SERBIA ECONOMY REPORT

Q2 2017

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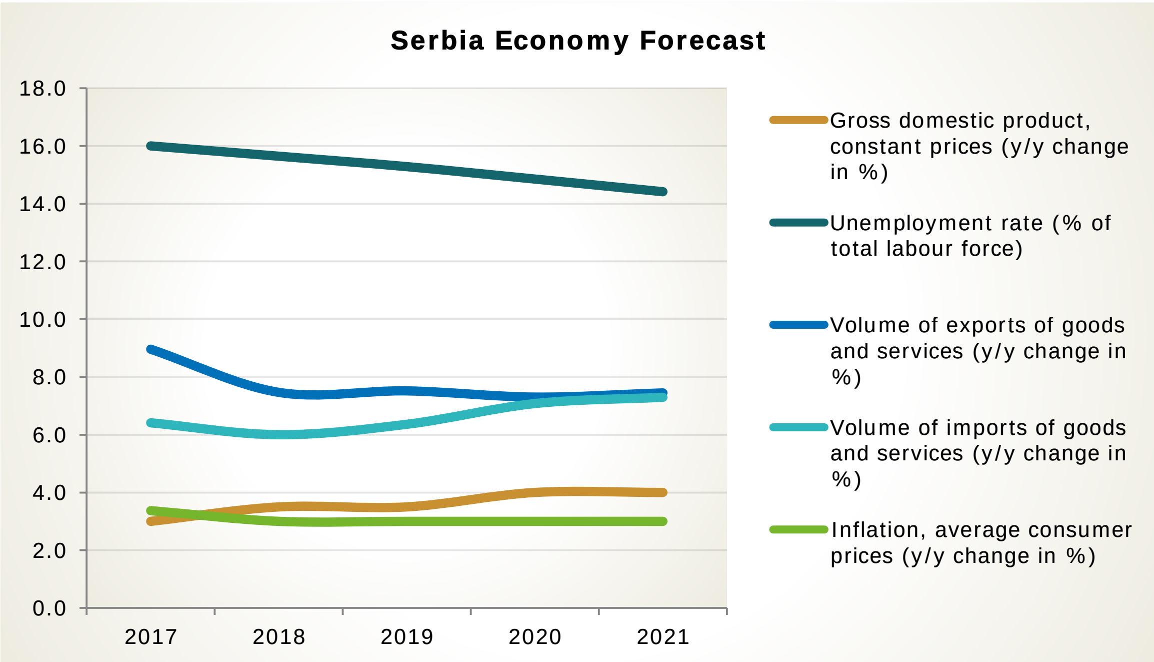
1. MACROECONOMIC SNAPSHOT AND FORECAST

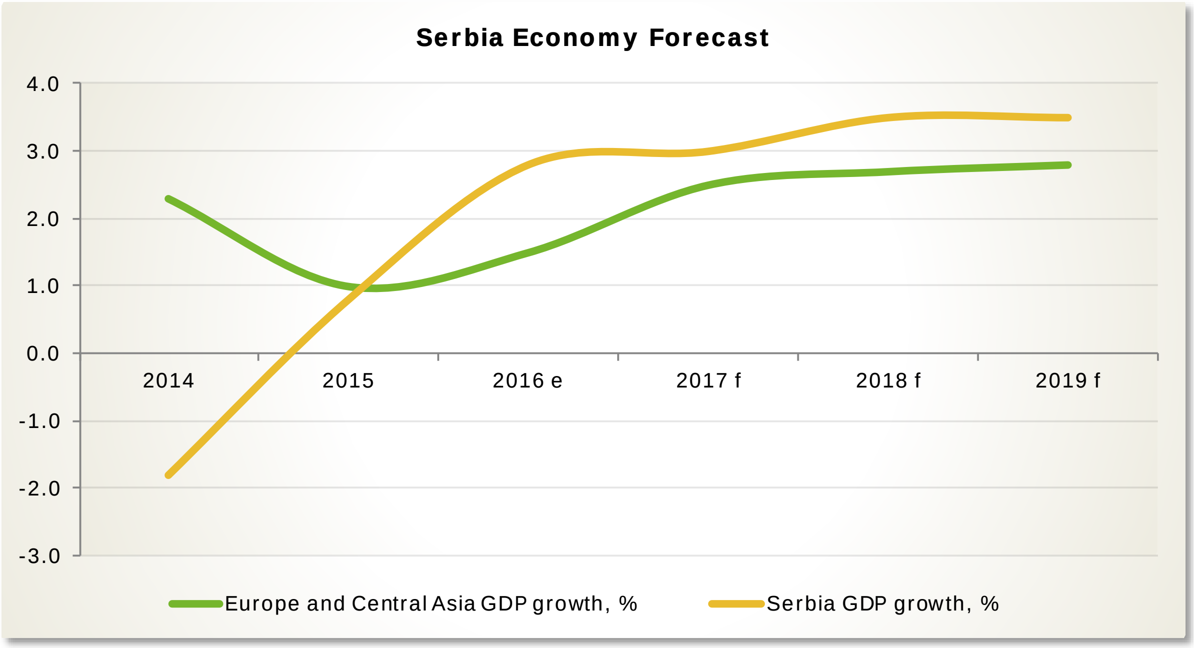
SERBIA – MACROCECONOMIC SNAPSHOT AS OF Q2 2017	
GDP Growth	*1.3% y/y*
Industrial output	*2.1% y/y*
Industrial sales	*8.7% y/y*
Retail sales	*5.3% y/y*
Average annual inflation	*3.4% y/y*
Unemployment rate	*11.8%*
Number of building permits	*51.6% y/y*
Money supply growth	*7.4% y/y*
Household loans	*10.3% y/y*
BELEX15 blue-chip index	*0.6% q/q*
Gross external debt	*EUR 25.425 bln*
Current account gap	*EUR 356.0 mln*
Net FDI inflow	*EUR 487.3 mln*
Foreign trade deficit	*EUR 1.065 bln*
Number of foreign tourist overnights	*23.1% y/y*



Source: International Monetary Fund (IMF) World Economic Outlook Database – October 2017

Serbia's real GDP growth is expected to accelerate to 3.0% in 2017 from 2.8% in 2016, according to an IMF forecast. The largest contributors to economic growth in 2017 will be government consumption and capital investments. The fund projects inflation to average 3.4% in 2017, up from 1.1% in 2016 on account of recovering demand and higher energy prices.

Risks to the IMF outlook include possible spillovers from regional developments and market volatility, political resistance to reform the state-owned enterprises (SOE), possible delay in delivering on structural reforms, as well as slippages in maintaining fiscal discipline.



Source: World Bank, Europe and Central Asia Economic Update, June 2017

The World Bank projects Serbia's GDP growth to accelerate from 2.8% in 2016 to about 3.5% over the medium term. Increases in the private consumption and capital investment are expected to be the main drivers of growth in 2017-2019. As domestic demand gradually recovers, the bank expects inflation to advance to 3.1% in 2017 from 1.1% in 2016. The current account gap is expected to expand to 4.9% of GDP in 2017-2019 from 3.2% of GDP in 2016.

As main risk to the forecasts, the World Bank points a possible delay in the implementation of structural reforms and the still high levels of unemployment, especially among younger generation.

Serbia – GDP, Inflation, Current Account Balance and FDI Dynamics (y/y change in %)

	2014	2015	2016 e	2017 f	2018 f	2019 f
Real GDP growth, at constant market prices, y/y change in %	-1.8	0.8	2.8	2.3	3.0	3.5
Private Consumption	-1.3	0.5	0.8	3.9	2.2	2.9
Government Consumption	-0.6	-1.5	2.0	5.2	1.6	-3.9
Gross Fixed Capital Investment	-3.6	5.6	6.8	4.6	7.3	10.4
Exports, Goods and Services	5.7	10.2	11.9	9.8	6.5	7.5
Imports, Goods and Services	5.6	9.3	6.8	9.3	5.9	6.4
Real GDP growth, at constant factor prices (by sectors)	-1.8	0.8	2.8	3.0	3.5	3.5
Agriculture	2.0	-7.7	8.5	-10.0	5.0	3.0
Industry	-6.4	3.0	3.1	4.5	4.0	5.0
Services	-0.5	1.1	2.8	2.3	2.3	2.9
Inflation (Consumer Price Index)	2.1	1.4	1.1	3.1	3.5	3.5
Current Account Balance (% of GDP)	-6.0	-4.8	-3.2	-3.9	-4.7	-4.9

