Republic of Serbia
FISCAL COUNCIL

ASSESSMENT OF THE FISCAL STRATEGY FOR 2016 AND ISSUES IN THE IMPLEMENTATION OF STRUCTURAL REFORMS

Summary

Fiscal consolidation and public sector reform are prematurely grinding to a halt, before the main objectives have been realized. Two years ago, Serbia was on the brink of a public debt crisis. To prevent this, the Government faced three main tasks: 1) decreasing the vast fiscal deficit, 2) reforming unsuccessful public enterprises and 3) resolving the fate of enterprises undergoing privatization. At the beginning of 2015, an arrangement with IMF was concluded, providing additional expert assistance in fulfilment of these tasks, but also the necessary credibility among investors. In summing up the results achieved so far, until the announcement of new parliamentary elections, we estimate that the success was partial, at best. The largest progress was made in the fiscal deficit decrease, primarily thanks to the necessary and inevitable pension and salary cut in the public sector. The deficit is no longer enormous, it has been decreased from 6.6% of GDP in 2014 to 3.7% of GDP in 2015, but remains unsustainable as it does not stop the public debt growth, it is among the highest in Europe and, very importantly, it cannot be significantly decreased further without additional difficult and unpopular measures. At first glance, resolving the statuses of enterprises undergoing privatization looks impressive - in terms of the number of companies, the majority have had their status resolved in 2015. However, these were mostly enterprises with few employees, for which privatization or bankruptcy were relatively easy. Approximately two thirds of employees remain in the enterprises with yet unresolved status, so the largest challenges still lay ahead. Least progress was made in public enterprise reform. The only enterprise with a relatively significant progress is Železnice (Railways), however, this reform slowed down the moment it came to the first difficult measures (redundancy of workers). As for the reforms of the remaining two public enterprises with major difficulties, EPS and Srbijagas, the process has not moved past "cosmetic" changes, giving rise to a legitimate question of whether the state has sufficient control over their operation. Taking all this into account, the hazard of a public debt crisis in the previous two years has been temporarily postponed, but not completely avoided, so fiscal consolidation and further reform of the public sector will have to remain a priority for the next Government - which will actually have to face the greatest challenges of their implementation.

The Government's plan, embodied in the Fiscal Strategy, is not good or convincing enough a program for public finance recovery. The main measures for fiscal deficit reduction envisaged by the Fiscal Strategy for 2016, with the projections for 2017 and 2018 (Strategy) are general government downsizing and pension and salary freeze in the public sector. However, even as the Strategy was being drafted, it was evident that the savings planned from this downsizing will not be achieved. In addition, after the pensions and the majority of salaries in the general government sector were unfrozen at the end of 2015, the increasing pressures for their additional increase, as well as the latest announcements from

the Government, also make the latter key measure from the Strategy highly uncertain. The reform of large public enterprises, which is, at the moment, an equally important (if not more important) part of the economic policy for public debt crisis avoidance, has only been mentioned in general terms - with no concrete plan or set deadlines for the resolution of their most pressing problems (redundancy, poor collection rate, inadequate prices and many other non-rational approaches). The Strategy uncritically accepts the plans envisaging resolution of all issues and statuses of enterprises being privatized in the first half of 2016 at no fiscal cost, even though it is almost impossible that this will be achieved, at least for those enterprises with the biggest problems (RTB Bor and Resavica). Finally, we estimate that insufficient attention was given to measures and reforms that could make up for some of the less realistic expectations presented in the Strategy - such as, for example, Tax Administration reform. Therefore, the Strategy has adequate general objectives of a strong deficit decrease and a wider public sector reform, but 1) the achievement of these objectives relies on unconvincing measures and reform plans and 2) no alternative measures have been proposed, in the case that some of the planned measures and reforms fail to meet their goals (which we believe to be almost certain). For this reason, we see the Strategy as an unconvincing and inadequate strategic document for the resolution of fiscal and reform challenges Serbia faces in the upcoming years.

The Fiscal Council recommends a decisive reform of EPS and Srbijagas, resolving the fate of the majority of remaining enterprises in privatization, Tax Administration reform and a renewed commitment to the policy of pension and salary freeze. These are the key measures that must be implemented in 2016 (and some in the years to come), so that the initiated fiscal consolidation process would not be reversed, bringing Serbia back into the danger zone at the brink of a public debt crisis - and the Fiscal Strategy fails to recognize them properly.

