This report is part of the Bertelsmann Stiftung’s Transformation Index (BTI) 2014. It covers the period from 31 January 2011 to 31 January 2013. 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.


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Key Indicators

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<td>Aid per capita $</td>
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Sources: The World Bank, World Development Indicators 2013 | UNDP, Human Development Report 2013. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than $2 a day.

Executive Summary

Between 2011 and early 2013, Serbia has made some progress in achieving its goals of moving closer to EU membership, bolstering a free market economy and strengthening the rule of law. Yet results have been mixed. The 2011 ruling coalition, dominated by the Democratic Party (DS) of President Boris Tadic, fulfilled one of the conditions for EU membership and arrested two remaining war crimes fugitives, Ratko Mladic and Goran Hadzic. Serbia also took a more pragmatic approach toward its ongoing claims on Kosovo. Because the European Union made it clear that normalizing ties with independent Kosovo was the ultimate precondition for further integration, Serbia agreed to hold talks on practical issues with Pristina, starting in March 2011. A year later, the European Union granted Serbia candidate status, having confirmed that sufficient progress in reaching and implementing agreements with Kosovo had been made. The government has also continued to harmonize the Serbian legal system with the EU’s standards, brought about prudent macroeconomic policy and fought the recession. However, Serbia’s leadership lacks the political determination to implement newly adopted legislation, to curb the bloated state bureaucracy and to stem rampant corruption in the country. The parliamentary and presidential elections, held in May 2012, profoundly changed the political scene in Serbia. Incumbent Boris Tadic was defeated by Tomislav Nikolic from the nationalist Serbian Progressive Party (SNS). After prolonged negotiation, the SNS formed a coalition government with former members of the DS, the Socialist Party of Serbia and another party, the United Regions of Serbia. Ivica Dacic, the leader of the Socialist Party of Serbia (SPS) leader, and a former close ally of Slobodan Milosevic, was elected the prime minister. The new government set European integration as its key foreign policy goal and consequently accelerated the EU-mediated dialogue with Kosovo, implementing a number of already reached agreements with Pristina. In January 2013, the Serbian parliament adopted a resolution on Kosovo, which represented a huge concession from Serbia. Apparently abandoning earlier requests for partition or return of Kosovo within the legal frame of Serbia, the resolution indicates that the current leadership in Belgrade might be satisfied with broad autonomy for Kosovo Serbs. Following the government promise to get to grips with deep-rooted organized
crime and corruption, a number of former ministers and officials, together with Miroslav Miskovic, a billionaire tycoon, were detained in the anti-graft probe. More than 70 laws, including the new Public Procurement Law, important for the government’s anti-corruption drive, were also adopted. Economically, Serbia struggled during the review period. Due to ongoing sovereign debt crisis in the Eurozone, as well the political elite’s reluctance to abandon failed populist economic practices, Serbia’s economy contracted an estimated 2% in 2012. Serbia ended 2012 with the highest inflation in Europe (12.2%), high unemployment, massive current account and budget deficits and depreciation of the Serbian dinar. The government also passed an austerity budget in 2013, and tried to restart frozen negotiations with the IMF. Also in response to its weak fiscal position, Serbia increasingly turned to Russia and China for investment and loans.

History and Characteristics of Transformation

Serbia’s transition to democracy and a market economy has been fraught with the statehood conflicts that marked the period that followed the break-up of the Soviet Union. The collapse of communism in Eastern Europe led to the disintegration of the former Yugoslavia and caused a series of wars in the Balkans in the 1990s. Tensions had been building between the republics that had made up the Socialist Federal Republic of Yugoslavia since the 1980s. They split into Bosnia and Herzegovina, Croatia, Macedonia and Slovenia. In 1990, Serbia’s socialist party, led by Slobodan Milosevic, won the first democratic elections and sought to reestablish a centralized federation and Serbia’s dominance in it. In contrast, the political leaders of Slovenia and Croatia wanted to advance the establishment of separate states. In Bosnia and Herzegovina, Croatia and Slovenia, wars of different durations and intensities began when the Yugoslav National Army attacked the republics, assisting the rebellions of ethnic Serb communities in Bosnia and Croatia against the secessionist republics. Facilitated by the wars and nationalist mobilization, Serbia’s President Milosevic established a semi-authoritarian system in the remaining parts of Yugoslavia and remained in power until 2000. Responding to its deepening crisis, Milosevic’s government increased political repression in Serbia proper and its violent military repression of ethnic Albanians in Kosovo. The country then slid into a full-scale war. NATO air strikes forced the regime to abandon its control over Kosovo and contributed to the demise of Milosevic after massive opposition-led demonstrations in Belgrade. The Democratic Opposition of Serbia (DOS), a coalition of 18 liberal, social democratic and moderate nationalist parties, 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 Prime Minister Djindjic in March 2003 limited the government’s capacity to sustain its initial dynamic policy of economic and political reform. 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 a more loosely integrated
state union mediated by the European Union. Following a referendum in May 2006, Montenegro became an independent state and the state union was dissolved. As a consequence of its military defeat in Kosovo, 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 Resolution No. 1244/1999 of the U.N. Security Council. On 17 February 2008, Kosovo declared its independence, subsequently recognized by the major Western states but fervently opposed by Serbia. In 2011, Serbia decided to heed the EU’s unambiguous message that the arrest of remaining war crime fugitives Ratko Mladic and Goran Hadzic as well as the normalizing ties with Kosovo were the key preconditions for further European integration. Mladic and Hadzic were arrested and transferred to the International Criminal Tribunal for the former Yugoslavia (ICTY) in The Hague in 2011. In March of the same year, Serbia commenced dialogue on practical issues with Pristina, and a year later, it obtained EU candidate status. The new Serbian government elected in May 2012 led by the Socialist Party of Serbia (SPS) and the Serbian Progressive Party (SNP), raised the prospects of progress in its bid for EU membership. Hoping to get the start date for accession talks later that year, the government accelerated dialogue with Kosovo, calling for autonomy for Kosovo Serbs.
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 in its territory, with the exception of Kosovo, which claimed its independence in 2008. By the end of 2012, 98 countries (including all major Western powers and 22 out of 27 EU members) had recognized Kosovo. The European Union and a number of Western leaders urged Serbia to accommodate Kosovo’s demands for recognition, openly making it a condition for Serbia’s EU membership. In spite of its promise never to recognize Kosovo’s independence, the new Serbian leadership decided to support the continuation of the EU-backed dialogue on practical issues with Pristina, opened in March 2011. On January 12, 2013, signaling apparent willingness to lose claims to its former province in exchange for EU membership, the Serbian parliament adopted the Resolution on Kosovo, a set of guidelines for reconciliation talks with Pristina, agreed between President Tomislav Nikolic and the rest of the Serbian government, especially urging for autonomy for Serbs in Kosovo. Yet Serbia faces other barriers to European integration as well. In 2011 and 2012, organized crime continues to be one of the biggest obstacles on Serbia’s path to EU membership, although improvements in police organization and capacities, and cooperation with foreign forces and agencies have reduced its threat to public order and safety. The Serbian parliament adopted a number of laws aimed at fighting organized crime, including amendments to the criminal code and the new Criminal Procedure Law. Still, inefficient judiciary, corruption, and political interference in the judicial system continue to hamper the serious and decisive fight against the organized crime. The authorities are saying that they are closing in on fugitive drug lord Darko Saric, accused of trying to smuggle more than two tons of cocaine from Latin America to Western Europe in 2009. Saric allegedly had links to high-ranking politicians and businessmen in Serbia and the region and was involved in money laundering through the illegal privatization of Serbian state-owned companies.
The constitution defines Serbia as the state of the Serbian people and all citizens who live in Serbia. In the 2011 population census, less than 13% of Serbia’s citizens (excluding Kosovo) identified themselves as belonging to national minorities. According to the 2012 census, Hungarians in the autonomous province of Vojvodina are the largest national minority, representing 3.5% of the population, followed by Roma (2%) and Bosniaks (Sandzak), who comprise 2% of the total population of Serbia. Among the largest territorial concentrated minority are Albanians in southern Serbia (0.08%) although these results are incomplete due to the partial boycott of the census. The constitution guarantees all minorities a number of individual and collective rights and the political parties of national minorities are represented in parliament. Following the 2009 Law on National Minority Councils (NMCs) clarifying the councils’ competences in education, culture, official usage of language and public information for each of Serbia’s national minorities, 19 NMCs were formed. (However, a Bosniak minority council in the Sandzak region was not formed due to local Muslim communities in-fighting. To address concerns of the ethnic Albanian minority in southern Serbia and accusations of ethnic inequality, the government formed a local multi-ethnic police force and established the Coordination Body for Southern Serbia, which conducted regular consultation with local Albanian leaders in the municipalities of Presevo, Bujanovac and Medvedja. According to the UNHCR, Serbia still hosts one of the largest populations of displaced people in Europe. According to the Serbian Commissioner for Refugees, in December 2012 there were 66,408 refugees and 210,000 internally displaced persons (IDPs), mostly victims of 1990s Yugoslav wars.

Serbia is defined by its constitution as a secular state, and its society is largely secular. According to the 2002 census, the Serbian Orthodox Church has the largest number of declared followers (85% of Serbia’s population), followed by the Roman Catholic Church (5.5%) and Islam (3.2%). For a majority of Orthodox Serbs, their religious affiliation is more a badge of their inclusion into the Serbian nation than confirmation of devout belief. Religious dogmas have no noteworthy influence on politics or the law. However, the leadership of the Serbian Orthodox Church has a prominent role in religious, social and political life, and enjoys certain privileges compared to other religious communities and the public as a whole. In spring 2013, the government will introduce 15 military chaplains (13 Orthodox priests, an Imam and a Roman Catholic chaplain) into the Serbian Armed Forces (SAF) for the first time.