Net Foreign Direct Investment (% of GDP)	3.7	3.7	3.7	4.8	4.3	4.2

Source: World Bank, Europe and Central Asia Economic Update, June 2017

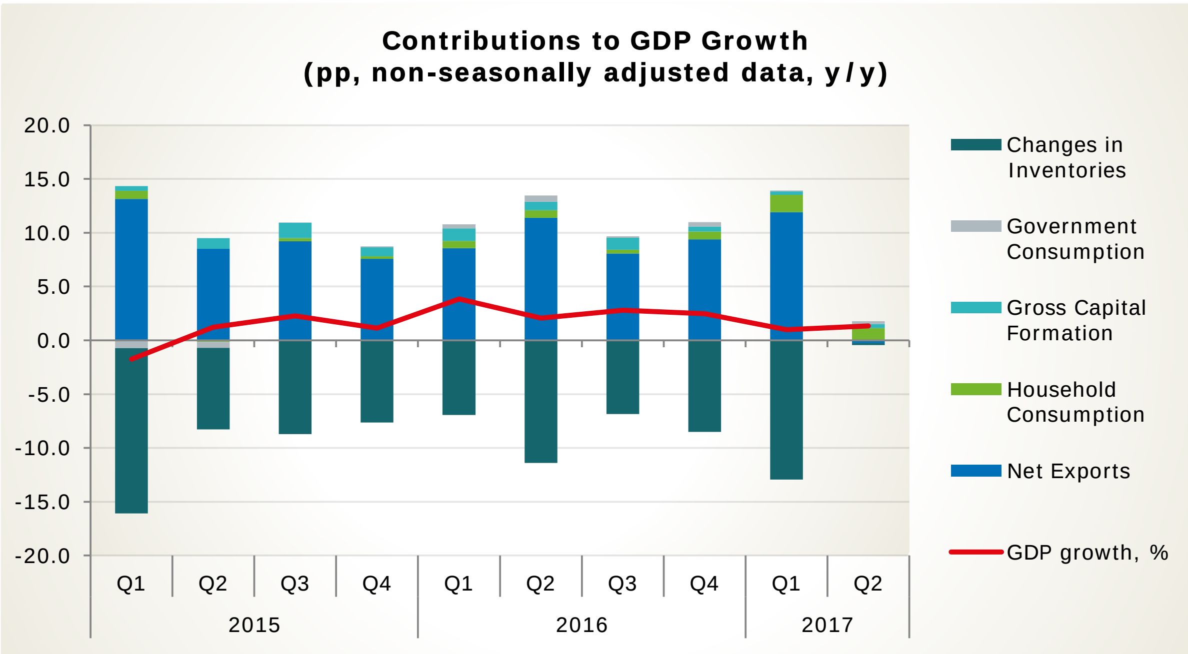
2. REAL SECTOR

2.1. GROSS DOMESTIC PRODUCT (GDP)

GDP growth increased to 1.3% y/y in Q2 2017

Serbia's GDP, including changes in inventories and net acquisition of valuables, increased by a real 1.3% y/y and totalled RSD 801.4 bln in Q2 2017, according to data of the Statistical Office of the Republic of Serbia (SORS). This is a notable increase compared to the GDP growth in Q1 2017, of 1.0% y/y.

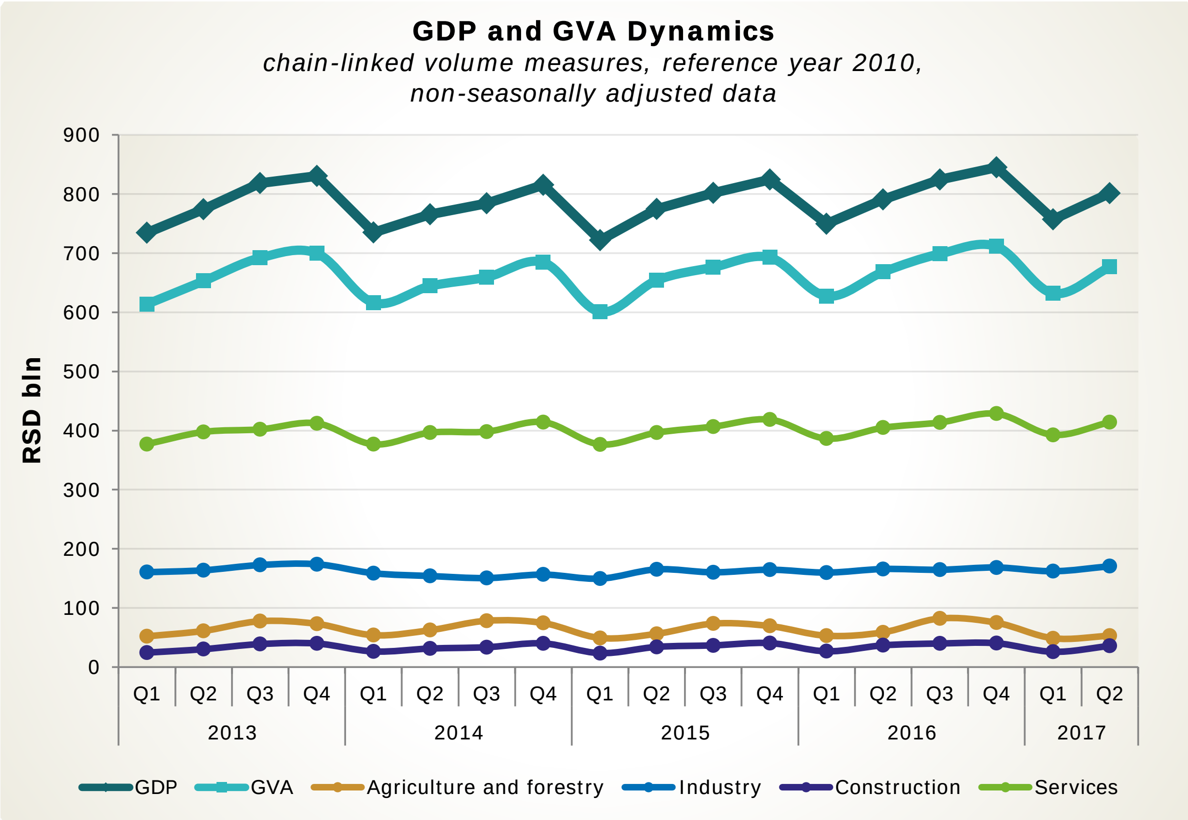
Exports grew by 11.5% y/y to RSD 475.5 bln, while imports increased slower at 10.3% y/y to RSD 586.5 bln. Final consumption inched up by 1.6% y/y to RSD 730.3 bln. Gross capital formation rose by 2.0% on the year to RSD 164.6 bln.



Source: SORS; SeeNews calculations

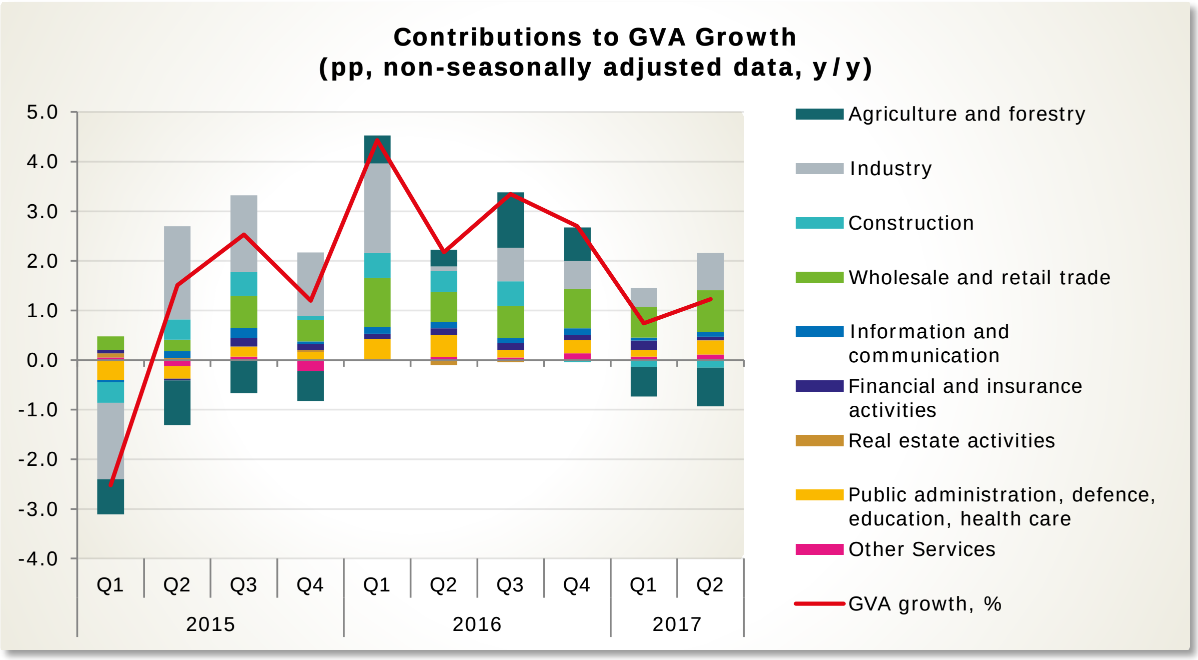
Note: Non-additive data due to direct chain-linking of GDP and its components. Contribution of changes in inventories has been derived as a residual.

The gross value added (GVA) generated by the national economy increased by 1.2% y/y in Q2 2017 and totalled RSD 676.5 bln. The industrial sector inched up in value by 2.8% y/y and accounted for a quarter of the total GVA. The services sector recorded a 2.3% annual increase, slicing a 61.2% share of the total GVA, up from 60.6% in Q2 2016. The agricultural and construction sectors, however, suffered in the period under consideration. Construction sector's GVA decreased by 2.8% to RSD 35.8 bln, while the agricultural sector registered an annual drop of 10.0%.



Source: SORS

In terms of sectors, the largest contributor to GVA growth y/y was retail and wholesale trade with 0.8 pp in Q2 2017. This is expected given the sector's higher correlation to household consumption which increased by 1.1% y/y in Q2 2017. The industrial sector contributed by 0.7 pp to the total GVA growth, while the public administration, defence, education and health care sectors added 0.3 pp to the annual growth in the period. Construction and agriculture sectors took away 0.2 pp and 0.8 pp, respectively, from the overall GVA growth.