- *EPS* has implemented some organisational changes in 2015 and received (a small part of) the electricity price increase from last summer; however, it seems that this was spent on a salary increase and not on enterprise performance improvements. At the same time, the enterprise continues to incur debt and unless certain significant and prompt changes take place, the repayment of these debts could very easily fall on the state budget (as was the case with Srbijagas). EPS's main issues have long been known and it is high time for their decisive resolution: excessive expenditure for employees (redundancy of workers and high salaries); insufficient collection rates; high technological losses and theft; obsolete, irrational and environmentally non-compliant system parts; low electricity tariff.
- *Srbijagas* was granted a respite in 2015, due to the historically low gas prices which allowed it to operate with more profit for a while, but this respite was not used for the resolving of some of its major problems - even the relatively painless legal status transition of the enterprise in line with the EU Directives has not been completely implemented. This enterprise must abandon the ownership of unsuccessful enterprises in the fields outside its core competence (enterprises owing gas fees, whose debt has been transformed into capital: Azotara, MSK etc) and it also must stop delivering gas to those that are not meeting their obligations regularly (Staklara Paraćin, for example).
- Of the remaining number of about 55,000 employees in the *enterprises still undergoing privatization*, it is unlikely that a solution will be found in 2016 for those enterprsies employing about 15,000-20,000 employees (RTB Bor, Resavica, employees in Kosovo etc). However, the status of the remaining enterprises, employing a total of 35,000 people (Železara Smederevo, Simpo, Galenika, Azotara etc) must finally be resolved.
- It is estimated that grey economy suppression could bring in about 1% of GDP in public revenue increase in the medium term, which is close to the planned savings from the general government downsize (which will not unfold as planned). The decisive factor in this

increase in public revenue collection will be *the Tax Administration reform*, for which there is already a good and detailed plan - the realization of which has been postponed for almost two years.

- Finally, *pension and salary freeze* in the public sector currently has no alternative (except perhaps for the economically inferior VAT increase) and the Government would have to be consistent in the implementation of this measure.

The Government's plan from the Fiscal Strategy fails to prescribe sufficiently credible and powerful measures for halting the increase of public debt relative to GDP in the medium term. The plan from the Fiscal Strategy is to reduce general government deficit from the (realized) 3.7% of GDP in 2015 to 1.8% of GDP in 2018 which is generally a good objective. In order to achieve the planned deficit reduction by 2018, in the upcoming three years' savings have to be made in the amount of approximately 2.3% of GDP. These savings are somewhat larger as the "true" deficit going into 2016 is not the realized 3.7% of GDP but higher, amounting to over 4% of GDP. Namely, one part of the deficit decrease in 2015 is temporary in nature (low execution of public investments, lower payments of severance fees resulting from delays in the general government downsize and resolving the statuses of enterprises undergoing privatization, but also the unusually high payments from public enterprises into the budget). The Fiscal Strategy plans for all the necessary savings by 2018 to be made almost exclusively on the public expenditure side and not on the public revenue side, with the main measures for their realization being: downsizing, pension and salary freeze in the public sector and subsidies decrease. However, the Fiscal Council estimates that these measures are insufficiently well prepared (subsidies), lack credibility (salary and pension freeze) and are unachievable (downsizing). In addition, the projected expenditures fail to include the almost certain additional expenditures from the budget (payment of the guaranteed debt of RTB Bor, for example). This is why we believe that the state deficit can only be reduced by about 0.5% of GDP by 2018, instead of the planned 2.3% of GDP prescribed in the plan presented in the Fiscal Strategy. This would leave the fiscal deficit at the level of 3.5% of GDP which is too high, as it fails to stop the growth of the share of public debt in GDP and brings Serbia closer to a public debt crisis.

