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ACHIEVEMENTS OF ECONOMIC POLICY IN OVERCOMING THE EFFECTS OF THE GLOBAL ECONOMIC CRISIS ON SERBIAN ECONOMY

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The paper deals with the extent to which the economic policy in Serbia has managed to respond to the economic problems imposed by the global economic crisis and how the restrictions in the form of political instability and political influence, also present before the crisis, influenced the economic policy formulated to combat the crisis. Globally, the economic crisis has resulted in the fact that, instead of the rules in economic policy making, with the key objective of maintaining price stability, now discretion and fiscal policies are being promoted, with the aim of overcoming the problem of unemployment. The significant use of discretion in the economic policy generally imposes the problem of the competence and possible political motives of economic policy makers. It is the limitations of underdeveloped institutions and a wrong model of growth that have contributed to the fact that the results of the economic policy in Serbia have not been significant. Serbia is facing the negative consequences of the measures implemented in the form of high budget deficits, public debt and inflation, while the effects on the economic activity and employment have failed, causing the present choice between rules and discretion.

Keywords: global economic crisis, economic policy, political macroeconomics

JEL Classification: E60, E62

INTRODUCTION

The global economic crisis (2007-2009) launched by the financial crisis and economic recession in the United States, officially in December 2007, as a single economic event that cannot be subsumed under the standard cyclical downturn in the economic activity has led to significant changes in the objectives and instruments of the economic policy (Prascevic, 2012, 626). After a decade of the domination of rules in economic policy making and the primary objective of price stability by relying on the monetary policy, the need for mitigation and an as-fast-as-possible recovery from the economic crisis imposed discretion in economic policy making, especially in terms of fiscal policy (Spilimbergo et al, 2008). Unemployment also became a key economic issue, which is why the economic policy and the fiscal policy in particular turned towards overcoming this problem.

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These changes in the objectives and the economic policy instruments used imposed the question of whether this is a definite change in the domain of macroeconomic theory (abandoning the neoliberal paradigm), i.e. whether this is a fundamental change of the economic policy (the abandonment of rules and return of discretion), or whether this is a short-term return of Keynesianism. In the years after the global economic crisis, marked by a slow recovery and problems of public finance in almost all the countries affected by the crisis, the effects of the measures taken to overcome the crisis are being considered. The aim of this paper is to determine the effects of the economic policy measures on overcoming the negative impact of the global economic crisis (2007-2009) in Serbia. The paper discusses the key elements of the measures taken, primarily of the fiscal stimulus, but also the impact of the monetary policy. The effects of the measures of the economic policy are herein discussed in light of the fact that they were preceded by a period of an extraordinary fiscal expansion, which was primarily politically motivated – by political instability and the model of growth based on domestic demand. The paper examines the hypothesis that the economic policy implemented in order to overcome the economic crisis was partly motivated by a real need to improve the economic activity, but also that partially it resumed the previously politically-generated stimulation, based on a combination of opportunistic and partisan motives. The previous abuses of the economic policy in Serbia have considerably limited the possibility of using the economic policy to overcome the economic crisis.

The paper uses relevant data – macroeconomic indicators in Serbia for the analysed period, and applies the key premises of the developed models of the political cycles – opportunistic and partisan (Nordhaus 1975; Hibbs, 1977; Rogoff, 1990; Rogoff & Sibert, 1988; Alesina, 1987). After the introduction, the paper comprises the following parts: The Effects of the Global Economic Crisis on the Serbian Economy, Fiscal Policy - the Way to Overcome the Recessionary Pressures or the Source of Political Manipulations, Economic Policy in the Pre-electoral Period and the New Economic Policy, and the Conclusion.

THE EFFECTS OF THE GLOBAL ECONOMIC CRISIS ON THE SERBIAN ECONOMY

The global economic crisis has significantly affected the economy of Serbia. The slowdown of the global economy, the problems of the financial sector and the functioning of the financial system, which have considerably impaired global lending and reduced liquidity, have also had a negative effect on the economies of emerging markets and the transitional economies, including the Serbian economy. These effects have related both to the problem of reduced global aggregate demand, which has resulted both in a slowdown in the economic activity and exports, and a reduction in the capital inflows in the form of investment and growth in the cost of borrowing due to the reduced global liquidity.

The start of the crisis spillover in Serbia took place in the last quarter of 2008, and was first marked by the fear from a significant impact on the banking sector, due to the frequent bankruptcies of financial institutions in the world. However, apart from a short-term effect on the withdrawal of foreign savings from the banks in Serbia (in October 2008, about 1 billion euros were withdrawn), significant effects were prevented and the banking sector remained stable, while the measures by which the state guaranteed for deposits led to the stabilization and return of savings to the banks.