Serbia has a differentiated administration that extracts and allocate state resources throughout the country, albeit with limited efficiency and effectiveness.
2 | Political Participation

Serbia’s most recent general and local elections, together with provincial elections in Vojvodina, were held as scheduled in May 2012. Early presidential elections were also held in May 2012 after incumbent Boris Tadic decided to resign. International observers described the elections as “competitive, held in a conducive environment and professionally organized” in spite of a certain lack of transparency in the proceedings of the State Electoral Commission and the administration of the new single voters’ registry. Election observers with the Organization for Security and Co-operation in Europe (OSCE) raised some concerns, including allegations of fraud (so far not explained by the authorities) and vote-buying, intimidation of employees by various sides and possible misuse of public funds. The electoral system in Serbia is a purely proportional system, practiced in a single constituency with 250 seats and a 5% electoral threshold. In order to enhance the political participation of minorities, Serbia abolished the electoral threshold for parties and coalitions representing ethnic minorities. Election reform legislation, enacted in 2011 and consistent with European standards, resulted in members of parliament being for the first time appointed in the order in which they appeared on the electoral list. The controversial practice of “blank resignations,” which could formerly be handed by the elected members of parliament to their respective parties, is now prohibited. Opposition members of parliament chair a number of committees, including the Committee for European Integration, but no longer those covering finance, security or internal affairs.

Serbia’s democratically-elected government has the effective power to govern. Parliament has democratic and civic oversight of the army and the secret service through its parliamentary defense and security committee. The committee is responsible for monitoring and oversight of the secret service, the army and the police. However, a NATO review from November 2012 stated that the committee has not fully deployed all its influence to provide effective oversight. The Law on Defense, the Law on the Armed Forces of Serbia, the Law based on the Security Services Organization of Serbia, and the Law on the Military Security Agency and Military Intelligence Agency guide the functioning of the Serbian Ministry of Defense (MoD) and the armed forces. In April 2012, the Constitutional Court of Serbia ruled that some articles in the laws are unconstitutional, namely in the Law on the Military Security Agency and Military Intelligence Agency that gives this institution access to personal records and related data of Serbian citizens, including telephone records.

The freedoms of association and assembly are constitutionally guaranteed, and the government generally respects these rights in practice. According to the Ministry of Justice and Public Administration, there are 91 political parties, including 53 representing national and ethnic minorities, registered in Serbia as of July 2012. The
rights of the activists of Serbian lesbian, gay, bisexual and transgender (LGBT) groups to openly exercise their freedom of assembly, expression, and association are largely denied.

Serbia’s constitution guarantees freedom of speech and freedom of the press, albeit with some restrictions, including limits on speech that jeopardizes the rights and reputation of others or national security. In September 2011, the Serbian government adopted a five year media strategy, with the aim to end state ownership over the media and pave the way for the privatization of the state-owned media. The state was to withdraw from the media within two years. At the same time, the strategy calls for an increase in the number of public service broadcasters from two to eight, which suggests the authorities are attempting to preserve or even increase their influence on the media. The Serbian Anti-Corruption Council said that around €40 million (a quarter of the overall media revenue) is allocated every year by the state authorities for placing ads and information about their work, and as such, constitutes a powerful mechanism for pressuring the media and entailing a significant risk of self-censorship. The ownership of the print media remains problematic; the real owners of 18 of the 30 most influential outlets in Serbia are still unknown. A 2011 survey from the Center for Media and Belgrade University Political Science College showed that the loss of autonomy and strong pressures on media were the chief problems faced by journalists in Serbia. Nearly 60% of respondents said they feared that they would lose their jobs, while over 20% said they would immediately change professions if they were offered a better job. Attacks and threats against journalists continue to occur though they have declined in recent years. In February 2011, after reporting about alleged abuses at a state-owned coalmine, the independent broadcaster B92 and its journalists received public death threats. Some investigative journalists live under constant 24-hour police protection. Police investigations and judicial processes involving assaults on journalist were often long and inefficient, the U.S. Department of State reported. In accordance with the 2012 amendments to the Criminal Code, defamation was decriminalized following numerous demands from the Serbian journalist association. The Serbian government is expected to adopt a decision on the establishment of a commission to investigate unsolved killings of three journalists, Dada Vujasinovic, Slavko Curuvija and Milan Pantic, in the 1990s and early 2000s.

3 | Rule of Law

The parliament and judiciary have yet to become fully independent institutions. In practice, power is concentrated in the executive and the ability of the parliament and judiciary to hold the executive accountable is questionable. A March 2012 report from the OECD and European Union concluded that, despite the separation of powers laid out in the constitution, parliament is unable to properly to check the power of the
executive and needs to have its capacities reinforced. In December 2011, Serbia endorsed an amended Constitutional Court law that would guarantee the court’s budgetary independence and ensure, among other things, increased operational efficiency. The law would allow a small group of three to eight judges to decide certain cases, while a full court session remains the norm for important cases. Though the Serbian constitution prescribes that the court’s decisions be made by a majority vote of all 15 judges, the Council of Europe’s Venice Commission of legal experts has suggested the constitution be amended. In September 2011, parliament adopted a new Public Property Law, restoring public property to local self-government units, making them the property holders. Also in 2011, amendments to the law on local self-government funding were passed, allowing the local governments to get 80% instead of hitherto 40% of the payroll tax in the future, except Belgrade, the most developed local self-government, which will get 70% instead of 80% of the payroll tax. The ten percent saved in Belgrade will go to all other self-governments, with the poorest communities getting the biggest share (B92, June 2011). In July 2012, the Serbian Constitutional Court proclaimed a number of provisions of the 2009 Law on Authority of the Province of Vojvodina, also included in the Vojvodina Statute, unconstitutional. The court disputed the designation of Novi Sad as the capital of Vojvodina and the existence of Vojvodina’s office in Brussels.

According to the Serbian constitution, the courts are independent and autonomous. Indeed, in practice, the judiciary operates relatively independently, but its functions are still somewhat restricted by political influence, inefficiency, nepotism, cronyism and corruption. According to the European Union, judiciary reform failed to produce substantial progress in enforcing new legislation aimed at improving the efficiency of the judicial system. In November 2012, the Serbian Ministry of Justice expressed its intention to introduce a new court system in order to improve rationality and efficiency. The Ministry of Justice plans to increase the number of basic courts from 34 to 65, noting that Serbia, in comparison to other former Yugoslav republics, has only 1.7 courts for every 100,000 citizens (Croatia and Slovenia each have 4.7). The planned increase in the number of courts is also a prerequisite for the reinstatement of judges and public prosecutors who were fired during the 2010 judicial reform. In July 2012, the Serbian Constitutional Court overturned all the decisions as not meeting the required standards and ordered the reinstatement of all judges and prosecutors who had appealed their non-reappointment. By 5 December 2012, a total of 542 judges had been reinstated in different courts. The 2012 Fund for Open Society Survey showed that only 2% of citizens and 9% of the political elite consider the current judiciary in Serbia to be independent from the government. Furthermore, the judiciary is marked by inefficiency notably in lengthy court proceedings and backlogs. According to the Supreme Court of Cassation, the total number of cases in all courts in Serbia in 2011 was almost 6 million with a backlog of almost 3.4 million cases. The survey, conducted by the Belgrade Institute of Comparative Law, shows
that the average length of court proceedings in Serbia is four years with 14% of proceedings lasting more than seven years.

Serbia has continued to implement its existing and amended legal framework to fight corruption, abuse of power and other corrupt practices. Yet despite its efforts, the results have been limited. Remarkably few high-profile corruption cases have made it to court, particularly those related to misuse of public funds. According to some estimates, Serbia is losing billions of euros a year because of corruption. The new ruling coalition has committed to fighting organized crime and corruption in accordance with a key condition for the nation’s bid to join the European Union. According to a TNS Medium Gallup poll from June 2012, almost 87% of citizens think that Serbian politicians lack the political will to fight corruption in earnest because they benefit immensely from it. The most corrupt institutions in Serbia, according to one opinion poll, are political parties (77% of respondents), health care (74%), and government and judges (69%). Still, the government has taken a number of actions to address the problem. During 2011, a number of arrests were made in an alleged corruption scandal case in the Kolubara strip mining complex near Belgrade. Also, a number of people, including former deputy prime minister Jozef Kasa, were detained in October 2012 in the investigation into the Agrobanka embezzlement scandal where almost €300 million disappeared. Moreover, in the second half of 2012, Serbian authorities arrested and investigated a significant number of prominent bankers and businessmen on suspicion of corruption. Former ministers were also arrested for office abuse, namely former Agriculture Minister Sasa Dragin and former Environmental and Spatial Planning Minister Oliver Dulic, both from the Democratic Party. At the time of writing, the investigation in these cases was still ongoing. Finally, in December 2012, Serbian police arrested the owner of Delta Holding Company, and also the supposed richest Serb, Miroslav Miskovic, on suspicion of abuses during privatization of road construction and maintenance companies. From 2009 to 2011, Serbian anti-corruption prosecutors filed nearly 6,500 charges against individuals (including judges, prosecutors and police officers), suspected of various corruption practices while the special division of the High Court in Belgrade convicted almost 3,000 people of corruption.

