

BTI 2012 | Serbia Country Report

Status Index	1-10	7.51	# 21 of 128	
Political Transformation	1-10	8.05	# 23 of 128	➔
Economic Transformation	1-10	6.96	# 31 of 128	➔
Management Index	1-10	6.06	# 30 of 128	

scale: 1 (lowest) to 10 (highest) score rank trend

This report is part of the Bertelsmann Stiftung’s Transformation Index (BTI) 2012. The BTI is a global assessment of transition processes in which the state of democracy and market economy as well as the quality of political management in 128 transformation and developing countries are evaluated.

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Key Indicators

Population	mn.	7.3	HDI	0.766	GDP p.c.	\$	11281
Pop. growth ¹	% p.a.	-0.4	HDI rank of 187	59	Gini Index		28.2
Life expectancy	years	74	UN Education Index	0.790	Poverty ³	%	<2
Urban population	%	52.4	Gender inequality ²	-	Aid per capita	\$	83.1

Sources: The World Bank, World Development Indicators 2011 | UNDP, Human Development Report 2011. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$2 a day.

Executive Summary

In the period between 2009 and early 2011, Serbia continued its uphill struggle to reestablish itself as a modern European democratic country with a free market economy and adherence to the rule of law, albeit with mixed results. The ruling coalition, dominated by the Democratic Party (DS) of Serbian President Boris Tadic and a government led by technocrat Prime Minister Mirko Cvetkovic faced numerous problems, the most challenging being the reconciliation of Belgrade's ongoing claims on Kosovo, which declared independence in 2008, and Serbia's EU aspirations.

During 2009 and 2010, the government of Serbia initiated major economic and political structural changes in the country and continued the harmonization of its laws with European standards. Serbia's parliament passed a number of long-awaited laws needed for the country's EU integration, including an anti-discrimination law, laws on associations, the status of the autonomous province of Vojvodina, and on the financing of political organizations. On the downside, the government's impotence in reforming its own bureaucracy and improving its capacity to implement new laws became more apparent. In addition, corruption, cronyism and nepotism remain significant problems in Serbia.

Regarding Kosovo, Serbia's official policy stayed the same during this period. Despite the International Court of Justice ruling in 2010 that Kosovo's declaration of independence was not contrary to international law, Serbia continues to negate its former province's statehood. At the same time, Serbia has demonstrated surprising pragmatism regarding Kosovo. Under pressure and influence from some of the European countries and the US, in 2010 Belgrade decided to revoke a controversial and confrontational draft resolution on Kosovo that it had submitted to the U.N. General Assembly and instead agreed to a draft prepared in cooperation with the EU. The new resolution opened the doors to the dialogue on technical issues between Belgrade and Pristina commencing in the first half of the 2011.

The 2008 arrest of Radovan Karadzic, former Bosnian Serb leader and war crimes indictee, brought a new quality to Serbia's cooperation with the International Criminal Tribunal for the Former Yugoslavia in The Hague (ICTY). In December 2009, the European Union accepted Serbia's bid for full membership and, following the positive assessment of Serbia's cooperation with the ICTY presented by the chief prosecutor Serge Brammertz, unblocked ratification of Serbia's Stabilization and Association Agreement (SAA). SAA was one of the key steps in the formal EU accession process. In late 2009, the European Union abolished visa requirements for Serbian citizens and removed restrictions against the Interim Trade Agreement, the trade part of the SAA. In an attempt to improve relations with its neighbors, in 2010 the Serbian parliament adopted a resolution condemning the Srebrenica massacre in July 1995. Facing a lackluster economic recovery in 2010 and growing inflation, Serbia intensified structural reforms and to some extent improved its macroeconomic policy under the watchful eye of the IMF. A number of laws regulating fiscal responsibility have been adopted, followed by the establishment of numerous bodies responsible for fiscal affairs and internal auditing. The ongoing problems in the Eurozone and spillover from the Greek crisis have, conversely, contributed to a massive depreciation of the Serbian dinar, which in 2010 lost more than 10% of its value. In 2009, the IMF agreed a loan of €3 billion to support Serbia's fiscal position. Serbia showed substantial fiscal prudence and implemented a number of measures in compliance with the IMF's fiscal austerity conditions.

History and Characteristics of Transformation

Serbia's transition to democracy and market economy has been fraught with the statehood conflicts that led to the disintegration of the former Yugoslavia and caused a series of wars in the Balkans. The toleration and emergence of political pluralism in the Socialist Federative Republic of Yugoslavia and its six constituent republics brought into power political elites that used nationalist ideologies and stereotypes to advance their nation-state projects. Led by Slobodan Milosevic, Serbia's state socialist party won the first democratic elections in 1990 and sought to retain its political power by reestablishing a centralized federation and blocking economic reform. The political leaders of the republics of Slovenia and Croatia wanted to advance the decentralization and the nonfederal reorganization of the federation, partly in the interest of facilitating market transition and liberalization and partly to exit the federation. Irreconcilable aims and nationalist mobilization led to the collapse of the federation and the emergence of Bosnia and Herzegovina, Croatia, Macedonia and Slovenia as independent states. In Bosnia and Herzegovina, Croatia and Slovenia, wars of different duration and intensity began when the Yugoslav National Army attacked the republics, assisting the rebellions of ethnic Serb communities in Bosnia and Croatia against the secessions.

Facilitated by the wars and nationalist mobilization, Serbia's President Milosevic established a semi-authoritarian system in the remaining parts of Yugoslavia and remained in power until 2000. His regime was based on clientelist networks in the state administration, police, military

and the state-dominated economy. These networks gave Milosevic control over the country's electronic media, the ability to forge election results and the power to effectively divide and isolate the political opposition. Responding to its deepening integration and legitimation crisis, the regime increased political repression in Serbia proper and its violent military repression of ethnic Albanians in Kosovo. The country then slid into a full-scale war. NATO air strikes forced the regime to abandon its control over Kosovo and contributed to the demise of Milosevic. That said, the democratic breakthrough in October 2000 was driven primarily by the united opposition and student protest movement and the electorate's growing discontent with Serbia's worsening economic and social situation.

The Democratic Opposition of Serbia (DOS), a coalition of 18 liberal, social democratic and moderate nationalist parties, won the federal parliamentary and presidential elections as well as the Serbian local and parliamentary elections in 2000. The opposition leaders Vojislav Kostunica and Zoran Djindjic became federal president and Serbian prime minister. Once the governing coalition had achieved its main aim, the overthrow of the Milosevic regime, internal tensions grew over fundamental policy choices. The heterogeneity of the coalition and the assassination of Prime Minister Djindjic in March 2003 limited the government's capacity to sustain its initially dynamic policy of economic and political reform. The breakup of the governing coalition necessitated elections in December 2003, which led to the formation of a four party coalition government headed by Kostunica.

Serbia's state framework has changed several times since the dissolution of communist Yugoslavia. Between 1992 and 2003, Serbia and Montenegro, the two still united republics of the former Yugoslavia, constituted the Federal Republic of Yugoslavia. In 2003, Serbia and Montenegro replaced this state with a more loosely integrated state union mediated by the European Union. The main aims of this union were EU accession and the creation of an internal market in accordance with EU principles and standards. The state union's powers were essentially limited to the enforcement of international law and cooperation with international courts, military issues and defense, standardization, intellectual property rights, statistics, borders, asylum, immigration and visa issues. Following a referendum in May 2006, Montenegro became an independent state and the state union was dissolved.

As a consequence of its military defeat in the Kosovo war, Serbia had to accept a U.N.-led interim administration in Kosovo. This administration has exercised political authority over the territory since 1999, based upon Resolution No. 1244/1999 of the U.N. Security Council. Serbia's government and major political actors interpret this resolution as the legal basis assigning Kosovo to Serbia as the successor state of the state union. Most Kosovo Albanians refuse to be citizens of Serbia because of their experience of violent repression and expulsion under the Milosevic regime. On 17 February 2008, Kosovo declared its independence. Independent Kosovo has been subsequently recognized by the major Western states but Serbia continued to oppose it fervently. The Kosovo conflict continues to burden the consolidation of a market-based democracy in Serbia and the country's path toward membership in the European Union.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 10 (best) to 1 (worst).

Transformation Status

I. Political Transformation

1 | Stateness

Question
Score

The Republic of Serbia has the monopoly on the use of force in its territory, with the exception of its formerly autonomous province of Kosovo and Metohija (in the following: Kosovo), the status of which is disputed. Serbia opposed the Kosovar parliament's declaration of independence in 2008 and sustained its claim on Kosovo. By the beginning of 2011, more than 70 states, including the United States, 22 of the 27 EU members and 24 out of 26 NATO member states had recognized Kosovo as an independent and sovereign state. Serbia's president Boris Tadic stated a number of times that Serbia's position on Kosovo is "set in stone" (i.e., it would never recognize an independent Kosovo). During 2009 and 2010, Serbia, through political, diplomatic and legal means, tried to prevent further recognitions of Kosovo's independence and its membership in a number of international and regional organization, primarily, the United Nations. After initial objections, Serbia accepted formation and establishment of the European Union Rule of Law Mission in Kosovo (EULEX) approved by the European Council in 2007. The United Nations' mission in Kosovo, established under Resolution 1244/1999, continues its presence but operates at a much lower level.

Monopoly on the
use of force

9

Organized crime continues to be one of the biggest obstacles on Serbia's path towards the European Union but improvements in police organization and capacities have reduced its threat to public order and safety. The Serbian parliament adopted a number of laws aimed at fighting organized crime (among others, a law preventing money laundering and the financing of terrorism and, in March 2009, the Law on the Confiscation of Property Acquired through Crime).

Sretko Kalinic and Milos Simovic, some of the most wanted members of the "Zemun Clan," the criminal network responsible for the assassination of former Prime Minister Zoran Djindjic, were arrested in 2010 and their trials are pending. A number of different Serbian criminal gangs (Saric's Clan, The Pink Panther criminal gang) involved in drugs, arms and people trafficking, money laundering

and high-profile jewelry thefts, became notorious during 2009 and 2010. Their almost global connections and reach, from Serbia and the region via Europe to South America, presented a serious challenge to the Serbian police and judiciary, hampering the efforts to pinpoint, apprehend and prosecute alleged perpetrators. A number of substantial reforms and improvements have been undertaken in police organization and management, operational capabilities and technical modernization.