The strongest impact of the crisis on the economy of Serbia was recorded in 2009 when, for the first time since the political changes in 2000, the GDP recorded a decline (Table 1). A significant slowdown in the economic activity was recorded in the second half of the year 2008, as a result of the decline in aggregate demand in both its components – domestic and export demand. The decline in domestic demand had a more significant effect, although it was smaller than the decline in export demand; however, due to a significant share in the total demand, its decline had a significant impact on the economic activity slowdown. (Prascevic, 2012b, 144)

All macro indicators in 2009 show adverse economic trends. Although it is certain that the effect of the global economic crisis was decisive for them, it is still important to note that the errors in economic policy making in the period before the year 2008 also had its share in such poor indicators (Stamenkovic et al, 2009, 24). This specifically refers to the two internal factors:

- the choice of the economic growth model based on aggregate demand, domestic demand, to be more precise,
- political instability and economic policy making in the coalition government environments,

These factors are interrelated and interdependent. First, the choice of the growth model that generated the insufficiently dynamic development of both internal and external imbalances had a foothold in the political factors that dominated the period after

Table 1 Key macroeconomic indicators in Serbia (2002-2012)

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	Q1 2012	Q2 2012	Q3 2012	Q4 2012
Real growth of GDP (in %)	4.3	2.5	9.3	5.4	3.6	5.4	3.8	-3.5	1.0	1.6	-2.3	-0.6	-2.5	-1.5
Consumer prices (in %, year-on year)	14.8	7.8	13.7	17.7	6.6	11.0	8.6	6.6	10.3	7.0	3.2	5.5	10.3	12.2
NBS foreign currency reserve (in million EUR)	2,186	2,836	3,104	4,921	9,020	9,634	8,162	10,602	10,002	12,058	11,073	10,161	9,833	10,914
Export (in million EUR)	3,125	3,847	4,475	5,330	6,949	8,686	10,157	8,478	10,070	11,486	2,519	3,031	3,083	3.293,6
- growth rate in % year-on-year	16.0	23.1	16.3	19.1	30.4	25.0	16.9	-16.5	18.8	14.1	-2.6	5.2	3.2	8,7
Import (in million EUR)	-6,387	-7,206	-9,543	-9,613	-11,971	-16,016	-18,843	-13,404	-14,643	-16,627	-4,042	-4,323	-4,235	-4.620,7
- growth rate in % year-on-year	27.2	12.8	32.4	0.7	24.5	33.8	17.7	-28.9	9.2	13.6	5.5	6.3	1.3	1,6
Current account balance														
in million EUR	-671	-1,347	-2,620	-1,778	-2,356	-5,053	-7,054	-1,910	-1,887	-2,856	-1,177	-738	-546	-685,8
as % of GDP	-4.2	-7.8	-13.8	-8.8	-10.1	-17.7	-21.6	-6.6	-6.7	-9.2	-16.9	-10.2	-7.3	-8,3
Unemployment according to Survey (in %)	13.3	14.6	18.5	20.8	20.9	18.1	13.6	16.1	19.2	23.0	/	25.5	/	22.4
Wages (average for the period, in EUR)	152.1	176.9	194.6	210.4	259.5	347.6	402.42	337.9	330.1	372.5	357.6	363.2	351.8	385.3
RS budget deficit/ surplus (% of GDP)	-4.3	-2.6	-0.3	0.3	-1.9	-1.7	-1.7	-3.4	-3.7	-4.2	-7.0	-7.1	-3.9	-5.0
Consolidated fiscal result (% of GDP)	-1.8	-2.4	0.8	0.9	-1.9	-2.0	-2.6	-4.5	-4.7	-5.0	-7.3	-6.9	-4.1	-7.3
RS's public debt, (external + internal, % of GDP)	72.9	66.9	55.3	52.2	37.7	31.5	29.2	34.7	44.5	48.7	52.0	56.0	55.1	59.2
RSD/EUR foreign exchange (average for the period)	60.66	65.13	72.70	83.00	84.10	79.96	81.44	93.95	103.04	101.95	108.11	113.73	116.95	113.45
RSD/EUR foreign exchange (end of period)	61.52	68.31	78.89	85.50	79.00	79.24	88.60	95.89	105.50	104.64	111.36	115.82	115.03	113.72

Source: Narodna banka Srbije. Statistika – Osnovni makroekonomski indikatori.

the democratic changes in 2000, which can simply be defined as political instability. Although in the literature it is defined in various ways and comprises different elements (Prascevic, 2008a, 259-261), in Serbia, in the period of 2000-2008, political instability can be identified with frequent elections at different levels (Prascevic, 2008b, 50) and significant political differences between the political parties, especially between the coalition partners in the government. Therefore, in addition to frequent elections, there were also very strong tensions within the government, which often resulted from political issues (the pace of the political reforms required for the EU accession) and economic issues as well. Among the most important ones were: the disagreements within the government (2003-2007), which started in May 2006, due to a freeze of the negotiations on the Stabilization and Association Agreement with the EU for political reasons, which ended in 2007, by calling the regular elections in November 2006 for January 2007 (the pre-electoral campaign lasted since May 2006, which is precisely the period in which the changes occurred in the form of an extreme expansionary fiscal policy), the differences within the coalition government (2007-2008) which occurred as soon as in late 2007, which ended in elections in 2008 (the entire 2007 was characterized by a significant fiscal expansion), the disagreements within the coalition government (2008-2012), which were primarily related to economic issues in February 2011, which did not result in the collapse of the government, but did result in the reconstruction of the government, as well as long-term consequences in the form of the alienation of the formerly crucial coalition partners.

For the key episodes of the economic policy in Serbia, the macroeconomic policy premises on the possible abuse of the economic policy by its creators were prominent in both its forms – the opportunistic and the partisan motives (Jaksic & Prascevic, 2010, 17-18). For the realization of its opportunistic objectives, the Serbian political elite received support from the Serbian economic elite, at least from one of its parts, which affected both the growth model, and the concrete of economic policy measures as well, but also the most destructive thing – the choice of almost completely dysfunctional institutions. This choice has had long-term negative effects on economic developments.