Serbia has an established a strong system for guaranteeing and protecting civil rights, and for protecting citizens from discrimination. During 2011 and 2012, parliament adopted several new laws essential for protection from discrimination and improvement of equality, including the Law of Civil Procedure, the Law on Social Protection, the Law on Youth, and amendments to the law on electing members of parliament. However, the most effective practical measures and efficient ways of implementing the legislation have not been fully developed yet. Recent opinion polls reveal that Roma, poor and disabled persons, old people, women and members of the LGBT population continue to face discrimination in Serbia (Center for Free Elections and Democracy, or CESID, opinion poll, December 2012). Although Serbian
officials argue that the position of the Roma people has improved thanks to the Decade of Roma Inclusion, discrimination against Roma is still prevalent in employment, education, health care and housing. The large number of Roma do not have personal documents, 62% of Roma children have never attended school or have dropped out, while 72% of 593 Roma settlements in Serbia are not legalized, with inhabitants often subjected to forced evictions. Disabled people face both direct and indirect discrimination, particularly in access to employment, education, services and independent living, not to mention building access. According to the World Health Organization, there are some 700,000 disabled people in Serbia, of which around 80% are unemployed. During the review period, there were many cases of physical attacks, intimidation and threats against members of the LGBT population, and some individuals were hospitalized; the Pride Parades in Belgrade were banned in 2011 and 2012 due to security concerns. In April 2012, Serbia signed the Council of Europe’s Convention on Preventing and Combating Violence against Women and Domestic Violence. In ten months of 2012, 24 women were killed in instances of family or gender-based violence. Official statistics in Serbia also show that almost 54% of all women in Serbia were subject to psychological, physical, sexual, or other forms of violence at some point in their lifetime. A number of cases of police and prison abuse and brutality have also been reported in Serbia. During first 10 months of 2012, more than 100 police officers were charged with criminal offenses, including abuse of power, gross misconduct and corruption. With regard to war crimes, domestic proceedings continued in 2011 with the Serbian War Crimes Prosecutor’s indictment of a total of nine individuals. A total of 9,700 applications against Serbia have been submitted to the European Court of Human Rights (December, 2012). Yet human rights abuses are not just a thing of the past. According to the Council of Europe, Serbia has retained first place in the number of complaints with the European Court of Human Rights in Strasbourg in 2012 with 6.77 accepted claims per 10,000 citizens. In addition, some segments of society are still burdened with extremist nationalism expressed in a strong presence of racist, neo-Nazi, and violent groups, notably among so-called sports fans who target the Roma, LGBT and other minority groups (Civil Rights Defenders Report on Serbia, October 2012). A survey conducted in December 2012 by Belgrade Weekly showed that 36% of the Serbian youth age 12 to 18 harbor negative attitudes towards persons of different sexual orientation, while 22% hold negative feelings towards other nationalities.

4 | Stability of Democratic Institutions

Democratic institutions continue to perform their functions, but often are inefficient due to frequent friction between departments, lack of an adequate financial and human resources, and the prevailing influence of political parties represented in the executive branch. Still, the role of Serbia’s parliament has been significantly strengthened, mostly through the introduction and implementation of a number of
new and amended laws and regulations that are enhancing its position and efficiency. These include the Law on Financing Political Activities and the Law on Conflicts of Interest, both of which are aimed at improving the transparency of political parties and campaign financing. Legislation was also introduced to end the established practice of awarding Serbian political leaders multiple elected and non-elected positions (Serbia Executive Summary, Freedom House 2011). In 2011, new legislation regulating parliamentary procedures were introduced to institute public hearing and parliamentary inquiry proceedings and to require ministers to keep relevant committees informed of policy implementation on quarterly basis. The position of an internal auditor exercising oversight of parliament’s budget was also introduced in 2011. During that same year, the Serbian parliament adopted 205 laws and numerous other acts. In December 2012, however, opposition parties and media pointed out that about 70 laws that have entered the procedure in the new parliament, 60 laws were adopted according to the urgent legislative procedure, which is contrary to the recommendations of the European Commission. Some laws, like the Law on Judges, the Law on the Public Prosecutor and Code of Civil Procedure, although planned, were not adopted at all. Inadequacy in numbers and lack of professionalism of clerical staff is also a factor in the parliament’s failure to cope efficiently with the large volume and complexity of the work. In 2012, the Serbian parliament and its 250 deputies have 352 clerical and other administrative staff (ratio of 1.4 staff per member of parliament, which amounts to much less than a regional average of 3 to 1).

All relevant political and social actors accept Serbia’s democratic institutions as legitimate. Newly elected President Tomislav Nikolic from the Serbian Progressive Party (SNS) and Prime Minister Ivica Dacic (Socialist Party of Serbia, SPS), once fierce advocates of Serbian nationalistic policies, adhere firmly to democratic principles in dealing with some of Serbia’s most politically sensitive issues such as corruption, EU integration and normalizing ties with Kosovo. The proponents of virulent nationalism and extreme anti-Western policies are rapidly losing their influence and popularity. The most vociferous among them are the center-right Democratic Party of Serbia (DSS) led by the former Prime Minister Vojislav Kostunica, remnants of now non-parliamentary right-wing Serbian Radical Party (SRS) and some circles in the powerful Serbian Orthodox Church. A number of violent, nationalistic football fan groups and clerical fascist organizations like Nasi, (Ours) Obraz and the Serbian Popular Movement 1389 (allegedly linked to some elements in Serbia’s civilian and military secret services) have played a leading role in numerous attacks on minorities, members of the LGBT population and journalists they consider anti-Serb, as well as symbols of multicultural and open-minded Serbia.
5 | Political and Social Integration

The Serbian party system, while largely established, is highly fragmented, moderately polarized, and mostly dominated by individual personalities, many of whom have been active in Serbia’s political landscape for more than two decades. After the May 2012 general elections, a coalition of parties led by the right-of-center Serbian Progressive Party (SNS) and its leader, former hardcore nationalist Tomislav Nikolic, won 73 seats in the parliament. The Socialist Party of Serbia (SPS) and its leader, Ivica Dacic, once a close confidant of Slobodan Milosevic, won 44 seats, securing itself a strong bargaining position in the negotiations on forming a new Serbian government. A reformist pro-EU coalition led by the Democratic Party (DS) and incumbent Serbian president Boris Tadic, got 67 mandates, but were unable to form a coalition and stay in power. Former prime minister Vojislav Kostunica and his strong nationalistic Democratic Party of Serbia (DSS) won 21 seats, the most pro-Western political force in Serbia, Liberal Democratic Party (LDP) got 19, and the United Regions of Serbia (URS), led by former finance minister Mladjan Dinkic, won 16 parliamentary seats. The ruling coalition of the SNS, SPS and URS and their allies, formed in July after prolonged negotiations, can count on 144 deputies in the 250-seat Serbian parliament, which is elected every four years. Most of the remaining mandates were distributed among the representatives of the regionalist parties representing national minorities. The new constellation of parties in the Serbian parliament was a further reflection of both existing socioeconomic and socio-cultural divisions and the significant change in priorities among the large majority of the Serbian electorate, which is more concerned about declining living standards than issues of nationalism. As a result, a number of the nationalistic and extremist parties and groups, including the Serbian Radical Party (SRS) did not reach the threshold for entering parliament. Overall, 45 political parties, associations and alliances were represented in the new parliament, which is twice more than in the last parliament. In 2012, the Serbian Anti-Corruption Agency started to implement 2011 legislation on the financing of political parties and began monitoring the electoral campaign.

Interest groups

During 2011 and 2012, economic stagnation, high unemployment, and unsuccessful and sometimes corrupt privatizations helped trade unions emerge as the most vocal interest group. However, the unions have not been very influential enjoy the confidence of only 15% of people, according to one report. Social dialogue in Serbia remains limited and ineffective. According to the Confederation of Autonomous Trade Unions of Serbia, in 2011 there were 60 strikes with more than 60,000 employees participating. The most frequently cited reasons for strikes were unpaid wages, poor working conditions, termination of privatization, and prevention of illegal or fraudulent sale of corporate assets. A new law on strikes, which should be finalized by April 2013, will supposedly provide more space for peaceful settlement of disputes between employers and employees, and determine which activities, like
education and health care, must respect minimum levels of service provision during the strike. The Social and Economic Council, established in 2001 as an institution of interest mediation and economic policy coordination, has in fact thus far been consulted more often about the draft laws. The existing Labor Law is also supposed to be amended by the end of 2013 and will redefine the rights and duties of both workers and employers. Business interests are organized in a network of local, regional and national economic chambers that function as interest associations. The amended Law on Economic Chambers, adopted in 2009 with delayed implementation of three years, provides for the abolition of compulsory membership in chambers of commerce, primarily to promote competition between the existing chambers. The Chamber of Commerce and Industry of Serbia, for its part, warned that compulsory membership could threaten the functioning of the republic chamber system. The links between business tycoons, (who still wield great influence in Serbia’s business sector, and apparently, also in its politics) political parties and media continue to exist in mostly a non-transparent and dubious way.

The concept of democracy is consensually embraced, and the constitutional framework is fully accepted. An opinion survey, conducted by Belgrade’s expert Jovanka Matic, revealed that Serbia’s citizens have high expectations of democracy but remain passive in building the democratic system because neither the political work nor the social environment stimulate them for civic engagement. At the same time, support for democracy and a market economy in Serbia has weakened significantly according to the June 2011 “Life in Transition” report the European Bank for Reconstruction and Development (EBRD) and World Bank. Less than 20% of respondents favored a combination of democracy and a market economy over other alternatives. Moreover, a lower level of trust and confidence in specific democratic institutions was noted among Serbian citizens in 2011, according to the Center for Free Elections and Democracy (CESID). Serbs have the highest degrees of confidence in the Serbian Orthodox Church, the police and the army, at 59%, 45% and 44% respectively. At the same time, Serbs have the least amount of respect for parliament (16%) and political parties with only 9%.

Serbia is home to a number of independent groups and organizations with strong and long-established histories, but the level of trust they enjoy among the population varies. NGOs that receive foreign donations and address issues such as war crimes, minority rights and the rights of LGBT population face public criticism, negative media coverage and overt hostility. NGOs dealing with consumer rights, ecology, personal information privacy and animal welfare are more popular among the public. Nevertheless, a relatively small number of citizens participate actively in their work. In November 2012, an extreme right-wing group, Serbian Popular Movement Ours (Srpski Narodni pokret Nasi) called on the authorities to outlaw 17 NGOs, which it said had violated the Serbia’s constitution, and requested that all the country’s NGOs and media funded from abroad be labeled as “foreign agents.” Ministry of Finance
plans, announced in winter 2012, to change the Law on Budget System, the Law on Bookkeeping and Accounting, and the Law on Income and Earnings Tax could undermine freedom of association, as well as the independence and financial sustainability of civil society organizations in Serbia. The European Bank for Reconstruction and Development (EBRD) and the World Bank “Life in Transition” survey, published in June 2011, showed that about 37% of Serbian respondents think that people in general can be trusted (35% in 2010).