The constitution defines Serbia as the state of the Serbian people and all citizens who live in Serbia. In the 2002 population census, 13.46 % of Serbia's citizens (excluding Kosovo) identified themselves as belonging to national minorities. According to the census, Hungarians in the autonomous province of Vojvodina are the largest national minority with 3.91% followed by the second largest national minority of Bosniaks (Sandzak) who comprise 1.81% of the total population of Serbia. The third largest territorially concentrated minority are Albanians in Preševo Valley (0.82%) (Source: Statistical Office of the Republic of Serbia 2003, figures excluding the territory of Kosovo). Roma also make significant national minority in Serbia. The constitution guarantees to all minorities a number of individual and collective rights. The situation of these groups has improved during the period under review. Political parties of national minorities are represented in parliament. Serbia adopted an anti-discrimination law in March 2009, which banned, among other things, discrimination on grounds of nationality or ethnicity.

In September 2009, the Serbian parliament passed a new Law on National Minority Councils (NMCs). The law clarified the NMCs' competences in education, culture, official usage of language and public information for each of Serbia's national minorities, while, according to Organization for Security and Cooperation in Europe (OSCE), also implementing a more transparent, democratic system of direct elections to select NMCs members. In elections conducted in June 2010, members of 19 national minorities elected their representatives to NMCs. The only council still not formally established is the Bosniak NMC in Sandzak in south-western Serbia. The row between different Bosniak religious factions (one loyal to Sarajevo, another to Belgrade) and last minute procedural changes in the election process introduced by the Serbian government, have blocked the formation of the council and caused turmoil and increased tensions in Sandzak.

To address concerns of the ethnic Albanian minority, the government has established a coordination body for southern Serbia. Government representatives conduct regular consultation with local Albanian leaders in the municipalities of Presevo, Bujanovac and Medvedja, while a local, multiethnic, mixed Serbian and Albanian police force was formed.

Most political elites and a majority of citizens still consider Kosovo to be a part of the Serbian nation-state. Refugees and displaced persons from the former Yugoslavia have been increasingly naturalized under the 2005 Law on Citizenship.

State identity

9

In August 2009, there were 86,336 refugees and 205,835 internally displaced people (UNHCR, 2008). The number of refugees in Serbia significantly decreased in 2009, due to their successful integration and return to their countries of origin.

Serbia is defined by its constitution as a secular state and its society is largely secular. The Serbian Orthodox Church has the largest number of followers (84.98% of Serbia's population), followed by the Roman Catholic Church (5.48%) and Islam (3.2%), (Popular census, 2002). Not all Serbians are, in reality, devoted believers. Religious dogmas have no noteworthy influence on politics or the law. However, the Serbian Orthodox Church has a dominant role in religious, social and political life. Critics have argued that the Serbian Orthodox Church enjoys certain privileges compared to other religious communities. The proper extent of separation between the secular state and the Orthodox Church in Serbia is not, therefore, always transparent and clearly defined.

No interference of
religious dogmas
9

Serbia has a differentiated administration that extracts and allocates state resources throughout the country, albeit with limited efficiency

Basic
administration
10

2 | Political Participation

Elections in Serbia take place regularly at national level. The next general election is due in spring 2012. The last parliamentary and presidential elections were held in 2008 in accordance with European and international standards. The electoral system in Serbia is a purely proportional system, practiced in a single constituency with 250 seats and a 5% electoral threshold. In order to enhance the political participation of minorities, Serbia abolished the electoral threshold for parties and coalitions representing ethnic minorities. Nevertheless, by allowing parties to distribute arbitrarily mandates among the candidates on their lists after the election, the system gives political parties rather than citizens the power to decide which individuals are elected. This provision was intended to eliminate practices of vote buying and deals over changing of party caucus. International organizations, however, criticized it for blurring the transparency of the electoral process. In 2011, Serbia took heed of that criticism. Parliament endorsed amended a law on the election of deputies and changed the disputed legal provisions, introducing "closed lists." The same law has eliminated yet another controversial convention, the practice of blank resignations, which could formerly be handed by the elected members of parliament to their respective parties. Blank resignations were seen as another mechanism used by Serbia's parties to discipline their deputies as they could use them to strip disloyal deputies of their mandates. These changes were one of the preconditions for Serbia's potential candidate status for membership of the EU.

Free and fair
elections
9

Serbia's democratically elected government has the effective power to govern and the parliament, through its parliamentary defense and security committee, which has democratic and civic oversight of the army and the secret services. As a part of final stages of the defense reform, a number of new laws including The National Security Strategy, Defense Strategy, Law regulating the Military Security Agency and Military intelligence Agency, were adopted in October 2010.

Effective power to govern

9

The government appointed an inspector-general of military secret services, in charge of supervising the work of the secret services and controlling its legality. The parliamentary defense and security committee is, among other things, responsible for monitoring and scrutinizing secret service, army and police activities, and the legality of their operations. He is also responsible for compiling reports for the parliament. In 2010, the European Commission expressed the view that civilian oversight of the Serbian security forces, including the work of the relevant parliamentary committee, needed to be reinforced.

The freedoms of association and assembly are constitutionally guaranteed and in place and are generally respected. In July 2009, the Serbian parliament adopted a law on associations. The law stipulates that the establishment and legal status of associations requires only three natural or legal persons. The rights of the activists of Serbian lesbian, gay, bisexual and transgender (LGBT) groups to exercise openly their freedom of assembly, expression and association are denied, on the other hand, by the high level of homophobia and prejudices in Serbian society.

Association / assembly rights

9

Serbia's constitution grants freedom of expression, and this is generally respected. Simultaneously, different political and economic groups and individuals, using their financial, party or official influence to protect and/or promote their own agenda and interests, frequently violate the freedom of a national media already suffering under a weak regulatory framework. In the opinion of the surveyed senior media editors in Serbia, compiled by the OSCE, the situation regarding media freedom has deteriorated since 2008. According to the survey, conducted in December 2009 and January 2010, two thirds of the 210 respondents (66%) felt that the freedom of their media outlet had been restricted in 2009 in one way or another.

Freedom of expression

7

During 2009, the number of physical and verbal attacks on journalists in Serbia halved in comparison to the previous year (146 according to South East Europe Media Organization, SEEMO). In 2010, courts in Belgrade ordered the arrests of two individuals suspected of beating up Teofil Pancic, a political columnist at the weekly Vreme. Another court gave a prison sentence to a football fan for making death threats against Brankica Stankovic, a journalist on Belgrade's independent radio station B92 in December 2009. Serbian and international media associations and institutions, on the other hand, complained that police and prosecutors made no progress in the investigations of the murders of journalists that took place in during the 1990s and in 2001. Serbian media outlets, pluralist in essence, are in many cases

financially weak and dependent on economic interest groups. State-owned media receive strong financial and other support from the government. The majority of printed media and broadcasters receive no government subsidies and are almost entirely in private hands. In July 2010, Serbia's Constitutional Court strengthened the legal basis of media freedom by declaring that some parts of the amended law on public information adopted in August 2009 were unconstitutional. This particular law was widely criticized by Serbian and international media activists, organizations and NGOs. Critics argued that some of the amendments introduced could lead to the introduction of increased self-censorship and even the closure of some media outlets. In its ruling, the Constitutional Court ruled that the law's provisions (restricting the right of domestic legal persons to establish a public outlet and introducing high financial penalties for rather vaguely defined libel) were not in accordance with the constitution and international conventions.

3 | Rule of Law

The parliament and judiciary are fundamentally independent institutions and hold the executive accountable. However, inefficiencies and a lack of capacities as well as a procedural delays and length of court proceedings weaken their powers. The Constitutional Court, established by law in 2008, has 15 judges who are elected by the National Assembly (five), the president of the republic (five) and by the Supreme Court of Cassation of Serbia (five). In its work, the court has been overburdened by a backlog of cases. In 2010, there was a backlog of more than 10,000 constitutional and other complaints previously submitted to the Constitutional Court of Serbia. The Serbian ministry of justice was preparing an amended Constitutional Court Law that would ensure, among other things, increased operational efficiency (allowing judges to deliberate in councils with fewer than 15 members as prescribed by the current law) and guarantee its budgetary independence. A number of laws adopted in 2007 regulated local self-government in Serbia. Although these laws expanded the powers of municipalities by, among other things, entitling them to manage their own property, they still prohibit municipalities from owning their property and deny them fiscal decentralization. In 2010, parliament amended the Law on Regional Development, introducing seven statistical regions in accordance with European Union's common classification of territorial units for statistical purposes. In November 2009, the Serbian parliament approved a new autonomy statute for the northern province of Vojvodina, ending political controversies over the province's degree of autonomy.

According to the Serbian Constitution (Article 91, Paragraph 1) the courts are independent and autonomous in their work. In practice, the judiciary operates relatively independently but its functions are partially restricted by corruption,

Separation of
powers

8

Independent
judiciary

6

nepotism and cronyism, political influences and inefficiencies. The fiscal and administrative autonomy of the courts is limited.

In January 2010, according to the Law on Seats and Territories of Courts and Public Prosecutor's Offices, the new structure of the court network was implemented. Serbia now has 34 basic courts, 26 higher courts, four courts of appeal (in Belgrade, Novi Sad, Nis and Kragujevac), 16 commercial courts, an administrative court and the Supreme Court of Cassation.

In a controversial reappointment procedure, Serbia's judicial self-governing body, the High Judicial Council (VSS), reduced the number of judges from 2,400 to 1,870.

This reduction was decided by Serbia's major political forces during the preparation of the country's new constitution for adoption in 2006. The main motive for reappointing acting judges, according to observers, seems to have been the fear that judges appointed under the Milosevic regime would not be held accountable for biased decisions or malfeasance. The reselection of judges was apparently considered essential to the elimination of corruption.

The professional associations of Serbian judges and prosecutors submitted a constitutional complaint against the laws authorizing the reappointment, arguing that it would risk a politicization of the judiciary and undermine its independence. The Constitutional Court rejected their complaint, and the VSS subjected all judges to a reappointment procedure. By February 2009, the ministry of justice had prepared assessments of all judges, reviewing the number of completed cases and the quality of their judgments. Roughly one third of sitting judges were not reappointed.

