

6. Fiscal Flows and Policy

In the course of the first quarter of 2010, public revenues still posted a downward trend in real terms. Seasonally adjusted consolidated revenues of the government sector fell by 2.7% in Q1 2010 against the previous quarter. Compared with Q1 2009, the real public revenues fell by 4%. Such developments resulted from a significant decline in revenues from taxes on consumption. At the same time, the fall in real spending slowed down, falling by 5.4% compared with the same period last year, while the decline in two previous quarters stood at 3.2% and 9.2% respectively. Compared with the previous quarter, seasonally adjusted public spending rose by 2.3% in real terms. The consolidated deficit of the government sector in Q1 amounted to 24 billion dinars or 3.3% of quarterly GDP in Q1. However, considering that under the influence of the seasonal component the deficit in the first quarter of the year usually tends to be significantly lower than in other quarters, the Q1 results indicate that the consolidated deficit for 2010 will be above plan. The negative trend in public revenues continued in April when the budget revenues of the Republic of Serbia fell by 5% against the same month of 2009, mainly due to the real decline in revenues from excise duties and non-tax revenues. The budget spending of the Republic of Serbia in April fell by 10% in real terms against the same month of the previous year, due to a significant decline in spending on workers' salaries and spending on purchases of goods and services. As a result of those developments, deficit of the budget of the Republic of Serbia in April stood at 12.4 billion dinars (while the average monthly deficit of the budget in Q1 2010 stood at 7.3 billion dinars). The public debt of Serbia at the end of Q1 2010 stood at 10.27 billion euros (around 31.1% of GDP), which is some 420 million euros (around 1.2% of GDP from 2009) higher compared with Q4 of the last year.

General Trends and Macroeconomic Implications

In the course of Q1 the decline in seasonally adjusted public revenues continues against the previous quarter

In the course of Q1 2010, seasonally adjusted revenues of the consolidated government sector continued to decline compared with the previous quarter, with the decline larger in Q1 at 2.7%. The consolidated public revenues in Q1 2010 fell by 4% in real terms against the same period last year. Q1 2009 was one of the worst quarter of that year (with real decline of 12.6% against Q1 2008), which makes the picture of public revenues developments at the start of 2010 even worse.

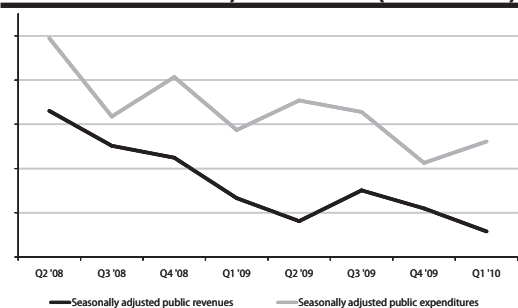
Revenues from taxing consumption fall, while revenues from taxing production factors rise

Looking at particular taxes, Q1 marked a turnaround compared with the previous quarter, with all revenues from taxing consumption falling, while revenues from taxing production factors rising in comparison with the previous quarter. Such results indicate negative trends in consumption and domestic demand, because revenues from taxing consumption are very flexible to consumption. Real seasonally adjusted revenues from VAT fell by 4.6% in Q1 compared with the previous quarter, while revenues from excise duties fell by 12.3% and revenues from customs

duties by 5% against Q4 2009. It is our estimate that such steep decline in revenues from excise duties is partially owed to weaker consumption of products subject to excise duties, due to their significantly higher (market) prices.

Seasonally adjusted public spending in Q1 rose in real terms (for the first time since Q2 2009) by 2.3% against the previous quarter. The public spending growth against Q4 2009 was largely the result of higher spending on purchases of goods and services (4.7%), spending on subsidies (12.2%) and capital spendings (12.6%).

Graph T6-1. Serbia: Seasonally Adjusted Real (Quarterly) Revenues and Spending of the Government Sector, in mln RSD (2005=100)



Source: Calculations by the author.