II. Economic Transformation

6 | Level of Socioeconomic Development

With a gross national income of $5,690 per capita in 2011, which is slightly less than a year before, Serbia maintained its position among the upper-middle income countries of the world. Yet the current economic recession in Serbia continues to cause an increase in social exclusion. As reported by the Ministry of Labor and Social Policy, the poverty rate in Serbia in 2011 increased from 9.2% in 2010 to 10% of the total population (7,186,862 in 2011). In other words, nearly 700,000 people are living below the absolute poverty line, established at €80 per month. The most vulnerable groups are the uneducated, single parents, the elderly, and woman-headed and rural households, particularly those in southern and eastern Serbia. Serbia’s HDI value in 2011 was 0.766, placing the country at 59 out of 187 countries with comparable data, and above the regional average (HDI Report 2011). At the same time, the Gini coefficient of income inequality recorded a slight increase in 2011, reaching 28.2 (28 in 2010), which is closer to the lower limit of the range (International Organization for Migrations, 2012). The bleak economic situation and laggard pace of structural reforms continues to affect the other indicators of social exclusion in the country. In October 2012, the rate of unemployment reached 22.4% (755,000 people of which women comprise 44%) according to government statistics. In terms of gender equality, Serbia ranked 50 out of 135 countries in the Global Gender Gap Index for 2012, and 67 in economic participation and opportunity (World Economic Forum, 2012). The same survey shows that the literacy rates in Serbia are 99% for men and 97% for women.
## Economic Indicators

<table>
<thead>
<tr>
<th>Economic indicators</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP $ M</td>
<td>40249.5</td>
<td>36990.0</td>
<td>43291.8</td>
<td>37488.9</td>
</tr>
<tr>
<td>GDP growth %</td>
<td>-3.5</td>
<td>1.0</td>
<td>1.6</td>
<td>-1.7</td>
</tr>
<tr>
<td>Inflation (CPI) %</td>
<td>8.1</td>
<td>6.1</td>
<td>11.1</td>
<td>7.3</td>
</tr>
<tr>
<td>Unemployment %</td>
<td>16.6</td>
<td>19.2</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Foreign direct investment % of GDP</td>
<td>4.8</td>
<td>3.6</td>
<td>6.2</td>
<td>-</td>
</tr>
<tr>
<td>Export growth %</td>
<td>-14.9</td>
<td>19.1</td>
<td>14.7</td>
<td>-</td>
</tr>
<tr>
<td>Import growth %</td>
<td>-22.9</td>
<td>4.1</td>
<td>15.4</td>
<td>-</td>
</tr>
<tr>
<td>Current account balance $ M</td>
<td>-2866.5</td>
<td>-2819.3</td>
<td>-3834.4</td>
<td>-4001.9</td>
</tr>
<tr>
<td>Public debt % of GDP</td>
<td>38.1</td>
<td>46.5</td>
<td>50.0</td>
<td>63.7</td>
</tr>
<tr>
<td>External debt $ M</td>
<td>33813.8</td>
<td>32934.7</td>
<td>31568.9</td>
<td>-</td>
</tr>
<tr>
<td>Total debt service $ M</td>
<td>4646.0</td>
<td>4306.9</td>
<td>5210.3</td>
<td>-</td>
</tr>
<tr>
<td>Cash surplus or deficit % of GDP</td>
<td>-2.8</td>
<td>-4.0</td>
<td>-4.5</td>
<td>-</td>
</tr>
<tr>
<td>Tax revenue % of GDP</td>
<td>22.4</td>
<td>22.8</td>
<td>21.7</td>
<td>-</td>
</tr>
<tr>
<td>Government consumption % of GDP</td>
<td>20.2</td>
<td>19.9</td>
<td>18.9</td>
<td>-</td>
</tr>
<tr>
<td>Public expnd. on education % of GDP</td>
<td>5.0</td>
<td>4.7</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Public expnd. on health % of GDP</td>
<td>6.5</td>
<td>6.4</td>
<td>6.5</td>
<td>-</td>
</tr>
<tr>
<td>R&amp;D expenditure % of GDP</td>
<td>0.92</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Military expenditure % of GDP</td>
<td>2.4</td>
<td>2.4</td>
<td>2.3</td>
<td>2.2</td>
</tr>
</tbody>
</table>


### 7 | Organization of the Market and Competition

Serbia has established an institutional framework for market competition, but the state sector remains large and mostly inefficient. It employs around 720,000 people, of which 450,000 are in the public service. In June 2012, the Fiscal Council of Serbia, a three-member body monitoring the nation’s budget performance, said the salaries in the public service are 40% higher than the ones in the private sector, despite the fact that the public sector operates with the yearly loss of around €1 billion, or about 40% of all losses in the economy. The size of the informal economy, which allegedly employs up to 1 million people, is large, and according to official estimates, close to 40% of GNP. The World Bank’s 2013 Doing Business report ranked Serbia 86 out
of 185 countries, nine places better than in 2011 (95). Serbia lags behind Slovenia, Croatia, Macedonia, and Montenegro, but in front of Bosnia and Herzegovina and Kosovo. Serbia is 42 for “Starting a business,” 179 for “Dealing with construction permits,” and 103 for “Enforcing contracts.” Trying to help domestic competitiveness, the government removed almost 140 parafiscal fees and charges in September 2012. Regardless of the sweeping system changes, entrepreneurial decisions are often constrained by state interference, widespread corruption, and red tape. As stated in the 2012 EU report on Serbia, price liberalization has stalled and has even been partially reversed. Determined to attract more FDI, Serbia introduced legislation outlining guarantees and safeguards for foreign investors, including the Law on Foreign Investments. The Serbian Investment and Export Promotion Agency (SIEPA) provides direct assistance to investors, offering duty-free exports to countries of Southeast Europe and Russia and corporate income tax rate of 15%, among other things.

The main element of Serbia’s legislation concerning antitrust and competition is the 2009 Competition Law, modeled after the EU competition law. This act includes standard regulations that pertain to averting restrictive agreements and practices, merger control and prevention of abuse of dominant position. Leniency has been introduced into the Serbian antitrust rules. The Competition Law also laid the foundation for the establishment of the Commission for Protection of Competition (CPC), which is charged with implementing the competition law, and independently imposing its own sanctions for violations of competition. As of June 2012, the CPC has imposed penalties amounting to nearly 3.5 billion RSD (about €37 million) and has fined a total of 36 companies and associations. The administrative court is in charge of deciding upon administrative disputes initiated by the parties disaffected by a decision of the commission. Although the court is supposed to reach its decisions within two months, this deadline is rarely honored due to the court’s weak capacity, and proceedings may be prolonged to up to two years according to the 2013 European Antitrust Review. At the time of writing, some sectors of Serbia’s economy like food production and retail, were still characterized by significant oligopolistic or monopolistic ownership structures. In its 2012 report, the World Bank noted that high volatility in prices of many agricultural and food products in Serbia indicated a lack of competition and efficiency in the marketing chains.

The ongoing process of European integration has been the main driving force behind Serbia’s trade and liberalization reforms and deregulation, entailing the total elimination or reduction of import duties and the simplification of customs procedure. The European Union remains Serbia’s main trading partner, accounting for 57.7% of the country’s total exports and 55.6% of its total imports in 2011. According to the 2008 Stabilization and Association Agreement and the Interim Trade Agreement between the European Union and Serbia, both contracting sides should establish a free trade zone within six years, with the full and free movement of goods, without
tariffs and taxes of equivalent effects and quantitative export and import limitations. On 1 January 2013, Serbia entirely abolished import customs duty for a large number of products produced in the European Union. Serbia also agreed to abolish the customs duty for about 96% of agricultural products as of 2014. Only those agricultural products produced by Serbia will continue to be subject to a 20% to 80% rate after the end of the transitional period. Consequently, in December 2012, the government decided that the import surcharge, introduced to protect domestic agriculture, will apply to 453 tariff lines, including a variety of agricultural and food products like all types of meat, milk, eggs and potatoes. Serbia has a preferential trade regime that applies to Russia, Belarus, Turkey, Kazakhstan, as well as to signatories of the European Free Trade Agreement members (EFTA) and the Central European Free Trade Agreement (CEFTA 2006). Serbia hopes to become a WTO member in 2013 and is making steady progress in multilateral and bilateral negotiations as part of the WTO accession process. The slowdown in negotiations is evident in talks with Ukraine and the United States. Ukraine demands free steel exports, which is unacceptable for Serbia. According to U.S. diplomatic cables released by Wikileaks in September 2012, the Americans pressed Serbian officials to change the Serbian Law on Genetically Modified Organisms (GMO) adopted in 2009. The Americans argued that the law was not in line with WTO regulations and as such represented an obstacle for Serbia’s future WTO accession.

According to the World Bank 2012 report, the Serbian financial system has weathered the first wave of the global financial crisis. The banking system is well-capitalized and liquid though still significantly fragmented. As stated in a document from the central bank (National Bank of Serbia, NBS), published in November 2012, the share of foreign bank subsidiaries in the country’s banking sector assets is 74%. Of the 31 banks operating in Serbia at the beginning of 2013, 21 are foreign owned (mostly Greek, Austrian, French and Italian), eight are state owned, and three are owned by private individuals. The five largest banks account for 47% of the total assets of the banking sector. The EU’s analysis indicates that a weakening economy and depreciating dinar point to a growing risk of further deterioration in the quality of the loan portfolio. The volume of non-performing loans (NPL) in October 2012 went up to 18.8% (20.4% in the corporate sector), but potential losses are fully covered with a regulatory loan loss reserve of 122.6% in that same year. In addition, the capital adequacy level of the banking sector is satisfactory, with the capital adequacy rate (CAR) at 16.4% (September 2012, relying on Basel 2 standards), above the prescribed limit of 12% and significantly above the international minimum of 8%. In June 2012, close to 75% of loans and 72% of deposits were in or indexed to foreign currency, predominantly to the euro. The interest rates on bank loans in Serbia continued to be high, mainly because of high inflation and the central bank’s attempts to tame accelerating inflationary pressures by raising the key policy rate to 11.5% in January 2013. Already nurturing a conservative regulatory approach, central bank supervision was tightened following the collapse of the state-owned Agrobanka bank,
de-licensed by NBS in May 2012 when it was discovered that the bank was €300 million in debt. In November 2012, the Serbian parliament revoked sections of the central bank law, trying to soften criticism from the European Union and the IMF that earlier legislation, introduced by the new ruling coalition, established parliamentary control over the monetary institution and therefore restricted the bank’s independence.

