

Radovan Jelašić: Serbia against the economic crisis

Speech by Mr Radovan Jelašić, Governor of the National Bank of Serbia, in a meeting of top officials and leading businessmen themed “Serbia against the Economic Crisis”, Belgrade, 9 January 2009.

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Your Excellencies, Ministers, Ladies and Gentlemen,

I am grateful for the invitation to attend this meeting and hope it will, if not resolve, then at least contribute to improved understanding of both current events and possible responses to the challenges our economy and the overall Serbian society are now facing.

Allow me to begin by emphasizing the following four items of concern:

1. The level of disruption in international economic relations is unprecedented since WW2. There is no institution, no scenario or study which offers a ready made solution to the current crisis.
2. Nobody, and absolutely nobody, can tell how long the crisis will last nor how deep the disruptions will cut into the tissue of the world economy. This fact should be born in mind by all decision makers when deciding on any measures, either those relating to the use of foreign reserves or measures involving changes in the exchange rate for the dinar!
3. To err is human, especially when the problem at hand and the urgency of quick response are so paramount. But it is also of ultimate importance to admit one’s mistake and to adopt corrective measures as the market is quicker than ever in dealing punishing blows for any mistake!
4. Of course, we need to face up to the reality, the reality which in Serbia is most commonly termed “harsh”. This time, though, this attribute is more than applicable, but should not be used as an excuse for us not to confront the reality.

Both the exchange rate of the dinar against the euro and the current movements in prices are the “blueprint” of economic and political reality in Serbia and beyond. Naturally, we may blame most of such problems on the movements abroad, but I hope we all agree on one point at least – movements in prices and the exchange rate depend heavily on the type of measures we undertake in response to internal and external challenges. And the challenges have never been so numerous! What with the recent gas crisis and its fallout on both prices and the exchange rate in Serbia! Out of the blue, we are hit by rising prices of coal and wood for heating and there are no electricity heaters in the market even if your life depended on it. That is what constitutes a market-run economy in its harshest form. A responsible state, however, takes precautionary measures. It anticipates movements and acts as a buffer in the most extreme cases. This role is now being played by the National Bank. But what can the National Bank responsibly commit to achieve in these turbulent times? Let me point out the main areas:

1. **Preserving stability of prices in the current economic environment** – In all its activities, the National Bank is committed to „achieving and maintaining price stability”. Achievement of its commitment determines the general economic environment and the standard of living of our citizens. Let me emphasize again: the real increase in wages once the exact nominal increase is specified, depends exclusively on consumer price growth, i.e. inflation. Any real growth in wages in the course of this year will be determined by the effectiveness of the government and the National Bank in terms of keeping inflation under control.

2. **Adoption of (additional) measures to prevent or moderate the effects of disruptions in the banking system and/or financial market** – a set of measures posted on the NBS website have already become operational, from measures to moderate the effects of changes in the exchange rate on debtor categorization, to measures aiming to create conditions to improve foreign liquidity of banks and enable access to cheaper sources of funding from abroad. Naturally, in time, this list will grow longer as movements in our economy and experiences of countries in the region and wider may command.
3. **Ensuring unobstructed functioning of the foreign exchange market** – Serbia's international reserves have risen quite substantially during the earlier period of high foreign exchange inflow. In addition, the National Bank has been engaged in the repurchase of foreign currency cash from exchange dealers, and in 2006 alone such repurchase came to as much as EUR 1,730 million, in 2007 to EUR 1,158 and in 2008 to EUR 507 million. Such activity, plus setting high reserve requirements and implementing prudential measures in the area of supervision have managed to preempt stronger appreciation of the national currency. Namely, strengthening of the national currency is a normal byproduct during the period of abundant foreign currency inflow from privatization and increased borrowing abroad. Yesterday we sold EUR 43.5 million in the fixing session, while the overall volume of trading among commercial banks reached EUR 17.5 million only. So, the NBS is doing its job and is supplying sufficient amounts of foreign currency during the current phase of high demand just like it did in earlier periods when the supply was not so low as it is now. But at times of low foreign currency supply and substantially increased demand for foreign currency resulting from an abundance of dinars on hand, the exchange rate for the dinar must bear the brunt.
4. **Additional measures to ensure the financial sector stability** – Allow me to point out that the NBS is currently preparing measures to ensure that the majority of profits earned in 2008 are retained in the country in order to strengthen the domestic banking sector. To that end, we have already undertaken measures to ensure more favourable terms of borrowing for our banks abroad. After all, the NBS has already proved its readiness to extend financial support to banks, which of course comes at a price – both financial and personal.
5. **Encouraging credit activity primarily in the area of productive sectors of the economy** – There will no longer be any reserve requirement on fresh borrowing abroad and no upper limit on the amount of credit granted to entrepreneurs and small enterprises. The approach to credit repayment by each and every client individually and by the economy as a whole will be much more relaxed. New credit lines with the guarantee of Republic of Serbia have been secured via the EIB and from the Government of the Republic of Italy in addition to the revolving loans of the European Agency for Reconstruction. However, substantial efforts will be required in the future by all involved, the Government of the Republic of Serbia, National Bank and international financial institutions. But, let us be realistic, harsh realities of the 21st century and the financial capacity of the country will act as restraining factors in this respect.

In my view, however, major challenges in the period ahead will concern the following:

1. **Increase in domestic savings should be made our key priority in 2009** through measures of the Serbian government and the restored confidence of our citizens in the domestic banking sector. The first steps to that direction have already been made: the level of insured deposits has been increased to EUR 50,000 and a draft bill has been sent for adoption by the Assembly, which should enable tax exemption of interest income from foreign currency savings. Bear in mind that if any sector in Serbia has won acclaim from international financial institutions, it certainly is the

banking sector. This calculation is simple, the volume of fresh borrowing determines the future volume of savings. In addition to earning interest, our citizens should know that by saving they help their neighbours buy a new flat and enable enterprises to purchase new equipment. Everybody does well if the saving and credit scheme runs smoothly.

2. **Economic growth by 3.5% in 2009 is very challenging indeed!** Lower economic growth implies lower income, and in case of no decline in spending, a higher than currently planned growth of 1¼% in consolidated budget deficit will automatically follow! Hence, it is of utmost importance that we design a set of measures to be implemented in case economic growth turns out to be lower than planned for the period ahead.
3. **Proving that Serbia is different than other countries in the region.** Serbia was the first country in the region to seek financial arrangement with the IMF as a precautionary measure. This proves that we are a responsible state and wish to implement transparent economic policy under the IMF umbrella. This is certainly a point in our favour and will prove useful in Serbia's attempts to remain an attractive foreign investment destination in the near future of extremely cautious capital spending and restrictions on investments.

Thank you for your attention!