Frequent elections were one of the key reasons for the slowdown of reforms, given that from one election to the next, the support for a rapid and radical reform decreased. The political elite (the pro-reform and pro-European one) opted for a more significant "purchase" of voters, precisely in the form of an increase in the purchasing power and the standard of living, above the possibilities dictated by the economic growth (Prascevic, 2010, 94). The growth in domestic demand was primarily funded through the capital inflows from abroad, from privatization, which meant a one-time influx of funds. The growth reached its downfall with the onset of the global economic crisis when the errors of the economic policy started to come to light, worsening the already bad economic situation.

The indicators of real private consumption in Serbia point to its prominent participation in the GDP (as much as above 90%), which is more than in all other countries, and significantly above the average for the EU27 countries (Radisavljevic, 2010, 28). This level of real personal consumption represents a significant constraint to economic growth. However, when we consider the actual height of the real per capita private consumption and compare it with the other countries of the Western Balkans and the EU, it can be seen that, in the period 2005-09, it reached 38 to 45% of the EU27 average, while in the same period, the GDP index was 32 to 37% of the average achieved in the EU27 (Radisavljevic, 2010, 32). Therefore, the growth of real personal consumption was faster than the growth of the GDP, but by the amount of its real personal consumption per capita, Serbia can be classified into and compared with the Western Balkans countries.

Even before the global crisis, the economy of Serbia was faced with a significant problem with the external imbalance and fiscal deficits. However, even such a small volume of exports registered a year-on year decline of 16.5% in 2009. At the same time, due to the fall in domestic demand, as well as the production, there was a significant year-on-year drop in imports by as much as 28.9%. It caused the improvement of the current account deficit, which amounted to 6.6% of the GDP, compared to 21.6% of the GDP in 2008 (Table 2), as a consequence of reducing the total foreign trade

Table 2 Serbia's Balance of Payments (2007-2011)

POSITIONS	2007.	2008.	2009.	2010.	2011.
I. CURRENT ACCOUNT	-5,052.5	-7,054.2	-1,910.1	-1,887.2	-2,776.0
CURRENT ACCOUNT WITHOUT OFFICIAL AID	-5,218.9	-7,216.8	-2,107.6	-2,080.3	-2,976.1
1. Goods (1.1-1.2.)	-7,068.7	-8,501.2	-4,946.4	-4,581.0	-5,318.4
1.1. Source of goods, f.o.b.	6,382.5	7,416.0	5,977.8	7,402.5	8,439.7
1.2. Import of goods, f.o.b	-13,451.3	-15,917.2	-10,924.2	-11,983.6	-13,758.1
2. Services (2.1.-2.2.)	-261.1	-184.7	20.5	7.7	163.2
2.1. Revenues	2,304.0	2,741.4	2,500.0	2,667.1	3,032.3
2.2. Expenditures	-2,565.1	-2,926.1	-2,479.5	-2,659.4	-2,869.1
3. Balance of goods and services (3.1.-3.2.)	-7,329.9	-8,685.9	-4,925.8	-4,573.3	-5,155.2
3.1. Export of goods and services	8,686.5	10,157.3	8,477.8	10,069.6	11,472.0
3.2. Import of goods and services	-16,016.4	-18,843.2	-13,403.6	-14,642.9	-16,627.2
4. Income	-598.7	-921.8	-502.5	-669.9	-757.9
4.1. Revenues	516.9	558.1	499.7	437.7	428.2
4.2. Expenditures	-1,115.6	-1,479.9	-1,002.1	-1,107.5	-1,186.2
5. Current transfers	2,876.1	2,553.6	3,518.2	3,356.0	3,137.1
5.1. Revenues	3,104.7	2,828.3	3,762.0	3,624.0	3,488.2
5.2. Expenditures	-228.6	-274.7	-243.8	-268.0	-351.0
II. CAPITAL ACCOUNT	-313.9	13.2	1.6	0.9	-2.5
III. FINANCIAL ACCOUNT	5,175.6	7,133.3	2,032.6	1,818.5	2,609.2
1. Direct investment - net	1,820.8	1,824.4	1,372.5	860.1	1,826.9
2. Portfolio investment - net	678.2	-90.9	-51.0	38.8	1,619.1
3. Other investment	3,418.7	3,713.2	3,074.6	-9.1	964.6
3.1. Assets (receivables)	-1,618.3	-1,451.1	75.3	-791.9	455.4
3.1.1. Trade loans	-860.0	-601.5	-394.7	-368.9	-300.2
3.1.2. Financial loans	1.1	-30.5	24.8	-34.0	-18.4
3.1.3. Cash and deposits	-710.3	-787.9	445.2	-389.0	774.0
3.1.4. Other assets	-49.1	-31.2			
3.2. Equity (liabilities)	5,037.0	5,164.3	2,999.2	782.8	509.2
3.2.1. Trade loans	1,619.2	1,558.6	873.9	284.6	808.3
3.2.2. Financial loans	3,402.1	3,529.2	1,388.7	863.5	-394.6
3.2.2.1. NBS	-91.5	0.0	1,114.4	341.0	44.8
3.2.2.2. Government	121.1	98.4	258.2	735.3	687.5
3.2.2.2.1. Long-term	121.1	116.3	256.7	736.8	687.5
3.2.2.2.2. Short-term		-17.9	1.5	-1.5	
3.2.2.3. Banks	166.6	155.4	869.1	659.7	-710.8
3.2.2.3.1. Long-term	-126.3	-260.2	474.2	651.9	437.8
3.2.2.3.2. Short-term	292.9	415.6	394.9	7.8	-1,148.5
3.2.2.4. Other sectors	3,205.9	3,275.3	-853.0	-872.4	-416.1
3.2.3. Cash and Deposits	68.8	75.3	314.5	-365.3	95.6
3.2.4. Other equity	-53.1	1.2			
3.2.5. SDR allocation			422.2		
4. Reservesi	-742.1	1,686.6	-2,363.5	928.7	-1,801.5
IV ERRORS AND OMISSIONS-net	190.8	-92.3	-124.1	67.8	169.3
TOTAL BALANCE	742.1	-1,686.6	2,363.5	-928.7	1,801.5