Very soon, a number of foreign observers (European Commission, the U.S. State Department) as well as local judges and the Judges' Association of Serbia expressed a serious concern regarding the reselection procedure. The European Union noted that, for instance, the objective criteria for reappointment that were developed in close cooperation with the Venice Commission, were not applied. Judges and prosecutors were not heard during the procedure and did not receive adequate explanation for the decisions made. The Venice Commission also noted the lack of available legal remedies other than an appeal to the Constitutional Court. In January 2010, the High Judicial Council sent an explanation of its decision to all judges who were not reselected but gave no advice on available legal remedies.

Under strong domestic and foreign pressure, particularly from the European Union, on 29 December 2010 the Serbian parliament adopted a modified set of laws dealing with the judiciary, including amended laws on judges, the public prosecutor's office, the High Judicial Council, the State Prosecutorial Council and the organization of courts. In February 2010, more than 820 judges who were not

reappointed filed complaints with the Constitutional Court. In two cases, the Constitutional Court has ordered the High Judicial Council to reconsider their applications.

Serbia has established and, in 2009, improved the legal framework needed for combating corruption and abuse of power (inter alia, an amended civil service law, a law on free access to information and the Criminal Procedure Code) albeit with limited effectiveness. There was a widespread perception of rampant corruption and impunity at all government levels among Serbia's citizens. According to one survey, 82% of participants considered political life as the most corrupt in Serbia (TNS/Medium Gallup, March 2010). Corrupt officials are prosecuted under existing laws, but are often able to ward off corruption charges using political influence and legal and procedural loopholes. The courts have successfully prosecuted only a few high-profile cases. The government, keen to show its commitment to fighting corruption, put on trial the former mayor of Zrenjanin and prominent politician of the governing DS arrested in 2009 on charges of abuse of office and accepting and offering bribes. In 2010, the former minister of defense was indicted and the ex chief of Serbian railways was arrested for suspected abuse of power. In 2011, a deputy minister for infrastructure and energy was arrested for participation in the allegedly rigged privatization of one company. In October 2008, the Serbian parliament adopted a new law on the prevention of conflicts of interests, which, among other things, provide monitoring for the National Strategy for the Fight against Corruption. The new Serbian Anti-Corruption Agency (ACA), which became operational from January 2010 onwards, is responsible for preventative measures and the supervision of conflict of interest cases and funding of political parties. According to an EU report, the ACA received asset declaration from around 16,000 of the 18,000 officials who were required to submit declaration. In line with the ACA's mandate, officials who hold multiple government positions were required to decide which one of these they would continue to perform. However, in 2010, the Serbian parliament amended the anti-corruption law to allow state officials to hold multiple, directly elected state functions for a two-year transition period. Some of the newly established anti-corruption bodies (including the ACA) were under-staffed, under-equipped and lacked adequate premises. In their joint 2010 report on Serbia (Support for Governance and Management) the OECD and European Union also noted a lack of clear elaboration of protection for whistleblowers that to some extent diminishes the likelihood of implementing the obligation to report on corrupt practices. In 2010, the government drafted a new law on the financing of political activities, aimed at introducing more transparent financing for political parties and effective control of parties' expenditure.

Roma, women, lesbian, gay, bisexual and transgender people, and national minorities still face discrimination in Serbia, as do journalists, human rights activists and disabled people. A number of verbal and physical assaults and acts of

Prosecution of
office abuse

6

Civil rights

8

vandalism against members of ethnic Hungarian and Croatian minorities in Vojvodina province were recorded in 2009 and 2010.

International human rights organizations and state institutions also highlighted the fact that the Roma continued to be the most vulnerable minority community and target of verbal and physical harassment from ordinary citizens, police violence and societal discrimination. During the period covered by this report, a number of Romanis were subjected to a numerous racially motivated verbal and violent physical attacks. The large number of Romani face sub-standard living conditions, deprived of regular medical care, education and job opportunities. In 2009, Serbia adopted a Strategy for the Improvement of the Status of Roma that envisaged measures to be taken in the areas of education, employment, personal documents, social insurance and care and healthcare.

Domestic violence remained a serious problem in Serbia. In 2010, almost 1,600 women in Serbia were registered as victims of domestic physical or sexual violence perpetrated by men but it was assumed that the real number was much higher. According to the Serbian ministry for work and social policy, 32 women were killed in 2010. In almost 70% of cases, the suspects were the victim's husband, partner, father or son. In 2011, the government adopted the National Strategy for the Prevention of Violence against Women in the Family and in Partner Relationships. There were also reports on the number of cases of police abuse and brutality.

Serbia has continued to improve further its institutional and legal framework to protect civil rights. During 2009 parliament adopted an anti-discrimination law, officially banning acts of discrimination based on racial, national and sexual orientation, among other grounds. It also passed a law on gender equality and a law on national councils of ethnic minorities. In May 2010, the Serbian parliament, following the provisions of the anti-discrimination law, appointed its first independent and autonomous commissioner for the protection of equal rights.

The government also took efforts to improve the share of national minorities in public administration, the judiciary and the police, particularly in ethnically mixed Vojvodina province and southern municipalities of Bujanovac, Presevo and Medvedja, where a large number of ethnic Albanians live. Parties of national minorities are exempted from thresholds to enter the national, provincial and municipal assemblies.

In June 2010, the first direct elections for the 19 NMCs were held in Serbia. NMCs' main role is to provide consultation on issues concerning the cultural, education and language interests of national minorities. The Serbian ministry for human and minority rights called for new elections to the Bosniak Council in the Sandzak region of southwest Serbia, provoking continued tension between authorities and some segments of Bosniak community.

The Office of the War Crimes Prosecutor and the War Crimes Chamber of the District Court Belgrade have continued their activity in prosecuting war crimes. According to the European Union, progress on domestic cases of war crimes continued to be slow. There are 20 ongoing court cases and investigations against 103 individuals.

4 | Stability of Democratic Institutions

Democratic institutions perform their functions in principle. The role of Serbia's parliament is weakened by inefficient procedures, a lack of capacity, political showcasing and deputies' occasional improper and rude behavior. In February 2010, parliament adopted new law on the National Assembly, granting, among other things, the financial independence of the parliament. New rules of procedure were adopted later that year. The executive branch of government continues to dominate lawmaking because of the pressure of transposing EU rules and speedily fulfilling EU requirements. To avoid obvious inefficiencies in parliamentary work, lengthy debates and polemical disputes unrelated to issues on the agenda, laws were passed by urgent procedure – thereby limiting the scope for substantive debate. Between April and June 2009, for example, parliament adopted 42 laws essential for Serbia's EU integration. According to Serbia's Lawyers' Committee for Human Rights (YUKOM), of 262 laws adopted in the Serbian parliament in 2010, the government drafted 257, members of parliament four and the national bank of Serbia one. In 2010, the Serbian government drafted 263 of 266 laws adopted. The Serbian parliament and its 250 deputies have less than 350 clerical and other administrative staff, which may explain the parliament's weak administrative and professional capacities.

Performance of
democratic
institutions

7

All relevant political and social players accept democratic institutions as legitimate. A traditionalist minority in the Socialist Party of Serbia (SPS) previously refused to accept the legitimacy of Serbia's democratic upheaval in October 2000, but has now apparently lost interest. The Serbian Radical Party (SRS), in contrast, is still committed to the idea of forming Greater Serbia (Program Declaration of the SRS, Article 1) incorporating Republika Srpska, the Bosnian Serb-dominated entity of Bosnia and Herzegovina, Montenegro and territories of Croatia that constituted ethnic Serb settlement areas prior to the wars. The party, however, has lost a significant amount of its influence after breaking away from its moderate wing in September 2008.

Commitment to
democratic
institutions

9

5 | Political and Social Integration

The Serbian party system is essentially established and only moderately polarized, though it is weakly rooted in society and mostly dominated by individual

Party system

8

personalities, many of whom have been active in Serbia's policy for more than two decades. Serbia's ruling coalition can count on 129 deputies in parliament numbering 250 members of parliament. The Coalition for a European Serbia (ZES) led by the center-left Democratic Party (DS) has 78 parliamentary seats, the G17 Plus party of economic reformers 24 (plus one contested) and Socialist Party of Serbia (SPS) and its partner, United Serbia party (JS) 15. Another coalition partner, Party of United Pensioners of Serbia (PUPS) has five members of parliament and two regionalist parties from Sandzak region and Vojvodina province and of the Croatian ethnic party together have seven members.

The SRS was the second largest parliamentary party according to the 2008 election results, winning 78 seats. It was significantly weakened after the defection of 21 deputies who formed Serbian Progressive Party (SNS) in 2008.

The SNS, which declared itself as a "democratic and pro-European" party, was created after political split between the imprisoned SRS Chairman Vojislav Seselj, who is on trial at the ICTY and his Deputy Chairman Tomislav Nikolic, who resigned and formed SNS.

In 2010, the leader of the G17 Plus, Mladjan Dinkic, founded United Regions of Serbia (URS), new, pro-decentralization political coalition of national, regional and local parties. URS aims to articulate the dissatisfaction of disgruntled voters in Serbia's regions who are unhappy with the perceived "Belgradization" of Serbia.

With 30 mandates, the center-right Democratic Party of Serbia (DSS) headed by former Prime Minister Vojislav Kostunica and its coalition partner New Serbia (NS), were less significant and their influence in Serbia's political life has considerably diminished. The current constellation of parties in the Serbian parliament is a further reflection of existing socioeconomic and sociocultural divisions in Serbian society. It pointed to a widening gap between urban and rural Serbia, between the limited number of winners and the growing army of losers in the process of economic transition as well as the apparent precedence of socioeconomic themes over nationalistic issues.

Overall, 23 individual parties were represented in parliament at the beginning of 2011. Bearing in mind the level of fragmentation indicated by the number of parties and the level of alliances, Serbia's political leadership instigated the significant legal changes required for substantial electoral-system reform. In 2009, parliament adopted a law on political parties that imposed stricter conditions for the registration of political parties, requiring 10,000 (instead of 100) signatures of adult citizens every eight years in order to register and prove the continued activity of the party.

In a wake of the world economic crisis and dire local economic problems, unemployment and often unsuccessful privatizations, trade unions in Serbia emerged as the most outspoken, although not the most successful and influential

interest group. Trade unions are also relatively weak and were often engaged in disputes with each other. Workers and trade unions who are trying to resolve grievances seek direct contacts with responsible ministers or even President Boris Tadic in most cases.

