# Jorgovanka Tabakovi: Serbia 2027 - striving towards a high-income economy

Speech by Dr Jorgovanka Tabakovi, Governor of the National Bank of Serbia, at the 32nd Kopaonik Business Forum, Kopaonik, 2 March 2025.

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Slides accompanying the speech

Honourable members of the Government, esteemed representatives of the diplomatic corps, respected business leaders, dear fellow economists, ladies and gentlemen,

I would like to begin by saying, after the introductory remarks, that we should remember that the word "artificial intelligence" contains an essential falsehood in its name: artificial intelligence does not exist because creativity is inherently human. Artificial intelligence operates based on algorithms and the data input into the tools you have, such as your mobile phone. The trend of applying so-called artificial intelligence in all fields will ultimately have two consequences that are unacceptable for human civilisation – losing the truth and not knowing what is true versus what is a deep fake, and losing the human being, who is the only creative entity capable of making decisions and creating what is called "intelligence". While artificial intelligence can perform many technical processes faster, easier, and more efficiently, it cannot think.

Some say that one should not live in the past but always move forward. However, we have an obligation to respect the past to better understand where we are today and to have guidance for the future.

And the past teaches us that nothing should be taken for granted, as there are no final victories! Neither peace nor stability should be assumed, as they are not a given! That is why I will reiterate my conclusions from the previous two forums – what distinguishes theory from practice is our responsibility towards people, growth and development, and social stability. We depend on the conditions of the times we live in, but also on the decisions which we make and for whose consequences we bear responsibility.

Ladies and gentlemen,

(Slide 2) In October 2024, Serbia officially received an investment-grade credit rating! Congratulations to everyone!

I always emphasise, and I will do so again today, that on the economic front, no one can achieve much alone. No matter how brilliant they may be. This historic success is the result of teamwork by the President, the Government of the Republic of Serbia, and the National Bank of Serbia, and it belongs to all our citizens.

By joining the ranks of the one-third of the world's countries characterised by high business certainty, i.e. low investment risk, we have received yet another confirmation of the economic progress made over the past decade.

Most of those present today surely remember the period when Serbia had one major portfolio investor who invested in the Republic of Serbia's bonds. Just one. And that investor only invested in our country's securities because the interest rates were exceptionally high, which brought them excellent returns.

For many years now, the Republic of Serbia's bonds have been recognised as comparable to those of countries with investment-grade ratings, sought after by a large number of the world's largest global investors – those who have recognised our economic reform programme and all the results achieved over the past decade.

And I will reiterate today that the credit rating is the result of good political and economic decisions in the country, as one cannot be separated from the other. The continuity of political stability is a necessary precondition for the substantial and by no means easy structural reforms that develop the society we are part of.

We must preserve stability if we want a high-income economy – and I am sure that is the desire of everyone present at this forum today!

We must preserve stability in this competitive world full of challenges, where changes in the global order are happening faster than ever, and where the economic gap between key economies is widening!

This stability, along with sound policies, has enabled Serbia, even in the most complex conditions, to achieve numerous records last year!

- Last year, we returned inflation within the target tolerance band of 3±1.5%, with growth that was among the highest in Europe!
- We secured the country's record-high FX reserves of EUR 29.3 bn, which is 120% higher than in the pre-pandemic period. Gold reserves also reached a record-high level, currently standing at 48.7 tonnes.
- Dinar savings increased by nearly 40% last year.
- We also saw record-high FDI worth EUR 5.2 bn.
- Formal employment in the private sector is at a record high, with over 160,000 more people employed than in the pre-pandemic period.
- The unemployment rate is at its lowest level.

(Slide 3) The list of achievements is quite long, but the list of global risks is growing longer... That is why today, as we summarise the results and analyse the challenges, I will divide my presentation into four parts:

1. I will start with inflation factors.
2. I will continue with the measures of monetary and macroprudential policy.
3. I will specifically discuss the indicators of our economy's resilience to external risks.
4. I will conclude with the National Bank of Serbia's February projections, with a special focus on risks, various forms of risks, and their different effects on society and the economy.

I will proceed in order.

(Slide 4) Excellent news – in June last year, inflation was twice as low compared to end-2023, based on all key components – energy and food prices, as well as prices within core inflation.

Amid unfavourable global and domestic weather conditions, inflation stabilised at around 4.3% in the second half of last year.