Implementation of structural reform is the most sensitive part of the fiscal consolidation and threatens to put the entire process of public finance recovery at risk. The initiated fiscal consolidation can be divided, roughly speaking, into two phases. In the first phase, in 2015, it relied on administrative measures with large effects on the fiscal deficit in the short term, such as pensions and salary cut in the public sector and, to a lesser extent, introduction of an electricity excise. Another favourable circumstance in 2015 was that the focused activities on combating grey economy (tobacco, oil) provided additional funds, that assisted in completing the first year of consolidation somewhat more successfully than was originally planned. However, the short-term measures have been exhausted in 2015, so further deficit decrease would have to rest on savings from structural reforms and this is, at the same time, the second (and critical) phase of fiscal consolidation. One of the most important reforms planned, general government downsizing, was set to fail from the beginning, which the Fiscal Council predicted back in 2014. During 2015, it was confirmed that the planned general government downsizing was unrealistic, as the number of employees decreased only slightly and not because of the layoff of redundant workers, but as a consequence of natural attrition - employees retiring, but not being replaced with new employees at the same rate. The fact that the layoff of the planned 9,000 surplus employees planned for December 2015 and January 2016 has not been implemented corroborates the doubts that this process will go as planned. We estimate that the maximum achievement of the planned downsizing will amount to a half of the original number planned (35,000 - 40,000 instead of the planned 75,000) and this is probably an optimistic assessment. The reform of public and state-owned enterprises is more both more important and more critical than downsizing - and it, too, is running late. The majority of this Fiscal Council Report is dedicated to this reform, or set of measures, pertaining to public and state-owned enterprises.

Increasing expenditures of enterprises undergoing privatisation have become an insufferable burden on public finance and it is necessary to resolve their fate as soon as possible. The price of copper has plummeted in the last year, but this cannot serve as an excuse for the catastrophic business results of *RTB Bor* in the last year. *Firstly*, the price of copper of about 4.500 dollars per ton, which is its current level, is not historically that low at all - the historical precedent was the price of 9.000 dollars per ton from a few years back; the current price is relatively common when observed over a longer time period. *Secondly*, even with the historically highest price of copper, RTB Bor's business operations were unsuccessful - the enterprise's debt rose to over a billion Euros by the end of 2014 (this debt cannot be repaid by RTB Bor, so part of the debt repayment will definitely fall on the state); and its poor operation, even with the high price of copper, was - as it still is - continues to be - an enormous cost for the country and public enterprises as the vast funds received from the Development Fund (about 200 million Euros) were not paid back and the enterprise failed to pay its taxes, electricity, railway transport and fuel bills regularly. The following example will probably best serve as an illustration of *Resavica*'s unsuccessful business operations: a (justified) question is being raised in public about the cost-to-benefit ratio of large subsidies that the state grants to foreign investors, amounting to as much as 10.000 Eur per workplace. However, there little attention is being paid to the information that the state has been subsidizing *Resavica* from the budget for a relatively long period of time, at 10.000 Eur per workplace - every year (which was already discussed by the Fiscal Council). The debt of *Petrohemija* towards NIS, which has increased to about 85m Eur will probably be paid from the budget in 2016, while the enterprise's debt to Srbijagas will probably never be collected. *Železara Smederevo* somehow managed to survive the year, among other things, thanks to the received loan from the Development Fund of over 100 m Eur in December 2014. For some time now, the state has been repaying the bank loans issued to *Galenika*, which this enterprise is unable to repay on its own. *Simpo* has been incurring losses for several decades, but has managed to survive thanks to more or less visible state support. All these expenditures stemming from the unsuccessful state-owned enterprises are enormous - a country far richer than Serbia would be unable to bear them and should not bear them.

In 2015, about a third of the problems have been resolved but the biggest challenges have yet to come. Fiscal Council strongly supports the Government's efforts towards a final resolution of the fate of enterprises undergoing privatization - meaning, their privatization (in their entirety, or the parts of those enterprises that have market prospects), or their bankruptcy. In 2015, this process started on a more decisive note, but the success achieved is nowhere near to what is being presented to the public. The number of enterprises that have had their status resolved is large, but the most challenging among them, with the largest number of employees and the largest negative fiscal implications are still state-owned. Not a single of these companies has had their status resolved, and there are numerous other similar examples. The best indicator of how far this process has come is, in our opinion, the number of employees. At the beginning of 2015, the enterprises undergoing privatization employed about 80,000 employees, while at the end of the year, 55,000 still remained. This means that approximately a third of the problems were resolved in 2015, while two thirds, the most difficult to resolve, were postponed for 2016.

A good objective in 2016 would be to resolve the status of companies undergoing privatization employing 35,000 employees. It is already clear that the state has no intention of resolving the fate of the two most troublesome enterprises in privatization in 2016 - RTB Bor and Resavica. In addition, there are examples of other, specific enterprises that cannot be expected to be resolved in short-term (enterprises in Kosovo and Metohija, for example). However, a small number of exceptions cannot be used as an excuse to give up the resolution of the statuses of the remaining enterprises in 2016. This is why we believe that a good objective for 2016 could be to resolve the fate of the ones employing a total of 35,000 employees and we shall be assessing the success of this process in 2016 in line with that. At the end of this privatization process review, we would like to strongly emphasize the hazardous practice of resolving problems only ostensibly - for example, by linking the unsuccessful enterprises with the military industry (Jumco, Trayal, FAP, Tools Production Factory etc) or with public enterprises (Azotara with Srbijagas etc).