Source: SORS; SeeNews calculations
Note: Non-additive data due to direct chain-linking of GDP and its components.

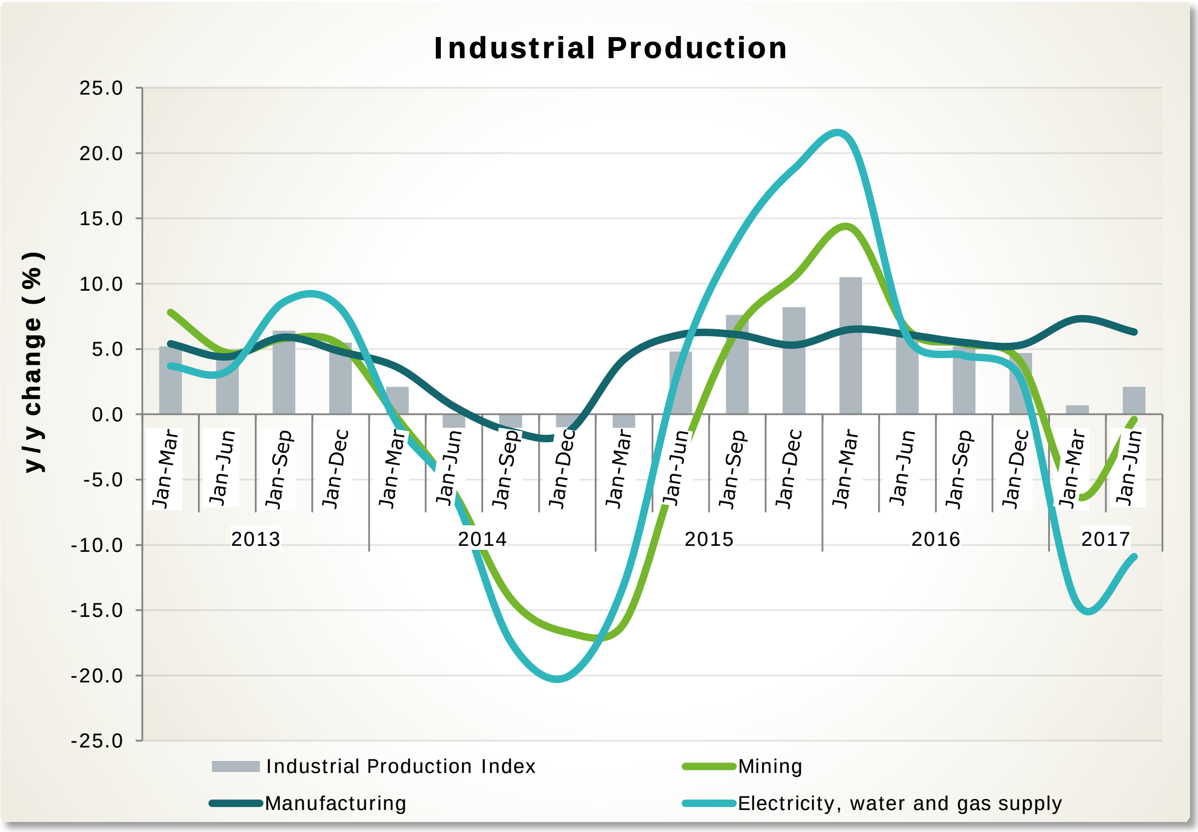
2.2. INDUSTRIAL OUTPUT

Industrial output growth slowed to 2.1% y/y in Q2 2017 on weak electricity, water and gas supply sector

The industrial output slowed its pace of growth to the minimal 2.1% in Q2 2017 from 6.1% y/y in Q2 2016, according to data from SORS.

The country's industrial production was negatively affected by weaknesses in the mining and quarrying, and electricity, water and gas supply sectors, which slumped by 0.4% y/y and 10.9% y/y, respectively.

On the other end was the manufacturing sector, which posted an annual rise of 6.3% y/y.

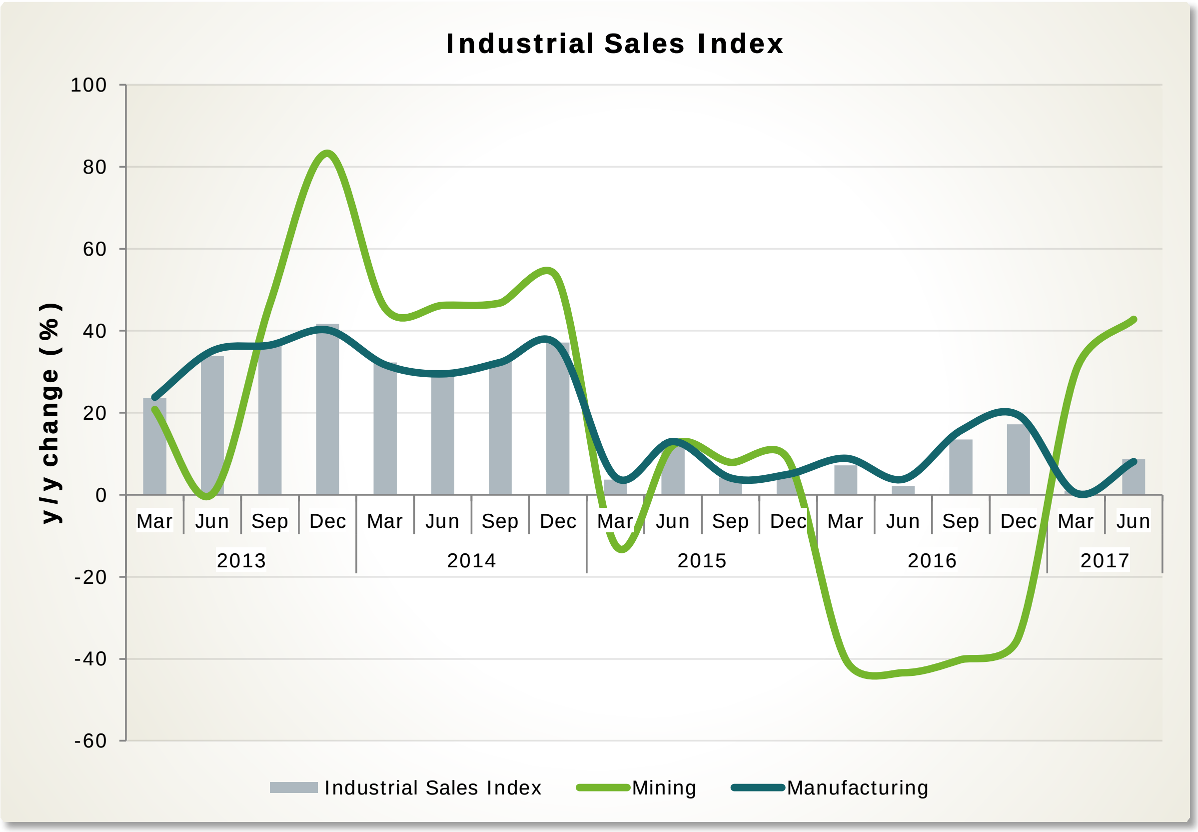


Source: SORS

2.3. INDUSTRIAL SALES

Industrial sales grew by 8.7% y/y in June 2017

The industrial sales increased incrementally in June, by 8.7% y/y, according to SORS. The manufacturing industry recorded an 8.1% annual increase in sales in June, while the mining sector posted a 42.8% annual rise.



Source: SORS

2.4. WHOLESALE/RETAIL

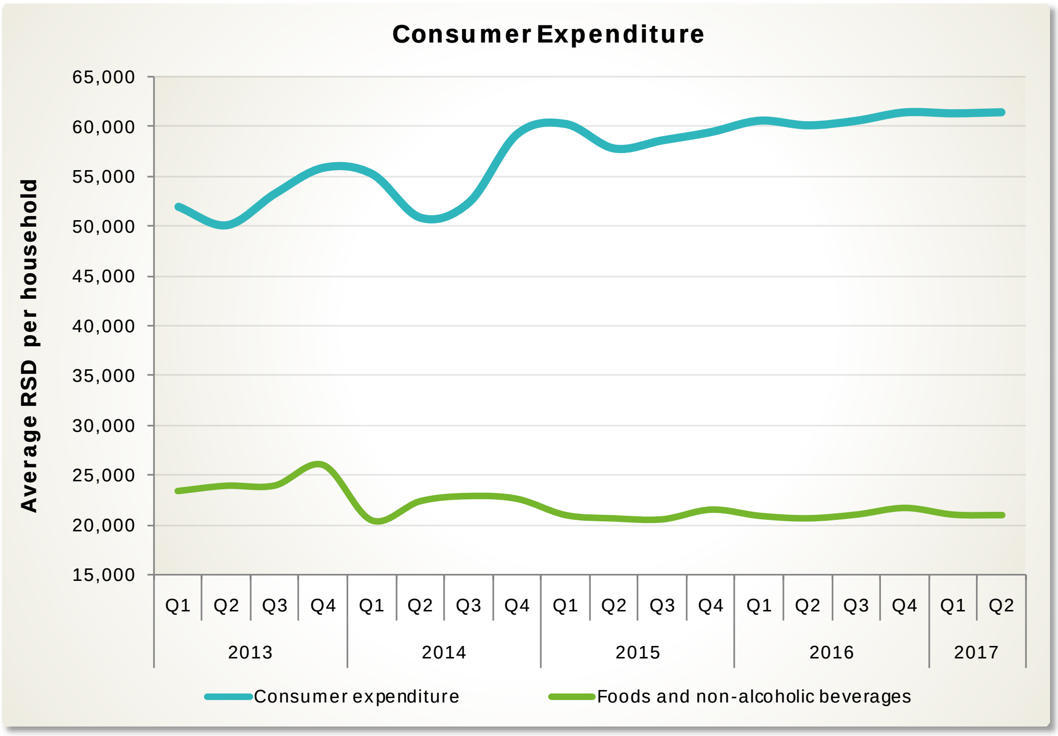
Retail sales grew by 4.7% y/y in constant prices in Jan-June 2017

In the period Jan-June 2017, retail sales in Serbia rose by 4.7% y/y down from 7.4% y/y in the same period of 2016. In June 2017 alone, Serbia's retail sales grew by 5.3% y/y in constant price, according to data from SORS. In current prices, retail sales went up by 9.9% y/y with sales of food, beverage and tobacco increasing by 8.1% y/y, non-food products, except motor fuels rising by 10.8% y/y and motor fuels achieving 12.4% growth due to the oil price recovery on the international markets.

