Eurobank Research
www.eurobank.gr/research
research@eurobank.gr

Eurobank EFG

NEW EUROPE ECONOMICS & STRATEGY

September 22, 2011

FOCUS NOTES: SERBIA

Growth revised downwards

Written By:

Ioannis Gkionis
Research Economist
Coordinator of Macro Research
igkionis@eurobank.gr

- Growth decelerated to 2.2% yoy in the second quarter compared to 3.4% yoy in the first on softer manufacturing readings;
- The prospect of a global slowdown worldwide and the shaky recovery from the net exports side compels us to downgrade our forecast for 2011 to 2.5% instead of 3% in our last New Europe Economics & Strategy

After a very strong start in the first quarter at 3.4% yoy, growth slowed at 2.2% yoy in the second quarter (flash estimate). On a seasonally adjusted basis, GDP remained flat in the second quarter compared to 1.4% yoy in the first. There is no official analytical sectoral breakdown of data from the supply or demand side at the moment of the writing. However, the Central Bank calculations bring the non-agricultural value added output to have slowed down to 1.4% yoy (-0.6% yoy in seasonally adjusted terms) compared to 3% yoy in the first quarter (+1.1% yoy in seasonally adjusted terms).

From the demand side, private consumption is exceptionally weak, having a 5.1pps negative contribution to growth. This is also evident in the recession of key retail trade sectors- retail sales have contracted by 14.2% yoy in Jan-July. Household spending (-1.1% qoq in Q2) was constrained by food and energy driven high inflation (average inflation stood at 13% in 1H), the weak labor market conditions (unemployment rose to 22% in last April).

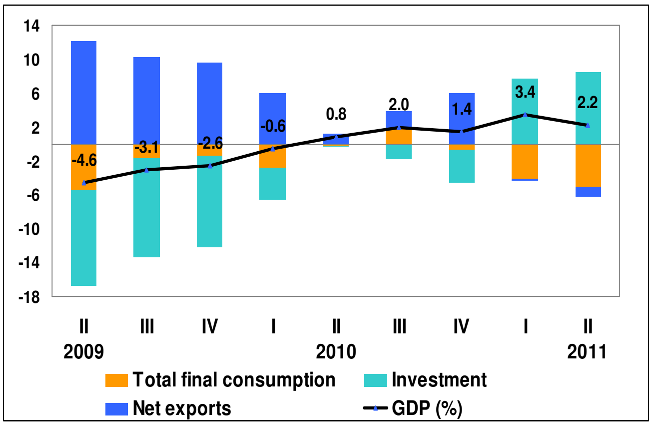
On the other hand, the contribution of net exports has turned negative in 2011. In fact, net exports' contribution became even more negative from -0.4pps in Q1 to -1.4pps in Q2. In contrast, investments contributed 8.4pps to growth compared to 7.8pps in the prior quarter. Investments have been mainly driven by the rebuilding of inventories (in capital and consumer durables) and to some extent by government infrastructure projects (+0.2% qoq seasonally adjusted). Private investment was still in contraction mode (-9.1% qoq seasonally adjusted) in Q2. However, the FIAT investment in automobile industry is expected to turn around the picture.

In our view, the second quarter is illustrative of softer growth readings anticipated ahead. The growth recovery which started last year was driven by net exports instead of domestic demand. Moving on to 2011, the dynamics of net exports have been fading away in Q2 influenced by the appreciation trend of the local currency (Dinar shot up on Q2 as much as 98/€ or 7.5% higher than the beginning of 2011), the slowdown in Europe (EU-27 generates 55% of total Serbian export revenues).

To make things worse, industry specific factors came into play such as the wheat exports ban during June10-March11. The slowdown of exports was also mirrored in industrial production indicators. Industrial production readings have been volatile throughout the 1H with ups and downs, recording negative readings from time to time. However, the overall performance to date is below expectations (Jan-July: +3.5% yoy).

Figure 1

GDP growth slowed down to 2.2% yoy in the second quarter



Source: National Bank of Serbia Inflation Report

All in all, recovery stemming from net exports is losing steam. In contrast, private consumption has not been a positive contributor to growth last year. Prospects in the current year are adversely affected by high inflationary pressures. On the other hand, output will receive support from a very solid agricultural season and a good tourist season (1.2 mn tourist visitors in Serbia this summer). This is expected to partially offset the negative trend from the trade flows.

The prospect of a global slowdown worldwide and the shaky recovery from the net exports side compels us to downgrade our forecast for 2011 to 2.5% instead of 3% in our last New Europe Economics & Strategy. The probability of shaky external demand conditions has a negative impact on the domestic growth environment. IMF forecast now stands at 2% in contrast to the growth forecast of the Central Bank which had maintained its 3% forecast until very recently. In addition, it is important to notice that there has been a major revision in the GDP calculation methodology. The Statistical Service now incorporates a new classification of activities in the calculation, while there has been a change in the prices deflator. The latter has shifted from constant prices to previous year prices which changes past records significantly. To give an illustrative example of the magnitude of change, GDP growth for 2010 was revised downwards from 1.8% to 1%, GDP growth for 2009 was revised downwards from -2.9% to -3.5%.

Research Team

Editor, Professor **Gikas Hardouvelis**
Ch ief Economist & Director of Research Eurobank EFG Group

Financial Markets Research Division
Platon Monokroussos, *Head of Financial Markets Research Division*
Paraskevi Petropoulou, *G10 Markets Analyst*
Galatia Phoka, *Emerging Markets Analyst*

Sales Team
Nikos Laios, *Head of Sales*
Vassilis Gioulbaxiotis, *Head of International Sales*
Yiannis Seimenis, Ioannis Maggel, *Corporate Sales*
Stogioglou Achilleas, *Private Banking Sales*
Alexandra Papathanasiou, *Institutional Sales*

Economic Research & Forecasting Division
Dimitris Malliaropulos, *Economic Research Advisor*
Tasos Anastasatos, *Senior Economist*
Ioannis Gkionis, *Research Economist*
Vasilis Zarkos, *Economic Analyst*
Stella Kanellopoulou, *Research Economist*
Olga Kosma, *Economic Analyst*
Maria Prandeka, *Economic Analyst*
Theodosios Sampaniotis, *Senior Economic Analyst*
Theodoros Stamatiou, *Research Economist*

Eurobank EFG, 20 Amalias Av & 5 Souri Str, 10557 Athens, tel: +30.210.333 .7365, fax: +30.210.333.7687, contact email: Research@eurobnak.gr

Eurobank EFG Economic Research

More research editions available at http://www.eurobank.gr/research

- **New Europe**: Economics & Strategy Monthly edition on the economies and the markets of New Europe
- **Economy & Markets**: Monthly economic research edition
- **Global Economic & Market Outlook**: Quarterly review of the international economy and financial markets

Subscribe electronically at http://www.eurobank.gr/research