The reform of large public enterprises has not gone far in 2015. The operation of three large (and unsuccessful) public enterprises has particularly strong implications on public finance, which is why we analyzed them separately. These are: EPS, Srbijagas and Železnice Srbije. *EPS's* business failures have so far not represented a direct burden on public finance. However, EPS is by far the largest enterprise in the country and if the burden of its unsuccessful business performance was to fall on the state, that would probably completely wreak havoc on Serbia's public finances. *Srbijagas* has been the country's largest loss-maker for years and its accumulated debt (of over a billion Euros) is being serviced from the budget by the state. *Železnice Srbije* are an enterprise completely dependent on state aid and the single largest recipient of direct budget subsidies (about 100 million per year). The Government made the first step in resolving the issues of these companies by admitting that these problems exist and requesting expert assistance in their resolution from international institutions. Thus, the reform of these public enterprises entered into the arrangement with the IMF, while the World Bank and EBRD actively participated in (and provided financial support for) the preparation of the plans for their reform. However, the implementation of the said plans has not come far. The largest step was taken by Železnice, but even there, the restructuring is not going smoothly. There are no significant positive changes in the operations of EPS and Srbijagas (although Srbijagas's business results in 2015 will be somewhat more favorable due to the strong drop in gas prices).

EPS is a public enterprise at the moment probably posing the highest risk to public finances in Serbia due to its poor performance, while its reform is not going as planned. The Fiscal Council pointed out EPS's largest problems on several occasions; these are: 1) excessive expenditures for *salaries* (due to surplus employees and large average salaries), 2) low *collection* rate for delivered electricity, 3) electricity *tariff* below the level guaranteeing business sustainability, 4) *losses in the network and theft*, 5) *organizational* weaknesses. In 2015, there were attempts at improving the performance of these companies, but they were insufficient. Electricity tariff went up in August 2015 (effectively, EPS received only about 3%), the enterprise's organizational structure was changed towards greater centralization and in June 2015 (with a 3-month delay) the financial restructuring plan for EPS was adopted, which is not available to the public. We estimate that very modest measures have been undertaken in 2015, especially bearing in mind the extent of EPS's problems, as well as the fact that all these problems have been known for a long time. The measures undertaken cannot begin to bring the necessary savings to overturn the enterprise's poor performance. In addition, there are indications that there has been an unjustified increase in salaries in 2015 - and the salaries are by far the largest individual expenditure of the enterprise that has to be significantly decreased by the reform. It is quite possible that this increase, if it did take place, has "eaten up" the increase in EPS's revenue due to the tariff increase and so annulled one of the rare reform measures of 2015, bringing everything back to the start. Such lack of efficiency and meandering in the implementation of reform are extremely dangerous as they lead to further accumulation of losses and other issues in EPS's performance which could fall to the state, as the last instance (as it has already occurred with

Srbijagas). If this does occur, due to its size, the EPS's problems would most likely completely wreak havoc on Serbia's public finance.