Source: Narodna banka Srbije. Statistika – Platni bilans RS.

of Serbia. At the end of 2009, the economic activity recovered, and again, there was a tendency of a faster growth in imports than it was in exports (an average of 6% versus 4%), which caused an increase in the current account deficit as well as in the trade deficit in goods.

During the period of the strongest impact of the crisis on the economy of Serbia in 2009, the financial account surplus decreased as compared to 2008. This was also partially caused by a fall in net foreign direct investment (from 1.824 million to 1.372 million euro), the portfolio investment deficit was reduced from 91 million to 51 million, and a decline was recorded in other investments as well (from 3,713 to 3,075 million euros). Within this position, there were significant financial loans taken by the banking sector (short-term), as well as the IMF loan disbursement for the state (from SBA 1,114 million euros and 422 million euros in Special Drawing Rights), but also the influx of cash and deposits (Table 2). At the same time, in 2009, there was an increase in foreign exchange reserves amounting to 2,363.5 million euros (contributed to by the funds received from the IMF, amounting to 1.54 bln. euros and 400 million euros from the sale of NIS), in contrast to the decline of the reserve in 2008 by 1,686.6 million.

During the recessional 2009, the inflation rate was declining (the annual total 6.6%, compared to 2008, when it was 8.6%), which corresponds to theoretical explanations, i.e. could be considered as the consequence of the decline in domestic demand (due to a wage freeze in the public sector and the growth of unemployment – layoffs in the private sector), as well as an increased uncertainty. During the period of the main effects of the global crisis, the exchange rate depreciated against the euro – the nominal depreciation by about 6% (February 2010 compared to September 2009), the real depreciation at the end of 2009 compared to September 2008 was about 14%.

As early as in late 2008, the monetary policy was directed at limiting the rapid depreciations of the dinar through the restrictive monetary policy and, at first, by raising the interest rates. This measure was also expected to have an effect on limiting inflation, whose trends at the beginning of the spillover of the crisis, in late 2008 and early 2009, were still worrying, although the rate of inflation stabilized by the end of 2009, only to become topical again with the recovery in 2010, which is consistent with the fact that the inflation rate is a lagging indicator. The depreciation of the dinar was stimulating for the economic activity, primarily in encouraging exports and restricting imports, but because of the fear of inflation, it was insisted on a limited depreciation involving monetary contraction.

In addition to preventing a more significant depreciation of the exchange rate, the monetary authorities were faced with the problem of reduced liquidity in the economy. However, this problem was not primarily addressed by the NBS because of the inflationary pressures and the inability to decrease the interest rate, but it was rather left to the fiscal policy. The monetary policy was not used for countercyclical purposes, but primarily for the maintenance of macroeconomic stability – price stability and to reduce the exchange rate fluctuations. Such a choice of the monetary authorities was not surprising if we take into account the fiscal constraints and other factors related to the previous character of the economic growth in Serbia. The monetary response was largely conditioned by the fiscal imbalance and the inability to address the fiscal imbalances that had existed in Serbia even before the crisis, which had political origins. Therefore, the monetary policy remained the guarantor of macroeconomic stability, which led to the conclusion on an insufficient coordination between the monetary and fiscal policies, which were implemented to overcome the effects of the global economic crisis.

FISCAL POLICY – THE WAY TO OVERCOME THE RECESSIONARY PRESSURES OR THE SOURCE OF POLITICAL MANIPULATIONS

Serbia entered the period of the global economic crisis with an open problem of public finances – the state budget deficit, which was the result of an expansionary fiscal policy in the period of 2006-2008, exactly coinciding with the politically motivated abuses of the economic policy and the slowdown of the economic reforms. The shifts in fiscal policy making precisely coincide with the election cycles realised in the period before the onset of the crisis in Serbia. The especially important years (in the context of the pre-electoral expansionary fiscal policy) are the years 2006, 2007, and 2008, i.e., the three years immediately before the onset of the global economic crisis.

