GRAY/20/2830

August 24, 2020

Statement by Mr. Fachada and Mr. Coronel on Republic of Serbia
(Preliminary)
Executive Board Meeting
August 26, 2020

1. We thank staff for the report and Messrs. Inderbinen and Djokovic for their insightful statement. The ongoing COVID-19 shock is having a severe impact on the Serbian economy, affecting the feasibility of the authorities to meet fiscal targets and reform objectives agreed under the Policy Coordination Instrument (PCI) program. Despite the adverse circumstances, performance under the program has remained broadly positive. Against this background, we support the completion of the fourth review under the PCI and the proposed modification of quantitative and reform targets.

2. We commend the Serbian authorities for the appropriate public health and economic response to the COVID-19 outbreak. Economic measures comprised a large and well-designed policy package to provide support to households and firms and increase healthcare spending, including wages for health professionals. It also ensured adequate liquidity in the banking system while relieving bank borrowers. The authorities' actions seem to have been effective in alleviating the impact of the stringent lockdown measures implemented in the period of the state of emergency (mid-March to beginning of May), which severely restricted people's movement.

3. That said, we are somewhat puzzled by the apparent contradiction between the stringency of the lockdown policies adopted by the Serbian authorities during the state of emergency and the relatively mild contraction in economic actively projected by staff for 2020 *vis-à-vis* other European countries. According to data by the University of Oxford's Blavatnik School of Government mentioned in Box 1, Serbia implemented the strictest lockdown measures in Europe—even more severe than in the countries most affected by the COVID-19. However, staff projects a relatively small GDP contraction for Serbia in 2020 (3 percent), compared to double digit drops in countries like Italy, Spain, and France. *Can staff discuss this apparent contradiction? Can the size of the fiscal support and other*

expansionary policies explain the milder GDP contraction in Serbia relative to other European countries?

4. We take note that policy priorities under the PCI have been appropriately streamlined and refocused towards mitigating the impact of the crisis and supporting the authorities' policy response while preserving macroeconomic stability. As expected, progress on fiscal and SOE structural reforms have slowed down, but we are encouraged by the authorities' commitment to accelerate reforms once conditions become more favorable. In parallel, we agree with staff's advice to contain fiscal risks going forward by maintaining a cyclically-adjusted broadly neutral fiscal stance in 2021, keeping public sector wages and pensions under control, and preparing contingency measures if risks materialize.

5. Finally, we missed in the External Sector Assessment (Annex IV) a deeper analysis of Serbia's reserves adequacy, especially considering the *de facto* "stabilized" exchange rate regime. We note that Table 1 (page 28) presents data for the IMF ARA metric, which seems to be based on the assumption that Serbia maintains a floating exchange rate regime. *Staff's further comments about the de facto exchange rate and reserves adequacy would be welcome. Could staff also confirm if the ARA metric presented in Table 1 follows the parameters of the current exchange rate regime?*