Srbijagas is facing difficult problems, making it the largest loss-maker of the entire Serbian economy for years, at a high cost to the state budget. The most serious issue of Srbijagas is the unsustainably low *collection rate*. For years, Srbijagas has been unable to collect the revenue for about 40% of its gas deliveries, which has had a decisive impact on the downward spiral of the enterprise's performance and has lead to enormous losses. Furthermore, to cover these losses, Srbijagas took out numerous liquidity loans, increasing the enterprise's debt to over 1 bn Euros. This opened a new issue - the enterprise's *over-indebtedness*. Since these loans were mostly approved with the state acting as a guarantor (now guaranteeing for about 90% of Srbijagas's loans) and Srbijagas was unable to pay them back on its own, they are now being paid from the state budget. In this manner, this enterprise costs the state, on average, 200 million Euros per year. In addition, poor collection has lead to merger of the *defaulting enterprises* with Srbijagas, by converting Srbijagas's claim to capital (Azotara, MSK, earlier - Agroživ). However, the merged enterprises are themselves poor performers, bringing additional burden to Srbijagas's balance sheets while the collection rate remains low. In addition to the above, Srbijagas needs to *be organisationally transformed* in line with the regulations of European Energy Community. In 2015, a certain "respite" in the unsustainable business operation of Srbijagas came from an extreme drop in gas prices. This allowed Srbijagas to increase the collection rate for the gas delivered, especially from the petrochemical complex (Azotara, Petrohemija, MSK) as the prices of their products are not that strongly correlated with the energy market and did not fall as drastically. In addition, low prices of fuel were also good news for city central heating plants, together with an unusually mild winter, allowing the heating plants to not only keep up with the regular gas payments to Srbijagas, but also to repay some of the debt that had accumulated over the years. This "respite", however, is only temporary and Srbijagas failed to use it to bring in substantial changes into its operations. In 2015, the status of the enterprises that had been merged with Srbijagas (Azotara, MSK) was not resolved; although it was announced, the principle of suspending the delivery of gas to buyers who were not keeping up with their bills regularly (Staklara Paraćin) was not applied; and Srbijagas failed to undergo even the relatively painless status change. Perhaps the most illustrative example of the irresponsible approach is the fact that the somewhat more profitable performance in 2015 was used up by generous bonuses distributed to employees. The fact that this happened in the year when the public sector salaries were cut speaks to a lack of control and awareness that practically all citizens in Serbia are paying enormous sums to cover for the poor performance of Srbijagas and that a reform of its operations is necessary.

During 2015, Železnice took significant steps forward in the reform – but impasse was reached as soon it came to certain painful measures (downsizing). Poor performance of Železnice is visible both on the expenditure and on the revenue side of their balance sheets. On the expenditure side, the largest problem is the surplus of employees estimated to about a third of the total number of employees, while expenditures for salaries even surpass the total operational costs of this enterprise (exclusive of the state subsidies). In addition, Železnice maintain a very irrational railway network, of which at least 20% is unjustifiable in terms of passenger and freight transport. On the enterprise's revenue side, the largest problems come from an inadequately low passenger ticket price and a low collection rate (both in passenger and in freight transport). From August 2015, first concrete measures were taken to improve the business performance of Železnice, through a status change: *Železnice Srbije* were divided into four separate companies (for passenger transport, transport of goods, infrastructure management and a holding company). This is a justified step from the viewpoint of increasing business operations efficiency and is in line with good international practice. In October 2015, *a good Plan for the reform of Železnice 2016-2020 was adopted*, recognizing practically all the burning issues of this enterprise and offering some concrete solutions and measures to be undertaken towards this goal. These measures are: 1) a decisive decrease in the number of employees (by more than 6,000, i.e. a third, in five years); 2) rationalization of the railway network (cancellation of lines in classes 5 and 6 by the end of 2017, i.e. reduction of the railway network by over 800 km); 3) increasing the price in passenger transport; 4) increasing the collection rate and 5) increase in investment activities. The fact that the downsizing plan calls for (justified) lay-offs of about15% of employees in the first year of reform attests to the serious and professional approach to the plan, unlike EPS, which plans to downsize by only about 1,000 employees in 2016, which represents the approximate number of employees retiring from this enterprise in a year under regular circumstances (and even this downsize in EPS will probably not take place). Finally, there have been changes in the *manner of subsidizing Železnice,* which occurred concurrently with the change in the organizational structure. Unlike the lump sum determination of total subsidies, from January 1, 2016, subsidies for Železnice are directly linked with the achievement of predetermined results (such as kilometers of passenger travel, railway quality, network capacity, safety in traffic etc). During 2016 after a successful start in 2015, the first problems in the reform of Železnice occurred in relation to downsizing. This is a bad sign, but hopefully not an announcement that the decisive implementation of the good reform plan for this enterprise is being abandoned.