The number of strikes in Serbia during the first quarter of 2010 reached 107, an average of 10 – 30 every month. In January 2011, strikes organized by education and police trade unions seeking wage increases took place. The Independent Socioeconomic Council (SES), comprised of government representatives, employers and trade unions was established as a facilitator of socioeconomic dialogue. SES apparently failed to establish itself as a credible institution of interest mediation and economic policy coordination.

Business interests are organized in a system of local, regional and national economic chambers that function as interest associations with voluntary memberships, introduced in 2009 by an amended law on economic chambers. Serbia's Chamber of Commerce has, in the meantime, indicated its willingness to draft a new law, which would introduce compulsory membership. Proponents of the changes insist that planned modifications would be in accordance with European Union's recommendation that the Chambers of Commerce of Slovenia and Macedonia return to the principle of compulsory membership.

In spite of that, a number of oligarchs and senior managers in some publicly owned companies wield extended, non-transparent influence in Serbia's domestic business sector, and apparently, its political environment. The links and connections between business tycoons and political parties are non-transparent.

The concept of democracy is consensually embraced and the constitutional framework is fully accepted. According to research published in Belgrade's Faculty of Political Sciences Yearbook 2008 and compiled by the Serbian political scientist Zoran Stojiljkovic, representative opinion polls suggested that 56% of Serbian citizens consider democracy, with all its flaws, better than other forms of government. Almost 15% of Serbs were dissatisfied with democracy and 28% have no clear stand on it. Another poll (by the Centre for Free Elections and Democracy, CESID, summer 2009), showed low trust and confidence in specific democratic institutions. The highest degrees of confidence Serbian citizens have resides in the Serbian Orthodox Church and the army, at 39% and 27% respectively. Serbs apparently have more trust in their president (17%) than in their government (7%) or parliament (2%) and 52% have no trust and confidence in the judiciary.

There is a rather strong and, in a number of cases, long-established layer of autonomous, self-organized groups and organizations but the level of trust they enjoy among the population varies from case to case. The new law on associations adopted in 2009 provides a complete legal framework for the creation, status and

Approval of
democracy
9

Social capital
6

operation of associations in Serbia. Many NGOs – particularly those receiving foreign donations and addressing war crimes – often face public criticism and animosity as they are perceived as anti-Serbian and exponents of foreign tutelage or improper meddling in Serbia’s internal affairs. Rather more popular in public were fledgling NGOs dealing with consumer rights, ecology, personal information privacy and animal welfare. Nevertheless, a relatively small number of citizens participate actively in their work. According to public opinion research conducted in 2009 by CESID, slightly less than half of surveyed citizens have little or no confidence in NGOs and 29% of people have formed no opinion. The European Bank for Reconstruction and Development (EBRD) and World Bank “Life in Transition” Survey, updated in June 2010 showed that only 35% of Serbian citizens believed that people could be trusted today. In 1989, the level of confidence in other people was, according to survey, much higher and reached nearly 70%.

II. Economic Transformation

6 | Level of Socioeconomic Development

With a gross national income of \$10,380 (World Bank Indicators, 2010, or \$6,000, GNI Per Capita, Atlas method, 2009), Serbia kept its position among the upper-middle income countries of the world. Serbia ranks lower than Slovenia, Croatia and Montenegro but higher than Macedonia and Bosnia and Herzegovina. Social exclusion is quantitatively and qualitatively on the increase and absolute poverty in Serbia, as it was indicated in the official data, showed a growing trend over 2008 – 2010. According to the Statistical Office of Serbia, in 2010, 9.2% of the total population (which reached 7,307 million in January 2010) is living below the absolute poverty level, because their consumption per consumption unit was on average under the poverty level of RSD 8,544 (\$123) per consumption unit. The percentage of poor people grew from 6.9% in 2009 to 9.2% in 2010. The vast majority of the poor, according to the same data, are people living outside the urban area in larger households or in households whose head is unemployed. On the other hand, the Gini coefficient of income inequality increased to 37 in 2007 only to drop to 28 in 2008 (World Bank data). Although lower numbers represent greater equality on the Gini coefficient, in the case of Serbia they could also suggest a relatively equal distribution of poverty. According to the concept of the relative poverty line (at a threshold of 60% of median consumption per adult equivalent), 18% of Serbia’s population were exposed to the risk of poverty in 2008 and 2009 (First National Report on Social Inclusion and Poverty Reduction in the Republic of Serbia, March 2010). Serbia’s HDI value for 2010 is 0.735 (positioning the country at 60 out of 69 countries and areas characterized by high human development, HDI

Question
Score

Socioeconomic
barriers
6

Report 2010). However, the consequences of the global economic crisis (economic growth decline) and government structural reforms, particularly in the public sector, strongly affected some of the other indicators of social exclusion in Serbia. In October 2010, the rate of unemployment reached 20% (around 730,000 unemployed individuals, more than half of them women). The number of employed persons in 2010 decreased by 4.9% on the previous year's total (Labor Force Survey). Many unemployed and even employed persons and dropouts from the official statistics work in the informal sector, which is estimated to employ 800,000 people (Serbian Association of Employers, June 2010 survey). Due to economic downturn experienced in 2009 and, to some extent, in 2010, regional disparities both in employment and unemployment rates that were already significant were further aggravated.

Economic indicators		2007	2008	2009	2010
GDP	\$ mn.	38952.1	47760.6	40147.7	38423.2
GDP growth	%	5.4	3.8	-3.5	1.0
Inflation (CPI)	%	6.4	12.4	8.1	6.1
Unemployment	%	18.1	13.6	16.6	-
Foreign direct investment	% of GDP	8.7	6.3	4.8	3.5
Export growth	%	17.2	8.9	-14.9	19.1
Import growth	%	26.0	9.3	-22.9	4.1
Current account balance	\$ mn.	-6889.8	-10394.8	-2866.5	-2819.3
Public debt	% of GDP	35.2	33.4	36.8	44.0
External debt	\$ mn.	26122.1	30406.1	33111.5	32221.8
Total debt service	\$ mn.	3232.0	4734.7	4644.4	4304.6

Economic indicators		2007	2008	2009	2010
Cash surplus or deficit	% of GDP	-0.9	-1.7	-2.6	-
Tax revenue	% of GDP	23.6	23.1	22.5	-
Government consumption	% of GDP	20.6	20.1	20.2	19.2
Public expnd. on edu.	% of GDP	-	4.7	-	-
Public expnd. on health	% of GDP	10.1	10.0	9.9	-
R&D expenditure	% of GDP	0.35	-	-	-
Military expenditure	% of GDP	2.5	2.3	2.3	-

Sources: The World Bank, World Development Indicators 2011 | International Monetary Fund (IMF), World Economic Outlook 2011 | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database 2011.

7 | Organization of the Market and Competition

Serbia has established an institutional framework of market competition since 2000, but the scope of the large informal and state sectors remains significant. The existing and vast state sector has more than a half a million employees, claims huge economic resources and continues to produce significant losses – worth 1.9% of GDP in 2008. The size of the informal economy in Serbia is large and, according to some estimates, close to 34% of GNP. According to the World Bank’s 2011 “Doing Business” report, Serbia’s overall world rank was 89 out of 183 countries. Serbia is, based on its business environment, ranked behind FYR Macedonia, Montenegro and Croatia and in front of Bosnia and Herzegovina and Kosovo. According to the 2010 index, Serbia ranked at 83 for “Starting a business,” 176 for “Dealing with construction permits,” 100 for “Registering property” and 94 for “Enforcing contracts.” Entrepreneurial decisions continued to be constrained by legal uncertainty, widespread corruption and red tape. Determined to attract more FDI, Serbia’s government introduced state budget subsidies (i.e., financial incentives for investment in manufacturing, the tertiary sector and R&D that granted specified amount of euros per job created).

In July 2009, the Serbian parliament adopted new laws on the control of state aid and the protection of competition in order to comply with EU competition policy rules. The new law on the protection of competition provided criteria for the definition of relevant markets, which were more precise, and granted extended powers to an independent Commission for the Protection of Competition. The most important new legal provision was the commission’s right to penalize any breaches of the market and impose fines on companies violating the competition rules. The Commission for the Protection of Competition keeps track of notified agreements

Market-based
competition
6

Anti-monopoly
policy
8

and of participants who have a dominant position in the market, and organizes, undertakes and supervises the implementation of measures to ensure the protection of competition. The decisions of the commission are subject to judicial control. Nevertheless, the commission suffers from insufficient institutional support and its work is severely constrained by numerous regulations exempting specific activities from competition. Some sectors of Serbia's economy like food production, retail outlets, and supermarket chains are still characterized by strong and widespread oligopolistic or monopolistic ownership structures. Many of the Serbia's best pieces of commercial land were allegedly also in possession of a small number of individuals and large, privately owned companies.

During 2009 and 2010 and under significant influence of its international partners, mainly the EU, IMF and World Bank, Serbia continued its thorough implementation of substantial trade and liberalization reforms and deregulation. In its 2009/2010 World Trade Indicators Serbia Trade Brief, the WTO highlighted Serbia's reduction of tariff and non-tariff barriers, elimination of import quotas, reduction of import licensing requirements and restructuring and simplification of customs procedures. Serbia is, on the other hand, more protective of its agricultural goods than on its non-agricultural ones and uses high import duties to ring-fence its agricultural sector.

According to the Serbian Chamber of Commerce, only 2% of goods (among other things, weapons, mineral goods, and precious metals, some chemical and agricultural products) were placed under a restrictive import or export regime that requires appropriate import or export permissions. Serbia has a preferential trade regime that applies to Russia, Belarus, Turkey, Kazakhstan, the European Free Trade Agreement members (EFTA) and Central Europe Free Trade Agreement (CEFTA, 2006) signatories. Bilateral trade relations between the European Union and Serbia were embodied in the SAA signed between the EU, its member states and Serbia in 2008. Due to an extended process of SAA ratification among EU 27 member states, an interim agreement on trade-related matters has been in operation since 1 February 2010 allowing for the early implementation of the trade provisions of the agreement. From 1 January 2009, Serbia unilaterally applied the reduction of customs duties for EU imports envisaged in the agreement. Under the agreement, Serbia had a transitional period of six years to phase out gradually tariffs on all industrial goods and duties for about 75% of agricultural products originating in the European Union (The EU Integration Office of Serbia). The agreement also stipulates that duties on some agricultural products will remain between 20% and 80% of their 2008 levels even after six years. In 2010, exports and imports to and from the European Union comprised 57.4% and 54.9% of total exports and imports respectively (Serbian Chamber of Commerce data). In January 2011, the European Union and Serbia signed a market liberalization agreement, part of Serbia's accession to the WTO.

