4. Balance of Payments and Foreign Trade

The current account deficit of the balance of payments for Q1 2012 has been increasing and moving away from its equilibrium level. The increase of current deficit, followed by a decline in capital and a significant spending of foreign currency reserves since the beginning of 2012 indicates that there might be a danger of a possible balance of payments crisis, if these trends were to continue. During Q1 2012, the current deficit was 1,159 million euros (16.5% of GDP), which is the highest quarterly amount of a current deficit since Q4 2008. This increase is the result of the rise in foreign trade deficit and a lower influx of current transfers. Domestic demand is rising (due to the high fiscal deficit), while the foreign demand is falling, which leads to lower domestic exports, while the imports have increased compared to the previous year. The trade deficit amounted to 1,542 million euros, i.e. 21.9% of GDP, and it is 4-5 percentage points of GDP above the average values of 2009, 2010 and 2011. Capital inflow in the first three months of the current year was extremely low, and the main source of covering the current deficit were the forex reserves of NBS, which were diminished in Q1 by 916 million euros. Unfavourable developments in the EU and neighbouring countries, together with a lack of important measures of domestic economic policies, can lead to further deepening of balance of payments imbalances and to the more pronounced problem of financing the growing current account deficit during 2012. On the other hand, the current depreciation of the dinar could affect favourably the current account in the future, given that its effect occurs with a time lag. Still, a strong fiscal consolidation and continued cooperation with the IMF are needed, as well as major structural reforms in order to reduce external imbalances in the medium and long term, as well as the pressures on weakening the local currency.

Balance of payments current account deficit was on the rise in Q1 2012

Balance of payments current account deficit is on the rise, and in Q1 2012 it amounted to 1,159 million euros (16.5% of GDP, Table T4-1). This is the highest quarterly amount of the current deficit since Q4 2008 (whether expressed in absolute terms or as a share of GDP, Figure T4-2 and Figure T4-3). In the last three years, the current account deficit of the national economy was well below the previous high values, i.e. much closer to long-term sustainable level. Increase of the current deficit since the beginning of 2012 means moving away from the equilibrium level again, which, together with a modest inflow of capital, had a negative impact on the value of dinar. The recorded growth of the current deficit is a result of the increase in foreign trade deficit and lower inflow of current transfers. The increase of foreign trade deficit is due to the growing domestic demand (due to high fiscal deficit at the beginning of the year) and the decline of exports caused by the decline in economic activity in the domestic exports, adverse weather conditions, and the departure of "US Steel Serbia". Since the changes in the exchange rate are reflecting on the foreign trade exchange with a time lag, we expect in the following quarters of 2012 a positive impact of the exchange rate developments, i.e. effect of real depreciation recorded in the second half of the previous and beginning of the current year. From the year on year perspective, the current deficit is higher by half of its value from Q1 2011.

In 2012, it is likely to expect a higher level of deficit as compared to previous three years, as well as problems in its financng.

By the end of 2012, the unfavourable external events (crisis in the Eurozone and the present uncertainty - and consequently lower private capital inflows and current transfers, as well as the unfavourable economic situation in neighbouring countries[1]), increased political and economic instability in Serbia could lead to further deepening of the balance of payments imbalances and the more pronounced problem of financing the growing deficit. On the other hand, the present exchange rate depreciation will surely have the opposite effect, mitigating the adverse impacts. In addition, a significant start of activities in the automotive industry could to a large extent have a positive impact on current deficit through the increase of exports. Finally, strong fiscal consolidation[2] and a continued cooperation with the IMF, as well as the policy implementation of

1 For details, please see section 8. „International environment" in this issue of QM.
2 On the necessity of implementing a strong fiscal consolidation, see Spotlight 1 in this issue of QM.

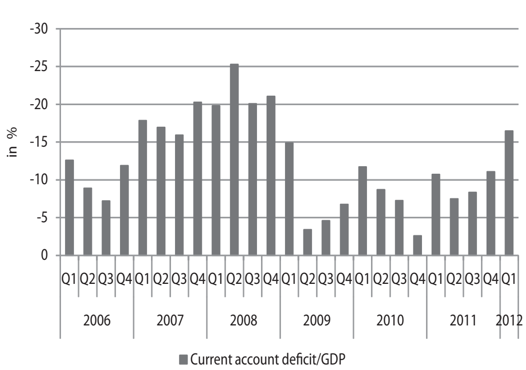
necessary structural reforms, would have long-term positive impact on the external imbalances. Specifically, the new agreement with the IMF would have multiple positive effects on stabilising the balance of payments. First, the necessary reduction of the fiscal deficit would lead to a decline in domestic demand and imports, which would further contribute to the reduction of foreign trade and, consequently, current deficit. Second, cooperation with the IMF would lead to increased investor confidence and significant inflow of capital. Also, the arrangement with the IMF would mean the direct protection from the balance of payments crisis with the withdrawal of funds that would strengthen the foreign reserves.