In Q1, seasonally adjusted public spending grew against the previous quarter

Consolidated deficit in Q1 stood at around 24 billion dinars

Spending on employees as well as spending on pensions posed a real decline by 2.2% against the previous quarter, which is mainly owed to a nominal freeze of public sector wages and pensions. Compared with Q1 of the previous year, the consolidated spending of the government sector in Q1 2010 fell by only 1.4% in real terms, while the decline in 2009 ranged between 3.2% and 9.2%, illustrating a slowdown in the real decline of public spending.

As a result of the listed developments, the consolidated deficit stood at 24 billion dinars in Q1, or roughly around 3.3% of (quarterly) GDP in Q1. Considering that the first quarter deficit is usually lower than in other quarters due to seasonal components, the results achieved in Q1 indicate that the consolidated deficit in 2010 will be above the planned 4% of GDP. A significant decline in revenues from taxes on consumption had a crucial impact on the deficit generation, while the impact of the spending growth was weaker.

Table T6-2. Serbia: Consolidated General Government Fiscal Operations¹⁾, 2006-2010

	2006	2007	2008				2009				2010		
	Q1-Q4	Q1-Q4	Q1	Q2	Q3	Q4	Q1-Q4	Q1	Q2	Q3	Q4	Q1-Q4	Q1
	in billions of dinars												
I TOTAL REVENUE	865.8	1,002.0	269.4	281.4	283.3	311.8	1,145.9	258.8	267.1	297.0	323.6	1,147	266.6
II TOTAL EXPENDITURE	-888.4	-1,031.5	-254.0	-295.8	-286.6	-359.3	-1,195.7	-270.3	-306.3	-315.1	-356.2	-1,247.9	-286.0
III "OLD" DEBT REPAYMENT, NET LENDING AND RECAPITALIZATIONS	-10.9	-15.3	-7.3	-5.2	-2.7	-3.9	-19.1	-0.9	-6.3	-5.8	-7.4	-20.4	-4.5
o/w Net lending ²⁾	-10.9	-15.3	-7.3	-5.2	-2.7	-3.9	-19.1	-0.9	-6.3	-5.8	-7.4	-20.4	-4.5
IV TOTAL EXPENDITURE, GFS (II+III)	-899.3	-1,046.8	-261.4	-301.0	-289.3	-363.2	-1,214.8	-271.2	-312.6	-320.9	-363.6	-1,268.3	-290.6
V CONSOLIDATED BALANCE (I+IV), GFS definition ³⁾	-33.5	-58.2	8.0	-19.6	-5.9	-51.3	-68.9	-12.4	-45.5	-23.9	-40.0	-121.8	-23.9
VI FINANCING (FREN'S definition)	119.6	24.2	7.9	-12.2	0.2	17.5	13.5	28.9	40.2	11.4	86.8	167.3	8.1
VII ACCOUNT BALANCE CHANGE (V+VI)	86.2	-34.0	16.0	-31.8	-5.7	-33.8	-55.4	16.4	-5.3	-12.4	46.8	45.4	-15.9
VIII TOTAL REVENUE/GDP (%)	42.4	41.9	43.5	40.7	40.3	42.7	41.7	38.5	36.0	39.0	41.1	38.7	36.6
IX TOTAL EXPENDITURE/GDP (%)	(44.0)	(43.7)	(42.2)	(43.5)	(41.1)	(49.7)	(44.3)	(40.4)	(42.1)	(42.2)	(46.2)	(42.8)	(39.9)
X CONSOLIDATED DEFICIT/GDP (%)	(1.6)	(1.9)	(1.3)	(2.8)	(0.8)	(7.0)	(2.5)	(1.9)	(6.1)	(3.1)	(5.1)	(4.1)	(3.3)

Source: Table P-10 in Analytical Appendix.

1) Includes all levels of government (central, provincial and municipal) and their budget beneficiaries and social security organizations (Serbian Pension and Disability Insurance Funds, Health Insurance Funds, National Employment Service, but not public enterprises and the NBS).

2) The item corresponds to the item "Net acquisition of financial assets for policy purposes" in the PFB (in accordance to GFS 2001), i.e. to the item "net lending" or "lending minus repayment" in the IMF presentation (i.e. GFS 1986). It comprises loans to students, financing of the National Corporation for Housing Loan Insurance and the like.

