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Serbia and Montenegro: Poverty Reduction Strategy Paper—Progress Reports

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Government of the Republic of Serbia

**First Progress Report on the
Implementation of the
Poverty Reduction Strategy in Serbia**

2005

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Acronyms:

AIDS/HIV	Acquired Immuno Deficiency Syndrome
AP	Autonomous Province
CARDS	EU Community Assistance for Reconstruction, Development and Stabilization; this refers to the countries of Albania, Bosnia & Herzegovina, Croatia, FRY Macedonia and FRY
CERI	Centre for Educational Research and Innovation of the OECD
DFID	UK Department for International Development
DPM PRS IFP	Deputy Prime Minister's Poverty Reduction Strategy Implementation Focal Point
EBRD	European Bank for Reconstruction and Development
EU	European Union
FDI	Foreign direct investment
GDP	Gross domestic product
IMF	International Monetary Fund
ISCED	International Standard Classification of Education 1997
LEAP	Local environmental action plan
MIER	Ministry of International Economic Relations
MOP	Family financial support
NBS	National Bank of Serbia
NEAP	National environmental action plan
NES	National Employment Service
NGO	Non-governmental organization
OECD	Organisation for Economic Cooperation and Development
PHC	Primary health care
PRS	Poverty Reduction Strategy
PRSp	Poverty Reduction Strategy paper
RS	Republic of Serbia
SAM	Serbia and Montenegro
SIDA	Swedish International Development and Cooperation Agency
SLSP	Survey on Living Standard of the Population
SMEs	Small and medium-sized enterprises
SMEE	Small and medium-sized enterprises and entrepreneurs
SCG	Serbia and Montenegro
SCTM	Standing Conference of Towns and Municipalities
SCW	Center for Social Work
SFRY	Socialist Federal Republic of Yugoslavia
SIEPA	Serbian Investment and Export Promotion Agency
SIF	Social Innovations Fund
UDR	Underdeveloped regions
UNICEF	United Nations Children's Fund
USAID	United States Agency for International Development
VAT	Value-added tax
WTO	World Trade Organisation

1. INTRODUCTION

1.1 Background

1.1.1. This document is the first annual report on the implementation of the Poverty Reduction Strategy paper for Serbia (PRSp), one of the two main pillars in the Republic's medium-term development framework, submitted by the Government of the Republic of Serbia to the citizens of Serbia and its international development partners, covering the period 2004 until the middle of 2005.

1.1.2. The Government of the Republic of Serbia adopted the Poverty Reduction Strategy paper for Serbia (PRSp) in October 2003, just prior to the call for parliamentary elections in Serbia, which were held on December 28, 2003. The new Government was formed in March 2004. In mid-2004, following an agreement with the Prime Minister, the Deputy Prime Minister of the Government of the Republic of Serbia assumed the responsibility for coordinating and monitoring the activities of the Government institutions with respect to PRS implementation¹. The Deputy Prime Minister's PRS Implementation Focal Point was established and consolidated in the course of autumn 2004.

1.1.3. The PRSp was prepared by means of a new approach—through a wide **consultative process** ensuring the inclusion of all stakeholders to which the PRSp refers. Bringing together these participants in the process of preparing the PRS gave the Strategy legitimacy, resulting in the adoption of the document by the newly elected Government of the Republic of Serbia, which overtook the responsibility for its implementation.

1.1.4. The PRS is a **multi-sector** strategy that serves as a basis for developing and integrating new and existing programmatic documents within different social sectors, i.e. the fields of work of the line ministries and other government institutions. The areas of employment, education, health care and social welfare have been identified as key priorities of the PRS implementation in 2004 and 2005.

1.1.5. The Poverty Reduction Strategy Paper for Serbia and its implementation **complement the efforts of the Republic of Serbia in the European Union integration process**. Both processes are complex and relate to all social and economic sectors. The European Commission's Multi-Annual Indicative Program for 2005-2006 emphasized the complementarity of the goals defined in the European Partnership and the PRSp. The recently adopted National Strategy of the Republic of Serbia for the accession of Serbia and Montenegro to the EU draws on the content and recommendations defined in the PRSp.

1.1.6. **The challenging reforms** facing Serbia are twofold: the post-socialist transition to a market economy and harmonization with the European Union. The previous period of international isolation and regional conflicts deepened these challenges, which from the outset have been complex and far-reaching. Both challenges bring considerable negative short-term effects—a transitional shock for most citizens of Serbia. The PRS thus enables Serbia, as well as other Western Balkan countries that have developed their respective Poverty Reduction Strategies, to alleviate the short-term negative effects of the transition and changes necessary for

¹ This duty was made official in February 2005 by a special decision of the Government of the Republic of Serbia.

accession to the European Union. In this way, the Poverty Reduction Strategy contributes to the building of long-term support for the reform process in Serbia.

1.1.7. The United Nations **Millenium Development Goals** are integrated into the Poverty Reduction Strategy paper for Serbia and the Government of Serbia will use the MDGs as benchmarks of development. The coming period plans a closer link between the methods of monitoring social and poverty-related statistics and the European Agenda on Social Inclusion².

1.1.8. The PRSp also includes a focus on the need to **reform the public administration** with the goal of increasing the efficiency and transparency of policy coordination and governance in implementing the programmatic documents of the Republic of Serbia as well as in improving the way of governing the overall and public sector policies. The work of public administration will be based on the concept of “open Government.” The Republic of Serbia still lacks the capacity for the efficient coordination of policies at the central level as well as the operational knowledge that would ensure the “translation” of the goals defined in programmatic documents into concrete measures and activities. Establishing links between planning and budgetary processes as well as between the planning process and the resources available from international assistance will be of key importance in the forthcoming period. This process shall be facilitated by the introduction of a programmatic budget³, on the one hand, and the efficient implementation of a sector approach in the allocation of international development assistance, on the other. Only this qualitative change in the way in which the public administration operates would ensure a fully transparent and efficient policy implementation, including that of the PRSp.

1.1.9. As the Poverty Reduction Strategy Paper for Serbia was adopted in October 2003, it could not influence the planning or allocation of **budget resources** for 2004. Although the Strategy was included in the Memorandum on the Budget and Fiscal and Economic Policy for 2005 (adopted in May 2004), the activities of public administration institutions in different sectors were not budgeted to directly match the priorities as defined in the Strategy. This was primarily a consequence of the political situation, the elections for the new assembly and the establishment of the new government in March 2004, which resulted in a situation where the national budget for 2005 was rushed through the Government and Parliament as soon as possible after they had been established.

1.2. About the Poverty Reduction Strategy Paper for Serbia

1.2.1. The Poverty Reduction Strategy Paper for Serbia is the **first multi-sector programmatic policy document** created by the Government of the Republic of Serbia, with the participation and contribution from many different—governmental and non-governmental—organizations and institutions. The process of Strategy preparation was marked by an extensive **consultative process** that strengthened the national ownership of the developed policy. As a result, the current Government is fully committed to the implementation of the PRSp even though it was developed under the auspices of the previous Government. Although this process was financed by international funds, the PRSp is a result of the work of national experts,

² The Government of the Republic of Serbia adopted the Review of the Implementation of the Millenium Development Goals in Serbia in May 2005.

³ The Ministry of Finance plans to introduce the programmatic budget as of 2007.

representatives of government agencies and the national and international organizations and institutions that took part in its elaboration⁴. Consequently, the PRS has support from the public and incites the interest of Serbian citizens—primarily because it recognizes that **poverty in Serbia is a problem**.

1.2.2. The Poverty Reduction Strategy represents a **medium-term development framework** directed at reducing the key aspects of poverty by means of creating material and other preconditions and providing opportunities to all citizens to ensure better lives for themselves and their families. The PRS is in line with the National Strategy of the Republic of Serbia for the accession of Serbia and Montenegro to the EU and contains an action plan for achieving the UN Millenium Development Goals (MDGs).

1.2.3. The PRS is founded on the premise that **poverty** is a multi-dimensional phenomenon which, apart from representing insufficient income to cover basic subsistence, also entails the inability to exercise human rights such as the rights to employment, adequate housing and access to social welfare, health, education and communal services. These aspects are particularly relevant to vulnerable and socially marginalized groups. Other key aspects relate to the barriers in exercising the right to a healthy environment and natural resources, primarily clean water and air.⁵

Poverty, especially its extreme forms, was not significantly present in Serbia until the early 1990s. Serbia, as an integral part of the former Socialist Federal Republic of Yugoslavia (SFRY), had a GDP per capita of over USD 3,000, with the majority of its citizens enjoying access to education, health care, social welfare and other services. In the economic and social crash of the 1990s, GDP declined dramatically (by approximately 50%), unemployment rates soared, and wages, pensions and other sources of personal income fell considerably.

The situation improved in the period 2001-2003, primarily due to the successful initiation of reforms and international support, which resulted in a significant growth of GDP, wages, pensions and other sources of personal income. However, this period was too short to compensate for the gap created during the previous decade.

1.2.5. The Poverty Reduction Strategy aims to cut poverty in Serbia almost by half by the year 2010. The main **recommendations/strategic directions** towards this aim are as follows:

- a. Dynamic economic growth and development with an emphasis on job creation within the private sector;
- b. Preventing the emergence of new categories of the poor, i.e. “new poverty” as a consequence of economic restructuring and rationalization of the public administration;
- c. Efficient implementation and preparation of existing and new programs, measures and activities directly targeting the poorest and most vulnerable social groups (children, the elderly, the disabled, refugees and internally displaced persons, Roma, poor rural populations and the uneducated), particularly in the least developed regions of Serbia.

⁴ The preparation of the Poverty Reduction Strategy paper for Serbia was financed by the World Bank-administered Poverty Reduction Strategy Trust Fund (Japanese and Dutch funds), the UK Department for International Development (DfID) and donations from the Danish and Norwegian Governments.

⁵ Poverty Reduction Strategy paper for Serbia, Government of Serbia, 2003.

1.2.6. The Poverty Reduction Strategy Paper for Serbia is implemented in line with the following **principles**:

- Mainstream poverty reduction efforts, i.e. become an integral part of the regular work of the Government (line ministries, central government institutions and bodies, local self-governments) and its partners according to their respective mandates and responsibilities.
- Build strong ownership of the PRS through an inclusive participatory process, emphasizing the active involvement of civil society, private and public sectors, and representatives of vulnerable groups in implementation, monitoring and evaluation.
- Ensure the effective integration and consolidation of European integration and the PRS implementation process, as the main pillars of Serbia's overall reform framework together with relevant sector strategies.
- Change the way the Government “does business” by achieving transparency through a well-defined planning process (including more efficient coordination and prioritization).
- Engage local-level PRS implementation through the participation and cooperation of representatives of local self-governments, the NGO and private sectors and donors as one of the preconditions for the successful implementation of the PRS in accordance with public administration reform and the decentralization process.
- Support partnership building in the PRS implementation with the aim of improving coordination and information sharing, in order to ensure the synergic effects of activities directed at poverty reduction.

1.3. About the Content of the Report

1.3.1. This report presents the results of PRS implementation since 2004 to the middle of 2005, as well as the available data on poverty trends in Serbia. A full PRS policy update can be expected by the end of 2006/ beginning of 2007.

1.3.2. The analysis of poverty trends is based on data from the 2002 and 2003 Survey on Living Standard of the Population (SLSP)⁶ conducted in the period before the PRS implementation. The most recent poverty assessment for Serbia is based on the Household Budget Survey of the Serbian national statistical office, the Republic Statistical Office of the Republic of Serbia. The analysis in this report is a result of the work of the Working Group for Poverty Measurement established by the Government of the Republic of Serbia in February 2005.

1.3.3. Results of the PRS implementation are presented through reports of the participating government institutions, which are organized in such a manner that they follow the structure of the PRSp. An overview of economic trends in the previous period is given in the parts of report that refer to macroeconomic indicators, fiscal policy and measures related to the transition to a market economy. The priority areas of the previous period—employment, social welfare, health care and education—are represented in the segments of report bearing these titles. The report takes into account the regional, rural and urban aspects of poverty, as well as the impact of the

⁶ Survey on the Living Standard of the Population (SLSP) is based on the World Bank's Living Standard Measurement Survey (LSMS) methodology.

environment on the quality of life. An analysis of the allocation of budgetary resources as well as an overview of international assistance is given in order to evaluate the amount of funds directed towards poverty reduction.

1.3.4. Several factors have contributed to the somewhat limited impact analysis of the activities presented in this report. The poverty reduction efforts of the Government of Serbia cut across a number of different sectors; both the complexity of the task and the lack of an established monitoring system contribute to the difficulty of fully assessing the scope of the achieved results. In addition, the existing statistical system is predominantly focused on collecting quantitative rather than qualitative data, while a poverty-related monitoring system will be developed only in the upcoming period.

2. POVERTY STATISTICS⁷

2.1. Activities Related to Poverty Measurement

2.1.1. One of the Government of Serbia's goals is the creation of a solid statistical base for continuous and reliable poverty measurement as well as the engagement of the expert resources in poverty diagnostics. Monitoring yearly poverty rates gives policy-makers powerful synthetic information about the trends in the standard of living and social inequality, while detailed poverty profiles provide key input for programs and policy measures aimed at both reducing specific forms of poverty as well as facilitating the social inclusion of the most vulnerable groups.

2.1.2. Since 2002 there have been two phases in the development of poverty statistics. The first phase was marked by two consecutive Surveys of the Living Standard of the Population (SLSP) in 2002 and 2003, conducted at the request of the Government of Serbia and supported by the World Bank's expertise. Creating the PRSp in 2002-3 would not been possible without the critical and timely input from the SLSP surveys.

2.1.3. The second phase is characterized by a 2004 strategic decision to base poverty statistics on data collected by the Household Budget Survey (HBS), conducted (unlike SLSP, which was produced by a private survey firm) on a permanent basis by the Republican Statistical Office. HBS data collection will secure full national ownership and much-needed long-term continuity in poverty statistics, as well as assist with capacity building within the RSO.

2.1.4. In order to facilitate this process, in February 2005 the Government tasked the Deputy Prime Minister with establishing the Working Group on Poverty Measurement. This group consists of RSO professionals as well as leading national experts who had also been engaged in the production and analysis of the SLSP surveys. The Group's task was to comprehensively analyze the methodological and empirical features of the SLSP and HBS and to suggest methodological solutions for creating poverty indicators based on the HBS. The Group should also facilitate wider discussion on the poverty line or subsistence minimum, suggesting the standard for monitoring the RSO, promote training in poverty analysis and encourage a wider research community.

⁷ Prepared by the Working Group for Poverty Measurement, established in February 2005 by a special act of the Government of Serbia.

2.1.5. Among the above-mentioned surveys there is a number of important methodological differences that are dealt with by the WGPM, RSO and the World Bank experts. The first set of differences derives from the way in which the SLSP and HBS gathered data on consumption: The HBS collected data throughout the year, while the SLSP took a measurement for a single month (June). The surveys also differ in the scope of food consumption modules. HBS followed a standard approach recommended by Eurostat, collecting detailed data on consumption based on the diaries filled out by respondents themselves. The SLSP used a shorter form but allowed the interviewers more active control over the data provided. The two surveys thus captured very different patterns of food consumption. The minimum food basket developed from the SLSP data must therefore be revised to account for the much more detailed set of items collected in the HBS.

2.1.6. The second set of issues arises from measuring the flow of services from owner-occupied housing. The SLSP relied on a special survey of the real estate market to impute the value of housing rents and arbitrarily set the interest rate to estimate the annual rents. The HBS collected data from households according to the owners' own assessment of the rental value of their housing. This data contained a number of outliers and problematic entries because the housing market remains very thin in many areas of the country, and respondents were not able to estimate the rental value of their homes. However, this implicit rent information can potentially be used in conjunction with other data to periodically assess on the value of housing in Serbia and the welfare of households. Such ongoing will result in a more realistic assessment of the poverty situation.

2.1.7. The third set of issues comes with the development of a non-food component in the subsistence minimum. The method selected for the SLSP used the well-known Engel law, which relates non-food consumption to the overall welfare of the household. Using the regularity of the relationship between the consumption level and poverty, the parametric analysis helped establish a level of total consumption that is required to meet basic food and non-food needs. Although there are advantages to the non-parametric approach, which relies entirely on capturing the poor's actual consumption patterns, the use of the parametric approach currently ensures a much needed robustness with respect to data problems. In any case, re-estimation of the non-food component is necessary as the nature of HBS data differs from that of the SLSP.

2.1.8. The forth and final set of issues comes from cleaning the data from outliers and inconsistent entries. The RSO, with the assistance of the WGPM and the World Bank, is developing procedures that have not yet been completed. The on-going work will result in the final dataset that will be used for poverty assessment.

2.2. 2003 SLSP Poverty Trends

As a part of efforts to better understand poverty and to create a comprehensive poverty profile for Serbia, the Government of Serbia and its then Ministry for Social Affairs conducted the Living Standard Measurement Survey for the two consecutive years of 2002 and 2003. The 2002 sample size included 6,380 households with 19,725 members, while the 2003 survey was conducted using a sub-sample of 2,548 households (8,027 individuals) which were all surveyed in 2002. Methodological solutions as well as timing (May15-June 15) were kept the same, in order to achieve full comparability. A panel feature in the 2003 survey was instrumental in following changes within the same households between the two surveys.

Main poverty indicators in Serbia in the period 2002-2003

2.2.1. The percentage of the poor and extremely poor remained unchanged irrespective of the significant economic growth recorded in the period 2002-2003.

2.2.2. In 2003 one in 10 citizens in Serbia (10.5%) was poor, with a consumption per adult equivalent below CSD 4,970/month on average. (Table 2.2.a.). Similar to the previous year, extreme poverty was negligible, with only less than one percent of the population recording an average consumption below CSD 2,097/month per adult equivalent—the amount of the minimum food basket.