Table T4-1. Serbia: balance of payments

	2009	2010	2011	2010				2011				2012
				Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
						mil. euros						
CURRENT ACCOUNT	-2,084	-2,082	-2,968	-760	-615	-519	-188	-760	-621	-683	-903	-1,159
Goods	-5,118	-4,774	-5,514	-1,186	-1,171	-1,244	-1,173	-1,314	-1,230	-1,271	-1,699	-1,542
Export f.o.b[1)]	5,978	7,402	8,438	1,473	1,861	1,938	2,129	1,955	2,163	2,169	2,151	1,852
Import f.o.b[1)]	-11,096	-12,176	-13,952	-2,659	-3,032	-3,182	-3,302	-3,269	-3,392	-3,440	-3,850	-3,395
Services	18	5	161	-19	5	-1	20	28	12	12	109	38
Export	2,500	2,667	3,032	537	635	737	758	631	720	816	865	676
Import	-2,482	-2,662	-2,872	-555	-629	-739	-738	-604	-708	-803	-756	-638
Income, net	-502	-670	-758	-167	-205	-127	-171	-112	-252	-195	-198	-229
Receipts	500	438	428	107	108	92	131	101	100	101	126	109
Payments	-1,002	-1,108	-1,186	-273	-313	-219	-302	-214	-352	-296	-324	-338
Current transfers, net	3,518	3,356	3,143	611	755	854	1,136	638	849	771	885	574
o/w grants	197	193	206	29	20	35	109	49	41	39	77	26
o/w private remittances, net	2,618	2,383	2,165	415	543	610	815	450	596	546	573	359
CAPITAL ACCOUNT	2	1	-3	0	0	1	0	-1	0	-1	0	-3
FINANCIAL ACCOUNT	2,207	1,986	2,752	698	596	488	204	644	566	642	899	1,008
Direct investment, net	1,372	860	1,827	284	136	176	265	307	259	661	600	-372
Portfolio investment, net	-51	39	1,619	38	35	4	-38	520	246	871	-18	76
Other investments	3,249	158	1,107	10	104	-6	50	-15	93	188	840	388
Trade credits	654	83	651	-109	125	249	-183	133	124	116	277	108
Loans	1,414	830	-413	523	-270	93	483	-879	34	226	206	-20
NBS	1,114	341	45	0	237	50	54	-4	52	-3	0	-4
Government	258	735	687	167	198	315	55	29	275	297	86	18
Commercial banks	894	626	-729	525	-396	-123	619	-691	-132	-10	104	-150
Long-term	492	619	419	558	-6	33	34	3	10	99	307	-84
Short-term	402	6	-1,148	-32	-390	-156	585	-694	-142	-109	-203	-66
Other (enterprises)	-853	-872	-416	-170	-309	-148	-246	-214	-160	-58	16	115
Currency and deposits	760	-754	870	-405	249	-348	-250	731	-65	-153	357	300
Other assets and liabilities	0	0	0	0	0	0	0	0	0	0	0	0
Allocation of SDR	422	0	0	0	0	0	0	0	0	0	0	0
Reserves Assets (- increase)	-2,363	929	-1,801	367	321	313	-73	-168	-33	-1,078	-523	916
ERRORS AND OMISSIONS, net	-124	96	219	62	19	31	-16	118	54	42	4	154
OVERALL BALANCE	2,363	-929	1,801	-367	-321	-313	73	168	33	1,078	523	-916
PRO MEMORIA												
						in % of GDP						
Current account	-7.2	-7.4	-9.3	-11.7	-8.7	-7.2	-2.6	-10.7	-7.5	-8.3	-11.1	-16.5
Balance of goods	-17.7	-17.1	-17.4	-18.3	-16.6	-17.4	-16.2	-18.5	-14.8	-15.5	-20.8	-21.9
Exports of goods	20.6	26.5	26.6	22.7	26.3	27.1	29.5	27.5	26.1	26.5	26.4	26.3
Imports of goods	-38.3	-43.6	-44.0	-41.0	-42.9	-44.4	-45.7	-46.1	-40.9	-42.0	-47.2	-48.2
Balance of goods and services	-17.6	-17.1	-16.9	-18.6	-16.5	-17.4	-15.9	-18.1	-14.7	-15.4	-19.5	-21.4
Current transfers, net	12.1	12.0	9.9	9.4	10.7	11.9	15.7	9.0	10.2	9.4	10.8	8.2
GDP in euros[2)]	28,966	27,956	31,744	6,491	7,070	7,166	7,229	7,096	8,297	8,190	8,161	7,039

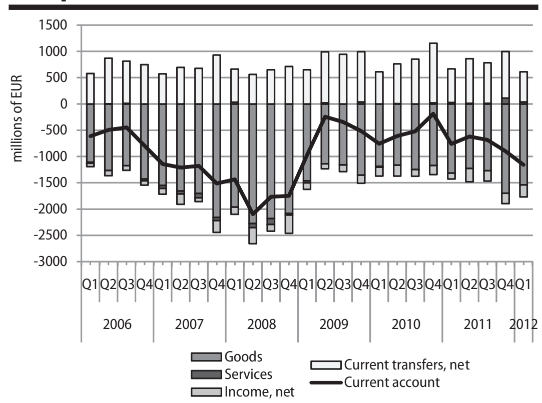
Source: NBS
1) Expot and Iimport f.o.b, according to the NBS methodology adjusted to IMF BOPM-5.
2) Quarterly values. Conversion of the annual GDP to euros is done according to the average annual exchange rate (average of official daily middle rates of NBS).