- (Slide 5) It was precisely the unfavourable weather conditions that caused the prices of certain food commodities, such as cocoa and coffee, to rise sharply on global exchanges, which affected global food prices.
- Additionally, the rise in prices of personal services remained elevated in many countries, which can be linked to the high growth in real wages, which constitute a significant part of the service sector's costs.

(Slide 6) When it comes to inflation factors, in the next few minutes, I will share the findings of our two studies.

The first analysis provides additional quantitative evidence in support of lower inflationary pressures by comparing the distribution of y-o-y price increases for goods and services in the consumer basket, as seen in the charts. The data confirm that in 2024, there was a significant reduction in the share of goods and services that recorded double-digit growth. Around 25% of goods and services did not become more expensive, and 100 products and services in the consumer basket became cheaper in 2024.

In the second analysis, we examined the phenomenon of faster price increases for cheaper brands compared to more expensive brands of the same products, creating an impression of higher inflation than the actual rate. This phenomenon has been colloquially termed cheapflation.

The analysis shows that in Serbia, during the period from 2022 to 2024, which was marked by increased global pressures, the cumulative price increase for cheaper brands within the food and beverages category was 5 pp higher than for more expensive brands of the same products.

- One of the reasons for this phenomenon is the low elasticity of demand for food, which is the lowest for the cheapest brands.
- Also, more pronounced price increases often lead to the substitution of more expensive products with cheaper alternatives, thereby increasing demand for the cheapest brands and generating additional price pressures.
- However, there is also the issue of an imperfect market structure, which makes it easier for increased costs of producers and merchants to be passed on to retail prices more than fully, a problem I have pointed out on several occasions.

To conclude the first topic.

Inflation has been curbed both domestically and globally. The good news is that in Serbia, we achieved this result in terms of inflation alongside high GDP growth!

However, there is no room for complacency. Uncertain and dynamic developments in international commodity and financial markets call for caution, as evidenced by the rise in inflation late last year in many countries.

(Slide 7) The second topic builds on the first – namely, the measures of monetary and macroprudential policy in 2024.

With inflation returning within the target band in May last year, and with projections indicating movement around the midpoint by the end of the monetary policy horizon, conditions were created for the start of monetary easing.

- Namely, we cut the key policy rate three times, by a total of 75 bp, to 5.75%.
- Our measures were transmitted to money and credit market interest rates, with lending activity increasing by 8.2% and the dinarisation of receivables also going up.
- Dinar savings recorded a record nominal increase of over RSD 53 bn, reaching over RSD 191 bn. This means that dinar savings are almost eleven times higher than in 2012! Let me remind you that the results of our latest analysis of the profitability of dinar and FX savings confirm that over the past twelve years, dinar savings have been more profitable than FX savings, both in the short and long term.
- To protect the interests of financial service consumers, we also decided to temporarily cap interest rates on loan agreements concluded with citizens, which will be specifically regulated by law.
- We also adopted regulations under our jurisdiction that will enable the implementation of the government programme for housing loans for young people.
- In addition, and thanks to all of this, the share of NPLs in total loans fell to its lowest level of 2.5% in December.

I conclude this topic by stating that our cautious approach is justified and that this is confirmed by the fact that we have achieved all three goals – low inflation in the medium term, high economic growth, and preserved financial stability of the country!

(Slide 8) The third topic I will discuss is the resilience of the Serbian economy, which was confirmed even during 2024, amid continuous external shocks.

- First, in 2024, we maintained relative stability of the dinar exchange rate against the euro, with the dinar gaining 0.1%.
- Last year, we bought over EUR 2.7 bn net in the FX market, or EUR 11.2 bn since 2017, which has been an important factor behind the growth in FX reserves.
- FX reserves stood at their record high of EUR 29.3 bn at end-2024, covering over seven months of imports of goods and services and 167% of money supply M1.
- Gold reserves, which traditionally serve as a safe haven, rose to a record level of 48.7 tonnes, with their value being over seven times higher than in July 2012. The adequacy of our decisions is also confirmed by the fact that the price of gold in the global market increased by around 30% last year, and the rise continues this year.
- GDP growth of 3.9% in 2024 was among the highest in Europe, driven by fixed investment and private consumption. The investment growth was supported by record-high profitability of the corporate sector, high FDI inflows, and government

capital investment. At the same time, the growth in private consumption was driven by further increases in employment and real disposable income of the population.

