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SERBIA
PM Vucic wins Presidential elections in 1st round

- Prime Minister and leader of the ruling Serbian Progressive Party (SNS) Aleksandar Vucic has won a decisive victory on the April 2nd Presidential elections. According to preliminary results, he scored a share of 55.1% of the ballot, exceeding the necessary threshold of an absolute majority in order to win the polls in the first round. His landslide victory does not come as a surprise as he enjoys strong popular support and most recent opinion surveys indicated he was well ahead of other presidential candidates and close to achieving around 50% of the vote.

- The runner up, Sasa Jankovic, ex-Ombudsman and a favorite of the civil society, achieved 16.3% of the ballot. Luka Maksimovic, who came third, received 9.4% and was followed by Vuk Jeremic (5.6%), ex-Foreign Minister and former president of the UN General Assembly who garnered support from a wide formation of EU-skeptics and moderate nationalists. Further behind were Vojislav Seselj (4.5%), Bosko Obradovic (2.2%), Sasa Radulovic (1.3%), Milan Stamatovic (1.1%), Nenad Canak (1.1%), Aleksandar Popovic (1.1%) and Miroslav Parovic (0.3%). The turnout at the elections is estimated to have slightly exceeded 50% of the electorate.

- Although a 2nd round will not be held, possibly to the opposition's disappointment which likely hopped for a run off in this election process, Sunday's results indicate potential changes in the domestic political landscape ahead. Independent candidate Mr. Jankovic's 16.3% score is quite an achievement for a newcomer in politics; he succeeded in attracting disgruntled Democratic Party (DS) voters, large parts of civil society and urban electorate. Be it with the DS or by creating a brand new political organization, he could position his party at the left center wing in the future. In the process, more clarity would be expected to be cast on his economic policies, which remain a bit of an unknown at the moment. At the same time, right after the polls closed, Mr. Jeremic hinted that he will form his own political party. Although he garnered just 5.6% of the votes, other right wing and Eurosceptic candidates (supported by DSS and "Dveri") did considerably worse. Given his past political experience it is possible that he may take up a center right position on the Serbian political scene in the longer run.

- The next test for Mr. Vucic and the Progressives is not that far away. The Belgrade elections, expected to take place early next year, - although local - are always more important than they formally appear, as Serbia's capital is home to more than a quarter of the electorate. These polls are considered as a gauge of the country's political orientation and any swings in the trend usually emerge then. Bearing in mind that Mr. Vucic won around 45% of the vote in Belgrade on Sunday's polls, some 10pps less than his countrywide score, it could be a challenging task retaining power in next year's ballot, especially having in mind the strengthening of the two new opposition figures.

- Incumbent President Tomislav Nikolic's 5-year tenure expires on May 31st. He is expected to remain in his post until then, with President-elect anticipated to be inaugurated in early June. It is not yet clear who would take over the post of the Prime Minister. But it is most likely that the successor will be a close ally of Aleksandar Vucic. Media currently speculate a number of names, such as incumbent Ministers of Finance and Public Administration, Mr. Vujovic, and Mrs. Brnabic, who are both expected to steer the country towards an even stronger pro-EU path with a continuation of public sector reforms, including a more ambitious revamping of the SOEs. Minister of Police, Nebojsa Stefanovic and ex-Minister of Justice, Nikola Selakovic, are also being mentioned. Socialist Party of Serbia (SPS) leader Ivica Dacic could also figure for the post.

- Although the President's position is largely ceremonial, the fact that the election is based on popular vote grants a high level of influence over national politics. Albeit executive powers are rather limited, the President can, among other, issue a decree on promulgation of laws or return legislation to Parliament for reconsideration and propose to the National Assembly a candidate for the Prime Minister. Albeit Mr. Vucic is anticipated to eventually resign from the SNS leadership after winning the presidential elections, his victory effectively grands him additional authority as he will most probably still bear high influence over the ruling SNS, which controls parliamentary majority, as well as over the new Prime Minister from his presidential post. As such his win last Sunday strengthens his as well as his party's position in the domestic political landscape.