Figure T4-2. Share of current account deficit in GDP, 2006-2012



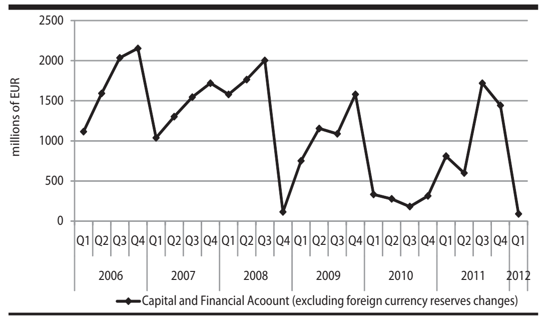
Source: NBS, *QM*

Figure T4-3. Current account and its components, 2006-2012



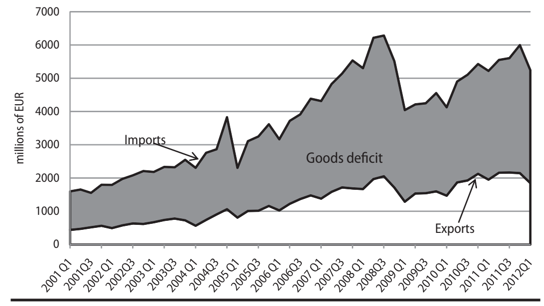
Source: NBS, *QM*

Figure T4-4. Capital and financial accounts, 2006-2012



Source: NBS, *QM*

Figure T4-5. Import of goods, export of goods, and trade deficit, 2001-2012



Source: NBS, *QM*

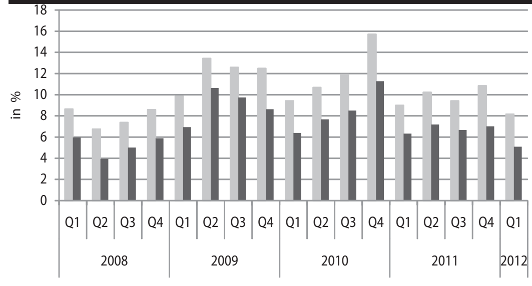
The increase in current account deficit in Q1 is the result of growing foreign trade deficit and lower inflows of current transfers.

The increase in current account deficit in Q1 is the result of growing foreign trade deficit, and of relatively low-level inflow of current transfers. Trade deficit amounted to 1,542 million euros, i.e. 21.9% of GDP. Realised trade deficit continues its rise recorded at the end of 2011 and it is one percentage point above the actual participation in the last quarter of 2011 (see Table T4-1). Trade deficit is above the average values of 2009, 2010 and 2011 by 4-5 percentage points (Figure T4-5). Rise of the trade deficit is the result of the growing domestic demand (due to high fiscal deficit) and declining foreign demand, which leads to a decrease of domestic exports, while the imports are on a slight rise compared to the previous year. In Q1, the exports amounted to 1,852 million euros (26.3% of GDP), while the imports were 3,395 million euros (48.2% of GDP). The exports are 5.2% below, while the imports are 3.9% above the values of Q1 last year. This brings the y-o-y deficit increase to 17.4%. The coverage of imports by exports in this period declined by 5 percentage points - from 60% recorded in Q1 2011 (and in the whole 2011) to 55% in Q1 2012.

Low inflow of current transfers is primarily due to lower inflows of remittances

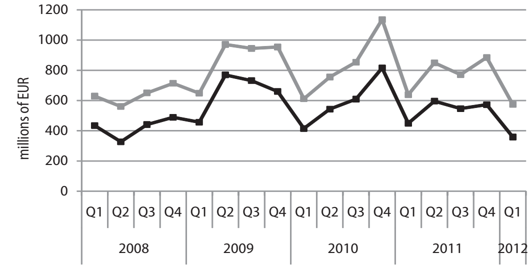
Inflow of current transfers, especially remittances, is in a noticeable decline. During Q1, inflow from current transfers amounted to 574 million euros, accounting for 8.2% of the corresponding quarterly GDP. Given the values of 2009, 2010 and 2011 (12.1% of GDP, 12.0% of GDP and 9.9% of GDP, respectively) this kind of inflow is reduced and closer to the values from the period before the crisis (e.g. 7.8% of GDP in 2008). The inflow of remittances amounted to 359 million euros, i.e. 5.1% of GDP, which is the value of pre-crisis level in 2008 (5.2% of GDP, Table T4-1) and significantly lower than the inflow of remittances in previous three years (Figure T4-6 and Figure T4-7). The current reduction in inflows of remittances (and consequently the current transfers) may be a result of a greater crisis in the Eurozone, i.e. significant economic problems faced by member states, such as job losses and increased uncertainty in both the EU and other countries, which are senders of transfers (remittances). On the other hand, the reduced inflow in Q1 could only indicate a short-term fluctuation of inflows, which is seasonal and is leading to lower levels of remittances at the beginning of each year (Figure T4-6 and Figure T4-7). However, remittances are by one fifth, and current transfers by one tenth below the values recorded in the first quarter of last year.

Figure T4-6. Share of inflows of current transfers and remittances in GDP, 2008-2012



Source: NBS, *QM*

Figure T4-7. Inflow of current transfers and remittances, 2008-2012



Source: NBS, *QM*

Capital inflow in the first three months of current year is extremely low

The problem of financing the deficit, that could possibly mark the entire 2012, appeared at the very beginning of the year – in Q1 2012. The capital inflow in the first three months of the current year was extremely low – 92 million euros (see Figure T4-4)[3]. The low inflow of capital in this period is the result of a high FDI outflow, the low amount of portfolio and other investments. So in Q1, foreign reserves were diminished by 916 million euros, which covered most of the current deficit (Table T4-1).