From the budget surplus of around 1% of the GDP achieved in 2005, the economy shifted to a deficit of around 2% of the GDP (2006, and 2007), or 2.6% of the GDP (2008). The first effects of the global economic crisis started in such unfavourable conditions when it was legitimate to assume that there would be a drop in the GDP, which, if the measures of the fiscal austerity or tax increase were not taken, would lead to an even greater deficit of the state budget. At the same time, it could be assumed that the restrictive fiscal policy would be difficult to implement in a time of crisis when the decline in tax revenues due to the economic downturn is inevitable, while an even greater pressure to increase budget expenditures in order to stimulate the economic activity of the state could be anticipated, through various forms of stimulations for the economy and consumers. The increased budget expenditures were aggravated by to the deterioration of the social status of the population and the inevitable growth of unemployment. Therefore, the deficit situation worsened, so that during the crisis year of 2009, the consolidated budget deficit amounted to 4.5% of the GDP, and due to the extraordinarily expansionary fiscal policy and the lack of economic recovery, it remained quite high even in the post-crisis years (4.7% in 2010, and 5.0% in 2011). In the last year 2012, which was also the election year and the year of the change of the government (the policy makers), the problem of the deficit culminated, the deficit being as high as 7.3% of the GDP in the last quarter (Table 1), imposing itself as the first and the most important issue for the economic policy makers.

In the domain of the political abuse of the fiscal policy for political purposes – electoral purposes (the budget political cycles), political macroeconomics distinguishes several forms, which were the basis for the development of the appropriate budget cycle models (Cukierman & Meltzer, 1986; Rogoff & Sibert, 1988; Rogoff, 1990; Drazen, 2000). Among them are: the models based on a fiscal illusion, the models in which the budget deficit is a strategic variable, the intergenerational redistribution models, the distribution conflict models, the geographically dispersed interest models, and the models of budgetary institutions (Jaksic & Prascevic, 2010, 279-290). The key mechanisms of the fiscal abuses discussed in these models can be applied to the fiscal policy in Serbia before, during and after the global economic crisis.

The models based on fiscal illusion imply that voters are characterized by "fiscal illusion", or that they do not understand the intertemporal budget constraint – overestimating the benefits of the current increase in expenditure and underestimating the current and future tax liabilities. Therefore, voters do not punish the opportunistically motivated policy of generating budget deficits. In Serbia, this form of fiscal illusion was supplemented by another factor – privatization revenues that could be used for opportunistic political purposes as well. One such example was the National Investment Plan – NIP (2006-2011), which defined a number of priorities in the fields of infrastructure, regional development, as well as education, health and culture. Instead of a carefully devised and planned state investment in the four sectors, which in the medium term would lead to the growth of productive potentials of the country, and thus future budget revenues, these effects did not materialise.

The fiscal policy in Serbia in the pre-electoral period fits with the models of rational budget cycles, which implies that voters are fiscally conservative and deceived by changes in the structure of the government expenditures in favour of those that are quick and easily "visible". Thus, in election years, a significant increase in the so-called discretionary public spending – public investment, subsidies, lending, etc. can be observed. These expenditures provide "competence" for monetary policy makers, which misleads the voters.

The fiscal policy measures with significant political stronghold in the period before the economic crisis (2006-2008) were the following:

- a marked increase in the salaries in the public sector during the electoral year 2006, which continued in 2007, based on the realization of the agreements between the trade unions and the government in the pre-election period in 2006;

- the launch of the National Investment Plan in 2006;
- the subsidy programs for enterprises (small, medium and those that were being restructured) in 2006;
- a reduction in the income tax and the introduction of non-taxable earnings in 2007, and
- a reduction in some tax rates – tax on transfer, VAT for certain products, total exemption from payment of VAT for first-time home buyers in 2007 (Prascevic, 2012b, 147)

This behaviour of the fiscal authorities in the pre-crisis period limited the possibility of its being used in stimulating the economic activity in Serbia during the crisis. The May 2009 revised agreement with the IMF increased the allowed deficit to 4.5% of the GDP, which was in line with the changes in the approach of the IMF due to a drastic economic contraction, but it was also an expression of the reality preventing the implementation of more significant austerity measures as they would contribute to greater recession.

Despite the limitations imposed by the past trends due to which, immediately after the formation of the previous government (in July 2008), a need for fiscal consolidation emerged, it is possible to observe the continuation of the politically motivated fiscal and broader economic policies to fight the recession, led by the government (2008-2012). The objective reason for this can be found in the fact that the previous government, at least initially, called itself "socially responsible government", whose key objectives, in addition to joining the EU, were a faster economic growth, a lower unemployment rate and an improvement of the living standards, the reduction of poverty and a more equitable distribution of the costs of the economic reforms and transition. The factors relating to the composition of the coalition government which brought together political parties of different orientations (with different economic objectives), as well as the coalition agreement on the functioning of the government (the division of the ministerial portfolios amongst the coalition partners) and the ruling majority, the management of public enterprises and the like, significantly aggravated the implementation of fiscal stabilization. Very soon, there was a problem known in the models of political macroeconomics as the distributional conflict, when the coalition partners in the government, who formulate fiscal policy, do not want to transfer the burden of fiscal stabilization to themselves or their constituents, but rather try to transfer that burden to other coalition partners (Alesina & Drazen, 1991, 1170).