The data for June 2017 indicates that the total value of sales and purchase of agricultural, forestry and fishing products in the Serbia increased by 2.7% y/y at current prices, and by 9.4% y/y at constant prices.

Source: SORS

In Q2 2017, consumer expenditure increased by 2.2% y/y to an average of RSD 61,477 per household. Expenditure on food and non-alcoholic beverages had the highest share in the total consumer expenditure, of 34.2%. The latter increased by 1.5% y/y to RSD 21,008 per household.



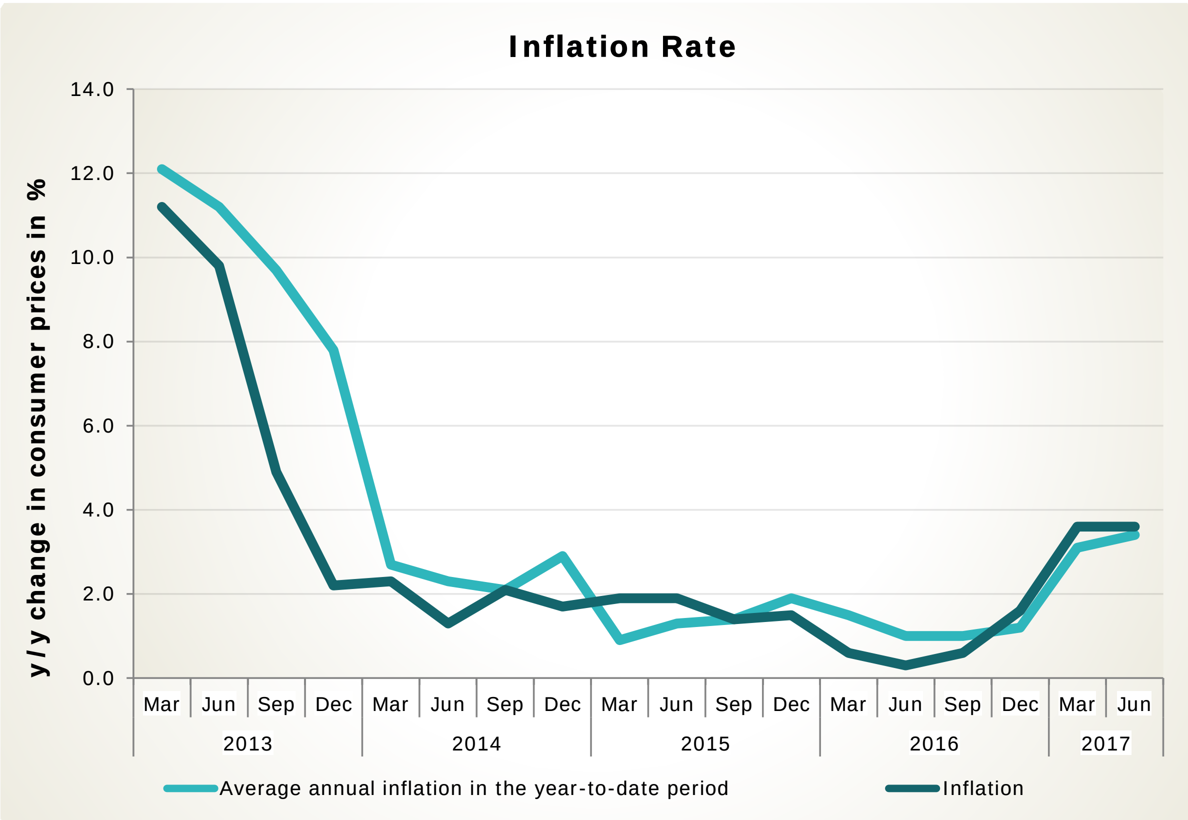
Source: SORS

2.5. INFLATION

Inflation surged in Q2 2017 to 3.4% y/y

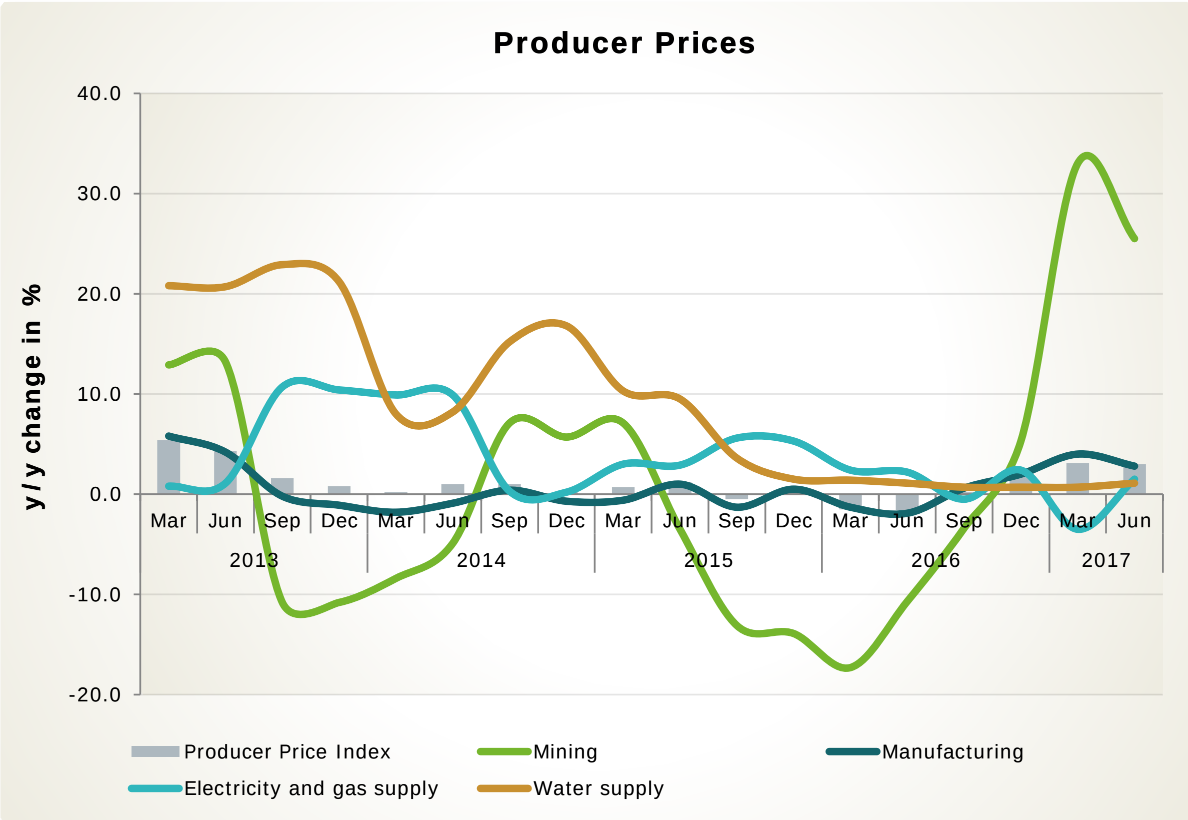
The average annual inflation increased to 3.4% in Q2 2017 from 1.0% in Q2 2016, according to SORS data. Headline inflation also went up, to 3.6% in June of this year compared to 0.3% in the same month of 2016.

Inflation pickup is determined mainly by the increase of consumer prices of recreation and culture activities by 7.6% y/y in the first six months of 2017, followed by transport with 6.5% and alcoholic beverages and tobacco with 6.3% y/y. Clothing and footwear was the only category to post a decrease in consumer prices in H1 2017, of 1.1% on the year.



Source: SORS

Producer prices (PPI) increased by 3.0% y/y in June 2017, according to SORS data. The mining and quarrying sector reported the sharpest growth in producer prices, of 25.5%, followed by the manufacturing sector with 2.8%, while electricity and gas supply sector prices increased by 1.5% on average.