...due to FDI outflows, modest portfolio investments and discharge of financial loans

During Q1, a substantial outflow of capital based on FDI was recorded – 372 million euros net. This is primarily a consequence of the repurchase of Telecom Serbia shares from the Greek telecoms company OTE in the amount of 380 million euros and the withdrawal of partial Telenor capital (around 120 million euros)[4]. Portfolio investments were modest, amounting to 76 million euros. Other investments amounted to 388 million euros, out of which 300 million euros was the inflow of funds to the *Cash and depo*mmercial loansTrade credits were 108 million euros, while the financial loan account recorded a slight discharge in the amount of 20 million euros. Banks discharged their net short-term and long-term loans. At the end of 2011, the banks pulled large amounts of money from their parent banks abroad in order to improve the state of annual financial reports, and then returned the money at the beginning of 2012. In Q4 2011, the companies reversed the trend of debt settlements abroad recorded since the onset of the crisis and in Q1 2012 borrowed the additional 115 million euros net, almost entirely in long-term loans.

No considerable inflow of capital is expected in 2012

No considerable inflow of capital is expected in 2012. The high amount of FDI in 2011 was related to several large projects, that are either completed or in final stages, as well as to the sale of the company "Delta Maxi". That is why we cannot count on a significant amount of FDI before next year. In addition, given the current situation in the EU and the national economy, aside from the lack of a significant FDI, the absence of a more significant activity of portfolio investors on the domestic market is quite probable as well. This indicates that without larger structural changes in the Serbian economy, that would lead to the increase of exports and creation of an investment attractive environment, the foreign loans and/or reduction in forex reserves would, in that case, be the main source of covering the current deficit. That is, the expected influx of investments of around 1 billion euros in 2012 (estimate of the level of investments as a sum of possible smaller investments) will be considerably below the expected level of the current deficit. Hence, if the current account deficit is around four billion euros, the difference will have to be covered either by additional loans or by the additional reduction in the foreign reserves, which will exert considerable pressure on the exchange rate and could cause a balance of payments crisis.

In the first four months of 2012, there was a decrease of foreign reserves by 1.67bn euros, out of which 709 million euros were spent on the defence of the exchange rate

Forex reserves were decreased by 916 million euros during Q1 (Table T4-1). In January, the outflow of capital through banks was around half a billion euros (return of funds pulled from abroad at the end of 2011 from parent banks, in order to improve the state of annual financial reports). In February, the biggest part of the forex reserve outflow was due to the matured RS state securities denominated in euros, in the amount of 204 million euros, as well as due to the NBS interventions in an attempt to mitigate excessive daily fluctuations in the exchange rate (189 million euros). In March, a net decrease in foreign reserves of 92 million euros was recorded, where the largest outflow was due to the NBS interventions on the interbank foreign exchange market in the amount of 310 million euros. Forex reserves were diminished in April as well, so at the end of the month they amounted to 10,387 million euros5. In April, the largest part of that reduction was the result of withdrawal of mandatory forex reserves of the banks. The banks withdrew 470 million euros due to the regulatory changes of NBS (reduction of rate at which banks calculate the mandatory forex reserves, followed by the increased rate of forex reserves of banks in dinars). Additional 210 million euros of foreign reserves in April were used for the defence of the value of the national currency. In total, in the first four months, just for the interventions on interbank foreign exchange market, the forex reserves were decreased by 709 million euros, while the total decline of forex reserves was 1.67 billion euros. Still, even though the foreign reserves are diminishing, they are still covering six to seven months of imports of goods and services.

3 247 million eurs with the Errors and omissions account.
4 Source: National Bank of Serbia.
5 http://www.nbs.rs/internet/cirilica/scripts/showContent.html?id=5756&konverzija=no

Trends

Exports

In Q1 exports recorded a decrease of 5.2% y-o-y

In Q1 2012, exports were 1,860 million euros, which is 5.2% below last year's value (Table T4-8). The decline in exports is the result of a considerable y-o-y decrease of value of *Bulky exports* (-30.6%), while the *Underlying exports* recorded a y-o-y growth of 7.4%. Primarily, the realised export performance was the result of a sudden drop in exports of *Iron and steel* (-63.0%), due to new circumstances at the "Železara Smederevo" steel factory. Additionally, the cold weather resulted in modest production results during Q1 and a lower level of exports of other export products.

A 1.7% year on year increase in prices in euros of exporting goods was recorded. Figure T4-9 shows that terms of trade (ratio of export and import prices) recorded a slight hight variation in the index. A certain decrease was recorded in Q4 2011 (probably due to a drop in food prices and a rise in global energy prices). Still, the index values shown were often above 100. Therefore, the fact that in Q1 the terms of trade index was 99.3, i.e. only by 0.7% lower than in Q1 2011(Figure T4-9) shows that the decline of foreign trade activity cannot be attributed to the deterioration of the price ratio of export and import goods.