The antirecession measures taken by the state (a support for the financial sector, deposit insurance, subsidized interest rates for certain loans, the provision of loans to small and medium-sized enterprises, encouraging public investment) had positive effects (Prascevic, 2012b, 152), although during 2009, there was also a pronounced effect of squeezing out as a consequence of the high state budget deficit, on the one hand, and large credit risks to the economy, on the other, which is the reason why banks preferred investing in the government bonds to investing in the economy. It was further emphasised by the fact that the fiscal deficit in Serbia in 2009 was financed primarily by borrowing, as the sources of privatization revenues had dried up. An important support to the economic policy in 2009 was an arrangement with the IMF encompassing the financial support of EUR 2.9 billion. The program stipulated a reduction of public and private sector consumption, since it could no longer count on the substantial inflows of foreign capital. The Program stipulated freezing the public sector wages and pensions, which remained valid during 2010 as well, and reduced discretionary spending on goods and services, subsidies, loans to all levels of the government. However, public expenditure recorded the highest decrease in capital expenditures, which indicated significant recessionary trends.

The year 2010 noted a weak recovery (the GDP growth of 1.0%), which continued in 2011 (the GDP growth of 1.6%), which was significantly lower than the rates that had existed before the crisis. During 2010, there was a recovery in aggregate demand and a significant growth in export demand, which can simply be explained by the fact that wages and pensions remained frozen, and the problem of high unemployment rates became topical again, which is the reason why a significant increase in domestic demand was not possible. The trends in the labour market in the post-crisis period (2010, 2011, and 2012) were not encouraging though (unemployment continued to rise and employment continued to decline – Table 3). It should also be stated that the number of persons who have lost their jobs does not apply to the public sector, because precisely due to the effects of the global economic crisis and negative economic developments in the country, the needed public sector reform that will inevitably involve layoffs in the sector and the growth of unemployment in this respect has been postponed. Still, the trends in the labour market have been extremely unfavourable – in four years (since 2008), the employment rate dropped by about 10%, which makes the situation in Serbia even more complicated and reflects a harsh economic situation for the majority of the population in Serbia.

Table 3 Employment and unemployment rates in Serbia, 2004-2012

	Employment rate (age 15-64)	Total number of the employed (age 15-64)	Unemployment rate (age 15-64)
Oct. 2004	53,4	2.735.977	19,5
Oct. 2005	51,0	2.574.139	21,8
Oct. 2006	49,8	2.516.794	21,6
Oct. 2007	51,5	2.525.570	18,8
Oct. 2008	53,3	2.646.215	14,7
Oct. 2009	50,0	2.450.643	17,4
Oct. 2010	47,1	2.269.565	20,0
Oct. 2011	45,3	2.141.920	24,4
Oct. 2012	44,2	2.083.604	26,1

Source: Republički zavod za statistuku. Anketa o radnoj snazi.

The recovery of the Serbian economy was very weak, and the issues related to the rising inflation, the budget deficit and the public debt became more prominent, so that in some periods, the monetary policy opted for marked tightening in curbing inflation. The exchange rate recorded significant fluctuations that, on the one hand, indicated a need for a further depreciation of the dinar, whereas on the other, the demands and to shift to a fixed exchange rate become increasingly more prominent, which would have been particularly difficult to implement in a situation of very unfavourable fiscal flows that were active in Serbia in the past several years.

The fiscal trends in Serbia show that the governments in unstable and polarized political systems, such as those in Serbia, are prone to high deficits, because the deficit is positively correlated with the degree of the political polarization potential between potential governments, the tenure of the government and the prospect that the government is not re-elected (Persson & Svensson, 1989; Alesina & Tabellini, 1990). The undisputed political polarization in Serbia has led to a situation where the budget deficit has become a strategic variable, which the current government uses to affect the fiscal policy of the future government, as the manipulation of the current fiscal policy affects the choice of a fiscal policy to be implemented by future policy makers, although they may have different preferences. An example of such a fiscal policy is the policy before and after the last elections (parliamentary and presidential, in May 2012).

ECONOMIC POLICY IN THE PRE-ELECTORAL PERIOD AND THE NEW ECONOMIC POLICY

Political instability in the country has intensified since mid-2011 (more significant differences between the coalition partners in the government and the pressure from the opposition parties to call early elections) significantly affected the economic trends, too. These tensions ended in the regular parliamentary (state and local) and early presidential elections, held in early May 2012. This is why the first half of the year 2012 was characterised by pre-electoral activities, and due to the change of the government at the national level (the government and the president of the Republic) and at the local levels, the second half of the year was largely devoted to the formation and consolidation of power, and the economic policy makers announced significant changes with respect to the preceding economic policy. Taking into account past experiences with economic trends in the pre-election and post-election periods in Serbia, it is not surprising that in 2012, they were very unfavourable. It should be added that the economic trends at the global level, and those in the euro area are particularly important to Serbia, became unfavourable as well (the euro are went back into recession again).

The fiscal policy had an especially important role, as it was recorded during the previous elections (at different levels). The fiscal policy remained the backbone of the overall economic policy on the following two grounds:

- due to a slight economic growth, there was still a need to affect the stimulation of the economic activity through the government fiscal policy;
- in the pre-electoral period, the fiscal policy remained the most important instrument of a possible impact on improving the economic position of the voters – through votes "purchase".