2.2.3. Compared to other countries in the region and using a poverty line of USD 2.15 /day PPP and the comparable consumption aggregate, the percentage of the poor in Serbia was similar to the rate of Romania, lower than in Albania and higher than in Bulgaria and Poland (ECAPOV II, World Bank, 2005).

Table 2.2.a. Poverty indicators in Serbia, 2002-2003 (in %)

The poor	Poverty index	Poverty Gap	Severity of poverty
2002	10.6	2.2	0.8
2003	10.5	2.0	0.6

Note: In 2002 the poverty line equaled CSD 4,489 per month per adult equivalent, while in 2003, it was CSD 4,970. Source: SLSP for 2002 and 2003.

2.2.4. In comparison to 2002, in 2003 the depth (gap) and severity of poverty declined slightly, although the percentage of the poor remained unchanged. The poverty gap in 2003 equaled 2%, indicating that if the country could mobilize resources amounting to 2% of the poverty line for each person (poor and not poor) and direct these resources towards the poor, poverty would, theoretically, be eliminated, provided that such assistance was perfectly targeted. The severity of poverty—the indicator which takes into account that some of the poor slide deeper into poverty, i.e. further than others below the poverty line and gives them greater weight—reached 0.6%.

Economic mobility of the population in Serbia 2002-2003

2.2.5. Though the percentage of the poor remained unchanged between 2002 and 2003 (4,5%), there was significant population mobility given the numbers that either

moved out of or fell into poverty (Table 2.2.b.)⁸. Slightly over one half of the poor recorded in 2002 improved their economic status and moved out of poverty one year later. However, approximately the same number of persons became poor in 2003, with the “new” poor comprising slightly over one half of the poor in 2003.

Table 2.2.b. Economic mobility of the population in Serbia, 2002-2003 (in %)

	Not poor in 2003	Poor in 2003	<i>Total</i>
Not poor in 2002	83.3	6.1	89.4
Poor in 2002	6.2	4.5	10.6
Total	89.5	10.5	100.0

Source: SLSP for 2002 and 2003.

2.2.6. The considerable population mobility towards/out of poverty results from a large growth in consumption of those who moved out of poverty (approximately twice, on average) and a large decline in consumption among those who became poor (43%). Growing consumption was also recorded among persons whose status remained the same (9.5% among persons who were not poor and 10.8% among those who remained poor).

Table 2.2.c. Mobility of the labor force in Serbia, 2002-2003 Status in 2002=100 (in %)

	Employed in 2003	Unemployed in 2003	<i>Inactive in 2003</i>
Employed in 2002	81.8	3.3	14.9
Unemployed in 2002	47.7	25.4	26.9
Inactive in 2002	15.1	3.0	81.9

Source: SLSP 2002 and 2003.

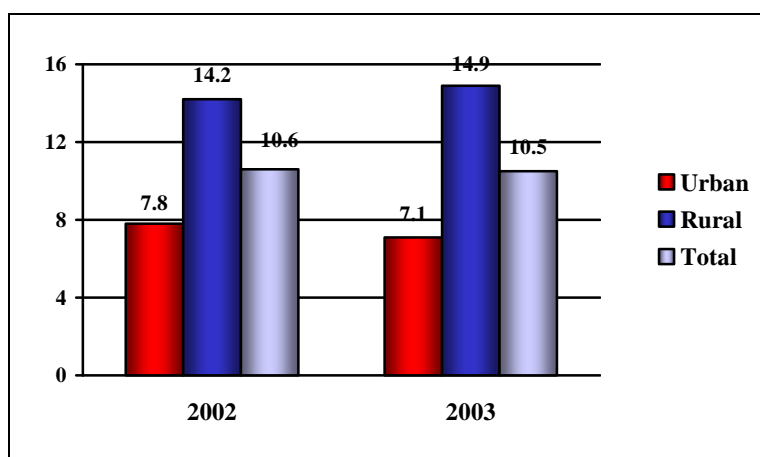
2.2.7. The significant economic mobility may be explained, *inter alia*, by the considerable mobility of the labor force. The percentages on the diagonal in Table 2.2.c. suggest a significant reallocation of the work force within a one-year period, especially in the case of the unemployed. One half of the unemployed in 2002 found employment in 2003, though one half of those jobs were in the gray economy. The informal sector has thus significantly improved the mobility of the labor force.

Poverty by regions in Serbia over 2002-2003

2.2.8. In Serbia, poverty is still a predominantly rural phenomenon (Graph 2.2.d.), like in most countries in transition (ECAPOV II, World Bank, 2005); in 2003, poverty in rural areas was twice as high (14.9%) as that in the urban areas (7.1%). The difference in poverty between urban and rural areas was slightly higher in 2003 as compared to 2002 (14.2% rural to 7.8% urban). This may be explained by the fact that the growth in employees’ earnings and pensions in real terms in 2003 relative to 2002 – the dominant source of income among the urban population—was relatively higher compared to the growth in other sources of income.

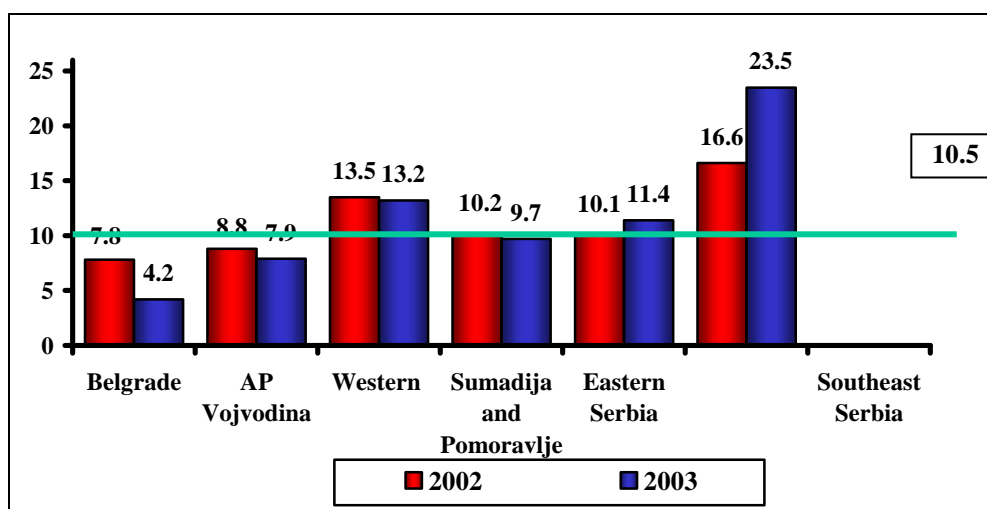
⁸ Based on panel data (SLSP 2002 and 2003), ensuring monitoring trends in living standards of the same persons over a one-year period (May-June 2002 and May-June 2003).

Graph 2.2.d. Percentage of the poor by type of region in Serbia, 2002-2003



Source: SLSP for 2002 and 2003.

Graph 2.2.e. Percentage of the poor by region in Serbia, 2002-2003



Source: SLSP for 2002 and 2003.

2.2.9. The largest share of the poor in 2003 was in Southeast Serbia (23.5%), while the lowest share was recorded in Belgrade (4.2%). In comparison to 2002, the highest growth of poverty was recorded in Southeast Serbia (41.6%), while the largest decline was registered in Belgrade, where the percentage of the poor was almost halved (Graph 2.2.e.). The data indicate widening regional differences in poverty: the ratio of the poverty index in Southeast Serbia and Belgrade equaled 5.6 in 2003, while only one year earlier it amounted to 2.1. The share of the poor in the total population declined slightly in the autonomous province of Vojvodina, Šumadija and Pomoravlje, as well as in western Serbia, while it increased slightly in eastern Serbia.

In spite of considerable impoverishment over the last 15 years, Serbia is still within the category of medium developed countries, although on a lower level when compared to the beginning of the crisis in the 1990s.

Serbia and the region. When compared to other countries in Eastern Europe, poverty in Serbia is almost at the same level as in Romania, lower than in Albania and higher than in Bulgaria or Poland⁹. When it comes to the Western Balkans, poverty is lowest in Croatia (8,4%) and highest in Albania (over 25%), as well as in Kosovo, where half of the population lives below the official poverty line¹⁰.

Objective and subjective poverty. The image of subjective poverty somewhat differs from the image suggested by the poverty line. The subjective perception of poverty in the Western Balkans is much higher—in Serbia, at least half the population is dissatisfied or mostly dissatisfied with their financial situation¹¹. Comparison with historically higher living standards has largely contributed to such a perception, as has high expectations concerning a faster overall economic revival after the democratic political change.

Preliminary Poverty Data Based on the Household Budget Survey (2003-2004)¹²

2.2.10. The SLSP data provided important insights on the situation, extent and profile of poverty in Serbia in 2002-2003. However, the SLSP was never intended to become a regular source of official statistical information on living standards and poverty. The improved design of the household budget surveys conducted by the RSO since 2003 has offered an excellent opportunity to use the HBS as the main permanent official source of information on poverty, providing both a wealth of data for research and crucial indicators for policy creation in this area. It is important to note that HBS data are not straightforwardly comparable to the SLSP.

2.2.11. Preliminary results based on the HBS indicate that there are no significant changes in the poverty level between 2003 and 2004. The data presented here are only indicative, with their main purpose to provide insight into the current trends.

2.2.12. Table 2.2.f. below shows a range of estimates obtained using several different, standard methodological approaches to estimate absolute poverty with the HBS data. The ranges are relatively wide, indicating a high concentration of the population around the poverty line. This is further supported by the preliminary results for the Gini co-efficient, which comparatively are quite low at slightly below 0.30 in both 2003 and 2004. The poverty rate ranges obtained from the HBS correspond with the ranges obtained by applying alternative methodologies to the SLSP data in 2002 and 2003.

⁹ World Bank, 2005, ECA POV II.

¹⁰ Matkovic, Gordana, 2005, *Overview of Poverty and Social Exclusion in the Western Balkans*, a paper prepared for the Western Balkan Forum on Social Inclusion and Millennium Development Goals, 23-24 June, Tirana, Albania.

¹¹ Ibid.

¹² The Poverty Reduction and Economic Management Unit for Europe and Central Asia Region participated in the preparation of preliminary poverty data as expert and technical support to the Working Group for Poverty Measurement.

Table 2.2.f. Upper Ranges for Preliminary Poverty Estimates, based on the 2003-2004 HBS

Region/Location	Poverty rates ranges for different methodologies, Serbian Scale (%)	
	2003	2004
Belgrade	2 – 7	2 - 5
AP Vojvodina	13 – 19	16 - 24
Central Serbia	12 – 27	16 - 26
Rural	15 – 28	20 - 31
Urban	8 – 14	7 - 13
Serbia	11 – 20	13 - 20

Note: Adjusted for inflation; the period March-December of each year is used for comparability.

2.2.13. Table 2.2.f. lists upper poverty rate ranges based on HBS data that have not undergone final consistency checking; final estimates will gravitate towards lower ranges. Although perhaps the exact level of poverty may still remain uncertain, the emerging poverty profile will not significantly differ from the final set of data.

2.2.14. Preliminary data reported in Table 2.2.f. show that pronounced regional differences in the living standards as revealed by the SLSP persist in the HBS as well. As noted in the analysis of the SLSP, despite an overall stable poverty level between 2002 and 2003 significant differences emerged. The gap between urban and rural areas has widened, and as well as between poor and rich regions, especially between Belgrade, which benefited the most from new economic opportunities and growth, and the rest of the country.

2.2.15. Fully in line with the SLSP results, the 2003 and 2004 HBS revealed that Belgrade's poverty incidence remains far below the national average, while rural areas clearly suffer from an elevated poverty risk. Over time, Belgrade's position compared to the rest of the country has continued to improve, while rural areas clearly lag behind. The persistency of rural poverty and the limited reduction in urban poverty suggest that the opportunities generated by substantial economic growth are not available to all citizens equally.

2.2.16. Compared to the SLSP, the preliminary HBS data implies that the relative position of the autonomous province of Vojvodina is significantly worse, counterintuitive to most observers. Such an indication may be a statistical artifact that may be resolved by further methodological and measurement refinements. However, the tentative results may also reflect some real problems in the region, ranging from a faster pace of transition and restructuring that temporarily brings greater inequality and higher unemployment rates, to an unfavorable demographic situation, reflected e.g. in a high number of elderly rural households and lower rental prices.

2.2.17. A more informative picture of regional differences requires analysis at a somewhat lower level of regional aggregation. The approach chosen in the SLSP, which divides central Serbia into three distinctive regions with different poverty rates and profiles, should be built into the future sampling design of the HBS.

2.2.18. The final data, once available, will be used to monitor the effects of the reform process as well as to guide policy making in order to address issues of rural poverty, lagging regions and socially excluded groups. Preliminary results for 2003-2004, based on the HBS, confirm that the insights provided by the SLSP could still be used to develop policies and programs aimed at poverty reduction.

3. PRS IMPLEMENTATION: REPORTS OF THE GOVERNMENT INSTITUTIONS ON POVERTY REDUCTION RELATED ACTIVITIES

Despite a number of initial challenges and barriers, the implementation of the Poverty Reduction Strategy Paper for Serbia witnessed significant progress in 2004. This section of the report illustrates the results achieved through activities undertaken by government institutions and represents a synthesis of their individual reports.

The ministries and other state institutions do not possess mechanisms at this point that would ensure the systematic monitoring of PRS implementation or activities directed at implementing its programmatic goals and priorities. Therefore it is the Government's priority to develop and set up an effective and transparent monitoring and evaluation system during the coming period.

In order to most adequately report on the implementation of the measures and activities recommended by the PRSp, governmental institutions prepared their reports on the basis of a tailored set of questions stipulated in the PRSp¹³ and related to the work of each institution. Thus this part of the report observes the structure of the Poverty Reduction Strategy paper for Serbia and offers an overview of the implementation of measures and activities across 12 segments, as structured in the Strategy.

Although the measures and activities directed at improving the status of vulnerable groups (refugees and the internally displaced, the disabled, youth, children, Roma and women) in the PRSp are also presented in a separate chapter¹⁴, reporting on the progress in the implementation of planned measures is an integral part of the report's 12 segments.

The first steps for creating a system for monitoring activities according to the programmatic goals are being taken through a pilot project entitled "Joint Project: towards a more efficient implementation of reforms," implemented by the Government of the Republic of Serbia¹⁵.

¹³ The questions were formulated on the basis of measures and activities stipulated in the PRSp, in the chapter "Resume and Activity Matrices."

¹⁴ PRSp chapter: "Cross-Cutting Issues in the Poverty Reduction Strategy."

¹⁵ For details on the project, see the chapter "Transition to market economy – Building more efficient state institutions."

3.1. Macroeconomic Framework and Factors of Sustainable Economic Growth¹⁶

Macroeconomic stability was established in 2001-2002, along with the initiation of the main structural reforms, representing a solid basis for continuing reforms and medium-term growth—the key prerequisite for poverty reduction. The macroeconomic policy was directed at removing the main imbalances and creating the conditions for medium-term sustainable macroeconomic stability.

The previous period was marked by continuous GDP growth (reaching 8.6% in 2004), a rise in FDI, a reduced foreign debt to GDP ratio and satisfactory progress in reform of the Serbian banking system. The current account deficit and the speed of structural reforms remain challenges for the future, which have already been addressed by various measures that should improve the competitiveness of the Serbian economy.

Notwithstanding significant progress in many areas of transition, deep structural weaknesses remain. The key determinants of the potential for growth, such as exports, investments and national savings, are still at a very low level. Macroeconomic imbalances and the burden of debts continue to render the economy sensitive to shocks.

3.1.1. The real growth rate of **Gross Domestic Product (GDP)**, following a modest growth of 2.4% in 2003, is estimated to have reached 8.6% in 2004, much higher than expected. A lower rate of real GDP growth (4.6%) is projected in 2005 as a result of planned measures directed at slowing the rise of prices and improving the trade balance. Over a medium-term period (2004-2006) average annual GDP growth rates of approximately 5.9% are expected. In the period between 2006 and 2008, a GDP growth of 5.7% is expected, while inflation should be brought down to 4.5% by the end of the same period.

3.1.2. The **current account deficit** in 2004 equaled USD 2.8 billion i.e. USD 3.447 billion¹⁷, excluding official international assistance, which is an increase of 43.8% when compared to 2003. Consequently, the share of the current account deficit (without official support) in GDP increased from 11.7% in 2003 to 15.6% in 2004. The major cause for the higher current account deficit is the increase in the trade deficit. At the same time, the rise in imports related primarily to production materials and equipment, giving 2004's higher current account deficit a predominantly developmental character. Although exports increased from USD 2 million in 2002 to almost USD 4 million in 2004, the imports registered a higher increase—from USD 5.6 million in 2002 to almost USD 11 million in 2004. The reserves of goods imported in late 2004 satisfied local demand for imports resulting in a significant reduction in the first months of 2005. The exports recorded considerable increase in early 2005 thanks, *inter alia*, to the introduction of a value-added tax (VAT).

3.1.3. 2003 was a record year for the influx of **foreign direct investments**, which reached USD 1.36 billion. Due to a slow-down in the privatization process in the first half of 2004, FDI fell to USD 966 million. The projected FDI in 2005 is a minimum

¹⁶ The institutions that bear greatest responsibility for implementing PRS aims with respect to macroeconomic policy are the Ministry of Finance, the National Bank of Serbia and the Serbia Investment and Export Promotion Agency.

¹⁷ EUR: USD: CSD= 1:1.2:69.99 (average in the period January-June 2004.), EUR: USD: CSD= 1:1.26:75.14 (average in the period July-December 2004.), EUR: USD: CSD= 1:1.30:80.75 (average in the period January-May 2005).

USD 1 billion. The Serbia Investment and Export Promotion Agency (SIEPA) initiated a project¹⁸ worth EUR 4.5 million that will enable Serbia to develop investment locations and launch new investment projects.