Source: SORS

3. LABOUR MARKET

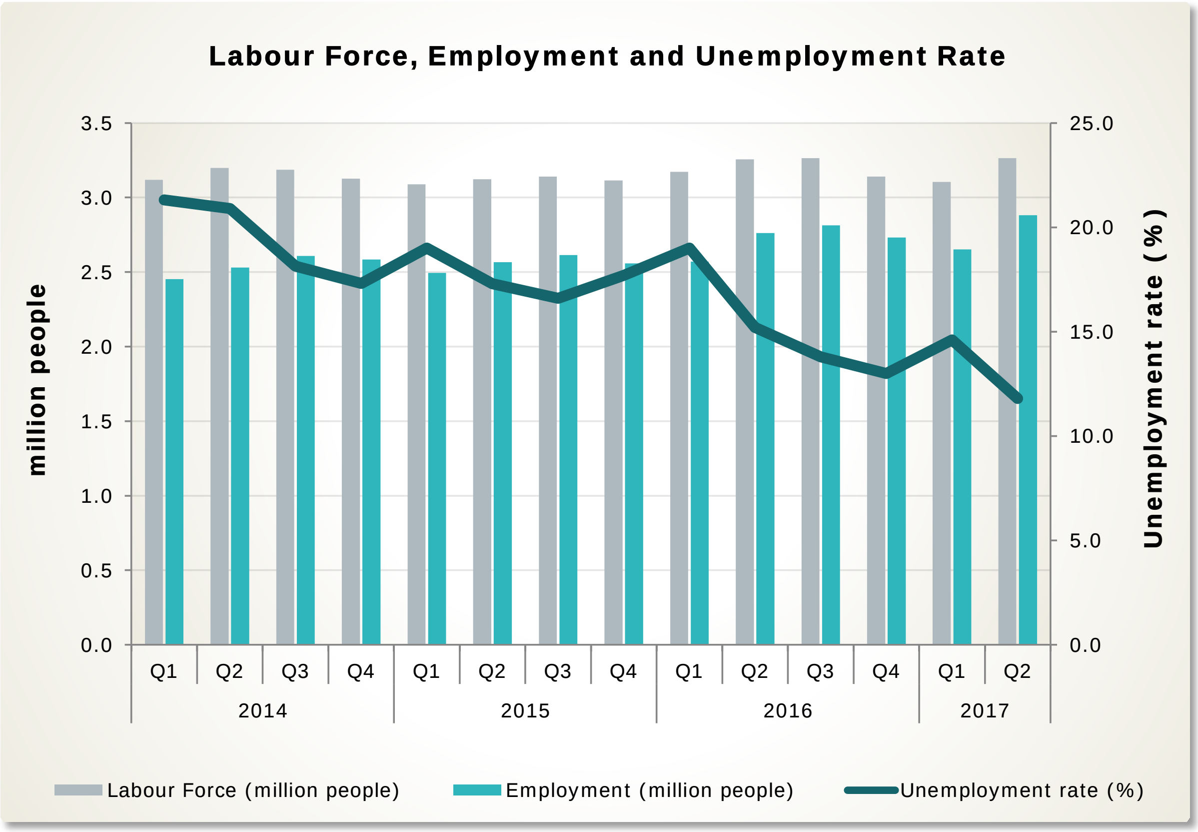
Unemployment rate went down to 11.8% in Q2 2017

Unemployment rate in Serbia decreased to 11.8% of the total labour force in Q2 2017 from 15.2% in Q2 2016, according to data of SORS. On a quarterly basis, the unemployment rate decreased from 14.6% in Q1 2017.

The employed population aged 15 years and older was 2.881 million, up by 4.3% y/y. The rise in employment on an annual basis is due to continued economic growth and stepped-up activities aiming to cope with the grey economy, according to NBS.

Youth (population aged 15-24) unemployment rate also went down, to 28.9%, compared to 37.1% as of March 2017 and 36.1% in June 2016.

The average monthly net salary as of June 2017 was RSD 48,670, up by 4.6% y/y.



Source: SORS

4. CONSTRUCTION AND REAL ESTATE

The number of building permits went up by 51.6% y/y in Q2 2017

The number of permits for new buildings in Serbia was 1,625 in Q2 2017, including 879 for housing projects and 28 for office buildings, according to SORS data.

The total number of permits for new buildings issued in the period under review increased by 51.6% compared to Q2 2016. Permits for housing projects went up by 50%, while permits for office buildings fell by 9.7%.

The total built-up area of office units, covered by the permits, was 20,702 sq m, down by 41.5% on the year. The total built-up area of new housing was 482,316 sq m in Q2`2017, or an increase of 49.8% compared to the same period of the previous year.

5. MONEY SUPPLY AND BANKING SYSTEM

5.1. RSD EXCHANGE RATE

The average exchange rate of the EUR against RSD inched up to RSD 122.9 in Q2 2017 from RSD 123.0 a year earlier, according to National Bank of Serbia (NBS).

Average Annual RSD Exchange Rate			
Foreign Currency	**Q2 2017**	**Q1 2017**	**Q2 2016**
EUR	122.9	123.9	123.0
USD	111.8	116.2	108.9
GBP	142.8	145.2	156.2
CHF	113.4	115.8	112.2

5.2. MONETARY POLICY

The national bank kept the policy rate unchanged at 4.0%

The NBS Executive Board kept the key policy rate on hold at 4.0% in May 2017 as the bank projects inflation to move within the new target band of 1.5%-4.5% around the bank's target inflation of 3.0%. The NBS expected that the gradual increase in domestic aggregate demand and inflation in the euro area would have a more inflationary impact in the period ahead, while the high base effect of petroleum product prices would act as a damper.

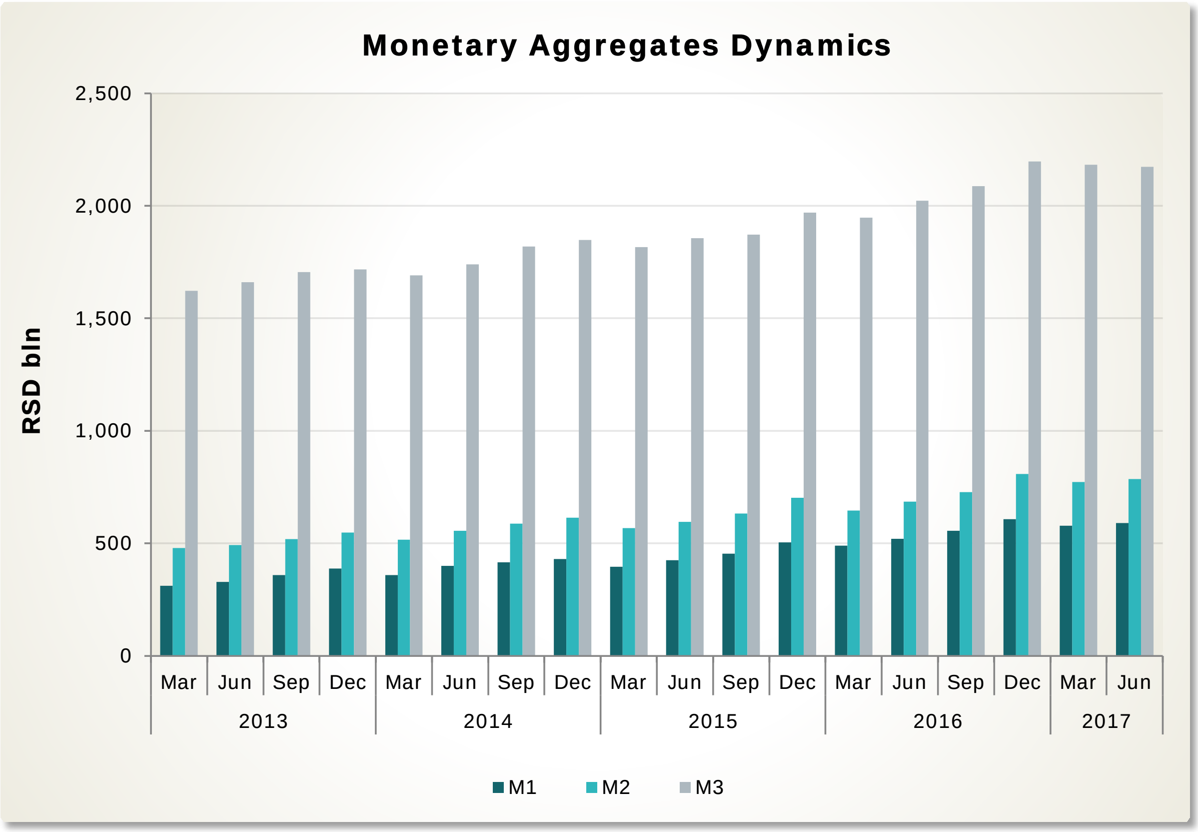
5.3. MONETARY AGGREGATES

Money supply growth was 7.4% y/y at the end of June

Broad money (money aggregate M3) increased by 7.4% y/y and reached RSD 2,173.3 bln as of June 2017, according to data provided by NBS. Growth in monetary aggregate M3 was driven by high growth in RSD and FX deposits of corporates and households, resulting from the economic growth and at the same time signals future economic strength.

The M2 money supply also grew, by 14.6% y/y, to RSD 785.2 bln.

Money aggregate M1, or narrow money, jumped by 13.3% to RSD 589.7 bln.