3) See Table P-10 in Analytical appendix and/or Box 2.

Serbia's budget revenues and spending significantly fell in April

Figures on revenues and spending of the Serbian budget for April 2010 show that budget revenues of the Republic fell by around 5% in real terms against the same month of the previous year. That decline is largely owed to a real decline in revenues from excise duties, which (despite multiple increases in excise duties over the past year) fell by 5% in April 2010 against the same month of the previous year. Also, real revenues from personal income tax fell (by 4%). VAT revenues in April 2010 posted a real growth of 11% against the same month of the last year. The decline in seasonally adjusted real revenues from VAT by 3% in April 2010 against March, indicate a continuation of a negative trend. The spending of the budget of the Republic in April fell by 10% in real terms against the same month of 2009, mainly due to a significant real decline in spending on goods and services (33%) and a significant real decline in spending on employees (9%). As a result of described developments, the budget deficit of the Republic in April 2010 stood at 12.4 billion dinars (while the average monthly budget deficit in Q1 2010 stood at 7.3 billion dinars).

Excise duties on fuel are relatively high, but the capacity for their cut is limited

Data on revenues and spending of the state in the first four months of 2010 indicate that budget revenues underperformed, mainly due to declining revenues from excise duties and VAT. A multiple increase in excise duties (first of all on crude oil derivatives) over the past year, along with an increase in global crude oil prices – led to a significant increase in prices of crude oil derivatives, which as a result had a falling consumption of those products and to some kind of tax arbitrage. That is why it has become an issue whether it is possible to lower excise duties on crude oil derivatives in order to steer retail prices lower. But as excise duties constitute a significant component of budget revenues, it is assessed that a cut in those excise duties could take place only if a significant increase in other excise duties or taxes was to take place to offset the decline. Despite opinions that lower excise duties would lead to higher consumption of crude oil derivatives and to higher revenues from excise duties, there is no such exact evidence.

No conditions met to unfreeze public sector wages and pensions in 2010

Speaking of public spending, a possibility to unfreeze public sector wages (and even pensions) already in the course of 2010 is mentioned all the more frequently, even though the agreement with the IMF says those two forms of spending need to be frozen throughout the year. In a situation when budget revenues are below expectations, the government manages the deficit most intensively through a cut in real spending on wages to public sector workers and pensions (through nominal freeze). It is therefore believed that unfreezing of nominal wages and pensions (even if the announcement of such moves only creates expectations) would have a very negative impact on the stability of public finances, i.e. on achieving the deficit target. Namely, based on movements in Q1 2010, when revenues were below plan, it is estimated that the fiscal deficit, even without an end to the nominal freeze in public sector wages and pensions, will reach 4.8% of GDP, which is 0.8 percentage points above the planned deficit. Having this in mind, the agreement reached during the fourth revision of the stand-by arrangement with the IMF in May 2010 is seen as appropriate, with the nominal freeze in public sector wages and pensions staying in place throughout 2010.

Table T6-3. Projected Fiscal Deficits in Central and Eastern European Countries in 2010

	Projected fiscal deficit (% of GDP)
Latvia	12.9
Lithuania	8.6
Poland	7.5
Montenegro	7.2
Romania	6.5
Slovenia	6.1
Slovak Republic	5.8
Albania	5.6
Czech Republic	5.1
Bosnia and Herzegovina	5
Serbia	4 (4.8*)
Hungary	3.8
Croatia	2.7
Macedonia	2.5
Estonia	2.4
Bulgaria	1.8
Average	5.5

* Official estimated fiscal deficit in Serbia in 2010 amounts to 4% of GDP. However, based on the trends in Q1, it is expected that the total fiscal deficit will be 4.8% of GDP. Therefore, it is may also be expected that projected deficits in other countries are somewhat underestimated.

Source: IMF Regional Economic Outlook: Europe, May 2010.