3.1.4. **The share of investments in GDP** recorded a more modest increase than the one projected. Total investments grew from 13.6% in 2001 to 16.4% of GDP in 2004. The Strategy provides that the share of investments in GDP should reach approximately 25% by 2010.

3.1.5. Following a drop in the **rate of inflation** from 14.8% in 2002 to 7.8% in 2003, the increase of prices in 2004 equaled 13.7%. In the first nine months of 2005, the growth of retail prices amounted to 11.8%¹⁹, and it is expected that by the end of the year inflation will not exceed the previous year.

3.1.6. Following **agreements with the Paris and London clubs of creditors**, the share of external debt in GDP was reduced from 78.6% in late 2002 to 63.8 % in late 2004. The external debt amounted to approximately USD 14.1 billion in late 2004. It is expected that the Paris Club of Creditors will write off over USD 700 million in debt by the end of 2005, after the satisfactory conclusion of the agreement with the IMF.

Table 3.1.a.: **Macroeconomic indicators**²⁰

	2002	2003	2004
GDP real growth (%)	4.5	2.4	8.6
Core inflation (NBS)	6.0	5.4	11.5
Retail prices (end of period)	14.8	7.8	13.7
Foreign direct investment (millions of USD)	475	1,360	966
Donations (millions of USD)	559	360	456
Trade deficit (%GDP)	24.8	24.7	32.8
Current account deficit (%GDP)	13.5	11.7	15.6
Public revenues	44.3	43.1	45.2
Public expenditures	47.7	44.3	44.6
Fiscal deficit/ surplus	-3.4	-1.1	0.6

Note: The data for 2005 will be comprised in the revised Memorandum on Budget and Economic and Fiscal Policy for 2006 with projections for 2007 and 2008.

3.1.7. **The reform of the banking sector** is entering its final phase following several years of restructuring and consolidation through the liquidation of insolvent and illiquid banks, the entry of foreign banks, strengthened competition among financial institutions, improved legal framework for bank supervision and the enhanced transparency of business operations and bank ownership structure. Reform of the banking sector shall be completed upon full implementation of the initiated **process of privatization of state share in banks** and full harmonization of laws and bylaws with the relevant directives of the European Union and the Basel Principles.

¹⁸ Implemented with an EU donation, through the CARDS program.

¹⁹ The Memorandum on Budget and Economic and Fiscal Policy for 2006 with projections for 2007 and 2008. At the time this report was prepared there were indications that the rate of inflation would exceed the projected level.

²⁰ The Memorandum on Budget and Economic and Fiscal Policy for 2006 with projections for 2007 and 2008.

3.1.8. The **promotion and increase of exports** have made significant progress due to regional free-trade agreements, favorable terms for exports to the EU, privatization and restructuring of formerly socially owned enterprises, easier access of new private companies to foreign markets, etc.

3.1.9. **Forthcoming challenges:**

- Increasing exports will require continued efforts towards improving the business climate, reduced costs for doing business and the creation of flexible and competitive market structures, which should lead to an increase in FDIs and consequently an increase in exports.
- Increasing the ratio of private investments to GDP. In the short term, attracting foreign direct investments should be the major policy for increasing the level of new private investments. So far, most private investments have been through privatization. The key challenge will be the creation of a business environment conducive to private greenfield investments.
- Raising the credibility of the banking sector, and thus creating incentives to encourage the long-term savings of citizens.

3.2. Fiscal Limitations in PRS Implementation²¹

The reform of public finances, which began in Serbia in 2001-2003, has achieved significant progress in transforming the fiscal system into a more transparent, simple structure aligned with European standards. Such reform has strengthened the ability of public finances in achieving the main goals of macroeconomic stability and sustainable economic growth.

Due to significant tax policy reform, a consolidated fiscal surplus is envisaged for 2005 and onwards. The continuing tax reforms aim to reduce taxes, broadening the tax base, raise the share of expenses in GDP related to investment, capital expenditures and education and lower the share of expenses related to defense, police, health and social welfare (social insurance funds).

The policy of the Government in the forthcoming medium-term period is to preserve fiscal stability while continuing to reduce public expenditures and taxes, make better use of fiscal resources and ensure greater mobilization of public revenues, including tax incentives and other reform measures aimed at raising the level of business activities.

3.2.1. Thus far the most important **tax policy reforms** were made in the course of 2004, signaling the third phase of earlier taxation regime changes and completing the planned modernization of the taxation system. The Republic Budget has reached fiscal surplus through tax policy reform measures directed at relieving the burden on the economy and the citizens, i.e. reducing taxes and increasing taxation capacity (introducing fiscal cash registers, enforcing the more efficient control of tax collection, etc.). These measures are expected to result in a decreased share of total expenditures in GDP, with greater allocations for investment and capital expenditures.

²¹ The institutions that bear greatest responsibility for implementation of PRS objectives with respect to fiscal restrictions are the Ministry of Finance and the National Bank of Serbia.

3.2.2. The most significant changes²² in tax policy in 2004 include the Law on VAT, the Law on Income Tax, amendments to the Law on Corporate Income Tax, the Law on Excise Tax, the Law on Property Tax, Amendments to the Law on Using, Holding and Carrying Goods, the abolishment of the Income Fund Tax and the Financial Transaction Tax.

3.2.3. The new **Law on Value-Added Tax (VAT)**, which came into effect on January 1, 2005, stipulates a **general VAT rate of 18%**, with a **special 8% rate** applicable to, *inter alia*, the trade or import of certain basic foodstuffs; medications paid from health insurance funds; certain medical supplies, text books and teaching materials; daily newspapers; communal services, etc. **VAT is not imposed on** services provided by health institutions, including the accommodation, care and meals of hospitalized patients; services provided by medical doctors, dentists, and similar professionals; social welfare and care services, including child and youth protection, social protection services; accommodation and meals for students in hostels and similar institutions; and education and professional retraining. These measures, therefore, include some of the most significant categories of interest to the Poverty Reduction Strategy paper for Serbia.

3.2.4. The first **results of introducing VAT** (combined with the introduction of fiscal registers) suggest significantly rising fiscal revenues and a declining gray economy. Local self-governments recorded a surplus of approximately CSD 4 billion²³. Judging by initial analyses, the introduction of VAT should have a neutral effect on rising prices: the calculated average tax rate decreased and conditions were created for a drop in prices of up to approximately 1.7%. Further to the decreased average tax rate influencing the slow-down of inflation, the initial period of VAT saw a slight rise in inflation due to other factors related to its introduction²⁴. Thus, the expert analyses²⁵ show a certain increase in the tax burden on the poor. To address this problem, in July 2005 the Government adopted **changes to the Law on VAT** by which additional categories of goods and services (medications, basic foodstuffs, new apartments, livestock, etc.) are taxed by a lower VAT rate of 8%. In addition, humanitarian aid and foreign donations are exempted from paying VAT.

3.2.5. In the forthcoming period, further **harmonization with EU legislation will be implemented** (including tax exemptions in the Law on Value-Added Tax, as mentioned above). A combined system of taxing personal income might be replaced by the synthetic income tax in effect in most EU countries; the system of taxing the yield on capital shall also be reformed to avoid double taxation.

3.2.6. One new measure that has already proved effective is the reduction of the **corporate income tax from 20% to 14% (2003), and subsequently from 14% to 10% (2004)**. This represents one of the lowest corporate income rates in the region and has already rendered an over 60% increase in the collection of taxes.

²² For comprehensive list of financial legislation, see Annex 6.2

²³ Source: Ministry of Finance.

²⁴ Since VAT moves the time of tax payment from the sale of goods/services to the moment of input procurement, one can expect that economic agents run into problems related to the decline of solvency and compensation accompanied by certain price increases. In addition, enhanced coverage of the gray economy may have led to a slight price increase in the prices of goods/services that have now become legal (with calculated and paid taxes).

²⁵ Supported by DFID.

3.2.7. Another priority of the medium-term period 2006-2008 shall be **adjusting the customs policy** to the dynamics of development and economic integration with the mandatory harmonization with WTO requirements. Customs policy measures will gradually reduce the level of customs protection, a condition for accession to the EU and membership in the WTO.

3.2.8. In 2003 payment operations were transferred to the banks and the **Treasury of the Republic Budget was established**.

3.2.9. The Tax Administration has been **modernized**, a continuing process that will improve the quality of the service and supervision of tax administrators, ensure strict implementation of tax legislation and improve the organizational structure and capacity of the administration. The introduction of an IT system in the Tax Administration, Customs Administration and UJP (“Uprava za javna plaćanja”) seeks a more efficient tax collection as well.

3.2.10. Reform of the tax system with regard to public revenues will be followed by reform of the public expenditure system at all levels. The reform will target budget expenditures as well as expenditures of the compulsory social insurance institutions. The reform of public expenditures requires gradual reform of the public administration system and public services as well as the careful evaluation of expenditures allocated for the main administrative services of the country (such as administration and defense), in line with the action plan for implementing public administration reform.

3.2.11. The current level of public expenditure remains too high and unsustainable—with the largest share used to subsidize pension funds (13.6% in 2004)—and may represent an obstacle to faster economic growth. Efforts to correct the pension insurance system have been insufficient, and further reform of the system is needed.

Table 3.2.a.: Consolidated public revenues, expenditures and deficit in % GDP

% of GDP	2002	2003	2004
Public revenues	44.3	43.1	45.5
Public expenditures	47.7	44.3	44.6
Fiscal deficit/surplus	-3.4%	-1.1%	0.6%

Note: Data for 2005 will be contained in the revised Memorandum on Budget and Economic and Fiscal Policy for 2006 with projections for 2007 and 2008.

3.2.12. The structure of public expenditures according to the functional classification will change in the future period. Expenditures for public services (public administration) should be decreased as well as those for defense and national security (in line with their reform).

3.2.13. The share of expenditures for social welfare will be decreased but not significantly since this category will include social programs that will complement the restructuring of the economy. At the same time, education, economic affairs and construction and infrastructure will receive a greater share.

Table 3.3.b.: Consolidated public expenditures in % GDP²⁶

	2005	2006	2007	2008
Total expenditures	45.7	44.6	43.5	42.5
1. General public services	5.1	5.0	4.9	4.8
2. Defense	2.8	2.6	2.3	2.0
3. National security	2.2	2.0	1.7	1.4
4. Economic affairs	3.9	4.0	4.0	4.1
5. Environmental protection	0.3	0.4	0.4	0.4
6. Building and communal services	2.0	2.0	2.1	2.2
7. Health	6.6	6.5	6.4	6.3
8. Recreation, culture and religion	0.6	0.6	0.6	0.6
9. Education	3.9	4.0	4.2	4.3
10. Social welfare²⁷	18.4	17.5	17.0	16.5

3.2.14. With the privatization and restructuring of socially and state-owned enterprises comes a gradual **reduction in the subsidies granted to them**. The share of subsidies-based expenditures in GDP in 2002 equaled 7.6% only to fall to 5.9% in 2004 with a tendency to further decrease over the following period. 2005 and the following years envisage a consolidated fiscal **surplus** so that the privatization gains shall not be used to cover the fiscal deficit.

3.2.15. Forthcoming challenges:

- Further decreasing the share of public expenditure in GDP. The major challenge in the long run will be to reduce subsidies to the pension funds and, in the short run, to socially and state-owned enterprises. While subsidies to companies will be reduced as privatization progresses, reduction of subsidies to pension funds will be the major challenge for the future. The population of Serbia is relatively old and aging and the political pressure to maintain or even improve its standard of living remains strong.
- Reforming property taxes and local public finances in general. Currently, property taxes do not represent an important source of government revenues. The creation of an efficient and equitable system of property taxation will require political consensus as well as a current lacking in expertise, both at the local level and in the Tax Administration.
- Reforming the budgetary process and introducing the programmatic budget. Although the fiscal system has seen fast and decisive reforms in the past four years, the system of budget preparation is still relatively unreformed. Due to the lack of capacity, the introduction of a programmatic approach to budget formulation is running late, although it represents a necessary step for further improving the use of budgetary resources, as well as monitoring and evaluating the government's performance.

²⁶ The Memorandum on Budget and Economic and Fiscal Policy for 2006 with projections for 2007 and 2008.

²⁷ Functional budget classification that calculates funds for mandatory pension and disabled insurance as social welfare expenditures.

3.3. Transition to a Market Economy: Establishing Conditions for Private Sector Development²⁸

According to the recent WB Country Policy and Institutional Assessment (CPIA) and Doing Business 2005, Serbia has made significant progress in tackling structural problems and in establishing a more conducive environment for private sector driven economic growth and in this respect ranked first in the effectiveness of reforms in 2004.

Despite recent improvements, the 2004 World Economic Forum's Index of Business Competitiveness indicates there are considerable potential for improving the business environment in Serbia to pave the way for building an efficient and competitive economy. The key role in this process should be played by the successful privatization and restructuring of companies, the development of entrepreneurship and the SME sector and the overall improvement of the investment and business climate.

In order to ensure an adequate legal and institutional framework conducive to private sector development, 50 new economic and system laws were adopted. A total of 1,631 companies were privatized by the end of August 2005, and it is expected that the share of private ownership in the total economy will reach 75% by the end of 2006.

Despite the growing private sector and improved access to the market, foreign trade remains un-restructured for the most part, with a very low reorientation towards the EU and an unchanged structure of goods²⁹.

3.3.1. **A transparent legal and institutional framework** is indispensable for attracting private investments. Fifty systemic laws in the economic sphere were adopted in 2004 and a number of new laws has been developed by the Government and passed by the Parliament during 2005. Once implemented, they are expected to create a favorable business environment for increasing the number of business activities and the efficiency of the economy. For instance, **the Law on Registration of Economic Entities and the Law on the Agency for Registration of Economic Entities** simplified registration procedures. In addition, poor functioning of the courts represents a grave problem—the average time needed for debt collection is almost three years—bearing negatively on the investment climate.

3.3.2. In 2004 the Government of the Republic of Serbia formed the Guarantee Fund³⁰ in order to create conditions for stimulating the development of business operations of small and medium-sized enterprises, entrepreneurs and farmers. Its mandate is to issue guarantees to banks amounting to 50-80% of their requisitions for loans granted to small and medium-sized enterprises which have growing potential but do not fulfill all conditions required to obtain loans from commercial banks. The Fund approved 950 requests and issued guarantees totaling EUR 7.5 million as of July 2004. For its

²⁸ The institutions that bear greatest responsibility for implementing PRS goals with respect to conditions for private sector development are the Ministry of Finance, the National Bank of Serbia, the Ministry of Economy, the Privatization Agency, the Ministry of Justice, the Ministry of Capital Investments and the Ministry of Trade, Tourism and Services.

²⁹ Export structure is characterised by too many different products, which is a sign of low specialization and low representation of more processed products with higher added value.

³⁰ Since July 2004 the Fund approved 950 requests and issued guarantees totaling EUR 7.5 million. For its activities in 2005 the Budget of the Republic of Serbia envisages the allocation of an additional CSD 1.5 billion for the capital increase of the Guarantee Fund. See www.gf.co.yu.

2005 activities the budget of the Republic of Serbia allocated an additional CSD 1.5 billion to the Fund.

3.3.3. In order to **eliminate administrative and bureaucratic barriers** to private sector development, a Council for Regulatory Reform was established at the beginning of 2004 as an inter-ministerial body that monitors development of private entrepreneurship, discusses legislative changes and drafts new laws conducive to private sector development. The activities of the council has resulted in better co-ordination and more effective regulatory reforms within the economic field and has also enable the Government to react more promptly on problems liked to implementation of adopted legislation.

3.3.4. **Privatization activities** focus on changing the economy's ownership structure, achieving more efficient companies and consequently improving the competitiveness of the overall economy. Following a slow down during mid-2004, privatization accelerated. In the process equal importance has been paid to the size of investments, social programs and sale prices. From 2002 until the end of August 2005, 50 companies were sold in tendering procedures, 1,191 in auction sales and 390 as minority packages of companies on the capital market. Consequently, 1,631 of the 2,027 companies offered in tender procedures were sold, with a sales success rate of 80%. The privatization proceeds equal EUR 1.68 billion, contracted investments amount to almost EUR 850 million and the proceeds of social programs amount to EUR 270 million. A considerable number of companies are currently preparing for privatization in order to successfully implement the 2005 privatization plan to put up for sale 318 companies and share packages for a minimum 200 others, with expected earnings of EUR 262.2 million. In 2005, 19 companies shall embark upon restructuring.

3.3.5. 2005 has seen a 65% **share of private ownership in the total economy**. Reaching the planned goal of 75% may be expected by the end of 2005 by completing 18 tendering and 300 auction privatizations, through the separation of non-core activities from the public companies portfolios and by establishing new special companies to be privatized through the implementation of the recently adopted Law on Bankruptcy Proceedings. Thus far 73 companies have been identified as needing restructuring prior to sale; if dependent companies³¹ were to be included, then the number of companies currently undergoing the restructuring process would equal 600. These companies employ 200,000 workers.

3.3.6. In early 2004, the European Bank for Reconstruction and Development in agreement with the Government of Serbia embarked upon a EUR 1.5 million **Turn Around Management Programme** (TAM), which supports the restructuring of 25 potentially viable SMEs as well as capacity building in management during a two-year period. The project seeks to select companies that have been privatized and assist them in adjusting to market economy conditions, develop three-year planning, define clear competition policy, etc. The program's special benefits include the direct cooperation of experienced managers from the EU with the management of local companies.

3.3.7. **The process of bank privatization** as part of banking sector reform entered its final phase. The number and relative importance of banks with majority or

³¹ Some of the 73 companies are very complex and own dependent (daughter) companies that have to be restructured as well

significant state ownership is decreasing due to their closure (Borska Bank), merger with other banks (Pirot Bank, the Serbian Regional Bank) or privatization (Jubanka). In 2005 three banks with state ownership have been sold, with proceeds equaling EUR 273.8 million, and three banks have just begun privatization.