In addition to a significant decline of exports in Iron and steel, a y-o-y decline in export value has been recorded in all other Bulky export goods as well

Besides the significant y-o-y decline in Q1 in export of Iron and steel, a y-o-y decline in the export value of all other goods within the Bulky export category was recorded as well. y-o-y exports of non-ferrous metals has dropped by 22.8%, partly due to the fall of prices, and partly due to the reduced export quantities. After the extremely high level recorded in Q1 2011, global prices of non-ferrous metals have gradually declined during 2011, only to rise again in Q1 2012. In Q1 2012, global prices of these products in euros were 13.9% below the average prices of Q1 2011[6]. Therefore, the decline in exports quantities was 10.3%, which is probably a consequence of diminished production due to the adverse weather conditions at the beginning of the year. The exported values of Fruits and vegetables and Cereal and cereal products were below Q1 of last year by 9.1% and 1.6% respectively (Table T4-8).

Underlying exports recorded a YOY growth due to the significant increase of Other exports

Underlying exports recorded a y-o-y growth of 7.4%. Within it, exports of goods in the *Core* group were almost at the level of Q1 of the previous year, while there was a significant rise of 12.6% of export of goods categorised under the group *Other.*

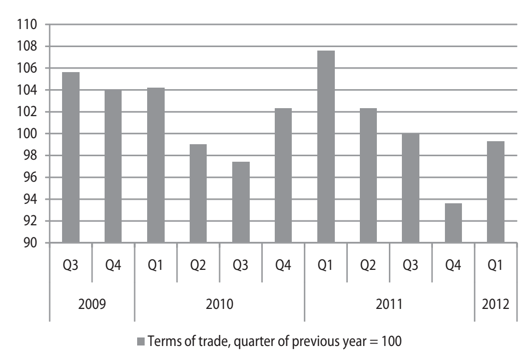
Table T4-8. Serbia: Exports, y-o-y growth rate, 2010–2

	Exports share in 2011	2011[1)]				2012[1)]	2011[1)]				2012[1)]
		Q1	Q2	Q3	Q4	Q1	Q1	Q2	Q3	Q4	Q1
	in %	mil. euros					y-o-y growth rate (in %)				
Total	100.0	1,961	2,157	2,157	2,162	1,860	33.7	14.5	11.7	2.1	-5.2
Bulky exports	27.7	649	574	566	551	450	53.9	15.7	5.5	-12.1	-30.6
Iron and steel	8.4	239	186	147	140	88	47.4	-4.8	-19.4	-23.3	-63.0
Non ferrous metals	7.4	164	178	158	128	127	50.5	34.9	3.7	-3.1	-22.8
Fruits and vegetables	5.6	92	92	147	141	84	22.4	15.4	29.0	9.4	-9.1
Cereal and cereal products	6.2	154	117	114	142	151	104.1	32.4	29.5	-22.4	-1.6
Underlying exports	72.3	1,312	1,583	1,591	1,611	1,410	25.5	14.0	14.1	8.0	7.4
Core	29.7	577	632	673	627	582	31.7	21.3	15.4	5.9	0.9
Clothes	4.1	82	80	96	89	89	13.5	15.3	18.2	5.9	9.1
Miscellaneous manufactured articles, n.e.s.	3.4	60	74	77	77	61	27.2	13.6	5.6	7.4	2.9
Manufactures of metals, n.e.s.	4.2	68	97	100	90	78	52.6	45.6	47.0	15.2	15.3
Rubber products	3.2	76	65	65	63	72	40.0	25.9	18.4	12.0	-4.4
Electrical machinery, apparatus and appliance	6.3	124	134	141	135	137	58.9	24.1	15.7	-3.0	10.6
Organic chemicals	0.6	12	12	11	15	9	-58.7	-56.3	-61.3	-16.8	-22.4
Plastics in primary forms	1.9	43	42	41	36	20	48.5	30.7	10.4	6.4	-53.0
Footwear	2.3	51	45	55	44	49	35.0	34.7	23.1	3.2	-3.3
Paper, paperboard and articles of paper pulp	2.3	45	52	50	49	48	26.5	25.4	24.6	15.9	6.4
Non-metal mineral produce	1.4	17	32	38	29	17	47.2	17.1	8.7	13.1	0.1
Other	42.5	735	951	918	984	828	21.0	9.7	13.1	9.4	12.6

Source: RZSSORS
1) data in millions of euros, as well as the year on year growth rates, were obtained based on the data from the Statistical Office of the Republof Serbia (RZSSORS) and calculated according to the new methodology. For details, see QM issue no.20, Box 1, "Changes to foreign trade methodology used by the Statistical Office of the Republic of Serbia".

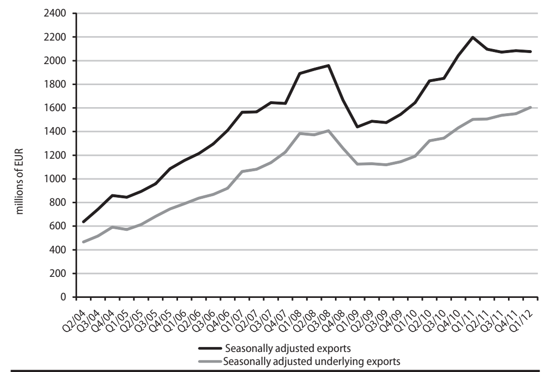
6 Fall of prices in dollars is more pronounced and it's 17.4%, due to the weakening of the euro against the dollar.