Source: NBS

5.4. BANKING AND INSURANCE

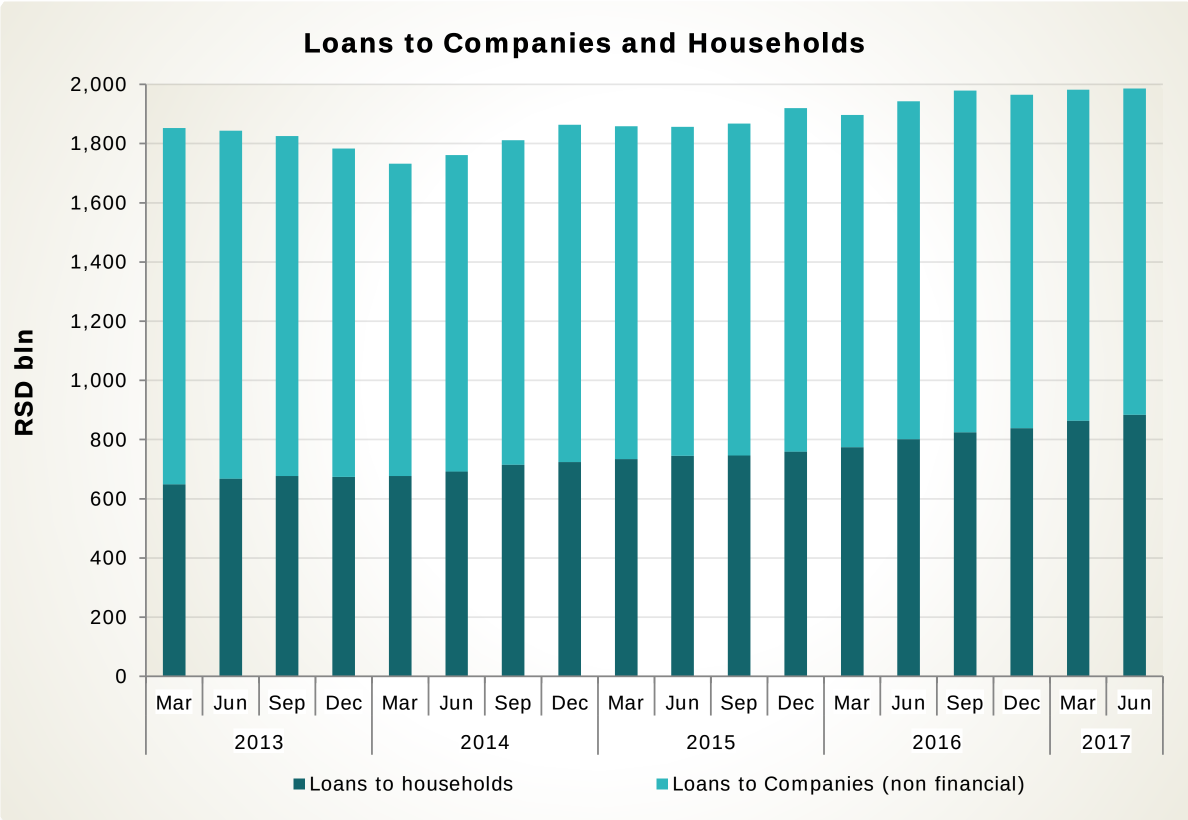
Household loans increased by 10.3% y/y in June 2017

Loans to the non-government sector totalled RSD 1,985.8 bln as of June 2017, up from RSD 1,942.8 bln a year earlier, according to NBS. Loans to non-financial corporations went down by 3.4% y/y to RSD 1,102.3 bln.

According to the August 2017 NBS survey, banks relaxed credit standards for SMEs in Q2 2017 primarily due to interbank competition, less expensive sources of funding and higher risk propensity, which, together with further growth in economic activity, should contribute to the easing of standards that is also expected in Q3 2017.

Household loans rose by 10.3% y/y to RSD 883.5 bln in June 2017, predominantly supported by cash loans, and increasingly more by elevated housing lending, according to NBS data. House purchasing loans grew by 1.6% to RSD 358.6 bln on higher refinancing of existing housing loans, given the considerable decline in interest rates in 2016.

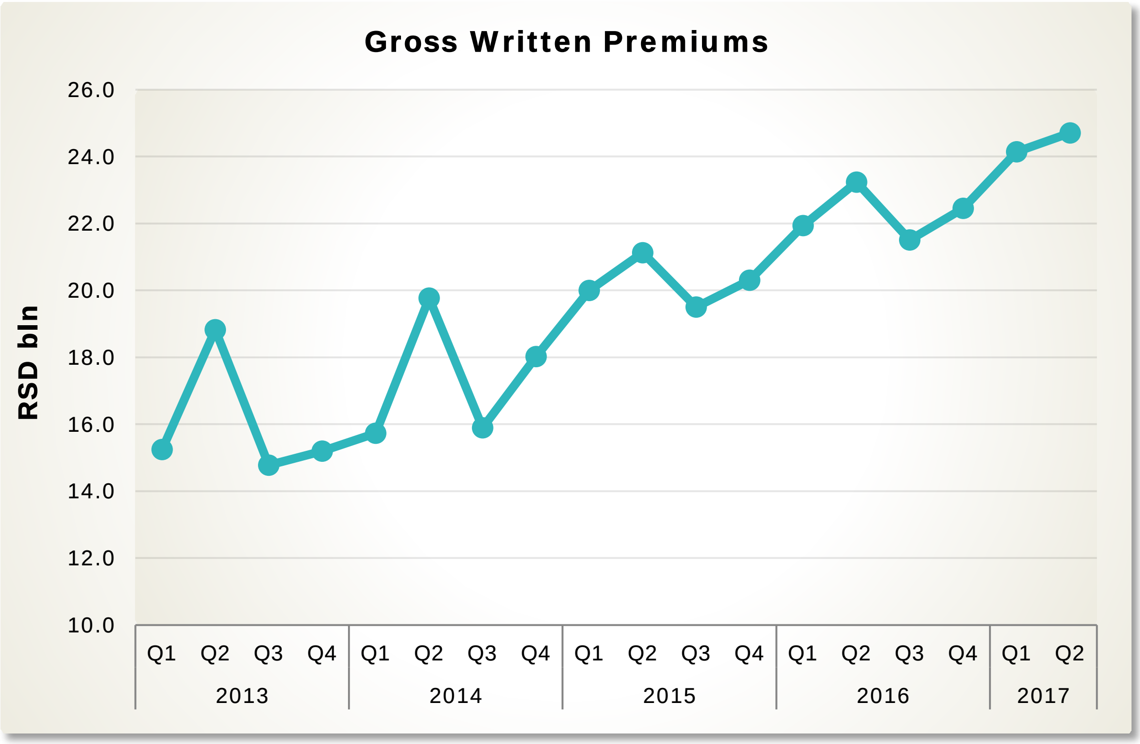
Consumer loans decreased by 0.2% on the year and stood at RSD 20.4 bln. According to the August 2017 bank survey of NBS, the easing of credit standards for households continued in Q2 2017. Standards were eased primarily under the sway of interbank competition and by less expensive sources of funding, more favourable outlook in the real estate market and positive expectations regarding economic activity. There was a considerable increase in demand, primarily for those loans for which standards were relaxed the most – cash loans and refinancing loans, as well as FX-indexed housing loans. Loan demand was pushed up mostly by the need to refinance current obligations and purchase real estate, and by the rise in private sector employment and wages.



Source: NBS

Insurance premium income up 6.3% y/y in Q2 2017

The total gross written premiums of the non-life and life insurance companies were RSD 24.710 bln in Q2 2017, up by 6.3% y/y, according to NBS data.



