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May 14, 2009

Statement by the Staff Representative on the Republic of Serbia
Executive Board Meeting
May 15, 2009

This statement provides information that has become available since the issuance of the staff report. The new information does not alter the thrust of the staff appraisal.

Macroeconomic developments. While most of the high-frequency economic indicators confirm that output dropped sharply in the first quarter of the year, some indicators (industrial production, credit) suggest a leveling off in the decline of economic activity in March. Nevertheless, downside risks remain dominant. Preliminary April data point to an only slight easing of inflationary pressures. The government recently expanded earlier measures to promote lending to corporates and households, with a view to mobilizing up to 6 percent of credit through a combination of interest subsidies, co-financing, and partial credit guarantees. The cost of interest subsidies (0.2 percent of GDP) is included in the revised 2009 budget, and the revised arrangement includes an indicative ceiling on additional public sector guarantees.

Fiscal policy. Preliminary fiscal data received from the authorities for the first quarter of 2009 suggest that the end-March fiscal performance criterion (PC) was met. However, the full data on the observance of the PC and the fiscal indicative target are not yet available.

Financial sector. By May 10, all ten foreign banks that participated in the financial sector coordination meeting in Vienna in late March had provided commitment letters to the National Bank of Serbia (NBS) and will participate in the Financial Sector Support Program. In these letters, the parent banks committed to maintain their external exposure vis-à-vis Serbia, which includes cross-border credit lines, at least at the end-December 2008 level throughout 2009 and 2010, subject to a review at end-2009. Most other foreign banks have also either provided or indicated their intent to provide similar letters. In addition, the NBS, based on end-March 2009 data, will conduct stress tests for all banks operating in Serbia using a uniform methodology and a downside scenario. The need and options for pre-emptive recapitalization will be explored with banks on the basis of these tests. Completion by end-September 2009 of the stress tests for the 12 largest banks (including all foreign bank subsidiaries present at the Vienna meeting) and the four banks with majority state ownership is a structural benchmark under the revised Stand-By Arrangement.

The EBRD recently announced an investment of €45 million in UniCredit Group's units operating in Serbia to boost credit to small and medium-sized enterprises, as part of a broader program for Central and Eastern Europe.