Liberalization of
foreign trade
9

The banking system and capital market are differentiated and oriented to international standards. According to the EBRD, the Serbian banking system “has continued to cope well with the effects of the financial crisis and the system overall is highly liquid and well capitalized.” Serbia also witnessed a consolidation of its restructured and privatized banking sector marked by the further diminishment of state ownership. In 2010, according to the Association of Serbian Banks, about 80% of the banks’ total capital is foreign-owned. The data provided by the National Bank of Serbia (NBS, the central bank) indicated that of the 33 banks operating in Serbia in 2011, 21 are in the hands of foreign shareholders (mainly French, Italian, Austrian and Greek), eight have majority state ownership and four are majority owned by domestic private individuals or legal entities. NBS has also showed prudence and caution in supervising Serbia’s banks. Thanks to the high compulsory reserves imposed by the NBS, banking sector capitalization was relatively high. IMF data shows that the capital adequacy ratio (CAR) in Serbia is 21% and that all systemic banks maintain CARs above the 12% prescribed minimum (8% as prescribed by the Basel Standard). However, the interest rates on bank loans in Serbia remain high mainly because of high inflation and the NBS’s key policy rate. Loans denominated and indexed by foreign exchange still comprised the lion’s share of the total loans. The euroization is high at 80% of loans and 70% of deposits and is the legacy of years of macroeconomic instability, hyperinflation in the 1990s and recent negative interest rates on dinar deposits (Serbia Banking Sector Soundness and Stress Testing, IMF and World Bank, 2010). On top of this,, general macroeconomic deterioration, exchange rate depreciation and loan-repayment problems caused by the crisis resulted in an increase of non-performing loans (NPLs), mainly to the corporate sector. According to the Association of Serbian Banks, the share of NPLs in overall lending rose to over 17% in 2011 as a further confirmation of significant exposure to foreign-exchange denominated and indexed loans among local firms and households. In adherence to the government’s de-euroization strategy and in full awareness of the currency risk for households and domestic firms, the NBS has promoted lending in dinars by subsidizing only dinar-denominated loans and by actively encouraged dinar lending. Foreign banks have kept up their earlier public commitment (via the 2009 Vienna Initiative, which has in the meantime expired) to maintain their exposure to Serbia.

Banking system

8

8 | Currency and Price Stability

The control of inflation and an appropriate foreign exchange policy are recognized goals of economic policy. However, these goals, even with an adequate institutional framework, have not been consistently followed. The inflation rate had flared up by October 2010, reaching 8.9% (IMF data) and later 11.5% at the end of 2010 (annual average, Statistical Office of Serbia).

Anti-inflation /
forex policy

8

Serbia's exchange rate regime is a managed float. The Serbian dinar has come under severe pressure in 2010, partially due to wider euro concerns and partially because of a deep-rooted lack of confidence in the national currency. Since the start of global financial crisis in 2008, the dinar has rapidly depreciated and lost nearly 40% of its value against euro (11% between January and August 2010). This rapid depreciation accelerated further after the Greek financial meltdown, and, noted before, contributed to the high inflation rate. During 2009 and 2010, the NBS used its considerable hard currency reserves – estimated to be almost €10 billion – to repeatedly intervene in the foreign exchange market in support of dinar.

Serbia's government is generally committed to macroeconomic and fiscal stability, and mostly follows recommendations from the IFIs – mainly the IMF. The government can also count on installed institutional safeguards but is sometime unable to challenge or resist populist or electioneering policy instigated by some of the members of the ruling coalition. The aftermath of the global financial crisis severely tested the government's commitment. Because of the crisis, Serbia's foreign trade and exports slumped, inflow of FDI diminished, and the market was deprived of liquidity. The government introduced a comprehensive program of measures and activities aimed at cushioning the impact of the crisis. The program itself was largely based on assistance from IFIs. Although the economy recovered after a contraction of 3% in 2009 and grew almost 1.8% in 2010, the remnants of the crisis were still present. In 2010, FDI and other inflows were still low (11% lower than in 2009), the current account deficit reached 7.1% of GDP while the public debt came to 43.5% of GDP (IMF data). Serbia's external debt at the end of 2010 grew further and reached 79.6% of GDP, very close to the level indicating high indebtedness (80%). According to the NBS, external debts of the public and private sector reached 30.4% and 49.2% of GDP respectively. Largely because of the economic crisis and serious concern over its external financing gaps, Serbia signed a €3 billion Stand-By Arrangement with the IMF in 2009 and committed itself to deep spending cuts and budget deficit limitation to 4% of GDP. With the IMF's permission, the projected fiscal deficit was later widened to 4.8%. Serbia has also agreed with the IMF that a 2011 general government deficit would not exceed 4.1% of GDP (prime minister's Letter of Intent to the IMF, December 2010). Seeking to restore further fiscal balance, Cvetkovic's government capped wage and pension increases in January 2011 at 2% and committed itself to limiting the share of salaries and pensions – one of the biggest budgetary expenditures – to 8% and 10% of GDP respectively in the 2011 budget.

Macrostability
8

9 | Private Property

Property rights and the regulation of the acquisition of property are well defined in principle and the legal framework that protects property is in place. The property

Property rights
7

exists in cadaster and in land books. Approximately 60% of all immovable property in Serbia has been registered with the cadaster while the remainder is either registered with land registry departments of courts, or simply not registered at all. The complete cadaster of all immovable property in Serbia should be completed in 2011. Municipal courts and cadastral offices dealing with property registration are highly susceptible to corruption. According to a survey conducted in June and July 2010, of the 81% of persons who have experienced corruption, 15.5% said that bribes were given to staff of the cadaster (Statistical Office of the Republic of Serbia). As an exception to the general rule that foreigners, under reciprocity requirements, may acquire ownership of real estate in Serbia, the Agricultural Land Law of 2006 does not allow foreigners to own agricultural land in the country. Churches and religious communities may claim the restitution of their nationalized property by using a law from October 2006. In 2010, the European Union expressed concern regarding the lack of progress in adopting an adequate legal basis for property restitution in Serbia. Organizations of former owners contested the privatization of some disputed properties. They insisted on the return of properties or, in a case where public buildings have been constructed on the land, they ask for alternative land to be provided. The European Parliament noted in 2010 that 76,000 formal requests for the return of confiscated immovable property had been lodged with the Serbian authorities. Well aware that passing the law on restitution has been one of the important preconditions for Serbia achieving EU candidate status, the government plans to submit the law to parliament in the fall, before the European Union decides on Serbia's request for membership in October 2011.

In 2010, private companies produced 60% of Serbia's GDP but state and socially owned enterprises still comprise a significant share of the economy. Serbia is one of the least privatized countries among the 29 client countries of the EBRD. According to official data (Serbian Business Register Agency), in the first months of 2011 the state owned more than 450 public companies at central and local level (including the electricity operator EPS, the Serbian Telecommunication Company Telekom, Belgrade airport, JAT airline and Serbian Railways) with around 116,000 employees.

The process of privatization in Serbia is often overwhelmed with corruption, cronyism, and a lack of transparency. In some more extreme cases, criminal activity and money laundering are also involved. The EU report on Serbia pointed out that the number of privatizations of socially owned companies annulled due to non-compliance with the contracted obligations rose to almost one quarter of the firms initially scheduled for privatization. The state continues to tolerate the presence of oligopolies in Serbia. In December 2009, the Italian firm Fiat signed an annex to their 2008 joint investment agreement with the Serbian government, clearing the way for a takeover of car producer Zastava Automobili from Kragujevac. Serbia's privatization revenues in 2009, when 95 socially owned companies were sold, stood

Private enterprise

7

at €2.1 million. The sale of a majority stake in the Serbian Telecommunication Company Telekom and privatization of other public enterprises like JAT airlines and pharmaceutical joint-stock company Galenika failed or were postponed due to the lack of interest, poor quality of assets, or unfavorable bids. In accordance with the law on the free distribution of shares in six state-owned companies, the first set of shares in the oil conglomerate NIS and Airport Belgrade were distributed to Serbian citizens and former employees,

10 | Welfare Regime

Existing social safety nets, already under heavy financial strain, were put under added stress by the drop in employment and the dramatic rise in unemployment, which reached 20% in 2010. According to data provided by the National Employment Service, there were 730,000 registered unemployed people in Serbia in January 2011 and more than half were women. The rise in unemployment left its mark on the level of poverty among the most vulnerable community members (i.e., elderly people, the less educated, the young and the disabled). As a group, Roma are particularly disadvantaged. Almost 9% or 650,000 citizens of the total Serbian population of 7,306,557 (national statistical data), were either on the verge of or in the poverty zone. Serbia has an advanced and complex social assistance system rooted in pre-transition practice. Despite this, social assistance, pensions, unemployment and health insurance struggled to compensate for broad social disparities and were limited in scope and quality due to financial constrictions. An average pension in Serbia, in February 2010, was 61% of an average salary, according to government sources. Further reforms of Serbia's pension system must count on the fact that the country's population has been declining since the early 1990s and is rapidly ageing.

During 2009 and 2010, as a result of the economic crisis the government reached an agreement with the IMF to freeze all public pensions. In January 2011 it capped all wages and pension increases at 2%. Despite this, IMF researchers argue that the Serbian pension system will remain one of the most expensive systems in the region in 2011. A number of voluntary private pension funds operate in Serbia but the government was reluctant to introduce mandatory private pension funds. The average life expectancy at birth, which can be interpreted as an aggregate measure of the health system's effectiveness, increased in 2009 to 71.1 and 76.4 years for the male and female population respectively. The average life expectancy in Serbia is still below the estimated 2010 EU averages of 75.7 and 82 respectively.

