this activity. Prolonged legal proceeding in many corruption cases limit effectiveness without an adequate penalty. According to an international survey, 40.2% of companies in Serbia think that their counterparts make informal payments in order to secure public contracts (World Bank, Enterprise Survey, 2013). Public procurement still remains one of the areas with high risks of corruption. In 2015, the independent body in the field of public procurement was included in 1910 procurement cases (Agency for Protection of Rights in Public Procurement, Annual Report) which is a significant increase from previous years.

Anti-corruption
policy



16 | Consensus-Building

General goals of development and transformation are regulated in existing strategic and normative framework. When it comes to democracy, separation of powers, functioning of parliament, government, judiciary and governance system are broadly in place at the normative level. All Serbian governments since 2000 have officially declared dedication to the EU integration of Serbia. Serbia's national parliament adopted the Resolution on the Accession to the European Union where EU integration was marked as the highest and undisputed political priority, which

Consensus on goals

8

implies harmonization with goals of the EU policies and Acquis in referring to democracy, rule of law and market economy. In practice, however, the consensus of major political actors over democratic values is challenged. The legislative process is characterized with the weak, non-coherent legislative procedures with conflict of laws marked in many cases and inconsistency with the constitutional provisions. The inclusivity, transparency and quality of lawmaking and effective oversight of the executive need to be further enhanced, and the use of urgent procedures limited. Understanding and acknowledgment of the remit of independent bodies, including the Ombudsman's Office, needs to be improved (Ombudsman report). Further efforts are needed to ensure systematic inclusion of civil society in policy dialogue and help develop its full potential. The interest of local authorities are broadly represented throughout the work of Standing Conference of Towns and Municipalities (SCTM), as the only association of local authorities in Serbia, but the work of SCTM is undermined with the lack of resources and existing vertical political subordination of local political elites which obstructs any kind of local and regional initiatives.

Market economy, free market, freedom of entrepreneurship, independence of business stakeholders and equality of private property and other forms of property are constitutional categories. The government of Serbia has produced the Economic Reform Program (ERP) as a mid-term strategic framework for moving forward the process of restructuring the Serbian economy, particularly the public sector, aimed at curbing unreasonable public consumption and increasing efficiency coupled with a better quality of services. In the prime minister Expose from August 2016, the values of market economy are recognized. However, Serbia has not applied in practice the frameworks of sustainable development strategy, while strategic development for regional development does not exist. Government debt is still very high. Credit activity is recovering but the high level of non-performing loans remains an issue. Unemployment is very high, particularly among youth. The private sector is underdeveloped and hampered by weaknesses in the rule of law.

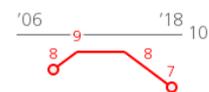
Political actors with anti-democratic interests entered national parliament after the 2016 election. The Serbian Radical Party won 22 seats becoming the third biggest political group in the parliament. Movement "Dveri" in coalition with Democratic Party of Serbia won 13 seats. Both parties are characterized with ambiguous political goals regarding the promotion and application of democratic norms and values in practice. The number of complaints to Ombudsman for breaching social and economic rights has increased, replacing the complaints on maladministration in the public sector. Civilian oversight of the security forces is challenged by the lack of initiative of parliament in performing its oversight role and the remit of the Ombudsman's Office in this field (Ombudsman report 2015).



1

Anti-democratic actors

7



1

The political leadership prevents cleavage-based conflicts from escalating. Governing political parties continue with the efforts to prevent potential conflicts based on ethnic, national or religious cleavages. Political leadership of the governing parties continues to oppose Kosovo unilateral independence. However, in 2016 continuous dialogue between Belgrade and Pristina over the implementation of the Brussels Agreement has continued with progress made in areas of free movement and telecommunications. The tensions between Serb majority and some ethnic groups, in particular Bosnians from southwest Serbia, Albanians from southeast Serbia remain. The government has adopted a strategy for long-term economic development of southern Serbia, with the focus on the local communities with majority Albanian population not implemented in practice.

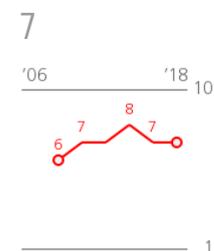
Media and journalists, particularly with critical approach towards government and governing political parties, are subject to threats and intimidation. Proceedings over the attacks and intimidation on journalists are sporadic. Several high government officials had public statements against certain media, journalists and CSOs accusing them of subversive activities against the government and the state. The government also ran a campaign against investigative journalism and involved media.