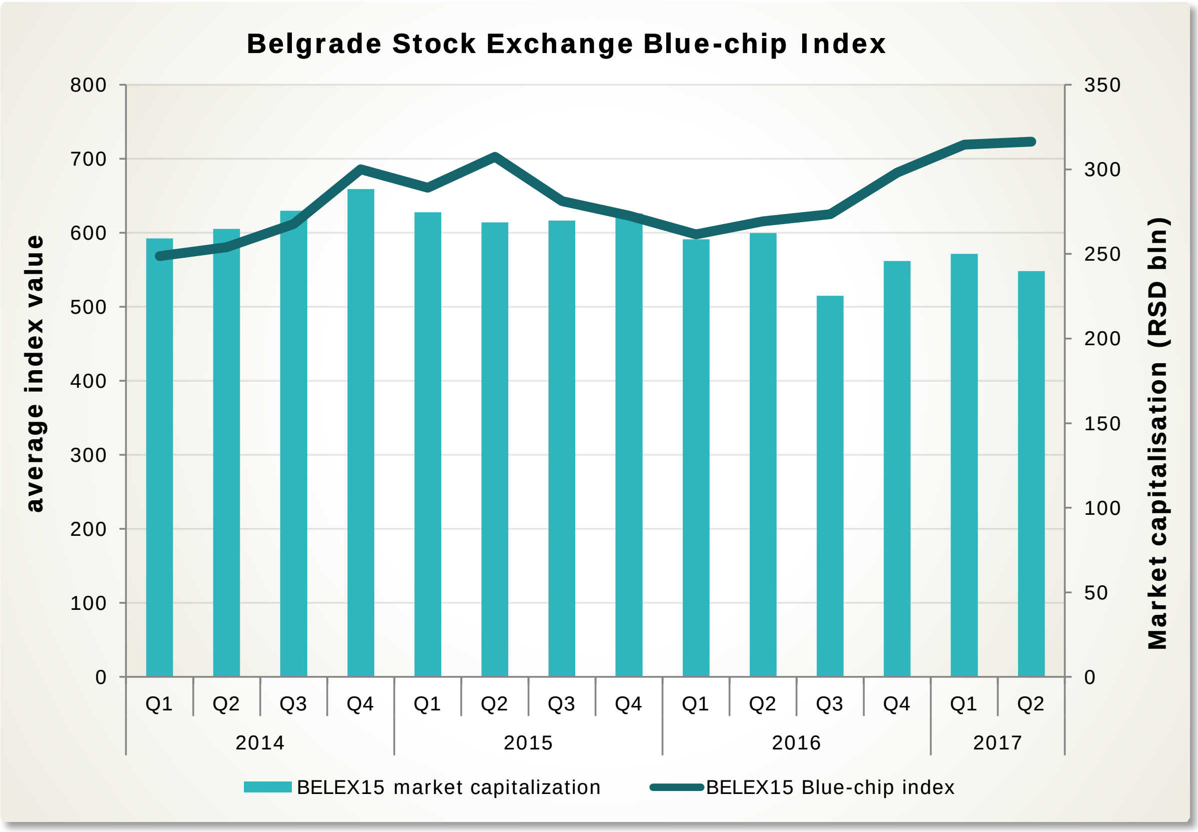
Source: NBS

6. CAPITAL MARKETS

Blue-chip index BELEX15 went up by 0.6% q/q in Q2 2017

The average value of BELEX15, the blue-chip index of the Belgrade Stock Exchange (BELEX), increased by 0.6% q/q to 723 points in the second quarter of 2017.

The total turnover of BELEX increased by 17.7% q/q to RSD 14.979 bln in Q2 2017. The number of transactions was 16,272 versus 19,390 a quarter ago.



Source: BELEX

7. EXTERNAL SECTOR

7.1. FOREIGN DEBT

The gross external debt inched down 0.8% y/y to EUR 25.425 bln at end-June 2017

The gross external debt decreased by 0.8% y/y, totalling EUR 25.425 bln at the end of June 2017, according to NBS. In comparison to March 2017 the gross external debt inched down by EUR 0.701 bln.

Source: NBS
Editor's note: No data is available for gross external government debt for June 2014

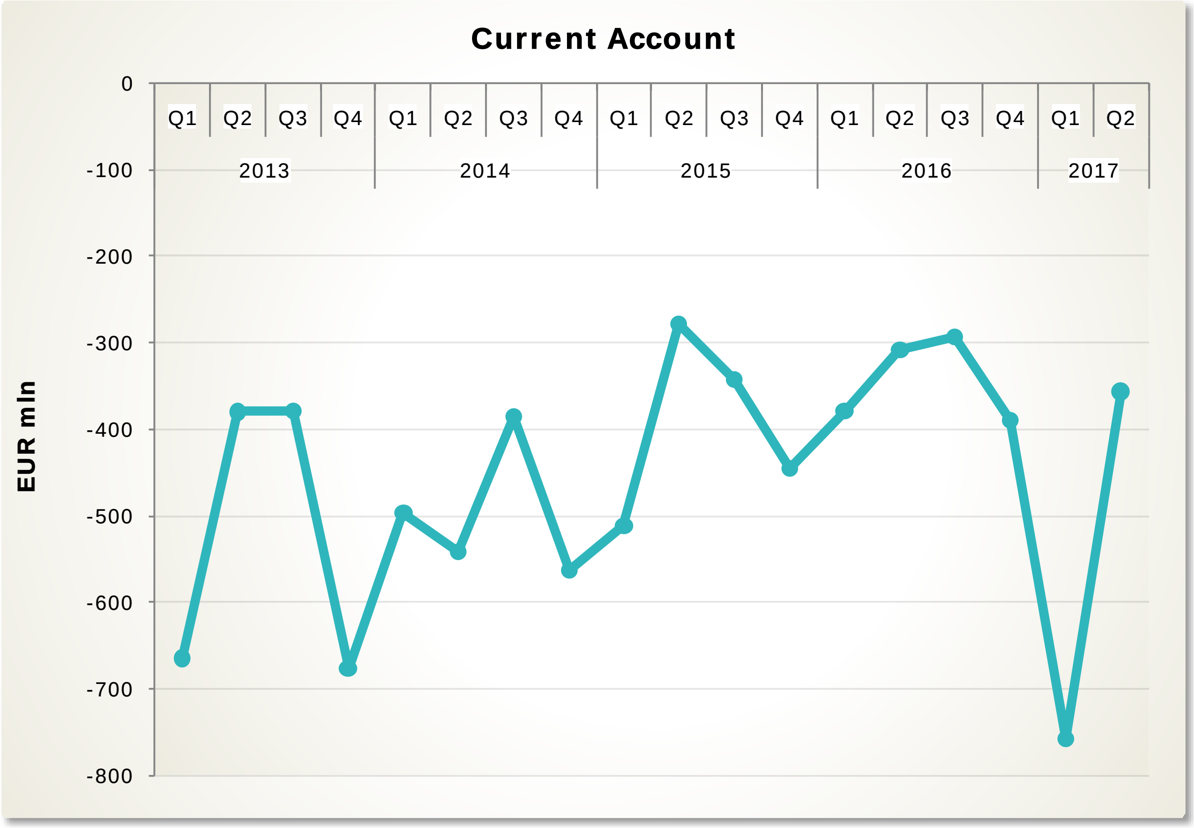
7.2. BALANCE OF PAYMENTS

Current account gap expanded y/y in Q2 2017 on worsening trade balance

For the second quarter of 2017, the current account deficit came in at EUR 356.0 mln, according to central bank data. The increasing current account gap was a result of the worsening trade deficit.

According to a World Bank forecast, the current account gap is expected to worsen to 3.9% of GDP in 2017 and 4.9% of GDP in 2019 from 3.2% in 2016.

Secondary income in Q2 2017 amounted to EUR 947.1 mln, up from EUR 894.8 bln in Q2 2016, or a 5.8% increase on annual basis.



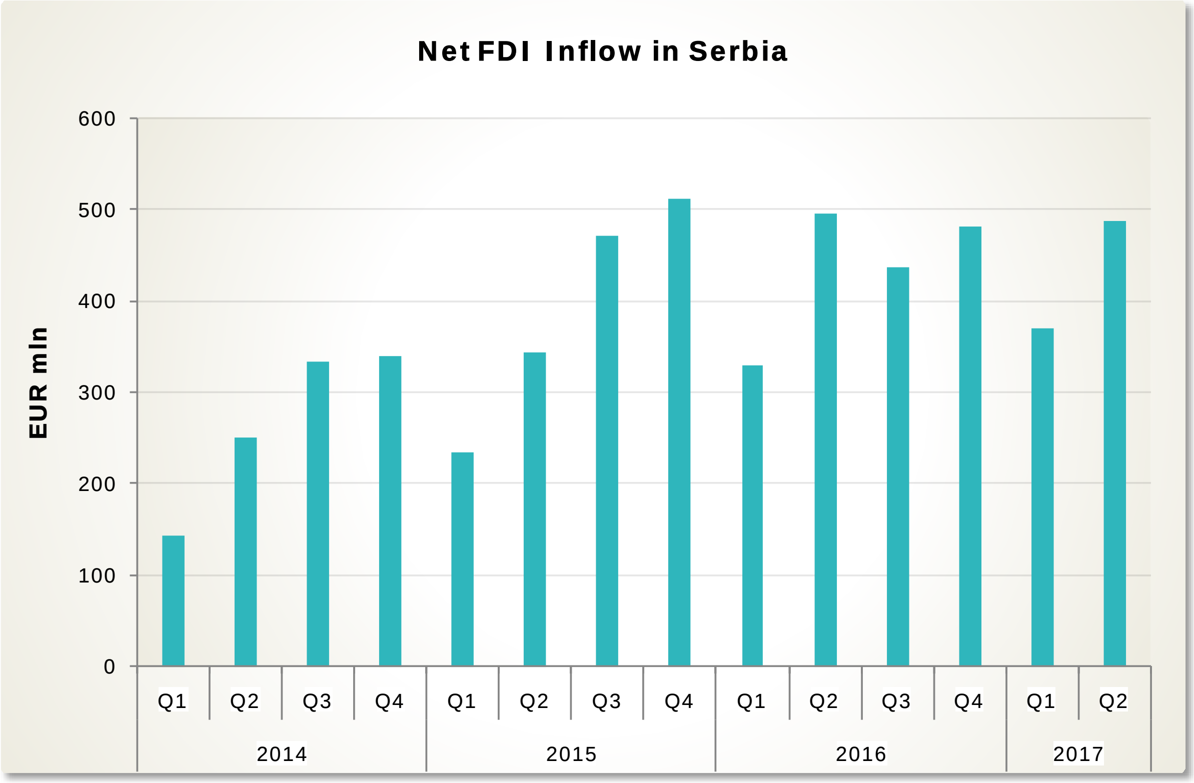
Source: NBS

7.3. FDI

Net FDI inflow stood at EUR 487.3 mln in Q2 2017

The net Foreign Direct Investments (FDI) inflow in Serbia in Q2 2017 totalled EUR 487.3 mln, according to NBS. The bulk or 70% of the investments came from EU members and 12% from Asian countries, such as China, Taiwan, Hong Kong and UAE. The largest amounts were invested in manufacturing, the financial sector, construction and trade.

The National bank of Serbia expects net FDI flows into the country in 2017 to amount to EUR 1.7 bln, encouraged by the macroeconomic stability, continued structural reforms and the improvement in the investment climate.