Figure T4-9. Terms of trade index, 2009-2012



Source: RZSSORS, *QM*

Figure T4-10. Serbia: Seasonally adjusted exports and seasonally adjusted underlying exports, quarterly, 2004-2012



Source: RZSSORS, *QM*

Seasonally adjusted values confirm the significant impact of the decline of* Bulky exports *on the reduction of total exports in Q1

Seasonally adjusted export in Q1 was 2,075 million euros and by 0.4% lower than the exports from the previous quarter – which represents a reduction of 1.6% on an annual level. Still, the seasonally adjusted *Underlying export*[7] has been recording a quarter on quarter value growth ever since Q3 2009. Thus, the seasonally adjusted value of the *Underlying export* is by 3.5% over the value of Q4 2011, i.e. by as much as 14.7% annualised (Figure T4-10). This confirms that the current decline in exports is the result of the recorded drop in *Bulky exports* – primarily the decrease of exports of iron and steel due to the exit of US Steel, but also of all other products in this category.

Significant impact of* Iron and steel *on total exports, but a small one on net exports

Just how much have the production and exports of US Steel been significant for the total exports of Serbia is also shown by the fact that the exports of *Iron and steel* made as much as 13% of total domestic exports in the period before the crisis (after the crisis, this share dropped to around 8% in 2009, 10% in 2010 and 8.5% in 2011). Thus, the exports in Q1 2012, after the exclusion of Iron and steel, recorded a rise as compared to Q1 2011 by 2.9%. Also, the seasonally adjusted value of such exports was by 3.2% higher than in Q4 2011, i.e. 13.6% annualised. However, it is important to mention that even though the American company was a large exporter, it was also a large importer. That is, the value of exports and imports of goods in the *Iron and steel* group compared to the GDP value indicates a low value of net exports. From 2004 to 2011, the export of Iron and steel was 2-3% of GDP, and the import was 1-2% of GDP, so the net exports were 1% of GDP at the most. So, even though the decline of *Iron and steel* production contributed significantly to the decline of exports in Q1 2012, it had almost no impact on the rise of the foreign trade deficit in this quarter (0.03 percentage points of GDP).

However, the lack of a substantial activation of the production of *Iron and steel,* coupled with the current economic problems in the EU and surrounding countries, will probably cause a continuation of a negative trend in the growth of total exports until the end of the year. This will further lead to a diminished coverage of exports by imports and a decreased inflow of foreign currency in this respect, which would, combined with the high domestic demand, exert additional pressures on the exchange rate and the forex reserves.

7 Total exports excluding the exporting values of Bulky exports: Iron and steel, Non-ferrous metals, Cereal and cereal products, and Fruits and vegetables.

Imports

Year on year growth of imports of 4.7% in Q1

In Q1, imports recorded a rise of 4.7% year on year[8]. Observed individually – by its components - *Energy, Intermediary goods, Capital goods*, as well as *Durable consumer goods* recorded a y-o-y growth of 10-12%. Over Q1, the imported value of *Non-durable consumer goods* was significantly above the last year's value (30.6%). On the other hand, the import of goods in the *Other* group was by one third below the value of the first quarter of 2011. It should be noted that the importing prices in Q1 were by 2.3% higher than the prices of the same period in 2011, i.e. the imported inflation contributed to a certain extent to the rise of the value of imports (especially in the import of energy, equipment, raw materials, and food)[9].

Unfavourable structure of imports still pronounced

The import of *Intermediary goods* is slightly accelerating the growth (y-o-y rate of 11.7%), while there is a decline in growth of imports of *Capital goods*. The imported value of *Durable consumer goods* in Q1 2012, after the negative growth rates of the previous year, recorded an increase of 12.0%, year on year (Table T4-11). A larger import of *Non-durable consumer goods* in Q1 2012, compared to the same period last year, indicates an unfavourable structure of imports. On the other hand, import of *Other* goods is on a significant decline.

Energy prices in the world recorded a rise at the beginning of 2012, so the y-o-y growth of global prices in euros in Q1 was 17.6%[10]. Thus, during Q1, having in mind the stated growth of prices, there was a drop in imported energy by about 5%, despite the rise of energy imports due to the extremely cold weather.

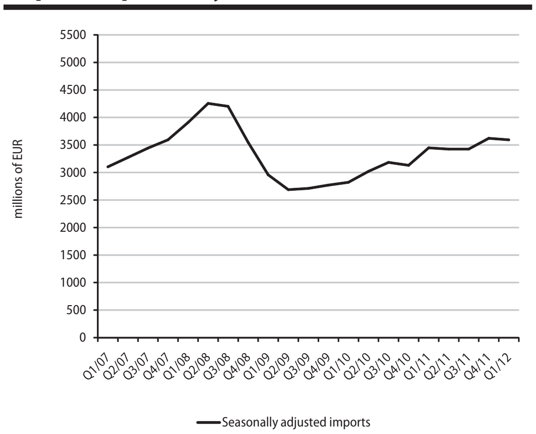
Table T4-11. Serbia: Imports, y-o-y growth rate, 2010–2012