3.3.8. The National Anti-corruption Strategy in Serbia was presented to the National Assembly of the Republic of Serbia, with special attention to anti-corruption efforts in the political system, state administration and public services, judiciary, economy and public finance systems. Consistent implementation of enacted laws and an independent judiciary is meant to secure a favorable investment climate and ensure fair play among international business partners.

3.3.9. **The Law on Protection of Competition**, submitted to the National Assembly, provides for establishing a Committee for the Protection of Competition that should ensure equal competitive conditions for all economic agents on the national market. The National Parliament is also in the process of adopting the Proposal of the Law on Consumer Protection that will positively affect the standard of living, similar to the Proposed Law on Trade and the Proposed Law on Prices.

3.3.10. **Forthcoming challenges:**

- Restructuring and privatizing large socially owned and state-owned public companies represents the most important economic challenge for the next medium term period, outside of pension fund financing. Organizational restructuring (horizontal and vertical separation), reduction in the number of employees and eventual privatization are preconditions for a sustainable fiscal policy, as well as for improving the business climate.
- Creating institutional capacity for the efficient protection of competition. The privatization of either natural or administrative monopolies requires strong and independent competition and regulatory institutions, without which the current status of Serbia's infrastructure cannot be improved nor its business climate enhanced.
- Removing administrative and legal obstacles for private sector development at the republic and local level. Although many legal and administrative barriers have been removed, some of them, such as the constitutional provision that urban construction land cannot be privately owned, still remain.
- Increasing the involvement of local self-governments in developing the environment—both at the local and regional level—conducive to economic growth taking into account competitive advantages, as well as social and environmental limitations and challenges. This includes fostering co-operation between local self-governments in developing strategic frameworks (socio-economic plans/local PRSs/ local sustainable development strategies building on Agenda 21), and support structures for employment generation and balanced socio-economic development.

3.4. Transition to a Market Economy: Building Strong Public Institutions³²

Public administration reform in Serbia has primarily focused on the transition from an authoritarian, administrative decision-making process to citizen services accessible to all. Efforts towards decentralization have given municipalities a more significant role in improving living standards and reducing poverty.

The Public Administration Reform Strategy, adopted in late 2004, aims to build a democratic state and a citizen-focused state administration. The new laws, regulations and solutions recognize the principles of decentralization, depolitization, capacity building, rationalization and modernization of public institutions.

3.4.1. The **Public Administration Reform Strategy** identified two general and inter-connected aims: **building a democratic state** founded on the rule of law, responsibility, transparency, cost-effectiveness and efficiency and **building a citizens-centered state administration**, capable of providing reasonably priced, high-quality services to citizens and the private sector alike. The main principles in the implementation of the reforms are decentralization, depolitization, capacity building (human resources development, establishment of a unified training center and permanent process of professional improvement), rationalization (avoiding duplicated jobs and realistically evaluating the required number of staff for each job), modernization and the principle of “open” government as a control mechanism of state administration (such as adoption of the Law on Ombudsman). The solutions provided in the new Constitution of the Republic of Serbia shall define the levels of sub-central government and stand as a foundation for the devolution of authority from the central to the lower levels.

3.4.2. The Public Administration Reform Strategy governs the responsibility of civil servants and introduces **salary reform within the public administration**. Establishment of an incentive-based system for salaries was necessary in acknowledgement that the salary system in practice does not adequately motivate employees to take more responsibility. New salary levels for public administration employees were introduced as of April 2005, pursuant to the type of job, level of responsibility involved and the complexity of tasks. A review of the systematization of posts in all public administration agencies has been finalized. The staff requirements were evaluated to raise the efficiency of the entire public administration, which resulted in the rationalization of public administration up to 10%. At the same time a system for monitoring and evaluating the work of civil servants was introduced, which will be used as a basis for rewarding employees in the public administration.

3.4.3. Human resources management units³³ have been established to **improve human resources management**. The central unit has been established in the Ministry for Public Administration and Local Self-Government. Training members of these

³²The institutions that bear greatest responsibility for implementation in this field are the Ministry of Public Administration and Local Self-Government, the Ministry of Justice, the Ministry of Economy and the Ministry of Finance.

³³ With the assistance and consultation of the Government of the Kingdom of Norway and the Swedish Institute for Public Administration (SIPU).

units is ongoing. A unified center for training and promoting professional improvement in public administration and local self-government agencies should be established by the end of 2006.

3.4.4. **Modernizing the public administration** in the Republic of Serbia aims to update the technical and technological capacity of the state administration and introduce the so-called e-government that would contribute to the efficiency and cost-effectiveness of public administration institutions.

3.4.5. In order to accelerate the reform process a pilot project entitled **Joint Project: Towards a More Efficient Implementation of Reforms** was launched with the aim of capacity building in operational planning, monitoring and reporting in public administration. The project seeks to integrate all relevant strategic priorities into the operational plans of public institutions and ensure better resource reallocation by introducing programmatic budgeting and the more efficient programming of international assistance. A unified information system will be introduced to ensure timely reporting on the reform progress for governmental institutions and the public alike. Nine state institutions are taking part in the pilot phase of this project, which shall last until October 2005³⁴.

3.4.6. The process of decentralization is tightly linked to the **process of fiscal decentralization**, which seeks to provide funds to local communities for financing devolved functions thus ensuring independence and funds for adequately responding to the needs of citizens in local communities. The Standing Conference of Towns and Municipalities (SCTM)³⁵ is actively involved³⁶ in the preparation of regulations that define municipal property and a new approach to financing local communities, which entails fiscal decentralization. Municipal authorities deem the absence of fiscal decentralization to be the main obstacle to the economic and social development of cities and municipalities.

3.4.7. **Cooperation and information exchange between municipal authorities and other stakeholders at the local level**, particularly NGOs, exists in municipalities where international donor projects have been implemented. Among other goals, these projects sought to improve the operation of municipal administrations and enhance information dissemination to citizens as well as establish local partnerships in various spheres. Once in place, these mechanisms proved their worth and continued to be utilized in local communities. To date 17 municipalities have founded citizen assistance centers that seek to raise the quality of the services municipal administrations provide to citizens and improve the flow of relevant information to the public.

3.4.8. The **Law on Local Elections** was adopted in 2002, providing that mandatory 30% of candidates be from the less represented sex and ensuring their equal

³⁴ The project is financed by the Ministry of Foreign Affairs of the Kingdom of Norway. The participants in the project's pilot phase are the General Secretariat of the Government of the Republic of Serbia; the DPM's PRS Implementation Focal Point; the Ministry of Finance; the Serbian European Integration Office; the Ministry of International Economic Relations; the Ministry of Health; the Ministry of Labor, Employment and Social Affairs; the Ministry of Trade, Tourism and Services, the Ministry of Public Administration and Local Self-Government and the Ministry of Economy.

³⁵ The Standing Conference of Towns and Municipalities (SCTM) is a national association of local authorities in Serbia. The Committee on Social Issues (one of the SCTM's 10 line committees) deals with issues of social policy and employment at the local government level.

³⁶ In cooperation with the Palgo Center and the Serbia Local Government Reform Program (SLGRP) supported by the United States Agency for International Development (USAID).

distribution on electoral lists. This measure, however, has not yet contributed to an increased representation of women at the local level.

3.4.9. The regulations most relevant to avoiding situations that could lead to violations of impartiality and ethical conduct in management positions in public administration are the Law on Prevention of Conflict of Interest in Execution of Public Functions and the Law on Free Access to Information of Public Interest. In addition, a citizens' rights guardian (Ombudsman) is currently being instituted; furthermore, an Anti-corruption Council was established and the Government presented with the National Anti-corruption Strategy. The overall aim of these measures is to **reduce corruption and promote an anti-corruption culture** in Serbia in line with international standards. The National Anti-corruption Strategy seeks to advance regulations relevant to preventing conflicts of interest in the execution of public duties, establish an efficient system of control and responsibility of public and civil servants, enact a code of conduct for public and civil servants (already adopted by the SCTM for local authorities), establish mechanisms for reporting illegal and unethical official conduct, link the information system of public agencies (Tax Administration, Customs Administration, Ministry of Interior, Directorate for Public Procurement, etc), introduce the rotation of civil servants on posts susceptible to corruption, etc. The Strategy proposes concrete measures with timeframes, and the Anti-corruption Action Plan should be adopted by the end of 2005.

3.4.10. In order to ensure **access to justice for the poor**, several laws were amended to provide that defendants, depending on their financial status, shall not bear the costs of defense if it would endanger their subsistence or the subsistence of their dependants. The Law on Legal Assistance is being drafted.

3.4.11. The Law on Civil Proceedings and the Law on Executive Proceedings have been harmonized with EU legislation and relevant standards of the Council of Europe. Novelties introduced by these laws (e.g. direct review, procedures for resolving disputable legal issues, an accelerated executive procedure, etc.) increase the **efficiency, speed and cost-effectiveness of civil and executive proceedings**. Reforming the executive procedure sought to ensure that its efficiency and speed do not endanger the protection of either debtors or creditors (separate procedure in commercial cases). A Judicial Center for Training and Professional Improvement was established to further improve the capacity, efficiency and material and technical conditions of the judiciary.

3.4.12. The project **Employment of Roma Coordinators in Local Self-Governments** began in line with the recommendations from the draft Strategy for Integration and Empowerment of Roma³⁷. It encompasses 12 municipalities in its first phase, aiming to employ Roma representatives in all 120 Serbian municipalities where Roma live.

3.4.13. Serbia lags behind other countries in the region in establishing mechanisms for gender equality as well as in the legislation that would govern this sphere. Work on the **Law on Gender Equality and the National Action Plan** has begun. The progress report on the Implementation of the Convention on the Elimination of Discrimination against Women (CEDAW report) has been prepared. The Government recently established Serbia's Council for Gender Equality and a body for gender equality

³⁷ Ministry for Human and Minority Rights with the support of EAR.

exists in the National Assembly. In the autonomous province of Vojvodina, there is a Secretariat for Labor, Employment and Gender Equality, achieving excellent results and the institution of an Ombudsman has been established. Initiated by the OSCE in 2002, 54 gender focal points have been established so far in local administrations across Serbia.

3.4.14. Forthcoming challenges:

- Introducing regulatory impact assessments. Legally, the submission of comprehensive regulatory impact analysis is not required in the process of drafting and adopting new legislation. In addition, the public administration lacks the capacity to perform this kind of task.
- Continuing judiciary reform, since an efficient judicial system and the protection of property rights are preconditions for a well-functioning market economy. The fight against corruption and the improved transparency of judicial decision-making, on one side, and reforms in courts financing, on the other, will provide a basis for maintaining the delicate balance between independence of the judiciary and responsibility to the public.
- Reforming the system of public and national security and defense. From a fiscal standpoint, downsizing the public and national security systems as well as the army will be one of the key political challenges in the next period.
- Improving overall policy coordination at the central government level as well as the institutional capacity for programmatic planning processes in the line ministries, with the goal to improve the process of policy making and link government priorities with both available budget funds and international assistance.

3.5. Transition to a Market Economy: Global and Regional Integration³⁸

The process of EU accession is one of Serbia's priorities and strategic orientations, relying on wide political and social consensus. On April 25, 2005, Serbia and Montenegro received a positive Feasibility Study for the initiation of negotiations on the Stabilization and Association Agreement from the European Union.

Membership of the Republic of Serbia in the World Trade Organization may be expected in the course of 2008. In December 2004 the World Bank approved a new three-year Country Assistance Strategy for SAM fully taking into account the Stabilization and Association process (SAp), and the implementation of the goals set in the PRS papers of both Serbia and Montenegro.

3.5.1. The process of EU accession and PRS implementation are closely connected. The results of PRS implementation relating to the level of economic development and social exclusion are a direct response to the challenges facing Serbia in the process of EU accession.

³⁸The institutions that bear greatest responsibility for implementation with respect to regional and international integration are the Ministry for International Economic Relations, the Serbian European Integration Office (SEIO), the Ministry of Finance and the Republic Commissariat for Refugees.

3.5.2. Serbia was granted asymmetrical trade preferentials and access to significant assistance that has a positive effect on poverty reduction through EU support to the Stabilization and Association process. The **European Commission's Multi-Annual Indicative Program 2005-2006**, which forms the basis for EU assistance to Serbia, underlines the complementarity of the priorities laid out in the country's Poverty Reduction Strategy and its European integration agenda.

3.5.3. The June 2003 EU-Western Balkans Summit in Thessaloniki included the so-called Thessaloniki Agenda, which, among other things, offered the countries of the region a **European Partnership** as an instrument of the EU's pre-accession, recognizing that the SEE countries are potential candidates for EU membership. This instrument exclusively governs relations between the EU and the State Union of Serbia and Montenegro until the signing of the Stabilization and Association Agreement (SAA). The Council of the EU adopted the decision on the principles, priorities and conditions contained in the European Partnership on June 14, 2004, based on which the Serbian Government prepared and on November 4, 2004, adopted the Action Plan for its implementation.

3.5.4. In October 2004, the **EU adopted a "twin-track" approach to this process**, which transferred the entire sphere of economy and trade to the member states of the State Union, i.e. Serbia and Montenegro separately. Thereafter, on **April 25, 2005, the EU adopted a positive Feasibility Study for initiating negotiations on the Stabilization and Association Agreement** for Serbia and Montenegro³⁹.

3.5.5. **The Serbian National Strategy for Serbia-Montenegro EU Accession** was adopted by the Government of Serbia in June 2005 and the Serbian Parliament Committee for European Integration in July 2005. The National Strategy represents a basis for the adoption of national programs for the harmonization of national legislation with EU regulations, following the conclusion of the SAA. The SAA's key goal is to promote economic and trade relations, with the future prospects of establishing the free trade area and regulating the free movement of labor, freedom of establishment, operation in the service sector and free movement of capital.

3.5.6. Aiming to forward the process of legal harmonization with the EU and following the results of the **Action Plan for the Harmonization of National Draft Laws with EU legislation for 2004**, in March 2005 the Government of the Republic of Serbia adopted the **Action Plan for the Harmonization of National Draft Laws with EU legislation for 2005**. This plan encompasses 41 laws, 11 of which the Government adopted by August 15, 2005, with six adopted by the Parliament. An **Action Plan for the Implementation of Priorities of European Partnership** was also adopted in 2004. The realization of both action plans is monitored by the SEIO through a screening report and monitoring tool for the partnership.

3.5.7. In order to prevent and eliminate obstacles to the **free movement of persons, goods, services and capital**, the Law on the Action Plan on the Harmonization of Economic Systems of the Member States of Serbia and Montenegro was adopted in June 2003⁴⁰. However, in line with the "twin-track" approach, the Law was amended in February 2005 to omit provisions relating to tariff rates, the foreign trade system,

³⁹ The European Integration Office is the youngest institution of the Government of the Republic of Serbia, established in March 2004 with a role to coordinate and monitor horizontally the EU-related workload in the line ministries. The work of the SEIO greatly contributed to Serbia obtaining the positive Feasibility Study.

⁴⁰ Official Gazette RS no. 67/03.

taxation, the WTO (joint accession) and the Joint Competition Commission⁴¹. Additionally, the agreement to liberalize the trade of textiles was signed with the EU in the beginning of 2005.

3.5.8. **Customs system reform** will include the gradual reduction of the level of customs protection, one of the conditions for accession to the EU and membership in the WTO. The Law on Customs Tariffs was adopted in July 2005⁴².

3.5.9. Signing the agreement on free trade under the auspices of the Stability Pact for South East Europe included trade liberalization with seven countries in the region. By 2008 a **regional free trade zone** should be created that will include liberalization in the service sector.

3.5.10. **Neighborhood programs** are a new EU vehicle that seeks to promote and support regional cross-border cooperation with the new external borders of the European Union. The programs seek to reduce the existing differences in regional development, advance contacts between local communities and strengthen cultural, social and economic cooperation. Serbia is cooperating with Hungary within the framework of this program and will establish cooperation with Bulgaria and Romania shortly.

3.5.11. **Resolving the problems of refugees and internally displaced persons** is an indispensable step on the road to regional integration. These issues shall be resolved through the local integration of refugees (granting of SAM citizenship), agreements on the two-way return of refugees that SAM has signed with the Republic of Croatia and Bosnia and Herzegovina and local integration or return of IDPs to Kosovo.

3.5.12. **The extended financing arrangement signed with the IMF** in 2002—totaling approximately SDR⁴³ 650 million—aims to attain sustainable economic growth, improve living standards, lower the rate of inflation and stimulate the continuous growth of foreign exchange reserves. By the end of July 2005 USD 587.5 million (approximately USD 860 million) has been spent, with the remaining sum to be spent by December 31, 2005.

3.5.13. **The membership of the Republic of Serbia in the WTO**, which is expected to take place in the course of 2008, shall have a positive effect on economic growth, lower the prices of certain products, further the liberalization of foreign exports and secure the preferential status of Serbia and Montenegro.

3.5.14. **Forthcoming challenges:**

- Dampening the effects of foreign trade liberalization on the poor living in rural regions, related to both the WTO and the EU accession process. Develop a coordinated government approach, which will consider the impact of the pace of liberalization on the living conditions of rural populations, especially the poor.
- Responding to the requirements of the European integration process, in particular:
 - Initial negotiations on the Stabilization and Association Agreement, expected in the fall of 2005.

⁴¹ Official Gazette RS no. 18/05.

⁴² Official Gazette RS no. 62/05.

⁴³ Special Drawing Rights (SDR) represent an international reserve asset, created by the IMF in order to regulate international liquidity, which IMF uses as a unit of account in all dealings and transactions with member countries. SDR are allocated to member countries in proportion to their IMF quotas. Their value is based on the currency basket comprising USD, EUR, JPY and GBP.