The laws on employment and unemployed insurance that were promulgated in May 2009 have so far failed to create a more flexible and competitive labor market, mainly because of the harsh economic climate and negative trends on the existing labor market. Laws adopted in December 2010 to amend and supplement the law on

Social safety nets

7

pension and disability insurance introduced, among other things, a gradual increase in the minimum age limit for retirement for men and women, from 53 to 58 years of age, until 2020. Further legal and procedural reforms of the pension system will apparently await the outcome of the next parliamentary elections in spring 2012.

Equality of opportunity is formally granted and is protected by the legal and institutional framework. In 2009, the anti-discrimination law that prohibited all forms of discrimination against individuals and groups in accordance with EU anti-discrimination rules, was promulgated and a new commissioner for the protection of equality appointed. However, in practice the very extent of the problem significantly minimized the new law's effectiveness. The law on gender equality was adopted in December 2009 and, among other things, should provide for the establishment of equal opportunities in the fields of employment, social and health protection, and in political and public life. Although women make up 51.4% of the population (OSCE), they are underrepresented in public positions. For example, 21.2% of Serbian members of parliament (54 of 250 deputies) are women, as are 21.3 % of members of local self-government assemblies. On average, women make 16% less than their male counterparts according to the Serbian commissioner for the protection of equality. The disabled are also among the most vulnerable groups in Serbia. Surveys show that in 2009 80% of people with disabilities were unemployed and almost 70% of them lived in poverty and on social security benefits.

Equal opportunity
7

11 | Economic Performance

Economic fundamentals in Serbia significantly deteriorated when, in the last quarter of 2008, the global economic and financial crisis spilled into emerging markets. In 2009, Serbia's economy contracted sharply and achieved a negative GDP growth of almost 3% although it moderately recovered in 2010 with real GDP growth of 1.76%. According to the IMF's projections, Serbia's real GDP in 2011 may expand to 3%. In the period under review, unemployment increased to almost 20%, notwithstanding the informal sector's influence on lowering that rate. In the same time, CPI inflation fueled by the increase of energy and food prices on world market rose to 10.29% in December 2010 and finally peaked at 11.5% at the beginning of 2011. High inflation and persistent unemployment could undermine Serbia's competitiveness in the international market. According to surveys, the Serbia's current account deficit improved from 17.8% of GDP in 2008 to 7.1% in 2010, mainly due to higher remittances, but also a narrower trade deficit. Serbia's FDI inflows in 2010 reached €61 million (\$1,237.3 million) in 2010 according to Serbia's ministry of finance. By comparison, Serbia's FDI in 2009 reached \$1.9 billion. It is worth mentioning that the government, within the framework of the IMF as stated in EBRD's 2010 report, committed itself to undertaking large-scale public sector reform. Since the global economic crisis in 2008, Serbia's external

Output strength
6

position has improved and further fiscal consolidation might be possible during 2011.

12 | Sustainability

With financial help and expertise from the EU, Serbia administered a number of environmental projects, mainly in the field of waste disposal, recycling and solid and liquid waste treatment. Against this, accelerated economic development, intensive agriculture and outdated technology (mainly in electricity production, chemical plants and copper mines and smelters), have resulted in air, soil and water pollution, energy waste and overuse of pesticides and fertilizers. More than two thirds of Serbia's electricity is generated by thermoelectric power plants, mostly based on outdated U.S. technology, which burn domestic coal. The National Program for Environmental Protection 2009 – 2010 was adopted and the Environmental Protection Agency of Serbia (SEPA) formed in December 2009. SEPA is, among other things, responsible for the development, regulation and maintenance of the national information system for environmental protection and air and water quality monitoring. A year later, the government introduced a National Strategy for the Incorporation of the Republic of Serbia into the Clean Development Mechanism under the Kyoto Protocol.

In December 2010, the Serbian parliament adopted another set of environmental laws required for alignment with EU legislation (for example, the law on air protection and the law on the prevention of environmental noise). After the 1986 Chernobyl disaster, the Socialist Federal Republic of Yugoslavia introduced a moratorium on nuclear power plant construction. To this day the moratorium remains in force.

State and private institutions for education, training and R&D are strong and in some cases quite advanced. Nevertheless, in its 2009 report the World Bank noted that Serbia's education system is performing below international averages when compared both to the OECD and to neighboring countries. In 2011, the government's budgetary spending on education was around 3.3% of GDP, which is much lower than EU average of around 6%–7%. Less than 0.5% of Serbia's GDP is injected into scientific R&D. For years Serbia has been facing a potentially catastrophic brain drain as many educated young Serbians, aware of the lack of job opportunities, leave the country in droves. Of 113 countries surveyed by USAID, only Guinea-Bissau is losing a higher percentage of its educated young people to other countries.

Environmental
policy

7

Education policy /
R&D

7

Transformation Management

I. Level of Difficulty

In Serbia, the structural constraints on governance are moderate. On the one hand, unresolved statehood problems and the economic, social and political legacies of the Yugoslav wars have burdened Serbia's path to democracy and market economy. On the other hand, Serbia's population is relatively well educated and the country's level of economic development has traditionally been relatively high. Serbia's 2010 HDI, according to the 2011 UN Human Development Report, was 0.735 and it ranked at 60 in the world.

Structural
constraints
4

However, the political leadership faces additional difficulties from occasional ethnic tensions in Serbia proper and the negative effects of the semi-authoritarian Milosevic period – such as a distorted, uncompetitive economic structure and widespread corruption.

Serbia has moderately strong traditions of civil society. This was initially because Yugoslavia's socialist system conceded niches for a small segment of urban intellectuals which subsequently headed the opposition protests against the Milosevic regime. In the course of the 1990s they turned into a broad popular movement that involved and mobilized many citizens beyond urban intellectuals. Numerous CSOs have persisted from this period and contribute to public accountability.

Civil society
traditions
4

Serbian society and the country's political elite are polarized along ethnic issues such as Kosovo and to lesser extent Vojvodina, Sandzak and three municipalities in southern Serbia inhabited by ethnic Albanians. Increasingly, more pressing social issues (unemployment, corruption, crime, wages, public services and living conditions) are causing further and deeper polarization and a significant and palpable loss of trust and faith in the political class. The radical political actors who remain and have decreasing influence have continued to mobilize support for ethnopolitical issues, like the notion of "Greater Serbia" or support for alleged war criminals. However, even the proponents of radical nationalistic ideas have noticeably shifted their political agenda towards social issues. Opposition center-right and even far-right parties are increasingly active in criticizing government for

Conflict intensity
3

the perceived failures and hardships of the transition, such as increased poverty, corruption and a lack of jobs.

II. Management Performance

14 | Steering Capability

Question
Score

In the period between 2009 and January 2011, Serbia's political leadership was often prompted by the external stakeholders like the European Union and the IMF to intensify its efforts to build and develop democracy and a market economy. At the same time, the short-term political benefits, coalition parties' interests and electioneering gained advantage over long-term aims, hampering their fruition.

Prioritization
7

The government demonstrated a strong commitment to European integration and to the reforms required to fulfill EU standards regarding democratic principles, the rule of law and a functioning and competitive market economy. Nevertheless, Kosovo remains the major hurdle on Serbia's path to European integration. President Tadic and high-ranking government representatives (e.g., Foreign Minister Vuk Jeremic and Deputy Prime Minister Bozidar Djelic) resolutely stated that Serbia would not join the European Union if that would require acceptance of Kosovo's independence. In practice, the government took some more pragmatic and less assertive steps in dealing with the Kosovo issue. One of these steps was the government's acceptance of dialogue with Pristina on technical issues in 2011. With the exception of an opposition pro-European Liberal Democratic Party (LDP) and a number of prominent public figures, most key political players – particularly conservative and more nationalistic ones – still consider the claim to Kosovo as a part of Serbia to be a more important and politically opportune, vote-winning issue than EU integration.

The Serbian government remains on the path to political stability and reform. It repeatedly declares its full commitment to democracy and the market economy. In 2009 the Serbian parliament adopted 266 new laws, and in 2010, a further 262 and 49 other acts, including the law on the National Assembly, the state budget for 2011 and the abolition of compulsory military service. However, internal political sensitivities, intra- and inter-party differences and disputes involving deeply rooted stakes occasionally slowed down the adoption of the new laws (e.g., the law on restitution). The privatization of large telecommunications, electricity-generation and other public companies has been postponed or stopped, partly due to unfavorable economic climate.

Implementation
7

During the period covered by this report, the governing majority demonstrated its capacity to implement fiscal adjustment measures when the parliament approved a budgetary system law and several other laws to reduce public spending and increase tax revenues in 2009 and 2010. Severe expenditure cuts in public administration as well as a restriction on public sector recruitment were introduced. Income taxes on dividends and royalties, excise taxes, property, luxury car and goods taxes were increased.

The new law on pensions was adopted and government initiatives froze the pensions and salaries of civil servants for 2009 and 2010 while cutting higher salaries in the public sector by 10% – 15%. The government was less successful or became less proactive, in reducing the planned number of public employees by 10% – 13% (current level: 60,000 – 80,000). In October 2010, the Serbian government adopted a bill to limit the number of employees in public administration; it will reduce the number of employees by approximately 3,400. In September 2010, the number of staff employed in the state administration was less than 28,500 according to the government, but the real number could be around 30,000. For example, almost 30 new state agencies were opened, employing nearly 1,300 individuals in total (Serbian Association of Employers). In November 2009, the Serbian parliament finally adopted the autonomy statute for Vojvodina. The statute grants the province extensive autonomy in the areas of local finances and economic development, and anticipated the province's cooperation with the corresponding territorial communities within the foreign policy of Serbia. It also provided for the establishment of Vojvodina's representative offices in regions of other European states and in the European Union. Opposition parties challenged the statute in the parliament, arguing that the document would encourage alleged separatism tendencies in Vojvodina.

Serbia's political leadership quickly adapted its economic policies to the global economic downturn and the decline of foreign capital inflows, although very frequently it did so under indirect or direct cajoling and pressure from the key external actors, mainly the European Union, United States and IMF. At the same time, the government continues to take a rigid position in denying Kosovo independence. This policy ignored the political concerns of the broad majority of Kosovo Albanians. The rationales that motivated major Western powers to recognize Kosovo were usually interpreted as an unjustified anti-Serbian bias and an example of perceived Western double standards.

Policy learning
6

15 | Resource Efficiency

During the period covered by this report, the government of Prime Minister Cvetkovic continued to improve efficient use of human, financial and organizational resources at its disposal, albeit at a slow and uneven pace.