Source: NBS

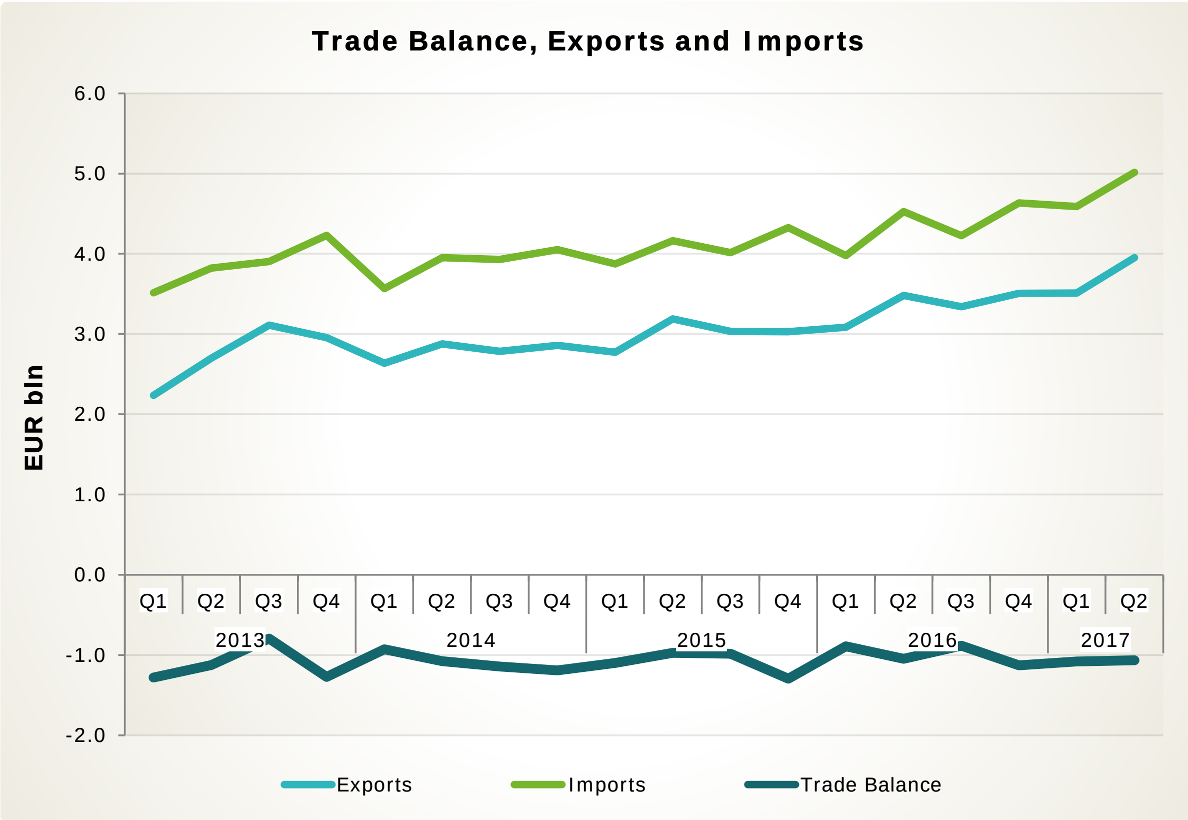
7.4. FOREIGN TRADE

Foreign trade deficit rose by 1.7% y/y in Q2 2017

The trade deficit stood at EUR 1.065 bln in Q2 2017, up by 1.7% compared to the same quarter of the previous year, according to SORS.

In the period April – June 2017, exports totalled EUR 3.951 bln, up from EUR 3.479 bln a year earlier, while imports grew by EUR 490.3 mln to EUR 5.016 bln.

Exports grew by 13.6% y/y in Q2 2017, almost at the same pace as the 13.8% y/y in Q1 2017. Imports, however, decelerated the pace of growth to 10.8% y/y from 15.2% y/y in the previous quarter.



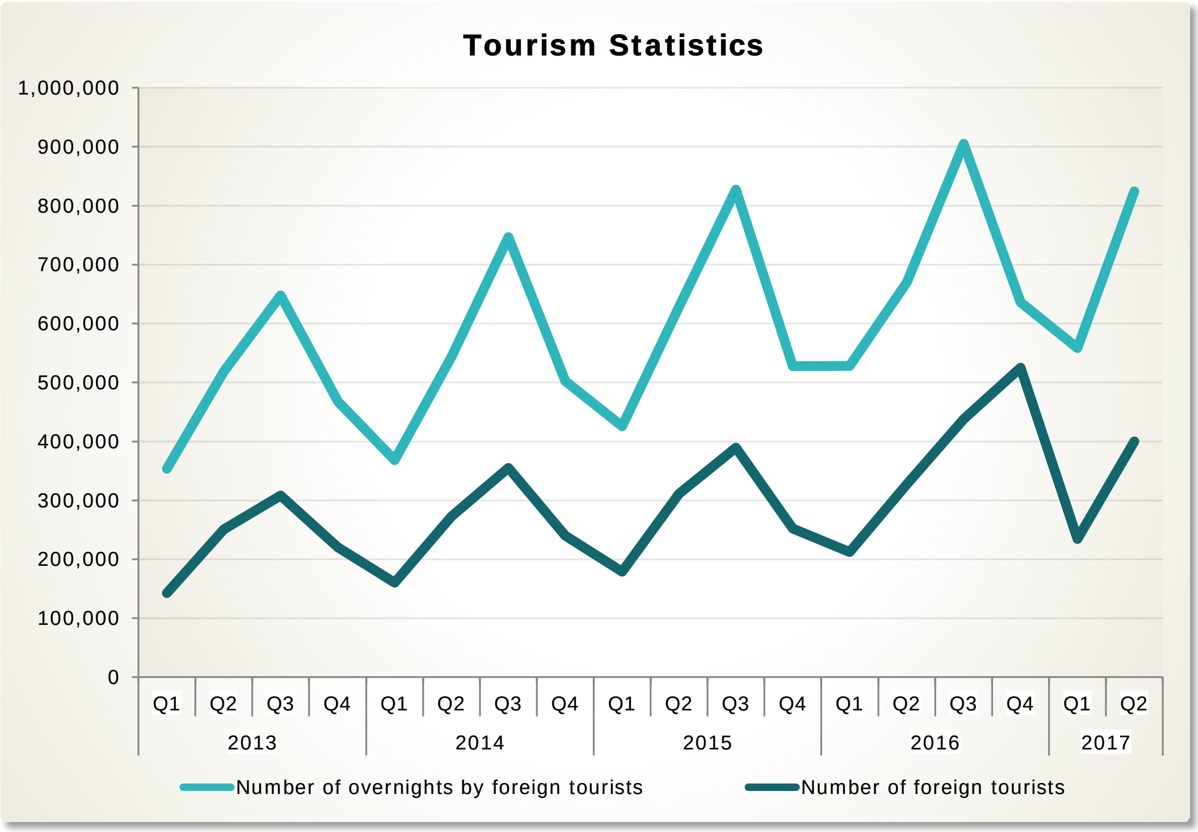
Source: NBS

7.5. TOURSIM

Number of foreign tourist overnights rose by 23.1% y/y in Q2 2017

Tourist overnights of foreigners increased by an annual 23.1% y/y to 824,221 during the second quarter of 2017, slicing a 36.6% share of the total number of tourist overnights in the country, according to SORS data. The total number of tourist overnights jumped by 15.0% on the year to 2,249,336.

The number of foreign tourists also went up by 22.2% y/y to 399,924. Most foreign tourists visiting Serbia in Q2 2017 came from Bosnia and Herzegovina – 7.3% of the total, followed by tourists from Turkey, which accounted for 6.4% and Slovenia with a 6.1% share.



Source: SORS

8. MAJOR DEVELOPMENTS

Serbia opens two more chapters in EU accession talks

June 21, 2017

The European Commission (EC) said it has opened two more chapters in the membership negotiations of Serbia during the Serbia-EU Intergovernmental Accession Conference in Luxembourg.

Read the full story here

S&P affirms Serbia ratings at 'BB-/B', outlook stable

June 19, 2017

Standard&Poor's Ratings Services said it has affirmed its 'BB-/B' long- and short-term foreign and local currency sovereign credit ratings on Serbia, with a stable outlook.

Read the full story here

Serbia gets IPA grant in support of SMEs, local administration

June 8, 2017

Serbia's government said it signed an agreement to receive a EUR 96.2 mln grant under the EU Instrument for Pre-Accession Assistance (IPA) to support small and medium-sized enterprises (SMEs) and the local administration.

Read the full story here

EBRD plans to boost annual investment in Serbia

May 23, 2017

The European Bank for Reconstruction and Development (EBRD) intends to increase its investment in Serbia up to some EUR 500 mln annually from EUR 300 mln currently, a senior EBRD official has said.

Read the full story here

World Bank urges Serbia to restructure state firms

Apr 27, 2017

The World Bank has said Serbia needs to focus on restructuring of state-owned companies, including the country's petrochemical industry, in order to lower fiscal risk.

Read the full story here

Serbia to invest EUR 400 mln to revamp 220 km of roads

Apr 6, 2017

Serbian infrastructure minister Zorana Mihajlovic said on Thursday the government plans to invest EUR 400 mln in the rehabilitation of 220 km of roads.

Read the full story here

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