	Imports share 2011	2011[1)]				2012[1)]	2011[1)]				2012[1)]
		Q1	Q2	Q3	Q4	Q1	Q1	Q2	Q3	Q4	Q1
	in %	u mil. euros					in %				
Total	100.0	3,374	3,502	3,538	3,983	3,534	24.3	14.2	7.7	16.5	4.7
Energy	18.6	729	583	545	823	814	32.5	7.0	-10.7	58.2	11.6
Intermediate products	32.2	1,023	1,240	1,197	1,175	1,143	38.9	29.3	9.8	6.7	11.7
Capital products	16.2	521	550	573	690	574	35.0	12.2	8.5	20.8	10.2
Durable consumer goods	2.3	72	78	83	100	81	-12.7	-4.7	-2.2	-5.2	12.0
Non-durable consumer goods	12.2	370	411	444	527	483	7.7	9.4	13.9	12.2	30.6
Other	18.5	659	640	695	667	439	7.2	4.0	19.6	2.8	-33.3
Imports excluding energy	81.4	2,645	2,919	2,992	3,160	2,720	22.3	15.8	11.9	9.1	2.8

Source: SORS

1) Data in millions of euros, as well as the year on year growth rates were obtained based on the data of the Statistical Office of the Republic of Serbia, calculated according to the new methodology. For details, see QM issue no.20, Box 1 "Changes to foreign trade methodology used by the Statistical Office of the Republic of Serbia".

Figure T4-12. Serbia: Seasonally adjusted imports, quarterly, 2007-2012



Source: NBS, SORS, *QM*

Seasonally adjusted imports indicate a slight growth trend since mid 2009, but also that its values are still below those before the crisis

The value of seasonally adjusted imports in Q1 2012 is below the values from Q4 2011 by 0.8% (3.0% annualised). Still, the figure shows a slight growth trend of imports as of the second half of 2009, with certain oscillations. A slow recovery of imports have impacted the levels of imports to still be lower than before the crisis. That is, after the sudden decline at the start of the global financial crisis, the imports at the beginning of 2012 still haven't reached the values from Q2 and Q3 2008 (15% below the imported values from that period, Figure T4-12).

8 The section of the article dealing with the balance of payments analysis uses data for exports and imports f.o.b. (free on board), published by NBS in line with the IMF methodology („Balance of Payments Manual", fifth edition, IMF; http://www.imf.org/external/np/sta/bop/BOPman.pdf.). Part of the article dealing with the analysis of imports and exports uses the data from the RZS, where the value of exported goods is expressed according to the f.o.b. type of value, and the value of imported goods according to the c.i.f. (cost, insurance, freight) type of value. That is why a discrepancy may occur in the stated imports, as well as in the growth rates.

9 SORS and NBS, Inflation report, May 2012, p. 11.

10 The year on year growth of global prices in dollars is 12.8%, which, together with the appreciation of dollar against euro, contributes to the energy prices expressed in euros in Q1 2012 being above the last year's levels by 17.6%.

Foreign debt

Serbia's foreign debt at the end of March was 24,068 million euros, i.e. 76.0% of GDP

Serbia's foreign debt at the end of March was 24,068 million euros, i.e. 76.0% of GDP, which is practically the same as at the end of 2011. As previously mentioned, on the one hand, Q1 saw a discharge of the banking sector's debt (short-term[11]), while the private sector took on an additional debt of 138 million euros for long-term loans[12]. Foreign debt of the public sector was by 118 million euros lower than in the previous three months (Table T4-13).

Table T4-13. Serbia: Structure of foreign debt, 2008–2012

		2010				2011				2012
	2009	Mar.	Jun	Sep.	Dec.	Mar.	Jun	Sep.	Dec.	Mar.
	stocks, in EUR millions, end of the period									
Total foreign debt	22,487	22,943	23,456	23,115	23,786	22,672	22,734	23,860	24,125	24,068
(in % of GDP) 2)	78	79	82	81	85	79	76	77	76	76
Public debt	7,764	8,122	8,921	8,874	9,076	8,861	9,138	10,433	10,773	10,655
(in % of GDP) 2)	27	28	31	31	32	31	31	34	34	34
Long term	7,762	8,122	8,921	8,874	9,076	8,861	9,138	10,433	10,773	10,655
o/w: to IMF	1,110	1,157	1,483	1,455	1,529	1,475	1,506	1,582	1,618	1,581
o/w: Government obligation under IMF SDR allocation	422	440	469	444	449	434	428	449	459	449
Short term	1	0	0	0	0	0	0	0	0	0
Private debt	14,724	14,820	14,535	14,241	14,710	13,811	13,597	13,427	13,352	13,412
(in % of GDP) 2)	51	51	51	50	53	48	46	44	42	42
Long term	12,720	12,919	13,076	12,945	12,880	12,696	12,630	12,569	12,704	12,834
o/w: Banks debt	2,597	2,867	3,195	3,279	3,362	3,347	3,413	3,551	3,782	3,784
o/w: Enterprises debt	10,123	10,052	9,881	9,667	9,518	9,348	9,217	9,018	8,922	9,050
Short term	2,003	1,901	1,459	1,295	1,830	1,116	966	858	648	578
o/w: Banks debt	1,713	1,691	1,304	1,146	1,731	1,036	895	785	582	515
o/w: Enterprises debt	290	210	155	149	100	79	72	73	66	63
Foreign debt, net 1), (in% of GDP)2)	41	43	45	47	49	45	43	41	38	41

Note: As of September 2010, the methodology of the statistics of foreign debt has been changed, so that now the public sector foreign debt includes obligations under the IMF SDR allocation (448.9 million euros), used in December 2009, as well as the capitalised interest towards the Paris club creditors (49.8 million euros), while the foreign debt of the private sector now excludes the loans concluded prior to December 20, 2000, for which no payments are made (867.3 million euros, out of which 403.3 million euros relates to domestic banks, and 464.0 million euros relates to the domestic enterprises). The foreign debt data shown in the Table were calculated according to the new methodology.
Source: NBS, *QM*
1) Total foreign debt less NBS forex reserves.
2) The sum of GDP value of the observed quarter and of previous three quarters was used.