The impact of recession on public finances in Central and Eastern European countries remains very pronounced in 2010, so that the average planned fiscal gap in 16 observed countries is around 5.5% of GDP, which is close to the average deficit achieved in 2009. Compared with other countries of Central and Eastern Europe, Serbia ranks 11 (of 16 countries) by the size of its planned fiscal deficit in 2010 (around 4.8% of GDP). That means that it is expected that Serbia is likely to achieve a somewhat better fiscal result in 2010 compared with other countries of the region, just like in 2009. Due to continued negative trends in respect to public revenues, some countries of Central and Eastern Europe (Romania and the Baltic countries) have, as part of fiscal stabilisation, been forced to significantly cut nominal wages to public sector employees, and also to cut down the number of employees.

Analysis of Particular Taxes and Public Spending Items

In Q1 revenues from taxation of consumption fell again

Taxation of consumption resulted in shrinking revenues in Q1 2010 again. Seasonally adjusted real revenues from VAT in Q1 fell by 4.6% against Q4 2009, which indicates the decline in demand (first of all domestic demand). The same pace of decline was seen in real seasonally adjusted revenues from customs duties (5%). Real seasonally adjusted revenues from excise duties posted a 12.3% fall against Q4 2009. It is estimated that this decline resulted from an overall shrinking of demand, additional fall in consumption of products subject to excise duties (crude oil derivatives, first of all) due to a significant price increase and widening tax evasion and arbitrage.

Table T6-4. Serbia: Seasonally Adjusted Quarterly Indices of Real Public Revenues (previous quarter = 100)

	Public revenues	Consumption taxes			Production factors taxes		
		VAT	Excise duties	Customs duties	Personal income tax	Social security contributions	Corporate income tax
Q3 2008	96.4	94.4	102.1	93.7	99.0	100.7	95.6
Q4 2008	98.7	96.3	97.2	89.8	103.7	100.2	91.9
Q1 2009	95.6	96.6	107.0	86.5	90.5	96.2	83.9
Q2 2009	97.4	92.0	99.3	89.4	96.0	98.8	89.5
Q3 2009	103.6	109.7	113.9	93.1	101.2	97.8	105.3
Q4 2009	98.0	100.6	103.5	95.2	95.2	95.0	91.8
Q1 2010	97.3	95.4	87.7	95.0	101.5	102.7	101.2

Source: Calculations by the author.

...while revenues from taxes on production factors slightly grew

Unlike developments in the previous quarter, revenues from taxes on production factors posted a mild growth in Q1. Real seasonally adjusted revenues from personal income tax and social contributions rose by 1.5% and 2.7% respectively against Q4, which can be the result of tax administration efforts to improve collection.

Real seasonally adjusted revenues from corporate income tax rose by 1.2% in Q1 against Q4, which can be mainly attributed to the fact that payments of the corporate income tax for the previous year are due in March of the ongoing calendar year.

Table T6-5. Serbia: Seasonally Adjusted Quarterly Indices of Real Public Expenditures (previous quarter = 100)

	Public expenditures	Staff expenditures	Purchase of goods and services	Subsidies	Pensions	Capital expenditures
Q3 2008	92.5	97.5	96.2	58.1	102.4	92.1
Q4 2008	104.1	99.9	100.7	141.1	105.1	97.4
Q1 2009	94.7	95.0	95.0	73.3	102.0	76.0
Q2 2009	103.1	100.5	103.4	96.9	98.2	110.5
Q3 2009	98.8	99.4	94.4	116.6	100.8	95.9
Q4 2009	94.7	98.1	99.9	76.4	98.9	98.2
Q1 2010	102.3	97.8	104.7	112.2	97.8	112.6

Source: Calculations by the author.

Seasonally adjusted public spending on purchases of goods and services and subsidies rise in Q1

Real seasonally adjusted spending on employees in Q1 was 2.2% below the previous quarter and spending on pensions fell by the same percentage. Such developments resulted first of all from a nominal freeze of public sector wages and pensions. This measure represents, in fact, the key instrument to cut public spending and maintain the fiscal deficit under control, because spending on employees and spending on pensions account for almost 60% of total public spending.

Real seasonally adjusted spending on purchases of goods and services rose in Q1 by 4.7%, spending on subsidies by 12.2% and capital spendings by 12.6% against the previous quarter. Such a result was partly caused by the fact that all three mentioned categories of spending in the previous quarter posted some decline, making the comparison base lower.