8 | Currency and Price Stability

Serbian policy makers have been trying to curb price increases and restart growth. However, Serbia failed to tame inflation and stabilize the national currency, the dinar. The acceleration of inflation in Serbia was influenced by a number of factors, notably hikes in the prices of food, political uncertainties linked to the general elections in May 2012 and the formation of a new government, weaker net foreign currency inflows, dinar depreciation and very expansive fiscal policy in the first half of the 2012. At the same time, the dinar’s depreciation was a result of Serbia’s flexible exchange rate regime, which stemmed from the country’s external and domestic debt in foreign currency and the a highly euroized economy. Depreciation against the euro since the beginning of 2012 amounted to 13.2%, according to the World Bank. During that time, the central bank spent more than €1.3 billion (almost 10% of its total foreign currency reserves) intervening heavily in the foreign exchange market, in order to support the domestic currency. The bank hoped that large forex reserves (€10.9 billion in December 2012) would serve as assurance that the system remains stable.

The Serbian government has declared that its long-term goals include realistic GDP growth and strengthening the competitiveness of the economy, while preserving macroeconomic stability and fiscal discipline. Although Serbian Prime Minister Ivica Dacici vowed that his government is not going to freeze pensions or government salaries, or generally pursue a policy of austerity, foreign financial markets have already noticed that his government has started to streamline and restructure spending to narrow the budget gap of more than 7%. The public debt that reached €17.56 billion, or 60.5% of GDP, in December 2012 puts Serbia in the company of highly indebted countries (Serbia’s external debt at the end of October amounted to €25.54 billion or almost 84% of GDP). According to SETimes.com, in the new cabinet’s first 130 days, the debt increased by about €2 billion, or the equivalent of €186 per second. The budget deficit target is 4.25% of GDP, as agreed to with the IMF, while the public debt administrative limit stands at 45% of GDP. Fiscal consolidation measures partly supported the budget deficit, undershooting the revised level in 2012. However, 2013 will be the turning point because the full effect of the fiscal consolidation package, including increased tax rates and revenues and reduced public spending, will be seen in 2013. After the 2% growth in 2011, the Serbian economy entered into a double dip
recession in 2012 and contracted by 1.9%, according to government figures. The ongoing EU sovereign debt crisis and unfavorable macroeconomic indicators in Serbia caused a fall in FDI in 2012, expressed in a net outflow of €21.2 million, as reported by the Serbian Chamber of Commerce in December 2012. All the other main indicators signaled that the country’s economy remains under stress. Inflation was 12.2% in December 2012, exceeding the NBS targeted range for November 2012 (4.0% +/- 1.5%) while the trade deficit in the first 11 months of 2012 hit almost $7 billion, 4.7% less than in the same period last year. According to available data, the Serbian current account deficit might reach almost €3.1 billion or 10.7% of GDP at the end of 2012. In its 2013 budget projections, the new Serbian government plans to cut the budget deficit to 3.6% of GDP, achieve an economic growth of almost 2% and a tax revenue increase of 15%, ultimately balancing the budget in 2016. In February 2012, the IMF put a loan worth more than a $1 billion on freeze after the government failed to meet its budget targets.

9 | Private Property

Serbia has an adequate legal framework for the protection of property rights, though the enforcement of these rights through the judicial system can be extremely slow. Even so, in its 2013 Doing Business report the World Bank ranked Serbia 86 out of 185 countries (92 in 2012). The same report ranks Serbia 103 out of 185 countries with respect to the time required to enforce a contract through the courts (average of 635 days). The regulation of the acquisition of property is well-defined and the legal framework that protects property is in place. However, municipal courts and cadastral offices dealing with property registration are highly susceptible to corruption, which undermines the protection of property rights in practice. According to a TNS Gallup survey conducted in June 2012, 45% of respondents think that the officials of the cadaster are corrupt. As an exception to the general rule that non-Serbian individuals, under reciprocity requirements, may acquire ownership of real estate in Serbia, the Agricultural Land Law of 2006 does not allow foreigners to own agricultural land in the country. However, the Stabilization and Association Agreement between the European Union and Serbia, which is currently in the ratification process, stipulates that Serbia has to grant all citizens of the EU the right to buy agricultural land four years from the time when the document is ratified by the last EU member state. In September 2011, Serbia adopted a general law on restitution, which establishes the principle of “in kind restitution.” In cases where in kind restitution is not possible or excluded, financial compensation, with an overall cap of €2 billion, is foreseen. Since March 2012, more than 10,000 requests for the return of property confiscated after World War II were lodged with the Serbian Agency for Restitution. The total value of the property returned so far is almost €60 million.
The state continues to exert strong influence over the economy and holds dominant ownership in key sectors of the Serbian economy, mainly telecommunications, energy (oil and gas), railway and air transport. In 2012, private companies produced only 60% of Serbia’s GDP, less than the regional average of 70–80%. Almost 1,340 enterprises are still under state control, employing nearly 100,000 workers and undergoing yearly losses of about €1 billion or 3.5% of the country’s GDP. According to data from the Fiscal Council of Serbia, there are 700 public companies at the central and local level (including the electricity operator EPS, the Serbian Telecommunication Company Telekom, Belgrade airport, JAT airline and Serbian Railways), employing 10% of the workforce in the country. In December 2012, the new Law on Public Companies went into effect, which is supposed to ensure professionalization of public enterprises, stop any future political meddling in their operations, and increase their efficiency and transparency. The Serbian Ministry of Finance and Economy cited the volatile global business environment in 2011 as the main reason that revenue from privatization was lower than in previous years. Over 11 months in 2012, Serbia privatized 12 enterprises for €15.4 million with another €2 million in investment, and over the past decade the state sold nearly 2,400 companies. Despite raising some €2.6 billion in revenue, and €1.1 billion in agreed investment, some 83,000 jobs – roughly two-thirds of all jobs prior to privatization – were lost, according to 2012 data from Serbia’s Social-Economic Council. The Privatization Agency cancelled 630 sale contracts so far due to a failure to fulfill the stipulated conditions, particularly with respect to investments and social programs. The process of privatization in Serbia is often marked by corruption, criminal activity, cronyism, and a lack of transparency. In 2011, the European Commission demanded that Serbia investigate the potential illegal privatization of 24 Serbian companies. Free shares in telecommunications company Srbija Telekom, one of the six largest publicly-owned companies, were distributed in April 2012 and may soon be floated on the stock market, depending on the decision of the Serbian state.

10 | Welfare Regime

Serbia continues to struggle with low innovation investment and a poor education system which, in turn, causes high unemployment and widespread poverty. During the period under review, social safety nets were put under added stress by the rise in unemployment, which reached a record 22.4% in December 2012. Since the beginning of the global financial crisis in 2008, unemployment in Serbia has risen by more than 11 percentage points, and almost 600,000 people have lost their jobs. Experts argue that the transition to a market economy and the current crisis have led to the development of significant structural problems in Serbia’s labor market, as well as failures in labor policy design and the lack of institutional support for implementation. The unprecedented rise in unemployment continues to affect the level and the extent of poverty among the most vulnerable community members: rural...
elderly, single generation households, large families, Roma, the less educated, the young and the disabled. The government has taken steps to address these problems with the passage of new laws. In 2011, the government adopted a new Social Assistance Act that governs the provision of last resort social assistance, linking it with social care and employment services and removing certain disincentives to look for work and participate in public works projects (World Bank, Serbia Partnership Program, October 2012). The New Law on Social Protection, also adopted in 2011, defines social protection measures focused on improving the quality of life of sensitive groups of citizens, and reforms the social protection system. The law has increased the number of beneficiaries and the amount of assistance they receive. Still, while aid has increased, it is still far less than the amount necessary to meet basic needs. The social services were limited in scope and quality due to financial constrictions and a widespread employer avoidance of paying social security, pensions and other contributions for workers. The 2011 census also shows that population numbers are declining and aging, which has put a further strain on social services. According to the census, Serbia has 7,186,862 inhabitants, which is 4.15% less than in 2002, and there are especially fewer young and educated people. Serbia is an aging country too; 40% of the population is older than 65, and the average age of the Serbian population is 42.2. Indeed, in May 2012, the number of pensioners (1,684,124) almost equaled the number of employed workers (1,734,000). An average pension in Serbia, in October 2012 was 62% of an average salary, according to Serbia’s Pension and Disability Insurance Fund. Planned reforms of Serbia’s pension system have been designed in response to the growing number of pensioners. The minimum retirement age was increased from 53 to 58 years, and the required contribution period from 35 to 38 years. As stated in the ASISP 2012 Annual Report on Serbia, the change of the contribution period will be implemented gradually between 2013 and 2021, increasing by four months a year. The minimum retirement age will likewise be increased from 2013 to 2016 by four months a year, and from 2017 to 2023 by six months a year. However, a rough calculation also shows that even by 2020, the share of pensions in Serbia’s GDP will not drop below 10% (12.6% in 2012). The private pension system is still underdeveloped, though the net assets, as well as the number of beneficiaries, increased in 2011. Only 10% of all employees made regular contributions to the private pension funds. The average life expectancy at birth, which can be interpreted as an aggregate measure of the health system’s effectiveness, increased in 2011 to 71.6 and 76.8 years for the male and female population respectively, which is still below the estimated 2010 EU averages of 76.4 and 82.4 respectively.