The fiscal trends in Serbia should be viewed in the context of a temporary suspension of cooperation with the IMF (the precautionary impossibility of concluding the second review of the arrangement agreed in September 2011 and worth 1.1 billion euros), which occurred in March 2012, due to the disagreements with the economic policy makers on curbing the budget deficit and the debt issuance. In contrast to the success of the first review in November 2011, which predicted that the budget deficit target in 2012 would be 4.25% of the GDP, with an expectation that the economic growth in 2012 would be 1.5%, the very unfavourable economic developments indicated that the projected economic growth would not be achieved, and that the deficit would be significantly higher. Therefore, the IMF set the following conditions: a request for the budget revision, a request for the reduction of additional spending and of the debt issuance, the adoption of a medium-term fiscal program and the acceleration of structural reforms. Due to the inability of the economic policy makers to implement significant fiscal tightening measures in the pre-electoral period (the spring of 2012), a temporary suspension of the cooperation with the IMF and the IMF's intention to continue discussions on arrangements with the new government was not surprising.

According to the macroeconomic indicators, the year 2011 was crucial for the negative trends, which later culminated in 2012. A large part of the responsibility for this lies with the economic policy makers. Despite a declarative commitment to a new growth model based on export demand, and thus on significant production and investments into the sectors producing tradable goods, it lacked realization. Instead, during 2011, there was a significant decline in net exports, which partially resulted from the real appreciation of the dinar in 2011 (due to a high influx of foreign capital which, however, was one-off) as well as from the reduced production and export of steel due to the deterioration of the business of U.S. Steel Serbia. In 2011, the current account deficit significantly increased (to 9.2% of the GDP – primarily due to the reduced inflow of current transfers). In 2012, due to the absence of significant capital inflows from abroad, this trend would continue in a further deficit increase and problems in maintaining the value of the dinar, which would inevitably record depreciation.

However, during the year 2011, favourable trends were recorded in the amount of the foreign direct investment (to recapitalize banks, the investment in retail trade, construction), investments portfolio and other investments. This growth, however, was short-lived and limited, and did not continue in the year 2012. In 2011, the value of the external debt continued to grow in the absolute amount (in millions of euros), while the real appreciation of the dinar decreased the ratio of the debt to the GDP, compared to 2010. The growth of the debt was caused by increased public sector borrowing abroad (with a slight decrease in borrowing by the private sector).

During 2011, inflation was brought under control (the realized inflation at the level of 7%), although the growth trend from the previous 2010 continued until May (year-on-year inflation in May was as high as 17.9%), after which point it stagnated and then declined. In terms of the exchange rate, the appreciation in the first half of the year was followed by its nominal depreciation, which continued into 2012, only curbed in the last quarter of 2012, and the average exchange rate restored the level from the second quarter of 2012.

The economic policy of the pre-electoral period, i.e. in the final months of the previous government, can be said to have been unsystematic and determined by short-term goals. Yet again, the policymakers repeated a significant fiscal expansion that had existed in all the previous pre-electoral periods (in the first half of the year 2012, the deficit was as high as 7% of the GDP). Regardless of such an expansion, the short-term effects on the growth of the economic activity did not materialize. On the contrary, the economic activity declined, a real year-on-year decline in the GDP in Q2 of 2012 was about 0.6%, only to increase in Q3 as a consequence of adverse weather conditions (drought) to 2.2% of the GDP (year-on-year).

The positive effects on the economic growth did not occur, neither in the short term, but the effects of the wrong dynamics in aggregate demand in terms of the increased inflation and the weakened local currency – namely the dinar did. These effects are recognized in the political macroeconomics models (within the opportunistic political cycle models), but the exploitation of the increased government spending is based on the right "timing", which did not occur in this case. Namely, the Serbian economy was already in recession and the election had to be called and they were scheduled within the final due date (in accordance with the Law), which means that the government did not have much choice with respect to "timing." In the meantime, some unforeseen circumstances occurred, which could not have been affected, or not fast enough.

The positive effects on the economic growth did not materialize, even in the short term, but the effects of a more dynamic aggregate demand on the inflation and the weakened local currency did. These effects are well-known in the political macroeconomics models (within the opportunistic political cycle models), but the success of the increased government spending is based on the right "timing", which did not occur in this case. Namely, the Serbian economy was already in recession and the elections had to be called (their latest due date was scheduled in accordance with the Law), which means that the economic policy makers did not have much choice with respect to "timing." In the meantime, some unforeseen circumstances occurred, which could not have been affected (the bad meteorological conditions in February 2012, which reduced the economic activity, the negative economic trends in the euro area and the growing complexity of the steel plant U.S. Steel Serbia case. Already in December 2011, it was speculated that it would be closed. Instead, the state "bought" the steel plant for a symbolic price of USD1, with a blurred vision of the future, but in order to avoid having about 4,500 workers out of work in the pre-electoral period).

The economic developments in Serbia were bad to the extent that no substantial public spending could reverse them (though in April and part of May, there was an upsurge in industrial production), because there was no increase in net exports and investments. This indicates that the current wrong model of growth and recovery in Serbia suffered a complete collapse, which means that the new economic policy makers will possibly abandon it.

The fact that the economic policy for overcoming the impact of the global economic crisis (2008-2009) was in fact wrong is reflected in the information that the economic activity has not yet reached the level it was at in the spring of 2008 (prior to the effects of the global crisis), but was lower by 3% in the second quarter of 2012, compared to the same period in 2008. The structure of the GDP use in electoral period completely corresponds to the populist and politically motivated economic policy:

- a significant increase in the government spending (on goods and services, increasing wages) – contributed to the year-on-year GDP growth by 2%;
- a growth in private consumption – came from the real growth of the average wage and the real growth of the total spending on pensions – contributed to the GDP growth;
- a decline in investments – contributed to a fall in the GDP;
- a decline in net exports – contributed to a fall in the GDP.