Table T6-6. Serbia: Consolidated General Government Fiscal Operations¹⁾, 2006-2010

	in billions of dinars										real growth, in %					
	2007	2008	2009				2010		2007	2008	2009				2010	
	Q1-Q4	Q1-Q4	Q1	Q2	Q3	Q4	Q1-Q4	Q1	Q1-Q4	Q1-Q4	Q1	Q2	Q3	Q4	Q1-Q4	Q1
I PUBLIC REVENUES	1,002.0	1,145.9	258.8	267.1	297.0	323.6	1,146.5	266.6	8.6	3.3	-12.6	-13.7	-4.2	-5.0	-8.7	-4.0
o/w Public revenues excluding VAT liabilities to enterprises and others with SZP ²⁾	996.5	1,145.9	258.8	267.1	297.0	323.6	1,146.5	266.6	9.3	3.8	-12.6	-13.7	-4.2	-5.0	-8.7	-4.0
1. Current revenues	995.4	1,143.1	258.3	266.2	296.2	318.3	1,139.2	265.7	7.9	3.5	-12.6	-13.7	-4.2	-6.3	-9.1	-4.2
Tax revenue	870.0	1,000.4	229.8	237.1	256.9	276.5	1,000.3	236.1	8.0	3.7	-10.8	-12.9	-5.4	-6.3	-8.8	-4.3
Personal income taxes	115.8	136.5	30.9	33.5	33.6	35.5	133.5	31.1	-8.4	6.3	-5.3	-10.8	-8.7	-16.5	-10.8	-6.0
Corporate income taxes	29.7	39.0	12.8	5.6	6.1	6.7	31.2	11.7	52.1	18.5	-22.2	-37.2	-25.4	-27.3	-27.0	-15.2
VAT and retail sales tax	265.5	301.7	69.4	67.9	76.1	83.5	296.9	71.9	10.6	2.5	-13.6	-19.9	-5.8	-1.5	-10.2	-3.5
o/w Net VAT and retail sales tax ³⁾	260.3	301.7	69.4	67.9	76.1	83.5	296.9	71.9	8.8	4.5	-13.6	-19.9	-5.8	-1.5	-10.2	-3.5
Excises	98.6	110.1	24.4	30.7	38.4	41.3	134.8	27.2	6.5	0.7	-6.2	4.9	18.8	24.6	11.6	3.9
Custom duties	57.4	64.8	11.5	11.7	11.7	13.2	48.0	9.5	18.6	1.8	-29.4	-37.4	-34.5	-27.8	-32.4	-23.1
Social contributions	270.3	312.7	73.4	79.7	80.9	84.8	318.8	9.8	9.6	4.3	-4.1	-4.5	-6.1	-12.2	-7.0	23.3
o/w contributors excluding others with SZP ⁴⁾	269.8	312.7	73.4	79.7	80.9	84.8	318.8	74.9	14.1	4.5	-4.1	-4.5	-6.1	-12.2	-7.0	-4.9
Other taxes	32.8	35.6	7.4	8.1	10.3	11.4	37.1	29.6	1.7	-2.3	-20.5	-16.8	6.1	10.0	-4.9	-62.5
Non-tax revenue	125.4	142.7	28.5	29.1	39.3	41.9	138.8	0.7	7.4	2.6	-24.6	-19.5	4.7	-6.7	-11.3	-97.8
2. Capital revenues	5.3	1.4	0.3	0.5	0.0	0.0	0.0	0.0	1,703.2	-76.8	-25.4	-3.2	-89.8	-83.4	-41.4	-100.0
II TOTAL EXPENDITURE	-1,031.5	-1,195.7	-270.3	-306.3	-315.1	-356.2	-1,248	-286	8.9	4.5	-3.2	-5.9	0.5	-9.2	-4.8	-1.4
1. Current expenditures	-919.5	-1,089.6	-259.0	-286.4	-292.0	-317.9	-1,155	-272	6.9	6.9	-2.6	-4.6	2.5	-7.4	-3.3	-2.0
Wages and salaries	-238.3	-293.2	-70.3	-75.6	-73.8	-82.2	-302.0	-72.2	9.4	10.9	-3.8	-7.1	-5.3	-7.5	-6.0	-4.3
Expenditure on goods and services	-168.1	-181.2	-35.9	-47.2	-46.2	-58.2	-187.4	-39.7	16.1	-2.8	-3.8	-2.9	-6.5	-8.1	-5.7	3.1
Interest payment	-17.9	-17.2	-5.8	-4.5	-7.1	-5.0	-22.4	-8.0	44.4	-13.3	-13.4	55.9	28.8	33.4	19.0	29.2
Subsidies	-63.7	-77.8	-11.0	-14.7	-18.7	-18.6	-63.1	-11.2	7.6	10.1	-24.7	-39.8	22.9	-39.8	-26.0	-5.3
Social transfers	-409.3	-496.8	-132.8	-139.1	-139.3	-145.2	-556.4	-137.1	6.5	9.5	2.4	3.3	5.7	-2.2	2.2	-3.8
o/w pensions ⁵⁾	-239.9	-331.0	-94.5	-96.6	-97.1	-99.2	-387.3	-97.1	7.1	14.9	15.0	7.7	6.7	-0.3	6.7	-4.3
Other current expenditures	-22.1	-23.5	-3.2	-5.2	-6.9	-8.7	-24.0	-4.2	1.1	-4.3	-30.9	-35.5	35.6	9.6	-6.7	21.4
2. Capital expenditures ⁶⁾	-112.1	-106.0	-11.3	-20.0	-23.0	-38.2	-92.5	-13.6	29.3	-14.7	-14.3	-21.3	-19.2	-22.0	-20.4	12.2
III "OLD" DEBT REPAYMENT, GOVERNMENT NET LENDING AND RECAPITALIZATIONS	-15.3	-19.1	-0.9	-6.3	-5.8	-7.4	-20	-5	-53.9	12.3	-88.6	10.3	97.1	74.7	-2.4	356.4
IV TOTAL EXPENDITURE, GFS (II+III)	-1,046.8	-1,214.8	-271.2	-312.6	-320.9	-363.6	-1,268	-291	9.2	4.6	-5.6	-5.6	1.4	-8.3	-4.8	-0.2