Equality of opportunity is formally granted and is protected by the legal and institutional framework. However, the 2009 anti-discrimination law that prohibited all forms of discrimination against individuals and groups, in accordance with EU anti-discrimination rules, is not always fully enforced and implemented. Those most vulnerable to discrimination, according to EU reports, are Roma, women, persons
with disabilities and the LGBT population. The ratio of female to male primary enrollment in Serbia was last reported at 99.50% in 2010, (tertiary at 129.84%), according to a World Bank report published in 2012. The government data show that 61% of women in Serbia are economically inactive. Although women make up 51.3% of the population (2011 census), they are underrepresented in public positions. For example, 32.4% of deputies in the new Serbian parliament (81 of 250 deputies, May 2012) are women. Among the 19 members of the new Serbian government, five members or 26.3% are women. On average, according to official data, women earn 3.5% less (unofficially even 16%) than their male counterparts, according to the Serbian commissioner for the protection of equality. The Roma population, and especially Roma women, along with the disabled, face the most discrimination in the labor market. Relying on a free visa regime with the European Union, thousands of Serbian citizens, almost 95% of them poor Roma, have been applying for asylum in EU countries because of alleged discrimination in Serbia, only to obtain the financial support given to the asylum seekers. Because of this, in October 2012 six EU countries demanded faster action to allow the suspension of visa-free travel. The capacities of the Serbian Commissioner for the Protection of Equality have been improved including provision of office space and clerical staff. During 2011, the commissioner received 335 complaints and 11 notices and initiatives (mostly relating to discrimination based on ethnicity, disability or gender). The number of complaints has tripled in comparison to 2010, which can be attributed to numerous public awareness campaigns implemented in cooperation with civil society organizations.

11 | Economic Performance

After a modest recovery from the global recession and weak GDP growth in 2011, Serbia entered into a second recession in 2012. According to the 2012 World Bank assessment, a weak external and domestic demand combined with a decline in investments, industrial production and exports have led to an economic slowdown. Unemployment rose in April 2012 to 25.5%, decreasing somewhat in December of the same year to 22.4%. After showing real GDP growth of 1.6% in 2011, Serbia’s economy contracted in 2012, showing negative growth of nearly -2%, according to the Ministry of Finance and Economy estimates. However, the World Economic Outlook 2012 projections envisage real GDP growth of 2% in 2013. The 2012 budget deficit, currently estimated to lie between 6.7% and 7% of GDP (EBRD 2012), significantly exceeds the target of 4.25% that had been agreed to as part of the International Monetary Fund (IMF) arrangement. Serbia’s full-year current account deficit in 2012 is projected to lie between 10.5% and 11.5% of GDP, which is higher than the 8.9% observed in 2011. At the same time, Serbian public debt continues to grow. At the end of 2012, the Serbian Public Debt Administration announced that public debt amounted to 61.5% of GDP. Serbia’s CPI rate of inflation is among the highest in Europe, having reached 12.2% by the end of 2012, though this should fall
somewhat by mid-2013. Increasing agricultural prices, a VAT increase, a cold winter, a summer drought that reduced agricultural output by more than 18%, and elections the May 2012 elections represent the main factors placing upward pressure on inflation. In 2012, U.S. Credit rating agencies S&P and Fitch lowered Serbia’s long-term credit rating by one degree, from BB to BB-. Thanks to strong international demand, in August and then in November, Serbia managed to sell $1 billion and $750 million respectively of its Eurobonds as the cash-strapped government sought to cover a vast hole in its budget.

12 | Sustainability

Serbia continues to administer a number of environmental projects, mainly in the field of waste disposal, recycling, solid and liquid waste treatment and renewable energy. Notwithstanding the significant financial and technical support from the EU, which invested €500 million over the past 10 years, and environmental awareness among the citizens, Serbia has made limited progress on environmental matters. Industrial development, intensive agriculture and outdated technology (mainly in electricity production, chemical plants and copper mines and smelters) have resulted in air, soil and water pollution, energy waste, and overuse of pesticides and fertilizers. In the European Union as a whole, on average nearly 90% of waste water is treated prior to discharge, and nearly 100% of municipal waste is collected, yet in Serbia, only 10% of waste water is treated and nearly 60% of municipal waste is collected. While in the European Union 40% of municipal solid waste is recycled on average, in Serbia the rate is only 4%. (The National Environmental Approximation Strategy, December 2011). Almost 69% of total electricity generation in Serbia is based on lignite, and three-quarters of lignite production is coming from the Kolubara basin, 55 kilometers from Belgrade. With an Environmental Performance Index of 46.14, Serbia is ranked 103 out of 132 countries in Yale University’s 2012 Environmental Performance Index. Despite this poor performance, progress may be on the horizon. In 2011 and 2012, Serbia furthered its environmental policy by adopting a number of strategies and laws directly related to the environment, its conservation and protection, namely the National Environmental Approximation Strategy, the National Strategy for Sustainable Use of Natural Resources and Goods, and the Law on Mining and Geological Research.

The majority of state and private of education, training, and R&D institutions are relatively strong and, in some cases, quite advanced. Some private universities are allegedly offering courses of dubious quality, however. Indeed, according to the Ministry of Education and Science’s estimates, one in ten diplomas issued by the Serbian University system are either forged or invalid. Based on 2012 data, the literacy rate in Serbia was 97.9%, while the 2011 U.N. Education Index reached 0.790. Serbia’s education system is performing below international averages in terms
of student achievements, warned the World Bank in 2012. The results of PISA
testing, conducted in Serbian high school in 2009, showed the reading, mathematics
and science scores well below the OECD average. As reported by UNICEF, in its
2012 report, Investing in Early Childhood Education in Serbia, public expenditures
for education in Serbia are below average for OECD countries (4.53% of GDP and
11% of public expenditures in Serbia versus 5.4% and 12.9% in OECD countries).
The Serbian National Alliance for Local Economic Development (NALED) warned
that only 0.9% of the budget was earmarked for higher education. The Serbian
Education Development Strategy envisages that by 2020, the budgetary allocations
for education should reach 6.5% of GDP. Some progress was registered in the area
of science and research, but public investment in research in 2012 was a mere 0.23%
of GDP, and the number of researchers has not increased. Serbia remains one of the
countries worst hit by the brain drain, ranked at 141 out of 144 on the Global
Competitiveness Report 2012 – 2013. More than 63% of Serbian students say they
want to leave the country.
Transformation Management

I. Level of Difficulty

The structural constraints on governance in Serbia have increased during the review period. The political leadership faces additional difficulties as a consequence of the global economic crisis, from which it has not yet recovered. These challenges include: high unemployment, a distorted, uncompetitive and technologically outdated economic system, obsolete infrastructure, rampant corruption and on-going ethnic tension. In addition to that, Serbia faces an aging population along with the exodus of young, educated, and more reform-oriented professionals. According to the 2011 census, more than 32,000 people leave Serbia for good every year.

Serbia has moderately strong traditions of civil society, which are deeply rooted in the opposition protests against the Milosevic regime spearheaded by the urban intelligentsia. According to the Law on Associations adopted in 2009, the Serbian government provides funding for civil society organizations dealing with social welfare, human and minority rights, and environmental protection. However, almost 75% of associations (16,500 in total) are funded from foreign sources (Civic Initiatives, April 2012). Some civil society associations argue that the authorities have their own Civil Society Organizations (CSOs), which they favor by ascribing so-called “political eligibility” to them.

Serbian society and the country’s political elite continue to be polarized along ethnic issues, such as Kosovo, and increasingly Vojvodina and its status in Serbia. Other contentious issues are the region of Sandzak, home to a Bosniak Muslim population, and three municipalities in southern Serbia, inhabited by ethnic Albanians. During 2011 and 2012 existing tensions were exacerbated by the deepening social issues of unemployment, corruption, crime, low wages, inadequate public services and worsening living standards. The irony was that the political success of once-staunch nationalist parties, like the SNS and the SPS, resulted in a tectonic ideological shift toward the pro-EU agenda, and in turn, more readiness to acknowledge Kosovo’s independence. There is, however, a persistent danger that economic hardship, and continued perception of hopelessness among the widening strata of the population, may cause a resurgence of nationalist radicalism.
II. Management Performance

14 | Steering Capability

Serbia’s new political leadership has reiterated its commitment to political stability, democracy, reforms and the market economy. As its main priority, the new cabinet listed the acceleration of European integration, and has put forth maximum effort toward getting a date to begin EU membership talks. Other strategic prerogatives of the Prime Minister Dacic’s government fall under the umbrella of conditions for EU membership. They include normalizing ties with Kosovo, fighting corruption and organized crime, further establishing the rule of law and sorting out other regional political matters. Although an obvious priority for the government, Kosovo remains the most contentious and polarizing issue both politically and societally, highly influencing the nation’s attitude towards future EU integration. One in five Serbian citizens claim Kosovo independence should be recognized, whereas over half of them (62%) would not give up Kosovo at any cost, according to a 2012 report from the Belgrade Center for Security Policy. Serbia’s new leadership has also reiterated a strong commitment to economic and political reform as an essential part of the nation’s European integration. Nevertheless, as Freedom House reported in 2011, the harmonization of Serbian laws with the EU is constantly undermined by lobbying interests and politicians’ pandering to certain demographics like public employees and pensioners.

The current parliament has continued with intensive legislative activity, adopting more than 70 laws and 40 other acts since May 2012. It should be noted, however, that most of the laws were drafted and adopted hastily with the use of an urgent procedure, which usually affects the quality of laws. Among the new and amended laws adopted in 2012 are the Law on Public Procurement, amendments to the Criminal Code (which introduces an abuse in public procurement as a new criminal offense), the Law on Budget 2013, and the Law on Public Companies that guarantees the substantial withdrawal of the state from the management of public enterprises. Parliament also changed the Central Bank Law in an effort to curb criticism from the European Union and the IMF that earlier legislation limited the bank’s independence. Demonstrating its capacity to implement fiscal adjustment measures, the new cabinet scrambled to balance the 2012 budget by attempting to significantly reduce public spending and to increase tax revenues. The Serbian leadership is apparently more reluctant to embrace more daring economic reforms. The state control over prices continues (about 22% of the goods and services in the consumer price index are administered), and price liberalization has slowed down. The new government has yet to prove its determination in further reducing the number of public employees.
According to 2011 reports, there were almost 28,000 people employed in Serbia’s public administration, not including members of the army and other security forces.