- Harmonizing SAM's legislation with the EU *acquis*, particularly in the key areas of the Union's internal market, pursuant to the SAA.
- Speeding up the pace of SAM's negotiation progress, depending on the pace of the adoption of European regulations and standards, and the country's ability to create the capacities for implementation of the Agreement provisions.
- Preventing the risk of interrupting the SAA negotiations in case of the delayed implementation of key EU requests.
- Ensuring full cooperation with the Hague Tribunal.
- Addressing the lack line ministry capacity to adequately link allocated budget funds and international assistance with the implementation of specific priorities in the European Partnership.
- Building the capacity of the public administration for the future use of the new Instrument for Pre-Accession of the EU.

3.6. Increased Employment Opportunities⁴⁴

The unemployed face the greatest risks from poverty and the highest and most severe poverty gap compared to other categories on the labor market. The principal aim of economic reform in Serbia is the establishment of a modern, export-oriented market economy grounded in the private sector and capable of generating dynamic economic growth and new employment.

Compared to the previous year, employment increased by 0.5% in 2004, whereas over the first seven months of 2005 the average number of the employed increased by 0.1% in comparison to 2004. Slightly increased employment opportunities are considered to be the result of economic reforms, active employment measures, favorable loans to private SMEs, the stimulation of foreign direct investments, investments in the development of the private agricultural sector and other similar measures. The 2005-2010 National Employment Strategy was adopted in April 2005.

The organizational, human resources and information system reform within the National Employment Service is under way.

3.6.1. During 2001-2003 a declining trend in overall employment was recorded as a result of company privatization and restructuring. In 2004 a 0.5% growth in employment was recorded in comparison to the previous year. In the first seven months of 2005 the average number of employed increased by 0.1% in comparison to 2004. A significant 16.5% real growth in net earnings was achieved in 2001, followed by 29.9% in 2002, 13.6% in 2003 and 10.1% in 2004.

3.6.2. **The National Employment Strategy** was adopted in April 2005. It aims to increase employment, investment in human capital, labor quality and productivity; reduce differences between regional labor markets; support gender equality and fight against discrimination in employment. The National Employment Action Plan for 2006-2008 is being drafted with EAR support. The table below presents the target values to be reached by 2010:

44 The institutions with the greatest responsibility for fulfilling the objectives of increased employment opportunities are the Ministry of Labor, Employment and Social Policy; the Ministry of Economy; the Agency for SME Development and the National Employment Service.

Table 3.6.a.: Target employment values

INDICATOR	Current STATUS	Current EU STATUS	YEAR 2010
Employment rate ⁴⁵	58%	65%	67%
Unemployment rate ⁴⁶	14.6%	6-8%	10.5%
Participation rate	68%	69%	72%
Youth employment rate	15%	40%	20%
Women employment rate	48%	56%	90% of men's employment rate
Reduced regional disparities in NES unemployment rates	1:3	-	10% difference
Reduced regional disparities in average wage	1:3	-	20% difference

3.6.3. Fulfilling these aims requires a wide range of harmonized policies, measures and activities to reduce the existing unemployment rate and prevent the long-term unemployment of the redundant labor force.

3.6.4. The number of persons involved in **active job-search** programs doubled in the period 2002-2004 (22,740 persons in 2002 and 50,586 in 2004).

Table 3.6.b.: Number of persons in active employment programs

TYPE OF ACTIVITY	TOTAL PERSONS			
	2002	2003	2004	2005*
Job clubs	-	-	120	1,586
Training for active job searching	6,238	12,362	14,471	7,126
Job fairs	4,086	8,207	13,324	6,710
Job centers	692	-	15,508	20,000
Training for business start-ups	-	-	-	1,200
Stimulation of new employment	1,861	-	98	250
Self-employment programs	1,305	-	2,646	2,500

* Planned number of persons

3.6.5. Of the total 2004 allocation of CSD 900 million, **CSD 410 million were spent on active employment programs** and almost CSD 250 million were undertaken for additional training and education. The 2005 budget of the Republic of Serbia has allocated CSD 750 million for these purposes. **The ratio of funds spent on active and passive measures is unfavorable** (10% to 90%), but the picture is far better when considering funds invested into active employment programs and general employment promotion by the Development Fund of the Republic of Serbia as well as international donors.

3.6.6. The Development Fund of the Republic of Serbia approved **CSD 4 billion in loans to small and medium-sized enterprises and entrepreneurs** in 2004. These programs are expected to create **5,000 new jobs**. The 2005 plan provides CSD 3.9 billion for SME development, CSD 220 million for individual small shops and CSD 600 million in loans to would-be entrepreneurs that are registered as unemployed with the National Employment Service. Currently, these micro-loans offer the most favorable conditions on the financial market, facilitating the approval of loans to

⁴⁵ Labor Force Survey (2003)

⁴⁶ Ibid.

businesses from underdeveloped regions, with lower interest rates and a higher share of Fund financing to projects.

3.6.7. In 2004 CSD 12.5 billion were paid in compensation and temporary compensation to employees from the territory of the Autonomous Province of Kosovo and Metohija and another CSD 410 million were allocated to active employment policy. This means that the share of financial compensation in total expenditures reached 86.54%. This ratio is expected to change shortly.

3.6.8. An employment support program, totaling EUR 9 million, is being implemented in Belgrade, Bor and Pirot with the aim of reducing unemployment and promoting social cohesion through a more effective labor-market policy. A project on employment promotion⁴⁷ is being piloted in the municipalities of Lazarevac, Pančevo, Kraljevo and Niš aiming at the more rapid and efficient employment of redundant workers, new (young) entrants into the workforce, the older unemployed, the disabled and minorities. The total value of the project is USD 4.75 million.

3.6.9. In order to **improve the quality of the labor force**, vocational training and additional education programs were organized involving 7,792 participants in 2002 and 7,007 participants in 2004. **The network of regional agencies** led by the Republican Agency for the Development of Small and Medium-Sized Enterprises and Entrepreneurship (SMEEs), providing expert services (consulting, training, seminars, promotions, etc.) to potential and existing SMEEs, is active throughout the Republic of Serbia.

3.6.10. The **privatization of companies** and the entry of foreign strategic investors will have a positive impact on the technological modernization of companies and the rise of production, exports and employment. The **sustainable development of the private agricultural sector** is a key contributing factor to the reduction of rural poverty in the short- to mid-run. Thus far CSD 350 million has been allocated towards this end, with the total investment expected to exceed CSD 750 million by the end of July 2005.

3.6.11. Participation in the gray economy remains one of the main means of survival for the poorest groups in Serbia but also an avenue for increasing profits through tax evasion. In order to **reduce gray economy**, preventive measures (such as awareness raising and education on the necessity legalizing businesses), stimulation measures (towards the legal operation of entrepreneurship and entrepreneurs) and penal measures have been put in place. In the course of 2002, labor market inspectors found 18,564 persons working but not registered as employed, which led to the formal employment of 12,695 persons. In the course of 2004, labor market inspectors found 46,635 persons working but not registered as employed, which led to the formal employment of 30,754 employees.

3.6.12. **The 2005 Labor Code** introduced new forms of flexible employment (contracts for representation or mediation, additional work, professional education and development), which do not constitute employment contracts but which lead to poverty reduction through an established right to award, i.e. financial compensation and other rights based on work. Furthermore, this Labor Law improves the position of employees in cases of bankruptcy, change of employer and termination of employment.

⁴⁷ Funded by the World Bank (IDA) and DFID.

3.6.13. **Measures targeting the employment of vulnerable groups** are implemented through programs such as public works, micro-businesses and employer subsidies. The EU-funded project Beautiful Serbia trained a total of 185 persons, 122 of whom have found employment with 37 others currently in the process of concluding employment contracts. The project targeted individuals with lower levels of education and provided the opportunity to acquire professional qualifications and experience. The 2005-2006 project supports public works in the Banat, Šumadija, Pčinj and Jablanica districts.

3.6.14. A social program targeting redundant workers is being implemented vigorously. The 2002-2004 programs involved 92,996 workers who lost employment due to **restructuring and privatization** and financed an additional 7,684 workers over the first three months of 2005.

3.6.15. Creating conditions for **including the disabled in the labor market** is implemented through efforts to generate employment (55 persons in 2004), provide equipment (55 persons in 2004) and assist with wage financing (111 persons in 2004). Financing 50 persons through self-employment programs and 100 persons through new employment programs is planned in 2005. As an additional incentive to employers, the law stipulates⁴⁸ tax exemptions on salaries for the disabled, as well as for their training and employment. The European Agency for Reconstruction will finance an income generation project targeting **290 refugee and IDP families**.

3.6.16. The Law on Income Tax has introduced employment promotion measures in which entrepreneurs are entitled to tax exemptions when permanently employing new employees. Two-year subsidies and exemptions from paying contributions on employing workers over 45 and 50 have also been introduced.

3.6.17. The permanent training of National Employment Service (NES) employees seeks to **improve the NES's quality of work and build its capacity**. Employees are being trained in three pilot municipalities (Sombor, Valjevo and Novi Beograd) to promote more efficient service provision⁴⁹.

Table 3.6.c.: NES Work Program for 2005

TYPE OF ACTIVITY	Number of people	Allocated Funds (EUR)
Active job search	8,912	63,898
Employment fairs	6,710	69,700
Additional education and training program	8,260	4,540,812
Developing entrepreneurship and employment incentives	25,650	4,672,500
Center for professional information and counseling		28,081
TOTAL FUNDS FOR ACTIVE LABOR MARKET PROGRAMS	49,532	9,374,992

3.6.18. The Decision on Establishing the Republic Employment Council came into effect in 2004. Local Employment Councils are in the establishment phase.

3.6.19. A 900,000 EUR Labor Market Institutional Building project⁵⁰ is currently being implemented in Belgrade, Novi Sad and Šabac. The project seeks to improve

⁴⁸ The Law on Income Tax (from the report of the Ministry of Finance).

⁴⁹ In cooperation with the Federal Employment Bureau of Germany.

⁵⁰ Funded by the Swedish International Development Agency (SIDA).

the functioning of the labor market and promote employment through establishing an efficient public employment service and improving organization, planning, operations, human resources and work conditions in the National Employment Service.

3.6.20. Forthcoming challenges:

- Developing efficient programs for employing redundant employees in the process of privatizing socially owned enterprises and restructuring public enterprises in the period 2005-2007 (emphasis on active measures instead of passive measures).
- Developing more efficient programs for employing the most affected and vulnerable groups, including the long-term unemployed, youth, the under-qualified and older workers, as well as persons with disabilities, Roma, refugees and IDPs.
- Establishing regional and local employment councils (coalitions) targeted towards efficient local development and employment strategies based on the analysis of risks and potentials, especially in the least developed regions.
- Continuing reform of the National Employment Service, especially towards a full client-centered approach, including contacts with employers and efficient, active job searches based on a unified information system, as well as the establishment of monitoring and evaluation systems.

3.7. More Efficient Social Protection⁵¹

The 2004 introduction of a minimum social security level for all of Serbia improved access to social allowances, raised its amount and increased the number of recipients in the poorest municipalities. The budget approved additional funds for such assistance through larger transfer amounts and better coverage of the most vulnerable groups.

More efficient social welfare mechanisms, the implementation of the Poverty Reduction Strategy, the revival of economic activity and an increased employment rate are expected to slow the growth of overall social benefits in relation to GDP.

Funds directed towards the Social Innovation Fund (FIS), a program of the Ministry of Labor, Employment and Social Affairs, are financing projects at the local level that are developing and testing innovative and more effective forms of social welfare services through cooperation between the Government, non-government and private sectors, public institutions and local self-governments.

3.7.1. The adoption of Amendments and Additions to the Law on Social Welfare and the Social Security of Citizens has changed the mechanisms for the social welfare index and introduced a minimum social security level as a criterion for receiving assistance from the Family Financial Support system (known as MOP⁵²). These

⁵¹ The institution with the greatest responsibility for achieving more efficient social welfare is the Ministry of Labor, Employment and Social Policy (MoLESP).

⁵² The right to receive Family Financial Support (MOP) is restricted to a period of nine months for households with able-bodied members with the goal of stimulating their employment (MOP does not apply to families with a majority of disabled members).

changes have **improved access to MOP in the poorest municipalities**⁵³ and **increased the number of families who are MOP beneficiaries**: from 48,000 in 2004 to around 52,000 families in 2005. A unified level has been introduced and the amount of social allowance for “care and assistance from another person” for persons who require assistance and care in order to perform activities for gratifying basic living needs has increased (from around 2,600 dinars to over 4,500 dinars for a total of around 20,000 beneficiaries). Mechanisms that determine the index according to living costs (rather than the previous practice that tied it to average salaries) have ensured the real value of social allowances and continuous access to social rights.

3.7.2. In response, the budget has approved additional funds **for expanding assistance** through larger transfer amounts and the inclusion of the most vulnerable groups. In that sense, MOP has included a number of families from the poorest municipalities, qualifying refugees who have acquired citizenship, internally displaced persons who fulfill the conditions prescribed by the Law on Social Welfare and Roma families who are offered assistance in gathering the necessary documentation.

Table 3.7.a.: Number of MOP beneficiaries and level of social transfers (CSD)

Year	Average number of		Total
	Families	Beneficiaries	
2002	39,430	90,336	921,296,000
2004	45,254	108,793	1,709,951,000
2005	52,000	127,000	2,800,000,000

Table 3.7.b.: Number of beneficiaries receiving children’s allowances and the level of social transfers (CSD)

	2002	2004
Number of families receiving children’s allowances	324,650	262,693
Number of children	573,187	489,803
Total amount of children’s allowances	6,598,308,482	6,567,688,714
Budget	214,801,643,633	308,798,239,522
Share of children’s allowances in the budget	3.07%	2.13%

3.7.3. In 2004, a program for **including displaced persons in the social welfare system**⁵⁴ was carried out. During the life of the program, 4,551 families turned to social work centers for assistance, out of which 1,961 families submitted applications, while 919 families were included in MOP. Most rejected applications were from applicants whose income was above the minimal level of social security.

3.7.4. **Over 140 centers for social work in Serbia** represent the basis for the state’s engagement in providing welfare services at the local level. With the continuing reform of the social welfare system, the centers for social work (CSW) will increasingly take over activities aimed at assisting social groups that face the risk of social exclusion. Despite the high education level of CSW employees, further training

⁵³ A number of poor families living in low-income municipalities were once ineligible to receive MOP because of an earlier decentralized eligibility criteria, which were based on a locally rather than centrally defined minimum social security level. In other words, the minimum level of security was not unified in the Republic of Serbia.

⁵⁴ In cooperation with the International Committee of the Red Cross and local centers for social work.

is necessary in implementing the new policies and approaches defined in the PRS. The quality of social welfare services also depends on developing social standards across the CSWs, which are being continually improved through a project entitled Improvement of the Organization and Professional Work at CSWs as well as through numerous professional gatherings, seminars and other educational efforts.

3.7.5. In order to **stimulate the role of local communities in providing social welfare services**, the social welfare rights for which local self-government is responsible were monitored. With the Amendments and Additions to the Law on Social Welfare and the Social Security of Citizens, certain **competencies were transferred to municipalities**, such as reception centers and stations.

3.7.6. The **Social Innovation Fund (SIF) program** enables projects at the local level to develop and test innovative and more effective forms of social welfare, which are financed and implemented through the cooperation of public and non-governmental institutions and organizations (NGOs, centers for social work and local authorities). In 2003, 88 projects were approved (for which EUR 1.2 million were allocated from a donation by the Government of the Kingdom of Norway and 44 million dinars from the budget of the Republic of Serbia). Out of this number, 39 continuing projects were approved in 2004 (through a EUR 150,000 donation by the Government of the Kingdom of Norway and an allocation of 24 million dinars from the budget of the Republic of Serbia). Among other activities, this project supported a number of programs aimed at improving the position a variety of populations, including the Roma, victims of abuse and neglect, children with and at risk of developmental problems, the elderly, children without parental care, etc. A new call for applications was announced in April 2005, and a total of EUR 900,000 from an EAR donation and CSD 32 million from the budget of the Republic of Serbia were allocated. The priorities of the 2005 call for applications were in full compliance with the PRS recommendations.

3.7.7. The third competition for **projects by organizations representing persons with disabilities** was announced in August 2004⁵⁵, through which 84 projects in the total amount of 34 million dinars were approved. This initiative respects similar principles and selection criteria as the SIF.

3.7.8. One of the benefits for socially vulnerable categories (MOP beneficiaries, families with low income) is the 30% discount on electricity costs. When the price of electricity increased in July 2004, a new program providing relief in electricity payments for vulnerable populations ensured subsidies for 142,000 families.

3.7.9. **The new role of the state** in the reformed social welfare system should focus on the definition of the legal framework, including the supervision and provision of basic forms of social security and assistance, as defined by the strategy for reforming the social welfare system. In that sense, work has continued on drafting new laws and regulations aimed at reforming the system.

3.7.10. The Ministry of Labor, Employment and Social Affairs produced a **Strategy for the Reform of the Social Care and Protection System**, which defines the main components of social policy reform: the de-institutionalization, decentralization and democratization of social care and protection services—including local community involvement in the provision of social services and partnerships with civil society. The Strategy is guided by the following principles: addressing the needs of

⁵⁵ The competition was opened by the Ministry of Labor, Employment and Social Affairs.

individuals within the context of family and community; emphasizing the participation of beneficiaries in the design and provision of social services; providing service diversity and choices to beneficiaries; maximizing community-based services over institutional services; and encouraging the plurality of service providers.

3.7.11. The two most important fields in **the process of transforming institutions and developing alternative social welfare services** are the improvement of family accommodation and protected social accommodation. Out of 4,471 assisted children without parental care, 2,705 are with foster families and 1,766 in orphanages. A system for educating and monitoring foster families has been ensured, programs for preparing and training candidates for foster parents as well as monitoring and supporting children and foster families have been prepared, and a database on family accommodation is being created. Around 1,500 foster family candidates have been prepared and trained, around 900 of which fulfill conditions of general eligibility for foster parentage.