Source: Table P-10 in Analytical Appendix.

1) See footnote 1) in Table T6-2.

2) Retail sales tax/VAT minus new tax credits to enterprises.

3) Social contributions reduced by refunds between Pension Fund, Serbian Development Fund and enterprises that are debtors of the Pension Fund.

4) QM's estimate, for details see Table P-10 in Analytical appendix.

5) Refers to the current expenditures on pensions.

6) Capital expenditures exclude projects financed from abroad (apart in 2004, see footnote 16 in Table P-10).

7) See footnote 2) in Table T6-2.

Note: Real growth is obtained comparing 2003 constant prices quarterly data.

Public Debt Analysis

Serbia's public debt rose by around 420 million euros (or 1.3% of 2009 GDP) in Q1

At the end of Q1 2010, Serbia's total public debt stood at 10.27 billion euros (31.1% of GDP¹⁾ and that was roughly 420 million euros higher than at the end of 2009.

There are, however, indications that the mentioned amount of the public debt (10.27 billion) does not include all the categories of government liabilities (such as debts by local governments, arrears in payments for purchases of goods and services, etc.), so that it is estimated that the real amount of the public debt is higher by several percentage points of GDP.

Even though the total public debt rose in absolute terms in Q1, according to official figures by the Ministry of Finance, the share of public debt in GDP fell in Q1 by 0.2 percentage points. It is estimated that in this case, the comparison base was an estimated GDP value for 2010. However, if this public debt growth figure (of 420 million euros) is compared with 2009 GDP, it can be concluded that public debt rose by 1.3 % of GDP in Q1.

The public debt rose mainly due to additional borrowing abroad (credits from the International Bank for Reconstruction and Development designed to help the development of the private and financial sectors and public finance management, as well as borrowing from other international financial institutions), and to a lesser extent due to issuing sovereign guarantees for public sector borrowing.