Variations of the exchange rate significantly impact the expressed dynamic of the foreign debt

Still, significant variations of the exchange rate are responsible to a large extent for the expressed changes in the foreign debt. That is, the current depreciation of euro against other currencies leads to the increase of debt expressed in euros, while the movement of dinar additionally affects the amount of GDP, thus contributing to the variations of the foreign debt activity expressed in % of GDP. In the foreign debt structure, the largest share belongs to the debt in euros (76.3%), then in dollars (13.3%). Special drawing rights make 8.5% of the foreign debt, the Swiss franc has 3.9%, while the rest of the debt (0.7%) goes to other currencies[13]. Having in mind this currency structure, during Q4 2011, out of 265 million euros of increase in the foreign debt, almost ¾ (195 million euros[14]) of the recorded growth were due to the weakening of euro against other listed currencies.

U odnosu na mart 2011 godine porast spoljnog duga posledica rasta duga javnog sektora

However, at present, the weakening of dinar could have a greater impact on the expressed level of the foreign debt. That is, the value of the national GDP expressed in euros declines with the fall of national currency. Thus, if we calculate the value of GDP realised in the last three quarters of 2011 and the first quarter of 2012, at the average rate in March 2012 of 110.9 dinars to a euro, and then compare the debt value with thus calculated value of GDP[15], we find that the foreign debt makes as much as 82% of its value.

11 Long-term loans of banks and the discharge of short-term loans from the private sector were negligable in Q1.

12 Here, we are repeating the citing of the debt of the banks and private sector from the section of the article on balance of payments because of the slightly different values due to different data sources: Sector for international cooperation of the National Bank of Serbia (foreign debt data) and Sector of economic analysis and research, Statistical department for balance of payments of the National Bank of Serbia (balance of payments data).

13 Debt Analysis of the Republic of Serbia, September 2011, NBS.

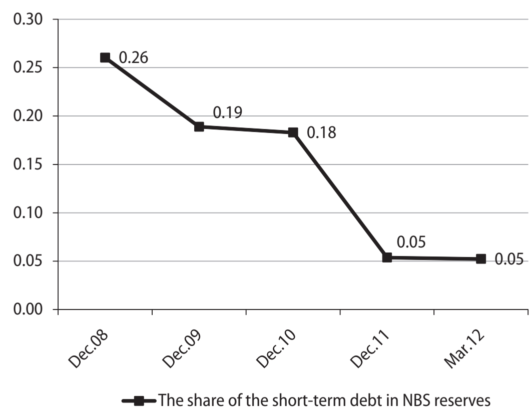
14 Debt Analysis of the Republic of Serbia, December 2011, NBS.

15 In the denominator we use the sum of GDP values of the observed and previous three quarters. E.g. If we want to calculate the share of foreign debt in GDP for Q1 2012, we divide the value of the foreign debt at the end of Q1 with the sum of quarterly values of GDP from Q2 2011, Q3 2011,Q4 2011 and Q1 2012.

Compared to March 2011, the rise of foreign debt is the result of the growth of public sector debt

For a period of one year (March 2011 - March 2012), Serbia's foreign debt grew by 1.4 billion euros. This is solely a result of additional borrowing of the state, since the private sector discharged 400 million euros of debt. The foreign debt of the public sector at the end of Q1 2012 was by 1.8bn euros higher than in the previous year. Discharge of the private sector is the result of a reduction of short-term loans of banks and enterprises. The private sector is indebted for 138 million euros. The banks increased the long-term loans by 437 million euros, while the enterprises reduced the long-term debt by close to 300 million euros, compared to March 2011. In this period, the share of short-term debt in total debt was decreased (from 5% to 2.5%), which slightly improved the structure of foreign debt by maturity according to the original maturity, as a result of a reduction of short-term debt of the banks (Table T4-13). One of the indicators of the vulnerability of an economy used is the share of short-term debt in the total foreign debt. In Serbia, this indicator has been on a considerable decline since 2008, and is currently 0.05 (Figure T4-14). This ratio of short-term debt and forex reserves is currently extremely favourable, but it still requires continuous monitoring, given the increased uncertainty.

Figure T4-14. Serbia: Share of short-term foreign debt in forex reserves, 2008-2012



Source: NBS, *QM*

Compared to the state of foreign debt at the end of March 2011, the foreign debt of the public sector has increased from 39% to 44% of the total debt value, while the foreign debt of the private sector has decreased from 61% to 56% of the total foreign debt value. It is our estimate that in 2012, the foreign debt will grow in favour of the public sector debt, while the private sector will have a smaller room for borrowing abroad, given the current events in Europe. Above all, unless the government spending is not strictly limited, there could be a significant increase of the public sector's foreign debt and thus of the total foreign debt.

By the end of 2012, the unfavourable external developments, combined with the political and economic instability in Serbia, may lead to further deepening of balance of payments imbalances and a more pronounced problem of financing the growing deficit. Therefore, in 2012, the expected growing current account deficit, if accompanied by a low influx of capital, could cause further borrowing or further reduction of foreign reserves, exert strong pressure on the currency and risk balance of payments crisis.