- The value of exports of goods and services in 2024 reached EUR 43 bn, which is nearly 85% higher than in the pre-pandemic year of 2019. Within the goods sector, manufacturing exports grew by nearly 3%, despite still weak external demand. The reason for this resilience is the strategic focus on production and geographical diversification of markets and investors. Exports of services are also growing on solid foundations, driven by exports of information and telecommunications services.
- (Slide 9) FDI inflows were also record-high at over EUR 5.2 bn, despite all the uncertainties in the global market.
- An important element of resilience is the responsible conduct of fiscal policy, with a fiscal deficit of 2% of GDP, despite strong government capital investment. Particularly important is the fact that the growth in fiscal revenues is based on solid foundations – increased profitability and positive factors in the labour market, while the application of special fiscal rules for pension and public sector wage growth continues.

Esteemed participants of the Forum,

All these results we are achieving, even in an environment characterised by low growth among our key trading partners, have secured us, for the first time in history, an investment-grade credit rating from Standard & Poor's. Once again, congratulating all citizens on this success, I would like to say that we would certainly have received not only a positive outlook from Fitch but also the rating if political circumstances had not led to the agency's caution.

(Slide 9) The final topic concerns our expectations going forward and the challenges facing economic policymakers. However, before I move on to the projections, I would like to highlight the trends I have been discussing for years, often at this very place. However, it seems to me that it has never been more important to discuss this!

"Say goodbye to the world you knew – today we live in a new era!" The conditions in which we operate economically are the most challenging, and technologically the most advanced! This is a time of enormous social divisions in all countries. In diplomatic terms, we define this as an unprecedented polarisation of society. "People always know about misfortune and evil, but good remains hidden", said Meša Selimovi.

A particular challenge today is conducting policies in the era of fake news, and in an environment where individuals believe that policies can be pursued through social networks. I have been highlighting this phenomenon for several years as a major risk to society and democracy. And it has long been said that people can be divided into two groups: those who move forward and achieve something, and those who follow them and criticise. I will reiterate: healthy scientific and social scepticism that questions everything is always welcome, and that is why we are here. However, scepticism that questions growth and development has no social or economic basis. And any influence that leads to a slowdown in potential growth has a direct negative effect on people's standard of living and prospects for progress!

I will now move on to the projections.

- Regarding inflation, we expect that in Q1, y-o-y inflation will move around the upper bound of the target tolerance band. For the rest of the year, we expect it to gradually slow down and approach the midpoint by the end of the year, which is the level around which it will move until the end of the projection horizon.
- Such inflation dynamics will be supported by continued restrictive monetary policy conditions, lower imported inflation, an expected slowdown in real wage growth, an expected decline in petroleum product prices, in line with futures, and an expected decline in fruit and vegetable prices, assuming an average agricultural season this year.
- In terms of economic activity, we expect a further acceleration in GDP growth to 4.5% this year. For the next two years, we project growth between 4% and 5%, i. e. closer to 5% in 2027, when the "Expo" will be held.Such GDP growth will be driven by domestic demand, with growth in private consumption supported by:
    - positive trends in the labour market and further increases in disposable income, as well as
    - more favourable monetary conditions.
      At the same time, we expect that wage growth in the medium term will be in line with productivity growth, contributing to medium-term price stability.
- Fixed investment growth will be supported by:
    - increased profitability of the corporate sector in previous years,
    - planned high government capital investment in transport, energy, and utility infrastructure, as well as
    - more favourable financial conditions.
- We also expect continued FDI inflows, which will, through new technologies and more modern equipment, as well as new knowledge, contribute to the growth in total factor productivity.
- All of this together will contribute to further growth in both private and government investment, as well as its share in GDP of over 25% in the medium term.
- Due to the acceleration of the investment cycle and growth in private consumption, we expect that this year and the next, imports of goods and services will grow slightly faster than exports, resulting in a negative contribution of net exports to economic growth. On the other hand, in 2027, when the "Expo" will be held, we expect the contribution of net exports to be positive.

Of course, these, like all macroeconomic projections, are accompanied by numerous global risks, which I will present in a slightly different way than usual. I repeat, I will provide a global context.