Box 1. The Use of Funds Raised Through Borrowing

Beside the volume of new borrowing and the relative indicator of the country's indebtedness, the public debt sustainability and the public finance sustainability depend on how the funds, raised through borrowing, are being used. When the funds raised through a public debt issue are used for public investment, net assets of the state will not change and the impact of transferring the debt burden to future generations is smaller, while in case of financing current consumption with new borrowing – the impact is the opposite. Therefore, starting from this QM issue, the analysis of Serbia's public debt will include an indicator of spending of the funds, raised through borrowing for the needs of public spending and public investments.

Since capital spending in Q1 stood at 140 million euros (13.6 billion dinars) and new borrowing in the same period reached 420 million euros, it can be concluded that most part of the new debt, around two thirds, was being used to finance current spending, while only one third of funds raised through additional borrowing in Q1 was used to finance public investments. After a period of continued public debt decline since 2000, it resumed growth at the end of 2008, when the first significant effects of the crisis on Serbia's public finances were felt. Compared with the entire crisis period from the start of Q1 2009 till the end of Q1 2010, approximately two thirds of funds raised via new borrowing were used to finance public consumption, and only around one third for public investments. Such a structure of spending of the funds raised through additional borrowing is very unfavourable, because it represents the spending of the current generations at expense of future generations, which deteriorates the country's net assets.

Of 10.27 billion euros in total public debt, 8.77 billion euros refers to direct government liabilities, while 1.5 billion euros refer to its indirect liabilities. Of the government's direct liabilities, 4.1 billion euros represent domestic debt and 4.67 billion euros represent external debt. Even though net liabilities based on Treasury Bill issues rose by around 25 billion euros against the end of 2009 (at the end of Q1 the outstanding stock stood at 120 billion dinars), the almost unchanged value of the domestic public debt shows that additional borrowing in the local market was spent on servicing other liabilities to domestic creditors, which partially offsets a crowding-out effect.

Table 6-7. Serbia: Public Debt, 2000-2010

	in billions of EUR									
	31.12.2000.	31.12.2005.	31.12.2006.	31.12.2007.	31.12.2008.	31.03.2009.	31.07.2009.	30.9.2009.	31.12.2009.	31.03.2010.
I. Total direct debt	14.2	9.6	8.6	8.0	7.9	8.0	8.5	8.5	8.5	8.8
Domestic debt	4.1	4.3	3.8	3.4	3.2	3.2	3.7	3.8	4.1	4.10
Foreign debt	10.1	5.4	4.7	4.6	4.7	4.8	4.8	4.7	4.4	4.67
II. Indirect debt	-	0.66	0.80	0.85	0.93	0.96	1.2	1.4	1.4	1.5
III. Total debt (I+II)	14.2	10.3	9.4	8.9	8.78	8.93	9.70	9.87	9.85	10.27
Public debt / GDP	169.3%	50.2%	36.2%	29.4%	25.6%	28.9%	31.4%¹	32.0%	31.30%	31.10%

Source: Ministry of Finance of the Republic of Serbia.

Even though the level of the public debt is moderate for the time being, it is believed that its sustainability will be exposed to numerous pressures. Dissatisfactory results in budget revenue collection and a consequently relatively high fiscal deficit indicate a need for further borrowing in the coming period. Also, further significant borrowing is expected from international financial institutions for infrastructure projects, as well as borrowing by public enterprises (e.g. Serbian Railways - Železnice Srbije) for the purchase of new capital equipment. This should be increased for growth in indirect state liabilities resulting from de-nationalisation. The dinar depreciation against the euro also has a negative impact on public debt sustainability. Besides, borrowing in international financial markets at an interest rate linked to EURIBOR (or some other benchmark rate) currently results in a moderate value of interest rates due to record low of EURIBOR. But with global economic recovery, benchmark rates are expected to rise, pushing spending on interest rate payments significantly higher. To that respect, caution and restrictiveness are recommended in public spending policy in the coming period (wage and pension policies first of all) as well as in selecting priority among infrastructure projects to be financed by new debt.