The uncontrolled growth of the government spending in 2012 resulted in the problems of Serbia's public and external debt. The total public debt at the end of the second quarter was 56% of the GDP, only to rise to as much as 59% of the GDP at the end of the year (the government borrowings by issuing euro-bonds), which significantly exceeded the required 45% of the GDP. In addition to borrowing abroad, the government also borrowed in the country (by issuing Treasury bills). However, the amount of external debt indicates that, at the end of 2012, it will exceed 80% of the GDP, with a high cost of its repayment in the future. In order to eliminate a threat of the foreign insolvency of the country and given that in 2012, there was a decline in the foreign currency reserves, it is necessary to have those economic policy measures which would reduce the current account deficit, i.e. increase exports, limit domestic demand and lead to the acceptance of the exchange rate policy based on the sustainable exchange rate (abandoning the overvalued dinar and the maintenance of an artificial exchange rate at the expense of spending the foreign exchange reserves).

The economic policy of the new government is facing significant limitations – dynamising domestic demand has peaked and no longer can it be counted on, the stimulating of the economic activity by means of the economic policy measures is very limited and can be related to a possible use of the exchange rate policy, primarily through its depreciation with the aim of improving Serbia's price competitiveness and exports. This leads to the conclusion that it is necessary that the system of economy and business operations in Serbia should be reformed. In this context, some measures to facilitate business procedures, various permits (including construction permits) obtaining procedures, tax procedures and most importantly – the elimination of all forms of corrupt behavior in business operations - have been announced.

The first task for the new government was to consolidate public finance, which is not uncommon either in terms of the past experience regarding the pre-electoral fiscal developments in Serbia or in terms of what models of political budget cycles we are taught. Such a high deficit and the debt increase are fully compliant with the assumption that in a situation where policy makers face a prospect of losing power, they opt for an extremely expansionary economic policy. In addition to the budget deficit, as a pressing issue, there was also the high inflation, and the depreciation of the dinar. This third problem – the decreased value of the dinar (nominal and real), was the first to initially be eliminated by nominal and then substantial real appreciation of the exchange rate (due to a high inflation rate, and a relatively stable nominal exchange rate). To solve the problem of inflation and depreciation, in addition to fiscal restrictions, it was also necessary to have a restrictive monetary policy, which the National Bank of Serbia's new governor continued as well. Amongst these measures, there certainly was a further increase in the reference interest rate, an increase in the dinar share in the foreign exchange reserve requirement, and the transition to standard repo operations.

In the future period, the fiscal policy will be the backbone of the economic policy, much as it was the case with the previous government. In the public finance domain, the new government has taken steps in limiting the government spending. At least officially, new economic policy makers consider that a future economic recovery and economic growth will not be based on an unrealistic growth in domestic demand, primarily in the government spending. One must not forget, however, that the previous government also adopted the "new growth model" in 2011, which was thought to have brought an end to the practice of growth based on domestic demand. Although officially adopted, this model has not taken root in practice, nor has it been supported by relevant economic policy measures.

CONCLUSION

The paper demonstrates that the economic policies to overcome the effects of the global economic crisis in Serbia have had mixed effects. The short-term, positive effects in the form of a slight recovery since 2010 have materialised, but in the medium term, the economic policy has failed. This has largely been so due to the significant restrictions that already existed in the period before the onset of the global economic crisis, such restrictions being the legacy of a high budget deficit and the poor state of public finances as well as a wrong model of growth based on the growth of domestic demand. These problems have deepened due to the necessity of the significant state intervention in the economy and a fiscal expansion. As a necessary way to stimulate the economic activity in the period of the economic crisis, the fiscal stimulus in Serbia has been related to the continuation of the opportunistic and partisan-motivated abuses of the economic policy. This paper demonstrates that throughout the period before, during and after the effect of the global economic crisis, the fiscal policy in Serbia has significantly been influenced by the political factors that caused its abuse in ways known in the literature of political macroeconomics. At the same time, the monetary policy has primarily served the purpose of maintaining price stability, often trying to limit the negative effects of the fiscal measures. Therefore, no coordination can be said to have been existing between the monetary and fiscal policies. The worsening economic trend was particularly evident in the last months of the previous government, right before and especially after the elections.

The political manipulation of the economic policy present in the earlier years has left a bad legacy to new monetary policy makers, conditioning some of their first moves. Thus, they have been imposed the necessity of fiscal consolidation, as stated in the models of the political budget cycles. Taking into account all the limitations of the growth model used until recently – the one based on domestic demand - monetary policy makers are left with no possibility of using it any longer. They rather need to focus on finding new sources of growth – especially exports, for which it is necessary to have production started, but structural reforms and the ever-so-delayed reform of the public sector are of equal importance as well. This provides a certain dose of optimism that the future will not repeat the mistakes – the intentional use of the economic policy instruments for political purposes, because the possibilities for this have almost completely been exhausted (extremely high fiscal deficits, a high public debt, the problem of curbing inflation).

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