3.7.12. **Accommodation in protected conditions**—a form of accommodation for the elderly, refugees, internally displaced and disabled persons, as well as others who have difficulty managing on their own—is realized through cooperation between the local self-government; the Ministry of Labor, Employment and Social Affairs; the Republic Commissariat for Refugees and donors. In 18 municipalities, buildings were constructed for roughly 900 elderly refugees and IDPs, as well as a certain number of the local population, who will provide assistance to residents. Some apartments have been provided for formerly institutionalized persons with disabilities, offering protected housing with organized support services.

3.7.13. In 2004, **living conditions** at institutions for the elderly, refugees and mentally disabled persons **continued to improve**, including living conditions in all 37 homes for elderly persons (expanded capacities, basic maintenance, rehabilitation, reconstruction and new equipment). All 15 homes for persons with developmental disorders have benefited from less crowded facilities, improved living conditions and new equipment.

3.7.14. For the first time, the Criminal Code of the Republic of Serbia (2002) treats domestic violence as a criminal offense, while the new Family Law (2005) treats violence against women as a social rather than personal problem and defines protective measures for family members against the perpetrators of violence. This law also introduces new legal provisions such as the emancipation of minors over the age of 15, mediation in marital relations, joint execution of parental rights, marriage contracts, a deed of gift, and the like; it also grants the centers for social work additional responsibilities in family protection.

3.7.15. In January 2004, the government adopted a decision on protective measures for economically vulnerable households in the process of building individual residential facilities and the legalization of illegally constructed buildings. The decision defines the right to subsidies for constructing individual housing facilities, as well as the issuing of permits for facilities constructed without a building permit. The realization of a program for the housing and permanent integration of refugees started in seven municipalities/towns in Serbia, through which 670 housing units for refugees and socially and economically vulnerable populations will be constructed.

3.7.16. Forthcoming challenges:

- Providing access to the social protection system to persons without identification documents, especially Roma living in slums or displaced from Kosovo.
- Creating space to better target MOP social transfers as the best form of targeted social allowance, as well as a reconsideration of the existing model, which is highly unfavorable for multi-member households.
- Continuing reform projects and further improving the SIF as the single most important mechanism for implementing reforms in this area, including efforts to mainstream lessons learned into government policies. Formulating other models that will stimulate local authorities to develop alternative social welfare services within their mandate.
- Developing control mechanisms that will prevent misuse and whose absence represents an obstacle for further decentralization.
- Building links between different sectors both on the central and the local level (employment, education, health, social protection) to ensure an integrated social welfare approach with an emphasis on active social policy measures.

3.8. Improved Status of Pensioners and the Elderly⁵⁶

Most elderly people in Serbia receive pensions, since pension insurance is mandatory for the largest part of the economically active population. The main goals of the state policy towards the elderly include an improved standard of living, the reduced number and share of the poor and the depth of poverty and strengthened institutional and non-institutional services for the most vulnerable as well as elderly persons.

In the previous period, considerable progress was achieved in the regularity of pension payments with pensioners receiving 12 payments in 2004. According to the most recent draft law on debt reprogramming, a remaining delay in pension payments will be solved in the next three to five years for different categories of pensioners.

3.8.1. The Amendments to the Law on Pension and Invalid Insurance increased the lowest pension protective level and offered the legislative framework for the consolidation of the three pension and disability insurance funds (Fund of the Employed, Fund of the Self-employed and Fund of Farmers).

3.8.2. Consolidation of the pension and disability insurance funds is expected to contribute to the sustainability of the overall pension system. Even though pensions are paid regularly, payments in the Fund of the Employed have been delayed 1.5 months and 20 months for the Fund of Farmers. Around EUR 215 million are necessary for paying farmers' pension arrears (20.5 pensions). The mechanism for addressing this problem is outlined in the new legislation,⁵⁷ which envisions reprogramming the debt in pension payments in the next three to five years, as well as beginning regular and timely pension payments starting with November 2005. In

⁵⁶ The institution with the greatest responsibility for more efficient social welfare is the Ministry of Labor, Employment and Social Affairs.

⁵⁷ Draft Law on the Overtaking of Obligations of the Republic Fund for Pension and Disability Insurance of the Employed, Created by the Delay in Payments of Pensions and Allowances, and a similar draft law for the pension fund for farmers.

addition, consolidation of pension funds is needed because contributions are insufficient for financing pension payments. The budget subsidizes around 40% (and for the Fund of Farmers, even more⁵⁸) of the pension fund's income (the deficit of all three pension funds in 2004 was 5.12% GDP). The consolidation is expected to raise the number of the insured as well as improve the collection of contributions to the Fund of Farmers⁵⁹. This, in turn, is expected to create a basis for the regular payment of pensions in the long run. At the end of May 2005, the World Bank granted USD 25 million to support a project related to this problem.

Table 3.8.a.: Basic Fund indicators in 2004

FUND	CATEGORY		
	Number of persons	Average pension	Subsidies from the budget
Fund of the Employed	1,241,082	9,578 dinars	62.67 billion dinars (34.14% of total Fund incomes)
Fund of the Self-Employed	43,938	9,360 dinars	-
Fund of Farmers	215,086	2,780 dinars*	5.66 billion dinars (60.28% of Total Fund incomes)

* Pensions paid in the period April 2002- April 2003

3.8.3. The National Action Plan for the Provision of Social Security and the Humanization of Living Costs of the Elderly—currently under preparation—will define how services and assistance will be offered to elderly persons.

3.8.4. The draft law on voluntary pension funds and plans, in its final stage, is expected to be adopted in the course of 2005, to be followed by the adoption of by-laws related to its implementation. The introduction of this third pillar, i.e. **voluntary private pension insurance**, will create conditions for additional income for the elderly in the future. The working group for the implementation of voluntary private pension insurance is established within the council for the reform of the pension insurance system.

3.8.5. The programs concerning support to elderly citizens include **de-institutionalization** (transformation of institutions where elderly people live), with the **piloting of alternative services** (family accommodation, home care and assistance, etc.) for elderly persons at the local level. Housing under protected conditions⁶⁰ encompasses around 900 elderly persons, refugees and displaced persons in a total of 18 municipalities: the pilot project of integrated home care includes 100 (elderly) families in Knić, Kragujevac and Knjaževac. Home care services are still developed within institutions for the elderly, with a trend towards the increasing participation of non-governmental organizations in the development of these services. **Home assistance** is provided for 2,500 beneficiaries, **clubs for the elderly** rally around 20,000 users and provide meals for around 6,000 people and **two-day centers for the elderly** serve citizens in Kragujevac and Novi Sad.

⁵⁸ Income into the Fund of Farmers includes transfers from the budget of the Republic of Serbia (60.28%), plus the obligations of the Republic of Serbia for solidarity veteran's service (26.09%), a total of 86.37% of the Fund's income.

⁵⁹ It is expected that timely payments to all beneficiaries will restore the confidence of farmers and increase the rate of their contributions.

⁶⁰ Residence with a family that, as a host, assists tenants and/or provides housing with support for disabled persons.

3.8.6. With the decentralization of the social welfare system, a large number of competencies will be transferred to local self-governments, which will have to ensure that services provided in cooperation with the not-for-profit and private sector are in accordance with the recognized needs of the citizens.

3.8.7. **The quality of living conditions** in all institutions for the elderly, refugees and mentally disabled persons has improved through building investments, expanded capacities, basic maintenance and investment, rehabilitation and reconstruction, as well as equipment, totaling around CSD 280 million in 2004. At the same time, with the help of donor funds, six collective centers for refugees have been transformed into homes for elderly persons. The conversion of yet another collective center with capacity for 100 is currently being completed. Larger and better quality institutions can also be achieved **through including the private sector in providing accommodation services for elderly persons**. The Ministry of Labor, Employment and Social Affairs has issued the first three licenses for private homes for the elderly, while a fourth decision is being prepared.

3.8.8. **Forthcoming challenges:**

- Further reforming the pension and disability insurance system in order to decrease the burden both on the overall economy and on the republic budget, while preventing the impoverishment of the elderly whose living standards depend exclusively on pensions.
- Consolidating the pension funds along with improving the information system and reorganizing the register of the insured⁶¹ (data collection, registration of insured and data management).
- Further improving control of contribution payments and discouraging contribution evasion.
- Further developing alternative forms of social protection for the elderly at the local level, especially home care and assistance.

⁶¹ Maticna evidencija osiguranika.

3.9. Health Care towards Poverty Reduction⁶²

Changing the model of financing primary health care and introducing a new model of payment by the end of 2006 is a precondition for the essential reform of the primary health care system in the Republic of Serbia. Access to basic health services of an appropriate quality without financial barriers for the whole population, particularly vulnerable populations, i.e. refugees, IDPs, Roma, poor people and others, is a key to health care reform. Such access should be achieved through numerous national health programs and strategies for specific sectors, including restructuring health care institutions, introducing a health benefit package, changing the way providers charge payment, introducing a reduction or exemption of out-of-pocket expenditures for vulnerable groups with regard to social protection costs and establishing a public/private mix in the health care system.

3.9.1. **Providing fair and equal access to health care** to all citizens of the Republic of Serbia represents one of the basic principles of its health care policy. The Draft Health Care Law seeks to better define the health rights of citizens and patients, strengthen the gate-keeping function of general practitioners, better specify the general (public) interest in the health care sector—including vulnerable groups—decentralize management and increase the productivity and quality of care. The Draft Health Care Law contains a list of vulnerable groups and describes the possibilities for protecting their health rights.

3.9.2. The adoption of the health policy document *Vision of Health Care System Development, Strategy of Health Care Reform*—together with the National HIV/AIDS Strategy, Tobacco Control Strategy, Public Health Strategy, Food Safety Strategy, National Blood Safety Strategy, National Mental Health Program and National TB Control Program—will improve the availability of health care, particularly for vulnerable groups, and reduce inequality in access. The Ministry of Health has been participating actively in the preparation of multi-sector government documents such as the National Action Plan for Children, the Action Plan for Women's Health and the National Action Plan for Improving the Status of the Roma Population. Other measures for protecting vulnerable groups include introducing a new positive drug list financed by the Health Insurance Fund, strengthening the protection of patient health rights, improving inspection control in cases of detrimental health consequences and establishing better cooperation with NGOs as well as providing financial and other support to projects promoting health and healthy lifestyles.

3.9.3. Through the project Development of the Health Care System in Serbia, the World Bank is financially and technically supporting the Serbian health care system, with a loan of USD 23.5 million until 2008. It is planned that the largest share of resources will be spent on restructuring health care centers including new information and communication technologies, changes in methods of hospital payments and the introduction of accreditation and licensing.

3.9.4. **To enhance efficiency and effectiveness in the use of resources**, evidence based clinical practice guidelines based on the National Burden of Disease Study were developed and are being implemented. New standards for health personnel, performance and hospital provisions were proposed and an action plan for capacity

⁶² The institution with the greatest responsibility for health care goals is the Ministry of Health.

building for the Ministry of Health and health professionals is in the preparation phase. A national plan for training health care professionals and associates in health management, continuous quality improvement and development of an information system for public health is consistently implemented in accordance with the needs of the system.

3.9.5. **The health information system** should also increase efficiency in the health care sector. A pilot project of basic health services in the Kraljevo municipality, which resulted in a software solution for supporting the work of a team in primary health care, will be implemented in Belgrade municipalities and a cluster of other municipalities in Serbia through a new EAR project. An existing EAR project, focusing on the development of a health information system for basic health and pharmaceutical services, will improve the Kraljevo software package and help develop an electronic health record as well as a national clearinghouse.

3.9.6. The pilot project of basic health services in Dom Zdravlja Kraljevo was completed in June 2005. In 2006 results and experiences from this project will help develop a **capitation formula** that will be used to finance service providers in primary health care as a pilot of a new model of payment.

3.9.7. The development of the basic health benefit package is in progress, and has been included in the Draft Law on Health Insurance. In addition, the Draft Law introduces new methods for financing service providers, better management of financial resources, the decentralization of the Health Insurance Fund, as well as voluntary and private health insurance. Strengthening health promotion and preventive health services aimed at the prevention of communicable and non-communicable diseases and the promotion of healthy lifestyles takes place through the concrete activities of an EAR project implemented in 25 health centers and public health institutes. Tobacco control activities are particularly developed within the National Strategy for Tobacco Control, still to be ratified, and intensive anti-smoking campaigns.

3.9.8. **Developing a private/public mix** is progressing only gradually due to financial constraints. The Health Insurance Fund, however, is now recognizing the prescriptions of private practitioners and contracts between private practice providers and the Republic Health Institute Fund are now possible for certain health care services that are not available in the public sector.

3.9.9. Activities for developing a process for licensing medical personnel and accrediting health care institutions and programs have intensified.

3.9.10. An expert group for youth is closely cooperating with UNICEF to improve the functioning of health care institutions working with young people by improving the quality of existing youth counseling centers and initiating the establishment of new ones that would operate in accordance with the recommended methodology. The Strategy for Improving the Health of Young People has been prepared and implemented, as have been the Mental Health Strategy and a law for its implementation. These activities will be initiated after adoption of the Health Care Law, which represents a precondition for the adoption of regulations in the field of mental health. The HIV/AIDS and TB Control Program in Serbia is supported by a donation from the Global Fund and realized according to the planned dynamic.

3.9.11. Forthcoming challenges:

- Health care financing reform including health insurance reform and development of a new model of provider payment in primary, secondary and tertiary care.
- Rationalization of health workers, starting from administrative and technical staff to nurses and medical doctors and dentists with the implementation of new standards of provision and performance.
- Searching for options and possibilities for privatizing the health care sector, particularly dental services, rehabilitating spa centers and increasing mixed public/private solutions in the health care sector.
- Restructuring clinical centers through EIB credit.
- Establishing and developing independent national bodies for licensing, health technology assessment, accreditation and continuous quality improvement in the health care sector.

3.10. Education and Poverty⁶³

The importance of education for poverty reduction was convincingly demonstrated by the results of the 2002 SLSP: 69% of poor people in Serbia had only elementary or incomplete secondary education, while only 2% had university degrees.

The gradual increase in the share of education expenditure in GDP continues: 3.9% in 2005 and set to rise to 4% in 2007. Reforms currently in process include the streamlining and reorganization of the educational institution network at all levels, implementation of teacher training and additional training programs and the review of school programs. The start of a nine-year compulsory education program is scheduled for the 2006-7 school year. Increased adult education, learning programs and projects, as well as the development of distance education programs, are planned as well.

3.10.1. The start of a nine-year compulsory education program is scheduled for the 2006-7 school year, with the introduction of a **compulsory, free-of-charge preparatory grade** for children 6 to 7 years of age. Also planned is the development of alternative half-day programs for children 5-7 years of age, particularly from vulnerable and marginalized groups. **The coverage of pre-school education is increasing** each year, and the assessment of existing facilities, programs and services in preschool institutions and the creation of a database are currently under way. Training⁶⁴ for the creation of development plans in pre-school institutions is planned until the end of 2007.

3.10.2. A joint effort of the Ministry of Education and Sport and the World Bank, the Republic of Serbia Education Improvement Project and its school grant component, enables schools to create development plans and projects and receive grants. Selection ensures that schools from the poorest regions with high percentages of children from IDP and Roma families receive preference in acquiring the assistance that will improve their living and working conditions.

⁶³ The institution with the greatest responsibility for realizing the goals of education with respect to poverty reduction is the Ministry of Education and Sport.

⁶⁴ The trainings are supported and implemented by the Ministry of Education and Sport with the engagement of school development consultants.

3.10.3. For the purpose of revising **the primary education methodology and curriculum**, the curricula for elementary school grades I, II, III and IV and teaching programs for grades I, II and III have been revised, while the programs for grade IV are under preparation. The programs have retrained teachers to teach foreign languages and civic education in lower grades. Training programs for teachers to teach bilingual classes are under way and seminars have been conducted for first-grade teachers in applying descriptive grading, as well as for history teachers to introduce a European approach to teaching history.

3.10.4. Preparatory activities have begun for projects that seek to develop the capacities of schools and teachers in the areas of the democratization of education, prevention of trafficking, protection of child rights (child ombudsman), and prevention of delinquent behavior in schools. School teams are also being trained to create safe and stimulating school environments within the UNICEF project Schools without Violence. These projects, as well as ongoing ones, have and contribute to the revision of the methodology of working with students that will be modernized, contemporized and made more topical in 2005-6, in line with the real needs of students and schools.

3.10.5. The **Secondary Vocational Education** Strategy draft is in the phase of public debate. During the process of reorganizing the vocational education system in accordance with the needs of the economy, 40 profiles were abolished and 27 new profiles introduced in pilot schools, along with the training of 650 teachers and a new modular principle in the program structuring. There are plans to determine the levels, character and duration of vocational education and training in Serbia in accordance with the 1997 ISCED⁶⁵. Since 2003, a pilot project named the Secondary Vocational Education Reform Program has operated⁶⁶ in 55 secondary vocational schools⁶⁶.

3.10.6. By signing the Bologna Declaration, Serbia joined the group of European countries that are coordinating their policies in the field of **higher education**, in order to establish the European Higher Education Zone by 2010, which seeks to preserve the specific cultural, linguistic and national characteristics of each member country. A draft Law on Higher Education, prepared in accordance with the principles of the Bologna Declaration, will soon be adopted and will represent the basis of accelerated higher education reform in Serbia.

3.10.7. Providing a systemic possibility for adults to obtain qualifications is in the phase of public debate. Other plans include increasing the number of adults in education and learning programs and projects, establishing a wide network of various institutions and organizations for adult education (including five regional training centers that have been organized in five secondary schools in Belgrade, Zrenjanin, Niš, Bor and Kragujevac) and developing distance education programs.