The policies of the new Serbian government under Prime Minister Ivica Dacic, just like its predecessors, have been significantly influenced by the direct input from international partners, making it impossible to gauge how much policy learning has occurred internally. Serbia’s freedom of action is often limited, managed or directed by the European Union, the United States and to a significant extent, the IMF and the World Bank. Although still politically prone to populism, and reluctant to perform some of the painful but necessary economic measures for political reasons, Serbia’s leadership continues to harmonize its economic and social policies with those of the EU. With regard to the Kosovo issue, Serbia has demonstrated more urgency and political pragmatism than before, firmly adhering to legal and political ways and means to speed up its EU integration. Nonetheless, a 2012 paper from the Center for European Studies concluded that the durability of the pro-European line in the Serbian government’s policy, and the implementation of agreements with Kosovo, is contingent on a positive response from the European Union.

15 | Resource Efficiency

The parliamentary majority of the new coalition government is solid (144 out of 250 seats) and much broader than that of its predecessor, which is bodes well for its stability. However, the difficult economic and social environment in Serbia severely limits the new government’s efficient use of available human, financial and organizational resources. One characteristic of the public administration is the excessive concentration of decision-making powers in the hands of politicians, who do not delegate to the public administration. The legal framework providing for public administration reform is largely in place, according to the European Commission, and administrative capacities are generally well developed, in particular at the central level. However, implementation at other levels is making slow progress. The merit system in Serbia’s civil service is not guaranteed, and the professionalism of the state administration is limited. Recruitment to the civil service system is still largely based on political affiliation and patronage, according to a 2012 OECD assessment. The Serbian media have reported that, among the newly appointed officials in government ministries and institutions, one can find ballet dancers, talent agents, people with recent criminal records and bankrupt businessmen whose main qualification for the job was their party membership or affiliation. The public expenditure management system, including public internal financial control, is based on a comprehensive budget system law introduced in 2010. An office for budget planning and analysis was established, and an internal auditor was appointed in April 2011. The State Audit Institution (DRI) found out that at the end of 2011, under the former government, Serbia’s public debt amounted to 51% of the GDP.
well above the 45% fiscal rule threshold envisaged by the budget system law and contrary to official records. As for non-compliance with certain provisions of the budget system, the same audit established that eight local governments took over the liabilities that exceeded appropriations approved by the budget in the amount of almost €1.65 million (DRI Report, December 2012). The central authorities have delegated competences to units of local self-government in areas such as building permits, utilities, culture, education, health, social and child welfare, protection of the environment and agricultural land. A Law on Fiscal Decentralization, aimed at providing municipalities with additional funding through allocations stemming from the income tax, was adopted in June 2011. In August 2012, the Serbian parliament passed a new Law on Public Property, which specified definitions of republic-owned, provincial and local government property.

In 2011 and the beginning of 2012, policy coherence and coordination in Serbia was weakened by the fact that the ruling coalitions were composed of multiple parties. The distribution of institutional power among coalition members usually impedes government effectiveness and efficiency, diminishes its ability to act with one voice, and cause overlaps and occasional frictions between the different ministries (like a public conflict between the Minister of Transport and Minister of Construction and urbanism in August 2012). The outcome of the 2012 parliamentary elections brought to power another coalition, this time led by the center-right Serbian Progressive Party (SNS) and the Socialist Party of Serbia (SPS). The new cabinet, formed in July 2012, is the smallest the country has seen since the 1990s. It has a total of 19 members, including four deputy prime ministers, 17 ministers and one minister without a portfolio. According to the coalition agreement, the positions of seven state secretaries were abolished and the new government has 87 deputy ministers instead of 94. Rules for the coordination of public appearances and statements of ministers relating to work and decisions of the government are now fully operational. While governmental coordination remains hierarchic–bureaucratic, political power this time appears to lie more inside the government than with the new President Tomislav Nikolic. The Prime Minister Ivica Dacic, who is also the Minister of the Interior, is apparently in a total control of state affairs with almost full responsibility for relations with the European Union and Kosovo. He coordinates his activities with president Nikolic, but with occasional differences. The new government has so far introduced a firm division of duties and responsibilities along the clear lines. Nonetheless, the government’s policy of consensus and unity may be put to the test if the current fight against corruption, led by the progressives, results in the implication of high-ranking representatives within the coalition.

Serbia has established the necessary institutional and legal framework for fighting corruption. The key elements of the framework are the 2011 Law on Financing Political Activities, which covers the financing of electoral campaigns with provisions on the transparency of funding sources; the 2012 Law on Public
Procurement; the Law on Conflict of Interest, passed in 2004, aimed at ending the established practice of awarding Serbian political leaders multiple elected and non-elected positions; and the laws of the State Audit Institution (SAI) and Anti-Corruption Agency (ACA), adopted in 2005 and 2008 respectively. The SAI reported that illegal acts in public procurement worth almost €415 million had been discovered in 122 departments in 2011. The State Audit Institution had filed 26 misdemeanor charges against 30 responsible individuals from the Ministries of Justice and Religion and 16 public enterprises. The Anti-Corruption Agency (ACA) took up its role in January 2010 to oversee the supervision of conflict of interest cases and funding of political parties. It has required public officials to declare their assets and has forced officials holding more than one public position to choose between them in an attempt to reduce conflicts of interest. In January 2013, the ACA initiated proceedings against seven members of parliament who failed to disclose information about their personal property on time, and against 40 of their colleagues for the delay in meeting these legal obligations. In addition, 39 misdemeanor charges were filed against political parties that have not submitted reports on the costs of their election campaigns. Even so, the agency’s inefficiency is best seen through the fact that none of those subject to criminal proceedings for corruption by other organs were identified by the ACA to have any conflict of interest or committed any crime of corruption (Collection of Policy Papers on Police Reform in Serbia, December, 2012). Serbia also has an Anti-Corruption Council, established in 2001, which functions as a government advisory body with a task of proposing legislative changes and other measures aimed at combating corruption. In December 2012, parliament passed amendments to the criminal code, introducing “abuse of public procurement” and “abuse of office by a responsible person” as a new criminal offenses. According to the Serbian Justice Ministry, the new National Anti-Corruption Strategy could be adopted in 2013, which would emphasize the necessity of media financing and advertising regulations and protect whistle-blowers.

16 | Consensus-Building

For now, the current Serbian leadership is unified in its commitment to the further consolidation of democracy, the acceleration of selective market and social reforms, and European integration as a strategic goal. The ruling coalition can count on the current lack of serious parliamentary opposition, with the once powerful Democratic Party still trying to gain strength after election defeat, and the nationalist Serbian Radical Party almost vaporized from the political scene. The government’s anti-corruption drive apparently cowed most local oligarchs, while the trade unions failed to challenge the government’s policy for the time being. The results of an opinion poll by the Faktor Plus agency taken in November 2012 showed that 38% of Serbian citizens believe the government is moving in the right direction, while 26% thinks it is doing a bad job. Notwithstanding the government’s strategic thinking and goals,
there is a possibility that deeper anti-reform and anti-European feelings will foment inside Serbia as a result of the economic depression and social tensions, in conjunction with perceived foreign meddling, mostly over Kosovo. A new poll, conducted in October 2012 by the Belgrade Center for Security Policy, revealed that only 47% of citizens now wish Serbia would join the EU, a 2% drop since the last survey in September. Almost 35% of respondents are explicitly opposed to Serbia’s EU membership, 10% more than in June.

Over the years, the Serbian authorities have achieved significant, though not a sufficient, progress in strengthening the legal framework for the parliamentary accountability of the army and the secret services. During the summer of 2012, the Serbian opposition sharply criticized the adoption of contentious changes in the Law on Security Services proposed by the ruling coalition. The opposition argued that the new law facilitated the appointment of Serbian Progressive Party (SNS) head Aleksandar Vucic (who is already a vice prime minister and Minister of Defense) as a Coordinator of Intelligence Services, which means that a party chief is de facto and de jure in control of secret services and also an official in executive power. This trend is confirmed by the appointment of Vucic as secretary of the National Security Council in August that same year. A few months later, an urgent investigation was ordered after the intelligence services discovered that a section of the police issued an order to wiretap phones of President Nikolic and Vice Prime Minister Vucic. Both the former and the new Serbian government have introduced and implemented tough security and legal measures against a number of violent far-right and clero-fascist groups and banned two such organizations, though with mixed results. As stated in the Freedom House 2011 report, this initiative marked the first time the Serbian government reacted to frequent calls from civic activists to deal with organizations that violate human and minority rights.

Serbia’s political leadership tried to prevent the emergence and escalation of conflicts based on ethnic, national or religious cleavages. The new government, just like its predecessors, remains adamantly opposed to Kosovo’s 2008 unilateral declaration of independence. However, having declared the continuation of EU integration and the quick start of accession negotiations with Brussels as its chief priority, Serbia has been making efforts to normalize relations with Kosovo. The first direct meeting between the representatives of Belgrade and Pristina focusing on technical issues was held on 8 – 9 March 2011, under the auspices of the EU High Representative for Foreign Affairs and Security Policy. In February 2012, Serbia and Kosovo reached an agreement permitting Kosovo’s participation in regional meetings held in the Balkans under the name “Kosovo*” (with an asterisk). The dialogue reached a real breakthrough on 19 October 2012, when the prime ministers of the two countries, Ivica Dacic and Hashim Thaci, met for the first time since Pristina unilaterally proclaimed independence. Since then, the two prime ministers have met four times. So far, 13 meetings have been held, and eight agreements have been reached. The
two sides have made agreements on cadaster records, civil registries, custom stamps, regional cooperation, mutual recognition of university diplomas, freedom of movement of persons and the appointment of liaison officers. The implementation of the Integrated Border Management (IBM) began in mid-December 2012. The agreement allows police and customs officers from Belgrade and Pristina, under the supervision of the European rule of law mission in Kosovo (EULEX), to jointly manage the administrative crossings between Kosovo and central Serbia. In addition, in January 2013, the two sides reached provisional understandings on the collection of custom duties, levies and VAT. Furthermore, in 2012, President Tomislav Nikolic called for direct high-level talks with Pristina, possibly with his own participation. Within Serbia proper, the political leadership has sought to integrate national minorities, but is facing the most pressing problems with the Presevo Valley, the ethnic Albanian majority region in southern Serbia. In the wake of the Kosovo War, this region was the scene of a short-lived conflict in 2000 – 2001 between ethnic Albanian insurgents and Serbian security forces. Although relatively calm since then, there have been sporadic attacks on Serbian police officers. Protesting their alleged disenfranchisement, ethnic Albanians occasionally take actions in defiance of the Serbian authorities. The latest of such acts was the erection of a monument to Albanian insurgents in town of Presevo. In January 2013, Serbian police removed the monument.