Combating grey economy suppression can significantly increase public revenue and thus make up for the absence of a part of the planned savings. Frequent (and unjustified) objection coming from the Government, sometimes even to the work of the Fiscal Council, is that the only comments heard in public are those criticizing its work, with no proposals of possible solutions for the problems it faces. One of the possible solutions that would have a serious fiscal impact is grey economy suppression. Serbia is a country with a high rate of grey economy and there are estimates that a more efficient fight against the grey economy in medium term could lead to a 1% of GDP increase in public revenue. This is the sum approximately equal to the planned savings from general government downsizing, in medium term (which will not unfold as planned) and could even make up for it completely. However, the options leading to quick solutions were exhausted in 2015 and further suppression of grey economy will require in-depth reform and systemic Tax Administration improvements. At the same time, the Fiscal Council estimates that the *National Grey Economy Suppression Program*, adopted by the Government in December 2015, is inadequate and that it will not lead to a significant increase of public revenue collection. Instead, the Government should direct its efforts to the Tax Administration reform. The plan for this reform has been in existence for almost two years (*Tax Administration Transformation Program for 2015-2020*), but it is not being implemented at an adequate rate. This is why it is necessary that the relevant state institutions recognize Tax Administration as a key institution in the suppression of grey economy and allow it and encourage it to keep improving its operations.

Consistent implementation of the planned salary and pension freeze in the public sector in the upcoming two years has no alternative. In addition to the aforementioned Tax Administration reform, the Government has at its disposal a limited set of measures for deficit decrease (apart from the economically inferior tax increase). There is certain room still for budget savings (about 0.2% of GDP) in the reform of local government funding, as there is currently a fiscal imbalance between the central and local governments. The Ministry of Finance has proposed a good draft of the new Law on Local Self-Government Funding, which the Fiscal Council supports, but its adoption is already running late and there are fears that it may be abandoned or substantially changed. It is particularly important that the new

Law be adopted as soon as possible, being that the local governments are not adhering to the legally prescribed limitations on expenditures for salaries (in 2015, due to the salary cut and hiring ban, the local government expenditures should have decreased by 10% compared to 2014, but were reduced by less than 7%). This is why there is a threat that the existing funds at the local government level would be used for irrational and unjustified increase in expenditures for salaries – which is difficult to reverse. In addition to the reform of local government funding, perhaps there is some room for savings in the reform of the social welfare system, being that only a small proportion of these funds is treated properly (financial welfare, former material provisions for families), while the majority of funds used for welfare are being spent unselectively and going to those that are not socially vulnerable. Still, the room for savings from this reform is probably even smaller than from the reform of local government funding. The analyses of the Fiscal Council therefore show that there are currently no measures powerful enough to serve as an alternative to the planned salary and pension cut, i.e. that this is still one of the crucial measures for public finance recovery that should absolutely not be abandoned.

The increase in public investments is probably the only measure on the expenditure side that could have a significant positive impact on economic activity, but there is no such increase in the Government's plans. Public investments increase would not only increase the GDP in the short term, but the improvement of infrastructure quality would encourage private investment in the medium term as well – giving public investments a double role in economic growth. However, the government is not only inefficient in their implementation, it is also not planning to increase them before 2018 – as can be seen in the Government's plan presented in the Fiscal Strategy. Government spending on investments has been planned at the same (inadequate) level from 2015, at approximately only 3% of GDP (even though they should be at about 4-5% of GDP for a country of similar development level). A more detailed analysis of the existing investment projects (and some of those planned) showed that not only the public investment plan for medium term is not harmonized with Serbia's real needs, but that it also does not correspond to the announced deadlines for the completion of the largest infrastructural projects.

Stopping the increase of public debt in comparison to GDP will be a major challenge for the Government. Graph 1 shows three public debt trends, depending on the fiscal policy implemented by the Government in the upcoming three years, summed up from the Fiscal Council's analyses. *The first* trend would correspond to a consistent implementation of the policy of salary and pension freeze, Tax Administration reform to make up for the now definite underperformance of savings from general government downsizing and successful reform of, or lack of unplanned fiscal expenditures on, Srbijagas, EPS, Železnice and enterprises undergoing privatization. *The second* trend would result from a partial implementation of reforms. In other words, public enterprises would be reigned in and the privatization process completed with no new fiscal expenditures, but an adequate Tax Administration reform would not be implemented and pensions and salaries would be indexed similarly to the end of 2015. *The third* and final trend would correspond to unchanged performance of public and state-owned enterprises and a slow implementation of the planned reforms in the fiscal sector (like that in 2015). The graph shows that only the first trend would lead to a decrease in the share of public debt in GDP, steering Serbia away from a public debt crisis. The Government, therefore, has little choice in 2016 and in several years to come and will need decisiveness and a sharp change in budget management and the management of enterprises under its control, in order to steer Serbian public finances into calmer waters.

Graph 1: Projections of public debt trends for the Republic of Serbia, 2016-2018