3.10.8. Compared to the earlier period, the **number of student loans** remained the same during the 2004-5 school year (with 240 allocated for occupations that are in short supply); the number of scholarships was reduced to 10,793 and the number of student loans increased (about 18,000). The aim is to further increase the amount of loans and scholarships as well as to increase the number of beneficiaries.

3.10.9. Reallocation of budgetary resources towards poorer regions and municipalities is gradually being implemented, with completion planned for 2010. The Decision on

⁶⁵ International Standard Classification of Education ISCED 1997.

⁶⁶ The program has been supported through CARDS.

Criteria for the Definition of a Kindergarten and Primary School Network has also been adopted, which should lead to the more rational use and reallocation of savings into building repairs, material needs and school equipment, with local self-government being responsible for the implementation. In addition, the program of continuous professional education of teachers for the 2004-5 and 2005-6 school years allocates the highest budgetary resources towards the poorest regions (territories of regional school administration offices in Leskovac, Vranje, Kraljevo, Niš and Požarevac).

3.10.10. **Teacher training** is conducted through public and social institutions, as well as non-governmental organizations. This goal is realized through projects for quality assurance, school development planning and decentralization; seminars for descriptive grading, student safety, civic education, religious instructors and school principals; activities of the center for the professional development of employees and professional associations of teachers and expert associates in educational institutions. In addition, the Education Promotion Institute and the Education Quality Assessment Institute have been established.

3.10.11. For the purpose of **implementing teacher training/additional training programs** on the basis of current sector needs, foreign language teachers in lower grades of primary school have received training, as have all first-grade teachers and expert associates in the area of descriptive grading (220 seminars were organized in 2003 with the attendance of 8,300 teachers, and 280 seminars were organized in 2004 with the attendance of 4,000 teachers). Social inclusion sensitivity seminars were also conducted for 1,200 education employees, parents and representatives of social work centers, in addition to seminars that trained several thousand civic education teachers and employees in preschool institutions. Other seminars addressed the introduction of the teaching program in the first grade of primary school (with 800 seminars organized in the previous two years, attended by 1,600 teachers and expert associates). The plan in 2005 is to train about 2,000 teachers for religious instruction, about 1,200 teachers for the optional "From Toy to Computer" subject and 600 teachers to work with children with special needs. Seminars will also be organized to train **teachers in areas such as civic education and the prevention of delinquent behavior.**

3.10.12. In order to increase the **inclusion and participation of marginalized groups** in the educational system, free-of-charge textbooks were provided for about 6,000 pupils in primary schools in 2002-3 school year and for 5,886 pupils in primary schools in 2003-4 school year. For poor Roma children, 74 school projects relating to the improvement of Roma education for 6,500 children were supported financially on the basis of the 2002-3 tender, as well as about 70 projects in 2003-4 school year. In the same school year, affirmative action⁶⁷ led to the enrollment of 42 Roma pupils in secondary schools and 51 students in two-year colleges and universities. Seventy pupils were enrolled during the 2004-5 school year, while 89 students were enrolled in two-year colleges and universities. An action plan for promoting Roma education in Serbia⁶⁸ was adopted in January 2005. An education program has been prepared for

⁶⁷ The Ministry of Human and Minority Rights in cooperation with the Ministry of Education and Sports and the National Council of the Roma Ethnic Minority.

⁶⁸ Serbia and Montenegro is included in the Roma Inclusion Decade 2005-2015, launched by the World Bank and the Open Society Institute.

Roma community members who are expected to enroll their children in elementary school as well as provide them with the support necessary to complete it.

3.10.13. **Special support for Roma teachers** has been ensured by their inclusion in the system of professional training and by promoting teaching colleges, the department of Romonology and the optional subject of Romany language with elements of national culture (introduced into 29 schools), in addition to a series of seminars for members of ethnic minorities named **Challenges of Education in Minority Languages**. Unfortunately, activities planned in the Strategy for Roma Education have not been fully implemented, primarily the introduction of Roma assistants as well as a Roma coordinator for cooperation with families, which have been delayed by laws and bylaws that fail to prescribe these positions in schools. Activities that will pilot new solutions are currently being developed. Nevertheless, positive discrimination measures for Roma students have been applied to enrollment procedures for secondary and high schools and faculties.

3.10.14. The preparation of an Education Strategy for Persons with Special Needs is underway (following an analysis of the current situation), as well as a three-year OECD/CERI project for disabled pupils and pupils at risk. Two pilot projects are being implemented, including an inclusive model at the preschool education level and a model for partial inclusion and new special schools. Vocational education for pupils with special needs, based on their functional capabilities, is regulated by the Law on Education System Fundamentals, through which schools have been allowed to organize an adapted school program for disabled pupils⁶⁹.

3.10.15. **Forthcoming challenges:**

- Improving the quality of education through the rationalization of programs, by introducing quality standards in specific scientific and educational areas, training teachers in primary and secondary schools and approving new school books in cooperation with the Ministry and professional institutions such as the Institute for the Improvement of Education and Upbringing and the Institute for Quality Control in Education.
- Reforming vocational education, to be carried out primarily by the Center for Strategic Planning (within the Institute for the Improvement of Education and Upbringing) and the Union of Gymnasiums and Vocational Education Schools. Pilot programs that will introduce new profiles in vocational schools and their application in a larger number of schools will be evaluated. Developing optional subjects in gymnasiums will introduce changes into the regular school curricula.
- Including marginalized groups and persons with special needs into the regular education system based on affirmative action measures proposed by expert teams, including the simultaneous implementation of seminars for teachers who will work with children with special needs.

⁶⁹ Two schools have realized such programs thus far, with the help of donations from the Norwegian government and the City Education Secretariat.

3.11. Regional, Rural and Urban Aspects of Poverty⁷⁰

Regional discrepancies in Serbia's development are the most pronounced in Europe and continue to increase from one year to the next. Apart from the traditionally undeveloped south of Serbia and Old Raška, the newly impoverished areas are east Serbia, parts of central Serbia and the regional centers of the mining and traditional industry, which have experienced further demographic outflow from rural and underdeveloped regions.

The network of regional agencies for SME and entrepreneurship development continues to expand. At the end of 2004 the network covered over 80% of the territory of the Republic of Serbia. The Development Fund of the Republic of Serbia also stimulates the development of entrepreneurship and employment with a special focus on underdeveloped areas.

Ensuring support to sustainable rural development, as well as to farmers who have been affected the most by economic reforms and further liberalization in the agricultural sector, are among the key goals of the Draft Strategy for Agricultural Development. The Strategy seeks to increase the competitiveness of Serbian agriculture by means of resource reallocation from price support to investment and structural support.

The Strategy of Local Sustainable Development, delivered for adoption to local self-governments in May 2005, is aligned with the PRS and presents a basis for local community development planning.

3.11.1. The adoption of the **Law on Balanced Regional Development**, in the final drafting stage, will create an institutional framework for establishing the National Agency for Regional Development and a special financial institution for promoting regional development, which would be in charge of implementing the goals and tasks defined in the Poverty Reduction Strategy for Serbia. Implementation would be ensured through a network of regional agencies and offices for regional development. In May 2004 the Ordinance on the Criteria and Indicators for Determining the Devastated Areas of the Republic of Serbia and the Decision on the Determination of Devastated Areas (Municipalities) of the Republic of Serbia were adopted. The **Law on Underdeveloped Areas (UDA)** has been proposed for the period until 2010,

3.11.2. One of the basic goals of the **Development Fund of the Republic of Serbia** is a more balanced regional development through the granting of soft loans to SMEs and entrepreneurs. Short-term export and liquidity loans are granted, with a repayment period of six months and an annual interest rate of 5%. During 2004, 1.38 billion dinars were extended, with another 520 million in short-term export loans planned for 2005. Long-term loans are granted with a repayment period of five years and a one-year grace period and interest rate depending on the development level of the municipality, based on the GDP average (Table 3.11.a.). During 2004, 7.86 billion dinars were extended, with 4.72 billion dinars to be extended in 2005. Apart from long-term loans from the Fund capital, long-term commission loans for promoting primary agricultural production were also extended. A total of 164 loans were granted

⁷⁰ The institutions with the greatest responsibility for reducing the regional, rural and urban aspects of poverty are the Ministry of Public Administration and Local Self-Government; the Ministry of Finance; the Ministry of Capital Investment; the Ministry of Agriculture, Forestry and Water Management and the Republic Development Fund.

for these purposes, in the total amount of 1.74 billion dinars. The Fund aimed to distribute the loans equally in the various regions and areas of the Republic.

Table 3.11.a: Lending terms of the Development Fund of the Republic of Serbia

Development level of municipalities based on GDP	% share of the Fund's loan in the estimated value of investment	Annual interest rate
< 33%	up to 80%	1%
33% - 50%	up to 60%	3%
50% - 70%	up to 50%	4%
> 70%	up to 40%	5%

3.11.3. The **Regional Development Agency** of Šumadija and Pomoravlje was established in Kragujevac, with others in progress for Banat in Zrenjanin and Southern Serbia in Leskovac, and another in development for east and west Serbia.

3.11.4. Expansion of the **network of regional agencies for SMEs and entrepreneurship development** continues. Since 2004 regional agencies in Leskovac and Vranje have been established, as well as the offices of regional centers in Apatin and Odžaci. The process of opening an office in Bujanovac is currently under way, with plans to establish an office in Medveđa as well. At the end of 2004 the Republic network covered over 80% of the territory of the Republic of Serbia (without Kosovo and Metohia), with a goal to cover the entire territory of the Republic. The Republic Agency for SME Development and the Republic Network of Regional Agencies provide, *inter alia*, legal and financial consulting to potential and existing SMEEs (Table 3.11.b.), organize seminars in the area of entrepreneurship (including 67 seminars attended by over 2,000 participants in 2004), promote expert and financial support to SMEEs (including 13 promotions attended by roughly 1,000 entrepreneurs in 2004), implement projects (e.g. Scanning of Innovation Capacity in the Šumadija and Pomoravlje Region) and participate in international cooperation programs.

Table 3.11.b.: Work of the Republic Agency for SMEE Development and Republic Network

Help line	Consulting (financial and legal)	Business plan (assistance and preparation)	E-mail responses	Training	
				No. of seminars	No. of participants
7,619	4,283	190	2,509	278	5,837

3.11.5. In 2003, the three-year, EU-financed **Regional Socio-Economic Development Programme** was launched in three regions in Serbia—Banat, central Serbia (Šumadija and Pomoravlje districts) and South Serbia—to promote a partnership approach to economic and social development. Thus far three Socio-Economic Development Plans have been drafted; the Regional Socio-Economic Development Fund (RSEDF) provides financial support of EUR 1.4 million to non-commercial projects developed from regional plans.

3.11.6. Stimulation of economic growth and development, and in particular export-oriented foreign direct investment, requires the implementation of new ideas, such as **clusters, business incubators, industrial zones, technological parks**, etc. The Ministry of Economy and the Ministry of International Economic Relations defined a pilot project for supporting the process of developing clusters in Serbia. Autoklaster Srbije, which gathers car-part producers, has been established. Moreover, a new concept of regional development should be implemented, with the active approach of all government levels. Proper results can be expected only based on the coordinated

action of players from the national to the local level. In 2005, business incubators—seen as one method for successfully resolving part of the problem of the surplus labor caused by large system restructuring—will open in Knjaževac, Niš, Bor, Subotica and Smederevska Palanka. Business incubators are thought to be one of the successful ways to partly solve the problem of workers who became redundant due to the restructuring of large companies.

3.11.7. An important pilot project named ENTRANS⁷¹ was launched in October 2004. The project seeks to establish a business incubator in Niš, prepare a business incubator establishment manual, design business start-up training, support the development of the Regional Agency for SMEE Development in Niš and serve as a resource center for incubators and training at the Republic Agency for SMEE Development.

3.11.8. The Serbian Investment and Export Promotion Agency (SIEPA) organized the **training of local self-government bodies** in over 90 municipalities. Common databases are being established, and the level and quality of communication between municipalities and investors as well as the level of cooperation between municipalities and the Agency is rising. On several occasions these measures enabled the faster realization of planned investment, better municipal communication with potential investors and the updating of databases of available land and plants, which are of great importance for attracting and swiftly realizing investment.

3.11.9. **The Draft Strategy for Agricultural Development** recognizes the economic, social, environmental and political goals of the agricultural sector, including building sustainable, efficient and competitive agriculture; ensuring food quality and safety standards; supporting agricultural producers affected by economic reform; encouraging sustainable rural development; protecting the environment from the effects of agricultural production; preparing the agriculture sector for EU integration and adjusting trade policies to WTO rules.

3.11.10. Implementation of these goals began through two previous budget cycles and the agrarian budget increased from 8 to 21 billion dinars. Such agrarian policy seeks to build competitiveness through decreased price support and increased investment and structural support. Budget resources directed to price support were significantly decreased (from 80% of the budget of the Ministry of Agriculture in 2003 to 40% in 2005), which in the short term decreases the number of budget beneficiaries, and in the long run creates preconditions for economic growth and a healthier economic environment.

⁷¹ Funded by the Government of Norway.

Table 3.11.c.: Total investment in the period March 2004-August 2005⁷²

Measure	No. of beneficiaries	Amount (in 000 of dinars)	Average amount
Credit support			
Short-term credits	51,467	3,187,337	61,929
Long-term credits	2,957	3,455,875	1,168,709
Rural development measures			
Grants for young agricultural producers, cooperatives and local communities	578	949,355	1,642,482
Other rural development measures*		1,240,000	

* Various types of rural development measures such as grants for investments, introducing standards and rural infrastructure, support to elderly households, improving soil quality, etc.

3.11.11. Short-term negative effects of the transition to a market economy will be addressed through increased social transfers to farmers who are not competitive on the market due to their small production capacity or unfavorable geographic locations, i.e. areas less favorable for agricultural production. Success of these measures will depend on the introduction of an adequate monitoring and evaluation policy that will enable identification of the most vulnerable groups living in rural regions. The registry of agricultural households is established to provide more complete information on the situation in rural areas and to define less favorable areas.

3.11.12. **The Agency for Rural Development**, in the establishment stage, should assist in developing activities that can be conducted regionally, with a special focus on assisting citizens in analyzing potential markets, planning production, diversifying the economy and providing financial support. Until the Agency is established, the ordinances on fostering agricultural production development and rural development in 2005 are implemented.

3.11.13. The *Rulebook on the Distribution of Partial Funds from Special-Purpose Revenues of the Republic Budget Collected from the Organization of Games of Chance, and Used for Local Self-Government Financing* seeks to create possibilities for **providing assistance to the most vulnerable and poorest local self-governments**, including those hit by natural or other large-scale disasters, as well as technical and other assistance to modernize local self-government bodies.

3.11.14. By mid-2005 the Housing Sector Study will be completed⁷³, which will present an analysis of the overall housing sector with recommendations that will form the basis of the future **national housing policy**. The Draft Law on Social Housing seeks to improve the legal framework for regulating the social housing sector and is currently undergoing a process of harmonization with other ministries in the Government of the Republic of Serbia.

3.11.15. **Forthcoming challenges:**

- Creating conditions for attracting investment to underdeveloped regions. The current legal environment provides local self-governments with insufficient space to independently create the fiscal and other incentives for potential investors that would increase their competitiveness. Although the Government has introduced

⁷² Budgetary resources of the Ministry of Agriculture, Forestry and Water Management.

⁷³ In cooperation with the UN European Economic Commission.

measures for helping the development of these regions, their poor public infrastructure often represents a key obstacle.

- Even regional development will require both political commitment and a coordinated approach that should include all levels of government, based on the best EU practices and serving to prepare for the future use of EU structural and regional funds.
- Sharing authority and responsibility with the local level. Decentralization of power, followed by fiscal decentralization, which will improve government responsiveness and accountability, will require substantive changes of the overall legal and constitutional framework. Among other things, the Law on Assets Owned by the Republic needs to be changed to allow local self-governments to own and manage public property on their territory.
- Developing a payment system in accordance with EU regulation that will ensure support to rural development.

3.12. Environmental Aspects of Poverty Reduction⁷⁴

The link between the state of the environment and poverty is reflected, primarily, in the impact on the health and quality of living of Serbia's population, whereby the poorest population is disproportionately affected by environmental degradation. The general tendency is to work simultaneously on minimizing the consequences of environmental degradation and promoting activities aimed at its prevention, with an ultimate goal of ensuring environmental sustainability in the long run.

Investments in water supply facilities, wastewater treatment plants and environmental hotspot clean-up programs have had a direct impact on poverty reduction. Indirectly, such activities have also contributed to the employment of a number of semi-qualified, poorer workers.

3.12.1. Current problems include continued unsatisfactory **water quality** in some regions, unprotected potable water sources, summer water shortages and excessive groundwater extraction in the Autonomous Province of Vojvodina. During the previous period, attempts to solve these problems were co-financed⁷⁵ in the total of CSD 237 million by the continued construction of three dams and reservoirs and the construction of water supply facilities in 23 municipalities. Investments in these infrastructure facilities are labor intensive and have stimulated the employment of semi-qualified, poorer workers in particular. Improved access and quality services in water management have contributed to lower prices and increased efficiency in the economic activities of affected locations. Investment in water management contributes to the overall development of an area, and therefore to poverty reduction. When it comes to **special water management incentives**, during 2005 the Government will finance the development of documentation for preparing investments, in case of projects where documentation exists.

⁷⁴ The institutions with the greatest responsibility for implementing the environmental aspects of the PRS are the Ministry of Agriculture, Forestry and Water Management; the Ministry of Science and Environmental Protection; the Ministry of Health and the Ministry of Public Administration and Local Self-Government.

⁷⁵ The Ministry of Agriculture, Forestry and Water Management; the Directorate for Water Management.