Serbia’s political leadership has taken a number of steps to support partnership with civil society. In January 2011, Serbia acted on the European Commission’s recommendation and opened the Office for Cooperation with Civil Society, tasked with initiating dialogue with civil society on matters of mutual interest. According to the Office for Cooperation with Civil Society, there were almost 16,500 citizens’ associations registered in Serbia as of December 2011. The overall role of civil society organizations (CSOs) still provokes the mistrust and a lack of understanding in some parts of the state administration. According to a study by the Bureau for Social Research (CSOs in Serbia: Challenges and Opportunities), the main problems that CSOs in Serbia face are a misuse of public funds for CSOs, political parties financing “via” CSOs, and ensuring that actions are sustainable.

The new Serbian leadership, overwhelmed by the Kosovo problem and the severe economic situation, has not been very active in addressing issues of responsibility and guilt for the 1990s wars. In fact, the coalition politicians have subscribed to the nationalist narrative of denying Serbian responsibility for the armed conflicts of the 1990s, which has already led to the deterioration of relations with neighboring countries (Warsaw Center for Eastern Studies, December 2012). Following the 2011 capture of the last two remaining war crimes fugitives, Ratko Mladic and Goran Hadzic, a new trial against a previously identified group of 10 individuals suspected of aiding Mladic to evade justice was restarted in 2012. Bosnia and Herzegovina (BiH) and Serbia agreed to the signing of a protocol on war crimes cooperation
between the BiH State Prosecutor’s Office and its Serbian counterpart. The protocol will pave the way for the two countries to eliminate parallel investigations and facilitate the mutual transfer of evidence. Domestic processing of war crimes continued with a number of new indictments, first instance judgments and final convictions. In November 2012, Serbia harshly criticized the International Criminal Tribunal for the former Yugoslavia (ICTY) after the U.N. court passed the verdicts under which Croat and Kosovo Albanian commanders were acquitted of war crimes committed against Serb civilians. In response, Serbia reduces its ties with the ICTY to the “lowest technical level.”

17 | International Cooperation

Serbia continues to be a recipient of significant financial and technical aid, though noticeably less than in 2009 and 2010 due to tighter donor budgets as a result of the ongoing economic crisis. The European Union was the biggest donor, having invested more than €2.4 billion in the country since 2000. Financial assistance, provided through the Instrument for Pre-Accession Assistance (IPA), is designed to support the reforms undertaken as part of the European integration process and is envisaged in the government’s Document for Planning International Development Assistance for the period 2011–2013, with a focus on the rule of law, institution-building, sustainable economic and social development, and support to civil society. U.S. aid to Serbia also declined sharply in recent years; for 2013, the U.S. government pledged $19.9 million to Serbia to aid in political and economic reforms. Hoping to offset the lack of Western funds, Serbia is looking east for aid and investment, with funds now coming from Russia, China and recently, some Middle Eastern countries. Although the European Union is the largest donor in Serbia, the survey carried out by the Serbian European Integration Office showed that, according to the public opinion, the EU is only in the third place after Russia and Japan.

Serbia strengthened and furthered its international credibility and reputation, successfully overcoming a number of longstanding obstacles on its path toward EU integration and membership, only to face new challenges. In 2011, Serbia’s accession prospects improved significantly after the capture of the last two Serbia’s war crimes fugitives, Ratko Mladic and Goran Hadzic. In March 2012, the European Union named Serbia as an official candidate after deciding that Belgrade had made sufficient progress in reaching and implementing agreements with Kosovo on a series of technical issues. However, no date has yet been set for beginning the accession talks. In its 2012 country assessment, the EBRD commented that the EU decision to grant Serbia candidate status is in “recognition of Serbia’s cumulative reform efforts.” Yet, financially, challenges loom. In February 2012, the IMF froze a $1.2 billion precautionary loan to Serbia because the 2012 budget deviated from the agreed fiscal program and Serbia’s spiraling public debt. However, parliament has
approved an austerity budget for 2013 that might pave the way for renewed talks with the IMF and further shore up the country’s fiscal credibility.

During the mandate of the Democratic Party’s government, Serbia had relatively good relations with Croatia, Bosnia and Herzegovina, and Montenegro. However, in the second half of 2012, the controversial nationalist past, and, as the EU puts it, unhelpful statements for reconciliation in the region made by the new Serbian President Tomislav Nikolic, have raised the political temperature between Serbia’s neighbors, particularly Croatia. President Nikolic caused controversy with his comments about 1990s wars, particularly when he denied the massacre in Srebrenica was genocide. Zagreb scolded the Serbian president for his statements, and President Ivo Josipovic of Croatia decided not to meet his Serbian counterpart. Additionally, the political leaders of Croatia, and Bosnia and Herzegovina, as well Slovenia, refused to attend the Nikolic’s official inauguration in Belgrade in June. Apparently keen to stop the further deterioration in relations, President Nikolic said in December that Serbia is committed to achieving the best possible relations with the region. Serbian Prime Minister Ivica Dacic, aware that his country needs good contacts with Croatia because of EU accession, said that Belgrade – Zagreb relations should be unfrozen and reset. As a sign of thawing of the relationship, he welcomed his Croatian counterpart Zoran Milanovic in Belgrade in January 2013. Relations with Montenegro improved significantly, and Podgorica welcomed the new Serbian president’s statement that Montenegrin independence is a done deal. However, a dispute between the Orthodox churches in Montenegro and in the former Yugoslav Republic of Macedonia remains unsolved. Relations with Turkey remained good, although Serbia expressed its concerns over Turkey’s alleged intention to promote Kosovo’s independence in the world. In 2011, Serbia presided over a number of regional initiatives, including the Southeast European Cooperation Process (SECP) and the Central European Initiative (CEI) and actively participates in CEFTA and the Regional Cooperation Council. Serbia is a member of NATO’s Partnership for Peace Program, but President Nikolic, who once admitted that he only loves Russia second to Serbia, promised that Serbia will never become a member of NATO. A survey, conducted in March 2012, showed that around 70% of Serbian citizens oppose NATO membership while only five percent had confidence in the military alliance.
Strategic Outlook

Serbia has faced a crossroads in its recent development, seeking further progress in its EU accession and economic prosperity as a solution to internal social and ethnic tensions. To reach its goal as a candidate for EU membership, Serbia has to follow a demanding path of painful political and economic reforms and the normalization of relations with Kosovo. Ironically, this path is being forged by the new ruling coalition, which is led by the once vocal nationalist Serbian Progressive Party and the Serbian Socialist Party. Facing a collapsing economy and the EU’s demands to normalize its day-to-day relations with Kosovo, the new leaders in Belgrade have been eager to get a starting date for EU accession talks as an additional impetus for ongoing reforms, making the process of EU integration irreversible. The new prime minister, Ivica Dacic, intensified the dialogue with Pristina; in January 2013, the Serbian Parliament adopted a set of guidelines for normalization of relations with Kosovo, asking for substantial autonomy for Kosovo Serbs and, indirectly, relinquishing any hopes of regaining Kosovo again. The European Union must be aware that cooperation so far shown by Serbia’s government regarding Kosovo went further than many Serbs expected, wanted, and liked. Nevertheless, Serbia stands to move ahead, as the country got a starting date for the accession talks in June 2013 as an acknowledgement for its existing efforts. However, the European Union may decide to up the ante and push for more concessions, given that more contentious issues still have to be tackled in northern Kosovo. On this issue, the European Union should tread warily. After all, support for EU membership among Serbs, while still high, is in decline, and Brussels would potentially threaten European wishes to cement the stability of the region. Pro-European forces in parliament hold more than 90% of seats, but the poor, impoverished, and disillusioned population can easily forget that the European Union is the largest donor to Serbia and its main trade partner, and succumb even more to an already present impression that Serbia is “constantly getting nothing for giving everything”. Yet, as one Serbian official put it, the EU integration amounts to state-building, helping Serbia to create modern democratic institutions based on the rule of law and enhancing its ability to manage any political pressure and threat within a democratic institutional setting. The potential source for the decline of EU support among citizens can be found in Serbia’s shrinking economy, a worsening fiscal crisis and a limited hope for growth. After all, the country is facing a “smorgasbord” of economic and financial malaise: high inflation, high unemployment, a high current account, and budget deficits. For years, Serbia’s economy has been plagued with fundamental and structural problems along with the lack of serious political will to implement structural reforms in the areas the labor market, the pension system, public companies and the business environment. Serbia is, after all, a country in which almost two-thirds of people receiving pensions and salaries, receive them from the state budget. The new government promised further austerity measures in the 2013 budget, pledging to provide for export growth and to slash the budget deficit almost in half. Nevertheless, the international financial institutions were apparently not convinced that Serbia’s estimates of its economic growth, revenue increase and costs slashing, envisaged in the 2013 budget, were realistic. The IMF, therefore, may not accept slow, steady medium term fiscal consolidation, which
would give Serbia breathing time to jump-start its economy and strengthen the viable and efficient social welfare net. Equally troublesome for Serbia’s future prosperity is its declining and aging population that can cast a pall over economic growth. Serbia, therefore, has to abandon the old practice of spending borrowed money on covering the budget deficit and public consumption, and redirect funds to attracting new investment and creating jobs. However, the enormity of vested financial interests in retaining the status quo in Serbia, and government’s persistent failure to implement the laws adopted under the EU harmonization rules, may seriously hinder the quality, speed, and effectiveness of reform. Serbia’s future transformation depends on its ability to update its inefficient and obsolete system, and abandon cheap populism and opportunistic politicking. Unpopular and painful choices and decisions – not only related to Kosovo – await Serbia in the near future.