The Constitution of the Republic of Serbia, Law on National Assembly, Law on State Administration, Rules of Procedure of the Government of the Republic of Serbia and National Assembly provide a framework for involvement of different stakeholders in legislative procedures, policy and strategic planning. In practice, civil society participation in policy making and legislative process is to a large extent ad hoc, which means that the full potential of the sector is not being realized (Serbia 2016 report issued by the European Commission).

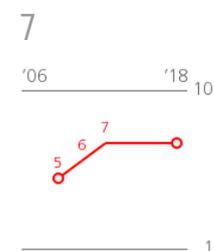
Some progress has been made for establishing an enabling environment for development and work of CSOs. A new Director of the Government Office for Cooperation with Civil Society was appointed in 2016. Cooperation between parliament and civil society in the EU negotiation continued. Serbia lacks a strategic framework for the involvement of civil society in policy and decision-making.

Notably, the National Strategy for an Enabling Environment for Development of CSOs in Serbia 2015-2019 (produced in 2015) is not yet adopted and a council for cooperation with civil society has not been established. A legal framework for volunteering needs to be improved. Tax exemptions, which could stimulate cooperate philanthropy, need to be adopted (Third Report on the Monitoring of Enabling Environment for the Development of Civil Society in Serbia 2016). An existing draft law on social entrepreneurship significantly undermines the efforts of the CSOs to act as providers of social services. Media coverage of CSO work continues to decrease, partially due to the heavy political influence on media (USAID CSOs Sustainability Index 2015). Participation of CSOs in policy and decision-making is to a large extent still ad hoc, undermining civil society to exploit its potential in this regard.

Cleavage / conflict management



Civil society participation



The reconciliation between the Western Balkans countries has been ongoing since the end of war and particularly after 2000 after the changes which resulted in the withdrawal of wartime leaders. One instrument for achieving reconciliation and determining the facts of war crimes was the International Court Tribunal for Former Yugoslavia. Although, still active, the mandate of this court is close to an end. However, this court has not significantly contributed to reconciliation attempts.

These steps were made mostly through mediation of the European Union and several initiatives and organizations. In past years, state officials of Western Balkans countries have publicly apologized in several occasions. When it comes to current public officials, there were attempts to pay respect to the victims of the Yugoslav wars in the 1990s. For example, Prime Minister Vučić, has visited the site of the Srebrenica massacre in 1995, but this act resulted in an assassination attempt. Nevertheless, Serbia has taken the role as one of the largest donors for developing the Municipality of Srebrenica.

Interestingly, today the officials in power in the four countries most affected by the 1990s war, Croatia, Serbia, Bosnia and Herzegovina and Kosovo, are members of former right-wing extremist parties or even former warlords. In the last two years, and in contrast to the 2000-2014 period, tensions and resentfulness have now resurfaced in the relations between Western Balkans countries. In such way, the issue of war crimes and the rehabilitation of persons accused even in the World War II were resurrected. To conclude, there has been a regression in terms of reconciliation.

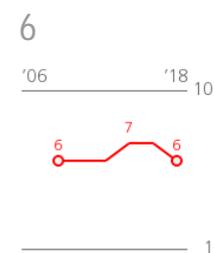
17 | International Cooperation

Serbia continues to be a recipient of financial and technical aid, especially through the European Union Instrument for Pro-Accession Assistance (IPA) II, which is designed to support the reforms undertaken as part of the European integration process. Serbia has up to 1,500,000 euros available to apply until 2020. The priority sector in this regard are democracy and governance, rule of law and fundamental rights, environment and climate action, transport, energy, competitiveness and innovation, education, employment and social policies, agriculture and rural development. The results of using this kind of aid are yet to be seen. Besides the European Union as the leading donor in past 17 years (51.18% of total funds donated), individually United States is the leading country as the external aid donor (13.05%).

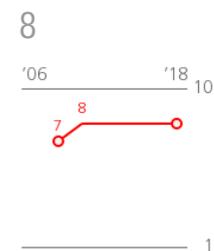
In following years, as the country will be accessing closer and closer to the European Union, it is to be expected that foreign donors will withdraw from Serbia.

Serbia is increasingly looking toward Russia, China and Middle Eastern countries for investment. Currently, along with other European Union member states, Norway,

Reconciliation



Effective use of support



Switzerland and the United States, foreign aid is provided by the Japan (2.15%) and China (0.1%). Aid from other countries has not reached such extent yet.