- All in all, the presidential vote was perceived as a key test to the SNS-led administration and economic reforms that have been adopted over the last couple of years. The election's outcome prompt us to believe that we should not expect to see any significant changes in the government's policies and foresee a continuation of the policies in place, a pro-EU, pro-reform path, with an accent on the restructuring of the public sector and SOEs.

- The recent notable improvement in Serbia's macroeconomic environment over the last couple of years is rooted in domestic political stability, the front-loaded implementation of a sound fiscal consolidation program (implementing a structural fiscal adjustment of 4ppts of GDP in 2015-2016), ongoing efforts to clean up an overgrown and highly inefficient state-owned enterprises sector and thorough efforts to improve the business environment leaving behind the legacies of the past. The economy has turned the corner, with GDP growth swinging from a negative reading of 1.8% in 2014 due to the floods-induced recession, to a positive print of 2.8% in 2016, the highest pace of increase in eight years. GDP growth is expected to accelerate further to 3.0% in 2017. On top of private investment and net exports which are expected to repeat their current strong performance, private consumption is expected to accelerate to 1.4% YoY, from 0.6% in FY2016. Private consumption, after several years of acting as a drag on growth, is expected to provide more meaningful support to overall economic activity, driven by real wage growth and the positive fiscal impulse emanating from the targeted rise in public wages and pensions.

- The country's fiscal position has also improved notably following strict austerity measures, such public sector wages and pensions' cuts as well as a reduction in the civil servants headcount and lowering financial support to State-Owned Enterprises (SOEs). Also assisted by better-than-anticipated growth dynamics and improved tax collection, the budget deficit was reduced to 1.4% of GDP last year, significantly outperforming initial and revised deficit targets for deficits of 4% of GDP and 2.1% of GDP, respectively. This development also resulted in the first primary surplus since 2005 and assisted in a drop in the public debt, which decreased in 2016 (72.9% of GDP) for the first time in nearly a decade. At the same time, a further improvement in Serbia's fiscal position is earmarked for this year. With regards to the latest inflation developments, the Central Bank target has been overachieved over the last five years, necessitating the reduction of the previous 4+/-1.5% target by 1ppt as of this year. External imbalances have also improved with the current account deficit estimated to have narrowed to 4.0% of GDP last year from double digits in 2011 and 2012.

- Serbia ranks among those few economies in the region that have accomplished to reverse the declining trend in the investment expenditure to GDP ratio. This is an important development supporting optimism for the sustainability of Serbia's medium-term growth performance. The said ratio is projected to increase to 18.3% of GDP in 2016, from levels around 17.5% in the prior two years and a pre-crisis high of 30.3% reached in 2008. The main driver behind this improving performance is increased inward foreign direct investment (FDI). Net FDI inflows have been incentived by recent improvements in the domestic business environment as well as generous subsidies scheme offered to foreign investors. According to NBS data, net FDI flows reached EUR1.9bn in FY2016, compared to EUR1.8bn in the prior year, up ca. 3.6% YoY. Net FDI inflows accounted for over 5% of GDP in 2015-16, a high ratio by both regional and international standards, providing more than full coverage to the current account deficit (135.8% of CA in FY2016 up from 114.4% in FY2015). More importantly, in contrast to the pre-crisis era, more than one third of these FDI inflows are channeled to tradable sectors e.g. manufacturing.

- Finally, the country's EU accession path continues, with negotiations having picked up pace lately. All these developments have also been reflected in a series of upgrades on the country's sovereign credit ratings. Moody's and Fitch upped their ratings on Serbia over the last few months, with all three major agencies currently rating Serbia equally. We reiterate that, provided that further progress is achieved on improving the country's macroeconomic fundamentals, further positive credit rating moves are on the cards in the months ahead.

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