Efficient use of
assets
7

Nevertheless, the government continues to be plagued by persistent and widespread corruption, politically motivated and induced favors, over-staffing and cronyism. Surveys show that, for example, after elections “public companies are essentially horse-traded among the governing coalitions in a bizarrely opaque fashion, and then discreetly re-staffed along party lines” (Local Government and Public Service Reform Initiative, May 2010). Public servants’ jobs are often awarded according to the party affiliation and personal connections rather than the candidate’s professional merit and competence.

The reform of Serbia’s public administration and civil service is patchy at best. During 2009 and 2010, Serbia endorsed an action plan for the implementation of public administration reform and adopted a number of legal acts important for the establishment of a public administration based on the rule of law. However, recruitment decisions in many cases are still in the hands of parties or party loyalists in managerial positions. This harms the professionalism of the civil service and signifies the importance of putting a merit-based career system into practice.

In one of its reports on Serbia in 2010, the European Union concluded that planning and budget formulation is weak and as a result limits both allocative and technical efficiency in delivering services that reflects government policy. In 2009, the IMF commended Serbia for solid advances toward compliance with the IMF’s Code of Good Practices on Fiscal Transparency. It highlighted laws for fiscal management, the establishment of taxpayers’ rights, and adherence to a precise budget calendar. In October 2010, the government endorsed an amended budget system law that introduced rigorous fiscal rules limiting, for example, public debt to 45% of GDP. According to the European Commission, this was an important step towards improving the quality of public finances in Serbia.

By passing a law on local government financing in 2006, Serbia endorsed the implementation of more effective, fairer and more transparent mechanism for financial equalization among local governments. Municipalities may possess and manage their own property, but municipal property has not been clearly demarcated from state property. The draft law on public property and income, which should define republic-owned, provincial and local government property, is still far from completion.

In 2009 and 2010, policy coherence and coordination in Serbia continued to be weakened by the fact that the ruling coalition is composed of multiple parties. This high level of segmentation is a reflection of the balance of power in the coalition, and influenced the shaping of the government. In 2010, Prime Minister Cvetkovic’s cabinet had 27 ministers, four vice prime ministers (including one who was also a deputy prime minister), 24 ministerial departments and one ministry without portfolio. Three of the vice prime ministers were also ministers. This distribution of institutional power between coalition members heavily affects government

effectiveness and efficiency, diminishes its ability to act with one voice and causes overlaps and occasional frictions between the different ministries. The government is, at the same time, prone to compromises struck to water down any serious rifts that could undermine its position. The leaders of smaller member parties in the ruling coalition are mostly engaged as ministers in the government and often use their position to promote their party's policies. In 2010, for example, Mladjan Dinkic, the chairperson of G-17 Plus and deputy prime minister responsible for economy and regional development, opposed the proposed rise in VAT. In 2011, Prime Minister Cvetkovic sacked Mladjan Dinkic and Slobodan Ilic, a member of President Tadic's DS and a high-ranking official in the finance ministry. In the early months of 2011, a government reshuffle took place resulting in a slightly smaller cabinet comprised of 21 members (17 ministries, 16 ministers with or without portfolio and four deputy prime ministers, some of them with ministerial portfolios). The basic reallocation of ministerial jobs among the ruling coalition members stayed the same bar the loss of some of the G17 Plus cadre's posts. While governmental coordination remains hierarchic-bureaucratic, political power evidently lies outside the government, with Serbia's president and DS leader, Tadic. On the positive side, now that the DS is a key player in the ruling coalition and a main actor in the government, Serbia's earlier experience with inter-party conflicts and unsuccessful cohabitations between presidents and prime ministers from different political groups has ceased to be a problem. In addition, the requirements of EU integration have, to some extent, improved inter-ministerial coordination and cooperation.

Most integrity mechanisms function with limited effectiveness in Serbia. In December 2005, the government adopted the National Anti-Corruption Strategy, which was translated into an action plan in late 2006. In 2008, the law on the Anti-Corruption Agency was passed by the parliament and the agency became operational in January 2010. As an independent and autonomous body the Anti-Corruption Agency is responsible for the implementation of its strategy and action plan, the enforcement of regulations relating to conflict of interest resolution for officials in all branches of the government and the implementation of regulations governing the financing of political parties and election campaigns. Nevertheless, a new national strategy was being envisaged in 2011, even though the Anti-Corruption Agency reported that only 15% of the existing strategy had been implemented. The European Union and other IFIs stated in unison that some progress can be reported in the introduction of good practices in public internal financial control in Serbia. A central harmonization unit for internal audit was established in late 2009. The State Audit Institution (SAI) was established four years earlier and has been operational since 2007. The SAI produced its first audit report on the government budget in 2009 for the first time since 2001. Research done by the European Union has showed that SAI reviewed aspects of expenditures in bodies responsible for approximately 50% of central government expenditures in

Anti-corruption
policy
6

2008. The audit report was sent to the parliament but the legislature did not exercise its full powers in terms of scrutiny (perhaps because this was the first time an audit report had been presented in the parliament). However, EU observers noticed that the SAI acted upon its own report. In February 2010, the SAI took 19 individuals (including 11 current and former ministers) to court based on the findings of the 2008 audit, which revealed their misconduct in the operations of the BSL, public procurement regulations and budget decrees. In 2010, internal audit units were established in only four ministries (defense, finance, work and social policy, and youth and sports).

16 | Consensus-Building

Democracy and the market economy are fundamental consensual pillars on which current political leadership in Serbia bases its operational and strategic policy. Despite this, at a tactical level, the ruling coalition tends to be prone to occasional foot-dragging and hesitation (i.e., over the introduction of necessary economic and political reforms), mainly due to party interests, especially in the pre-election period. The strongest opposition party is the moderate centrist SNS, which was formed in 2008 as a breakaway faction of the traditionalist, nationalist SRS. The SNS embraced democracy and the market economy but with largely populist political gospel. The party was also able to acquire and, through local election successes, confirm significant support in some municipalities.

Trade unions and local oligarchs with significant economic influence were, at the same time and for different reasons, less susceptible to undeniable economic hardship and loss of power, envisaged by the necessary and pending political and economic reforms Serbia has to face and implement on its path towards the European Union.

Prime Minister Cvetkovic's government has continued to strengthen the parliamentary accountability of the army and the secret services. In its 2010 progress report on Serbia, the European Commission noted that the Serbian parliament adopted six new legal acts to complete the legislative framework for defense reform. Nevertheless, according to the European Commission, civilian/parliamentary oversight over security forces in Serbia remains weak as legislation is not proactive and lacks capacity. Thanks to thorough police reforms, the influence of organized crime has been reduced.

The authorities decided to act swiftly following the killing of a French football fan in Belgrade in September 2009, violent riots after the Belgrade Pride Parade in 2010 and unrest during a Serbian football match in Genoa, Italy in October 2010. The government and president declared that extreme right groups were trying to undermine the state itself. Tough security and legal measures were introduced and

Consensus on goals
10

Anti-democratic
actors
9

implemented against a number of football-hooligan groups and members of far right, neo-Nazi and extreme religious organizations. Several organized gatherings of these groups were banned and the state prosecutor's office filed motions to disband some of the most extreme organizations.

Serbia's political leadership tried to prevent the emergence and escalation of conflicts based on ethnic, national or religious cleavages. The government and almost all major political actors remain adamantly opposed to Kosovo's 2008 unilateral declaration of independence. However, the government contested Kosovo's independence by peaceful and diplomatic means and in accordance with international law. In July 2010, Serbia's government rejected the unfavorable International Court of Justice in The Hague (ICJ) ruling that Kosovar statehood was legal. A week later, in the UN, Serbia tabled a confrontational draft resolution asking the UN General Assembly opinion on the ICJ ruling and called for new talks on all open issues, implicitly including Kosovo's status. After strong warnings from the United States and the European Union that such a resolution could seriously jeopardize Serbia's chances of EU accession, Serbia backtracked and, in active cooperation with the European Union, drafted a new resolution on Kosovo, which the UN Security Council adopted by acclamation. The new resolution didn't mention any talks on all open questions and, under the auspices of the European Union, opened the way for talks between Belgrade and Pristina on matters important to ordinary people and their lives (cadaster and land registry books, power supply, custom seals, telecommunications). Serbia has also tried to stop any further international recognition of independent Kosovo and its membership in some international organizations, primarily the UN. Within Serbia proper, the political leadership has sought to integrate national minorities but is facing significant problems in Sandzak region, caused by the bitter and prolonged conflict between two organizations of local Bosniak Muslims that claim to represent Muslims in Serbia.

Cleavage /
conflict
management

7

Serbia's political leadership took a number of steps to take the civil sector into account and support partnership with civil society. In July 2009, the Serbian parliament approved a law of association, which, according to the International Center for Not-The-Profit Law, brought the legal framework for association in Serbia closer to international standards and regional best practices. The Serbian government has established a commissioner for information of public importance and personal data protection. In January 2011, the Serbian government followed the European Commission's recommendation and opened a civil society cooperation office. Despite these steps, the overall role of CSOs still provokes mistrust and a lack of understanding in some parts of the state administration. Insufficient financial provisions could also undermine the partnership between state and CSOs.

Civil society
participation

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Serbia's political leadership and President Boris Tadic have sought to address the republic's responsibility in the wars of the 1990s by undertaking concrete political and legal steps. In March 2010, the Serbian parliament passed a resolution proposed by the ruling coalition that condemned the 1995 Srebrenica massacre and apologized for it while stopping short of calling the killings genocide. In May 2011, the government managed to arrest the former Bosnian Serb General Ratko Mladic, who is considered to be the main agent responsible for the massacre. Serbia continues to cooperate with the ICTY in The Hague. According to the War Crimes Chamber of the Belgrade District court, 65 cases have been processed during 2010 concerning individuals suspected of involvement in war crimes in the former Yugoslavia. However, the remarks made by the Council of Europe's Commissioner for Human Rights remain valid. He noted "an absence of successful transitional justice processes, such as formal truth-seeking efforts, reparations to victims, and the vetting of officials who may be implicated in past crimes... There is a tendency for state institutions to diminish the role of Serbia in the conflict."