Serbia has overcome a number of long-standing obstacles to European Union accession, demonstrating its commitment to political and economic reforms. The Brussels Agreement normalized relations between Kosovo and Serbia, thus clearing some of the barriers for continuing the EU accession process. Serbia has opened seven out of 35 accession negotiation chapters. The accession to the EU still remained the most important strategic goal of Serbia and most policy actions follow this agenda.

In 2015, Serbia has also acted as the chair country of the Organization for Security and Cooperation (OSCE) in Europe trying to develop its mediating role on the burning issue of Ukrainian conflict. In last two years, even with the downfall in relations with other Western Balkans countries, some aspects of mutual cooperation, such as economy or diplomatic relations has remained untouched.

When it comes to judicial cooperation, Serbia's lack of cooperation with the International Crime Tribunal for the Former Yugoslavia in 2016 is noted.

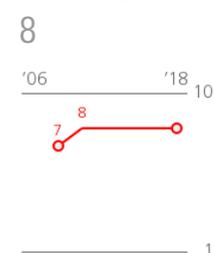
Serbia's political leadership cooperates with most neighboring states and complies with the rules set by regional and international organizations. There are some disputes which needs to be solved, such as border, citizenship, historic or minority issues, but these are ongoing processes which have been peacefully developing up to 2015.

However, in 2015 and 2016 there was a huge turn in regional relations, and relations began to regress. Statements and certain actions made mostly by state officials in Serbia, Croatia, Bosnia and Herzegovina, Montenegro and Kosovo have significantly threatened political relations and even increased conflict tensions.

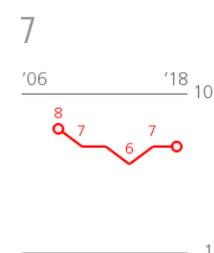
Beside such rhetoric and actions, disputes with the neighboring countries, such as borders/territory and ethnic (Croatia, Bosnia and Herzegovina, Montenegro, Kosovo), legal (Croatia, Montenegro, Kosovo) and diplomatic (Kosovo) still exist. Regarding relations with Kosovo, the Brussels Agreement is yet to be implemented, as the Community of Serb Municipalities, along with other aspects of the agreement, are not realized.

Serbia presided over a number of regional initiatives, including the Southeast European Cooperation Process (SEEC) and the Central European Initiative (CEI). Beside this, Serbia is actively participating, along with other Western Balkans countries within the so-called Berlin Process. Serbia is a signatory party of the Central European Free Trade Agreement (CEFTA), along with other Southeastern Europe European Union non-member states. In 2015 and 2016, the trend of trade within the CEFTA has decreased to some extent.

Credibility



Regional cooperation



Strategic Outlook

Serbia is an European Union candidate country in the process of the EU accession process. According to these goal, it is expected that regional relations, border and territorial disputes, as well as human and minority rights will improve. Serbia has opened and is currently opening the accession chapters which will be actively monitored and evaluated, both by the European Commission and internal actors, such as civil society and media. Some of the chapters are crucial for overcoming above mentioned problems, such as Chapter 23: Judiciary and Fundamental Rights, Chapter 24: Justice, Freedom and Security and Chapter 35: Other Issues (in case of Serbia, this chapter is dealing with the Kosovo dispute). Therefore, it is expected that the European Union accession process and country's transformation will serve as a leverage for overcoming current problems. This should eventually bring more stability within the political and election system, more efficient public administration and the removal of authoritarian tendencies. Parliamentary elections frequently organized since 2012 on every second year seriously undermine any kind of continuity in mid-term and long-term strategic planning, so European integration remains the main strategic framework for policy development in Serbia.

The country is on the path toward establishing a functioning market economy. However, the state still accounts for a large share of the economy, through state owned and public enterprise that are active in many different sectors where state intervention is not considered important. State enterprises are inefficient and are a drain on limited public resources, and serve as a focal point of corruption, political influence trading and a pool of employment opportunities for people with political connections to ruling parties. The privatization process of designated state-owned enterprises is continuing very slowly, as well as the process of introducing independent management of public enterprises. The fiscal austerity program implemented via curbing the public sector wage bill and pensions, followed by policies curbing the shadow economy, significantly reduced public deficit and lead to the stabilization of the public debt level at 72.00% of GDP in 2016. Although, limited action is still necessary in order to alleviate the burden of accumulated public debt and strong fiscal risks associated with the management of public enterprises. Total level of investment is still below the regional average, but public investment in infrastructure is increasing, as is its actual implementation.