- First, long-standing geopolitical tensions have been further exacerbated by the rise of global protectionism. Along with disruptions related to climate change, they continue to influence the volatility of global energy and other primary commodity prices and may have negative effects on both global economic growth and inflation.
- Furthermore, one of the growing structural problems, which the IMF particularly highlighted in October, is the widening income gap between Europe and the United States. The income gap reflects declining productivity growth in Europe,

which extends to the level of individual enterprises. The response to such movements implies structural changes in the European economy, of which we are a part, with the aim of increasing productivity and competitiveness.

- This is also supported by the accelerated development of the so-called artificial intelligence, which brings enormous transformative changes, creating both opportunities and challenges! According to the findings of the World Economic Forum, in the period from 2025 to 2030, structural changes driven by artificial intelligence in the labour market will create around 14% of new jobs, while around 7% of existing jobs will be eliminated. Thus, the net effect of these changes will be positive in terms of creating new jobs, but the distribution of these changes across regions and countries remains to be seen. For our region to have such an outcome, we must work together to ensure that the transformation, which is inevitable, proceeds in a way that the closure of some jobs opens doors to others, of higher quality.
- This also requires a deeper analysis of demographic trends, namely the process of reducing the working-age population, which is a challenge for all countries. And that is why it is important to invest in people and activate that part of the population that is outside the active labour force.

**When it comes to new sources of growth, I first want to state that the current growth model in Serbia has proven to be good. Ten years ago, in 2014, the share of investment in GDP was around 16%, and in 2024 – around 24%. The share of government investment was only 2.2%, and in recent years, it has been over 7%. The unemployment rate has been reduced from over 20% to around 8%, while youth unemployment has more than halved, and the number of formally employed people has increased by almost 400,000! The coverage of the average consumer basket by the average wage is at its highest level, around 95%, and is 30 pp higher than ten years ago! Thus, the current growth model has proven to be good!**

When we talk about the coming period and new sources of growth, it is certainly best to have innovations and new technologies, where domestic companies should also play a significant role. Unfortunately, the key new technologies that will shape the world in the coming decades are in the hands of the United States and China, and the technological gap is widening. And it is precisely here, and for this reason, that there is room for greater cooperation and integration at the level of the entire European market.

I will also recall the October analysis by the IMF, which highlights that a deeper and larger single European market would stimulate the necessary growth in productivity. It notes that the two previous waves of enlargement – in 1995 and 2004 – brought benefits not only to the countries joining the EU but also to the founding member states of the EU, which experienced significant income growth. Therefore, a joint response in terms of developing new technologies could have a multiplier effect on the growth and development of all European economies!

Esteemed participants of the Business Forum, I have spoken about global risks and potential responses, particularly from policymakers in Europe, of which we are a part. Among domestic risks, I highlight the potentially missed opportunities for high growth and the time needed to return to the trajectory we have secured, which places us at the top of Europe in terms of growth.

That is why today, as in previous forums, I will remind everyone that we have an obligation never to forget that stability is priceless, and there is no alternative to it. Without stability, any discussion about sustainable income growth and societal development loses its meaning!

On behalf of the NBS, I can promise:

- we will continue to work in the public interest,
- relative exchange rate stability has no alternative,
- there will be no negative interest rates in Serbia, as money must fulfil one of its fundamental roles – to earn through savings and the concept of interest. "Negative interest rates are a sign of central banks' desperation, not a solution to economic problems."

In every decision we make, we have been and will continue to be guided by the stability of the system! I believe that in these uncertain times, this is the key to duration. We cannot influence the policies and decisions of major powers, but we can and must support our development opportunities.

Finally, I congratulate the Serbian Association of Economists on their well-deserved selection as the host of the 21st World Congress of Economists, which will be held in June next year!

And finally, I ask you all, not expecting an answer: how many phone numbers do you know if you were to lose your phone and the contacts stored in it? Do you know how to calculate a discount on prices when you're out shopping? And how will your children, who rely on ChatGPT and mobile phones to do their homework, manage if, at some point, they can't charge their phone or if someone, just for fun, takes away their phone and all these devices that represent progress and development? Never forget that, above all, we are human beings who must think for ourselves, make our own decisions, and not forget the most basic things – to use our own brains and our own hearts!

Thank you all. I wish you a successful 32nd Kopaonik Business Forum.