Reconciliation

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It is safe to conclude that the Srebrenica Resolution and Serbia's cooperation with the ICTY were examples of the government's pragmatism, pressure from IFIs and other nations, and the desire for EU accession rather than a broad-based domestic recognition of the necessity of coming to terms with the past.

17 | International Cooperation

As it sticks to its reform agenda, Serbia's government has established healthy relations with foreign donors and in most cases has adequately and effectively used foreign financial and technical assistance. According to the European Commission, since 2007 Serbia has received EU annual pre-accession assistance worth, on average, €90 million. The government is also enthusiastic in adapting external advice to domestic realities, again in the sectors that are of the utmost importance for Serbia's EU integration process. This means its chief priorities have been reforms of public administration and the judiciary as well as help for education, energy and transport sectors. In one of its performance reports on Serbia, the European Union noted that the vast majority of donor support came through programs and projects. Only recently have relatively small budget support packages been conducted through the government's own system.

Effective use of support

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Due to the global financial downturn and Serbia's perceived progress in economic and social development, the number, scope and financial basis of foreign development aid to Serbia has decreased. In 2011, the British government even stopped direct development aid for a number of countries including Serbia. In its attempt to attract foreign aid, Serbia's government is apparently more willing to

accept any form of outside advice or assistance in matters which were until recently considered to be of national interest, like Kosovo.

Serbia's refusal to cooperate fully with the ICTY has been, for years, the main obstacle to the re-establishment of the country's credibility and reliability. The arrest and subsequent extradition of former Bosnian Serb President Radovan Karadzic in 2008 was an important boost for relations with ICTY and Serbia's international partners. Although two remaining war crime fugitives – the Bosnian Serb war commander Ratko Mladic and one of the war-time political leaders of Serbs in Croatia, Goran Hadzic – were still at large, the European Union granted Serbia, Montenegro and Macedonia visa-free status. In addition, in December 2009 Serbia formally submitted its bid for EU membership. The SAA between the European Union and Serbia provided a political, legal and economic framework for cooperation between the European Union and Serbia; it was signed in April 2008. EU member states launched their ratification process in mid-2010. The transitional, interim trade agreement with Serbia has been successfully implemented since February 2010. The Stand-by-Arrangements granted to Serbia by the IMF between 2009 and 2011 and the completion of a number of revisions to Serbia's IMF arrangements were seen as signals that the country was on the right path to fulfilling its international obligations. In its 2010 report on Serbia, the EBRD concluded that "the country enjoys strong support from international financial institutions and from parent banks of subsidiaries in Serbia and this is expected to continue."

Credibility

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The Serbian political leadership cooperates with many neighboring states and actively participates in regional and multi-regional cooperation initiatives such as CEFTA, the Regional Cooperation Council, the Central European Initiative, the Black Sea Economic Cooperation and the Regional Anti-Corruption Initiative. Serbia's regional credibility has been, to some extent, augmented by its support of unified Bosnia and Herzegovina and the Dayton Peace agreement. In April 2010, leaders of Turkey, Serbia and Bosnia and Herzegovina met in Istanbul to sign a declaration endorsing the territorial integrity, sovereignty and legal personality of Bosnia and Herzegovina. Despite this, Western countries would like Serbia and President Tadic to become more active in supporting efforts to further centralize the fragmented Bosnia and Herzegovina governmental structure. They would also prefer Serbia to be less amicable to the Republic of Srpska leadership that constantly opposes reforms intended to make Bosnia more coherent state. Serbia established good relations with Croatia but some issues remained open (i.e., border disputes, minorities, refugees and those missing in war). Serbia and Croatia are also pursuing genocide suits against each other over war crimes committed in the 1990s and during the World War Two. Serbia ratified the Extradition Treaty with Montenegro albeit without provisions for the extradition of its own nationals. The two countries still have to resolve some outstanding issues like the right to citizenship. There has also been a significant development in Serbia's relations with

Regional
cooperation

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Turkey, which is actively helping to solve unresolved issues regarding Bosnia and Herzegovina and inter-Bosniak conflict in Serbia's Sandzak region. Serbia's cooperation regarding Kosovo is almost nonexistent; it remains unwilling to accept Kosovo's participation as an independent state in a number of regional meetings. However, the government in Belgrade has established working relations with EU's Rule of Law Mission in Kosovo (EULEX). Serbia's ministry of the interior has signed a protocol on technical cooperation with EULEX aimed at fighting criminal activities on both sides of the administrative line. For all these efforts, the political leadership in Serbia called on Serbs in Kosovo to boycott local and parliamentary elections in 2009 and 2010, complaining that the right conditions had not been met to invite the Serb population to take part. At the same time, the government indicated that there would be no sanctions against Serbs who take part in Kosovar elections. Serbia is a member of NATO's Partnership for Peace Program and the country's National Defense and Security Strategy envisages cooperation with NATO. Nevertheless, the latest surveys indicate that two thirds of citizens strongly oppose Serbia's full membership of NATO because of the organization's 1999 air campaign over Kosovo (Belgrade's Centre for Free Elections and Democracy, 2011).

Strategic Outlook

The four heavily interconnected and almost inseparable factors that will shape Serbia's near future are the EU accession, Kosovo's status, an economic recovery and the country's internal social tensions. The first significant indicator of the course Serbian people and their political representatives will choose regarding these factors will be the spring 2012 general elections. Almost ten years after the overthrow of the Milosevic's regime, Serbia has indeed made considerable progress in developing democratic institutions and its market economy. Nevertheless, the fall-out of the global financial and economic downturn combined with inherited weaknesses in Serbia's structurally outdated economy and political system (a de facto patrician) to hamper the implementation of more consistent and substantial political reforms and economic restructuring. Simultaneously, some parts of Serbia's political and economic establishment are staunchly opposed to the country's adjustment to European norms as it could vitally endanger their vast and lucrative interests.

Serbia has done a good job in largely harmonizing its laws with the EU legislature. The overall progress is, at the same time, impeded by the insufficiencies in restructuring legislative implementation mechanisms, an ineffective and bloated public administration and partially unreformed state institutions. Even with an adequate legal framework in place, the numerous inconsistencies and debilitating politically motivated obstacles hindered the establishment of an impartial, professional and efficient judiciary and public administration, as well as effective integrity mechanisms to prevent corruption.

Serbia pulled itself out of the recession caused by the 2008 global economic downturn and the export-led economic recovery and GDP picked up after a dismal performance a year earlier. However, foreign financial risks were still present due to a large trade deficit, subdued capital inflow and the danger of fresh and harmful spillovers from the region and from the eurozone periphery crisis, particularly in Greece. Equally worrying are delayed and almost stalled cuts in public expenditure and public jobs as well as urgently needed restructuring, privatization or liquidation of the often loss-making public and socially owned enterprises. Those changes, if fully implemented, would result in massive lay-offs. Serbia's private sector, already heavily taxed and legally restrained, is currently not in a position to absorb newly redundant public-sector workers. The main obstacles on Serbia's road to economic recovery and political reforms were, undoubtedly, dangerously high inflation and rampant unemployment that fostered social discontent and political divisions. The ruling coalition, dominated by President Boris Tadic and his DS was thus well aware that the forthcoming elections might be critical for the realization of Serbia's EU ambitions. They hope that if EU candidate status is achieved by Serbia before the elections, it could serve as solid confirmation that the government has kept its promise of advancing Serbia's EU integration agenda. The risk is that for so many unemployed and impoverished voters the EU story and promises of a better life in the distant future could sound hollow and irrelevant in the face of the deterioration of everyday living standards. As the 2012

general elections loom, the coalition pro-European government, motivated by myopic electioneering, may therefore resort to relaxing its financial discipline, postponing hugely unpopular spending cuts and watering down any significant reforms. These are short-term and dubious vote-winning concessions with possible adverse effects in the long term. Due to the worsening economic situation, the pool of liberal-minded and pro-European or just pragmatic and not necessarily pro-Western voters has been depleting. The young, urbane and well educated are emigrating in droves as the crisis bites while corruption and cronyism pervade almost all segments of Serbian society. Political disillusionment, apathy, and lack of trust in the ruling political class were widespread and almost palpable.

After 16 years in hiding, the most wanted war-crime suspect, Ratko Mladic, was arrested in Serbia in May 2011 and transferred to the ICTY in The Hague. In the wake of Mladic's arrest, the European Union commended Serbia for the almost total fulfillment of its cooperation with the ICTY. Two months after Mladic's arrest, Serbia finally closed a chapter of its recent troubled and difficult past by apprehending the last fugitive war crimes suspect, the former political leader of Serbs in Croatia, Goran Hadzic. Without speaking openly on the subject, Serbia's leadership clearly expects the European Union to respond adequately and deliver the best possible pre-election reward to President Tadic and his allies: EU candidate status for Serbia with a date for negotiations for full membership set by the end of 2011.

Despite all the prizes for Serbia that followed Mladic's arrest, the European Union indicated that the next step would require Serbia's much wider and more significant cooperation over Kosovo. The European Union has made implicit suggestions that Serbia might have to revoke its negation of Kosovo's independence as a precondition for EU membership. Nonetheless, Serbia's political establishment, pro-European or otherwise, is still far from changing its attitude towards Kosovo, notwithstanding the EU accession. The Serbian political leadership is well aware how politically dangerous that emotionally charged question remains. The Serbian ruling classes and people are also aware that any real benefits of having impoverished and crime-ridden Kosovo and its restive ethnic Albanian population back under Serbian control were at best highly doubtful. However, it will take some time for the full reality of Kosovo to sink in Serbia. For now, even with Serbia's EU candidacy approval apparently coming down the pipeline, Brussels should be aware of sending mixed messages about its preferences for Belgrade's future policy towards Pristina, especially during an election year in Serbia.

Ratko Mladic's arrest and the recently commenced dialogue between Belgrade and Pristina may reaffirm long-standing beliefs among leading EU powers that Serbia reacts constructively only when it is exposed to significant outside pressure. For a growing number of Serbs – even those who have never favored nationalism – any EU pressure that results in no apparent tangible gains for the common person increasingly amounts to blackmail and unfair tutelage. Furthermore, such a perception may easily provoke defiance and even deeper disillusionment and growing resentment of the European Union, endangering the electoral chances of the ruling coalition. Serbia and its people are going to face numerous and far-reaching challenges in the near future and the forthcoming elections may only herald the real severity of the times to come.