3.12.2. The **collection and disposal of municipal and industrial wastewater** is less developed than the water supply. Out of a total of 152 existing wastewater treatment plants, it is estimated that currently less than 15% are operating with satisfactory results. In 2003, the investments were co-financed in the area of wastewater treatment and the construction of collector canals for supplying water to the wastewater treatment plants in 11 municipalities. In 2004, in order to ensure **wastewater treatment capacities**, activities were implemented in the total value of CSD 85 million. Facilities for water protection were financed in five municipalities.

3.12.3. In 2003, **activities for the reconstruction and rehabilitation of flood control facilities** were financed on 13 rivers. In 2004, similar activities were also financed in a considerable number of locations. **The natural disaster in April 2005**, in the central Banat region, underscored the need for higher investments in the maintenance of the existing flood control systems, and most importantly, dams and retaining walls.

3.12.4. **In order to clean up environmental hotspots** (thermal power plants, locations destroyed during the NATO bombing or areas where ammunition containing depleted uranium was used), the remediation of the contaminated soil was completed in Pljačkovica near Vranje, as well as in Bratoselce near Bujanovac. The clean up of Borovac near Bujanovac was planned during 2005, as well as Reljan near Preševo during 2006. The plan⁷⁶ envisages the **development of a radioactive waste management program**, the completed decontamination of soil contaminated with depleted uranium by 2008 and the establishment of a depleted uranium environmental impact monitoring and assessment in the municipalities of Bujanovac, Preševo and Vranje. **Remediation projects** in Kragujevac (4) and in Novi Sad (6) were completed. The feasibility study **Serbian Thermal Power Plant Emission Reduction was finished**, and financing provided for solving top-priority problems in the Nikola Tesla B Thermal Power Plant, as well as in the Thermal Power Plants Kostolac A and B.

3.12.5. **In order to improve waste management**, CSD 61 million was allocated⁷⁷ in 2004 to co-finance 30 projects in 61 municipalities, including the development of project documentation for the rehabilitation and remediation of municipal landfills and the construction of regional landfills. In addition, solutions to waste management problems in the municipalities of Zubin Potok, Zvečan and Leposavić were supported. The Public Invitation for Co-financing Waste Management Projects for 2005 was also completed, and inception of the World Bank project Serbian Danube River Enterprise Pollution Reduction, in the total value of approximately USD 20 million, was agreed and planned for September 2005.

3.12.6. In addition to specific measures and activities, the relevant ministries have also achieved considerable results in adopting environmental legislation: the Feasibility Study for Hazardous Waste in Serbia, including medical waste, which was prepared with the support of the European Agency for Reconstruction. The EAR also supported the first phase in construction of the Hazardous Waste Treatment Center. Furthermore, all preparatory activities for implementing a project to equip mobile ecotoxicological units were completed. In December 2003, the Agency for Environmental Protection was established, taking over some of the activities of the Directorate for Environmental Protection. The Sustainable Development Council of

⁷⁶ Short-term objectives of the Directorate for Environmental Protection.

⁷⁷ Ministry of Science and Environmental Protection, Directorate for Environmental Protection.

the Government of the Republic of Serbia was also established, as well as the Fund for Environmental Protection, as of the beginning of 2005.

3.12.7. Drafts or final versions of **Local Environmental Action Plans (LEAPs)**, which should support local authorities in performing their duties and responsibilities in the field of environmental protection, have been finalized in 13 Serbian municipalities. LEAP is being developed in six municipalities with financial support from the Ministry of Science and Environmental Protection, as well as in another twenty municipalities with own financial resources and donor support. Numerous seminars have also been organized to help raise public awareness in the Republic of Serbia about environmental protection and sustainable development. The campaign Clean and Green Serbia is also under preparation.

3.12.8. Supported by the EAR, the Draft National Environmental Action Plan (NEAP), which presents the basic document for planning, managing and integrating environmental protection over the next 10 years, has been prepared and will be submitted by the end of the year to the Serbian Parliament for adoption.

3.12.9. The **preparation of a number of action plans** are expected by December 2006, including spatial planning and development, soil protection, water protection, air and atmosphere protection, forest protection, ecosystem protection, protected areas, chemical management, protection against ionizing and non-ionizing radiation, protection against accidents, protection against noise and vibrations, sustainable energy management, information system development, development of scientific research, education and training, and the development and implementation of economic instruments.

3.12.10. **Forthcoming challenges include:**

- Setting up an independent Agency for Environmental Protection, as an obligation outlined in the EU Feasibility Study, to serve as an inter-sector service in the area of environmental protection.
- Effectively implementing a series of new pieces of legislation in the area of environmental protection as well as of a number of the already existing action plans.
- Building the capacity of local-level administrations for implementation of new obligations in the area of environmental protection, as stipulated by a set of new laws adopted in December 2004.

4. ANALYSIS OF BUDGET AND INTERNATIONAL ASSISTANCE RESOURCES

The absence of a model for systematic monitoring of the allocation of resources available to the Republic of Serbia based on programmatic goals represents a main obstacle for assessing the overall amount of resources allocated for poverty reduction activities, either domestic or foreign. Overcoming this problem, common to all institutions of the Republic of Serbia, poses the main challenge in the forthcoming period.

4.1. Analysis of budget resources allocated to poverty reduction-related programs

4.1.1. For the purpose of this report, an effort has been made to estimate the level of funds from the 2004 and 2005 Budgets of the Republic of Serbia that were allocated for the implementation of activities in public administration institutions, which are directly or indirectly aimed at poverty reduction.

4.1.2. Several reasons do not allow for any explicit conclusions relating to the resources allocated for achieving goals identified in the Poverty Reduction Strategy for Serbia.

4.1.3. The first reason relates to the dynamics of the budget process itself. As the Poverty Reduction Strategy in Serbia was adopted in October 2003, at the end of the budget preparation process for the following year, it was unable to affect the planning of the allocation of these resources for the year 2004. On the other hand, although the PRS was included in the Budget Memorandum for 2005 (adopted in May 2004), the activities of the public administration institutions, i.e. activities in individual sectors, were not directly linked to the priorities defined in the Strategy—which is not an exception when compared to other programmatic documents.

4.1.4. Another obstacle in conducting the analysis is the character of the budget of the Republic of Serbia, a so-called **line type of budget**, which does not provide insight into the link between identified programmatic priorities and the allocation of budgetary resources. This kind of budget is characterized by the distribution of funds according to budget beneficiaries⁷⁸ (organizational classification) and the type of expenditure⁷⁹. **The presentation of the distribution of budgetary funds in such a manner does not allow for the possibility to clearly establish the link between certain expenditures and their effect.**

4.1.5. These reasons prevent the precise identification of the category of expenditures directed at poverty reduction, or an estimation of the amount of allocations directed at the implementation of the Poverty Reduction Strategy for Serbia.

⁷⁸ The distribution of funds according to budget beneficiaries represents the **organizational budget classification**.

⁷⁹ The distribution of funds according to the type of expenditure represents the **economic classification**.

4.1.6. **The line type budget** offers the possibility of an indirect analysis under the assumption that certain state functions⁸⁰ contribute entirely to poverty reduction (for instance social welfare, education, health care, etc.). Taking this into account, and in the absence of higher-quality data sources, a special methodology was developed in order to identify the level of funds directed at the state functions whose activities can indirectly influence poverty reduction⁸¹.

4.1.7. The state functions that were included in the analysis as those that directly or indirectly contribute to poverty reduction are economy, labor and employment; social welfare and insurance; health and education.

4.1.8. Overall allocations directed at these state functions compared to total public spending accounted for 67.7% in 2003, 70.3% in 2004 and 71.0% in 2005. These proportions not only represent the allocations for activities that directly aim at poverty reduction, but also include a multitude of other expenditures linked to other activities of Government institutions which cannot be shown separately.

Table 4.1.a. Spent budget funds according to state functions (share in total public spending)

State functions	Budget funds		
	2003	2004	2005
Economy, labor and employment	9.5	9.2	9.3
General economic and commercial affairs and jobs related to the issue of labor	2.6	2.0	2.2
Agriculture, forestry, hunting and fishery	1.5	2.5	2.2
Transport	3.4	2.2	2.2
Community development	0.1	0.1	0.1
<i>National employment service</i>	<i>1.9</i>	<i>2.4</i>	<i>2.6</i>
Social welfare and insurance	36.7	39.0	38.9
Illness and disability	1.3	1.4	1,5
Family and children	2.7	2.4	2,5
Social welfare for vulnerable populations	1.1	1.1	1.4
Social welfare not classified elsewhere	1.3	1.2	1.2
<i>Pension and disability pension funds (PIO)</i>	<i>30.3</i>	<i>32.8</i>	<i>32.3</i>
PIO for the employed	28.2	30.2	29.7
PIO for farmers	0.9	1.5	1.6
PIO for self-employed	1.1	1.1	1.1
Health care	13.5	14.5	14.4
Health care not classified elsewhere	0.6	0.8	0.8
<i>RHIU</i>	<i>12.9</i>	<i>13.8</i>	<i>13.6</i>
Education	7.9	7.5	8.3
Pre-school and primary education	3.9	3.8	4.2
Secondary school education	2.0	1.8	2.1
Two-year post-secondary school and university education	1.2	1.2	1.3

⁸⁰ The IMF's functional classification of state functions according to the type of service that a Government institution provides for citizens (economic affairs, public services, social welfare, health care, public order and security, etc.).

⁸¹ See Annex 6.1

Auxiliary services in education	0.7	0.6	0.6
Education not classified elsewhere	0.1	0.1	0.1
TOTAL	67.6	70.2	69.9

Source: The Treasury System on budget execution for the previous period, i.e. data on the planned budgetary resources for the current fiscal year.

4.1.9. The large share of public spending in the field of social welfare and insurance (39%) and health care (14,5%) in 2004, compared to the economy and education, speaks in favor of the social rather than developmental character of public spending during the first years of transition in the Republic of Serbia.

4.1.10. Changes in the structure of public spending are planned for the next medium-term period (2006-2008). Instead of social welfare and health care, economy and education should become the leading strategic fields. These two fields play a crucial role in the long-term development of preconditions for preventing the creation of new poverty, but also in reducing the existing level of poverty in Serbia⁸².

4.1.11. The adoption of the programmatic budget will enable the possibility to define in detail the implementation and monitoring of programs and projects within PRS strategic fields, enabling as well the precise presentation of planned and allocated budgetary resources directed at the achieving goals defined in the PRS.

4.2. Realization of international assistance to the Republic of Serbia

4.2.1. While many of bilateral and multilateral donors as well as international non-governmental organizations present in Serbia support programs and projects in line with the PRS objectives, the Republic of Serbia does not have the data that would provide for an accurate report on international assistance allocated for poverty reduction⁸³. This applies both to the funding received for public administration activities as well as non-governmental organizations in Serbia. Therefore, this summary report refers to the overall international assistance received by the Republic of Serbia.

4.2.2. In the last three years, external financing contributed significantly to the economic growth rate; without it, the problems in some sectors (energy, health, social sector, refugee and IDP assistance) would have been considerably worse. Efficient use of donor assistance was achieved through continuous consultations between the donor community and the institutions of the Republic of Serbia.

4.2.3. For the period 2000-2005, a total of EUR 5.3 billion in donor assistance was allocated to Serbia. Out of that amount, approximately EUR 3.1 billion was used during 2000-2004. In the course of 2005, the allocation of an additional EUR 620 million is planned. The outstanding funds in the total of approximately EUR 1.6 billion will be used within the programs that are currently in various stages of implementation.

⁸² Memorandum on the Budget and Fiscal and Economic Policy of the Government of the Republic of Serbia for 2006, with projections for 2007 and 2008.

⁸³ The preparation of the PRSp in Serbia was financed by several donors through the Fund for Poverty Reduction Strategies administered by the World Bank (Japanese and Dutch government grants). The preparation was also supported by the UK Department of International Development (DFID) and the Danish and Norwegian governments.

4.2.4. 2004 marked the transition from a humanitarian to a development phase of financing in international assistance and a complete withdrawal of humanitarian support is expected by 2006.

4.2.5. The overall amount of international assistance is gradually decreasing, with a steady decrease in the share of grants in relation to the assistance approved in the form of concessional credits.

Table 4.2.a.: Ratio of received grants and concessional credits (in EUR million)

	Grants	%	Concessional Credits	%	Total
2000	187.21	100%	-	0%	187.21
2001	592.86	69%	269.80	31%	862.66
2002	554.27	68%	261.28	32%	815.55
2003	354.12	55%	287.69	45%	641.81
2004	124.60	22%	431.26	78%	555.86
2005	72.94	12%	551.98	88%	624.92
TOTAL	1,886.00	51%	1,802.01	49%	3,688.01

Source: MIER

4.2.6. One weakness in the previous period was the unsatisfactory coordination of international assistance, equally on the part of donors as well as on the part of the Republic of Serbia.

In the forthcoming period, the following will be of greatest importance:

- a) Coordination and harmonization of international assistance directly allocated for achieving goals defined in the PRS.
- b) Harmonization of resources intended for the implementation of the PRS using EU resources allocated for the Republic of Serbia.
- c) Further efforts linked to the harmonization of international assistance resources with the budgetary resources allocated for the PRS implementation.

4.2.7. In cooperation with the Development and Aid Coordination Unit⁸⁴ under the Ministry of International Economic Relations, the development of an international assistance classification system has been planned to monitor expenditures related to the implementation of the PRS objectives, within the existing reporting system (ISDACON)⁸⁵.

⁸⁴ The Development and Aid Coordination Unit (DACU) was established in November 2000 under the Serbian Ministry of International Economic Relations to promote national priorities through close cooperation with donors and development partners.

⁸⁵ ISDACON – Inter-sectoral Development Assistance Coordination Network.

5. CONSULTATIVE PROCESS—ACTIVITIES OF THE POVERTY REDUCTION ADVISORY COMMITTEES

The Poverty Reduction Strategy Paper preparation process represented the first time that governmental, non-governmental and business institutions and organizations in Serbia, both on the national and local level, participated in a joint process of preparing a national strategic document of the Republic of Serbia. What made the PRSp preparation process unique was also the number of institutions involved. In order to make the consultation process as comprehensive as possible, seven representative Advisory Committees were established: the Parliamentary Committee for Poverty Reduction in Serbia, the Civil Society Advisory Committee, the Local Self-Governments Advisory Committee, the International Development Partners Advisory Committee, the Trade Unions Advisory Committee, the Business Advisory Committee and the Inter-Ministerial Operational Advisory Committee.

The cooperation of a large number of partners participating in the preparation of the PRSp resulted in wide support for the PRS, and its recognition as a genuine national document.

When the PRS implementation process was initiated, it was necessary to reconstitute these Committees with the aim of monitoring the PRS implementation. In order to achieve this, the Deputy Prime Minister's Poverty Reduction Strategy Implementation Focal Point (DPM PRS IFP) has initiated the reconstitution of cooperation with the Parliament Committee for Poverty Reduction, the Civil Society Advisory Committee, the Local Self-Governments Advisory Committee and the International Development Partners Advisory Committee. In the ensuing period the DPM PRS IFP will support the reconstitution of the Trade Unions Advisory Committee, Business Advisory Committee and Inter-Ministerial Operational Advisory Committee.

PARLIAMENTARY COMMITTEE FOR POVERTY REDUCTION IN SERBIA

5.1.1. The Parliamentary Committee for Poverty Reduction in Serbia was established on May 30, 2003, and became active on April 8, 2004. The Committee comprises 15 members from six parties represented in the Parliament: 3 members—Democratic Party of Serbia; 1 member—Serb Renewal Movement; 2 members—Serbian Socialist Party; 5 members—Serbian Radical Party; 2 members—G17 Plus and 2 members—Democratic Party.

5.1.2. The Committee defines the participation of the Parliament of Serbia in the PRS implementation process; reviews drafts of laws, other regulations and general documents from the aspect of PRS implementation; monitors the budget preparation and allocation process as related to the PRS implementation; provides comments and assessments regarding the PRS implementation and works on the institutionalization and participation of citizen representatives in the PRS decision-making process.

5.1.3. By June 2005, the Committee had 13 sessions, promoted the PRS among MPs in the Parliament of Serbia and participated in numerous meetings with institutions and organizations that are taking part in the PRS implementation process. In cooperation with the Organization for Security and Cooperation in Europe, the Committee is implementing a project on new legislative solutions with the purpose of reducing poverty among children in Serbia.

5.1.4. In the past period the Committee established good cooperation with the United Nations Development Programme (UNDP), with whose support the Committee organized a seminar on the implementation of Poverty Reduction Strategy for Serbia in November 2004. In June 2005 they organized a study visit to the Parliament of Israel.

5.1.5. Following the initiative of the DPM PRS IFP and the Parliamentary Committee for Poverty Reduction in Serbia, UNDP will provide financial support for an expert who will assist Serbian municipalities flooded in April 2005 with drafting project proposals for the economic development of flooded areas.

5.1.6. In the ensuing period the Committee is planning to monitor and analyze the effects of adopted laws and new legislative solutions from the aspect of poverty reduction and prevention, expand cooperation with other committees within the Parliament of Serbia, become acquainted with the experiences of parliamentary committees in other countries and organize a regional conference on the means for fighting poverty.

CIVIL SOCIETY ADVISORY COMMITTEE

5.1.7. Representatives of 11 NGOs, nominated by the three largest networks of non-governmental organizations in Serbia (Civic Initiatives, the Center for the Development of the Non-Profit Sector and Network Serbia Without Poverty), participated in the PRSp preparation process through the work of the Civil Society Advisory Committee. The main goal of this Committee is to improve the dialogue between the government and non-governmental sector and to enable the participation of the civil sector in the development and implementation of strategic documents related to poverty reduction. The Committee was established in autumn 2002 and has facilitated the involvement of around 250 non-government organizations in Serbia in the PRSp preparation process. During 2003, the Civil Society Advisory Committee was also active in local PRS initiatives, which worked toward establishing national ownership of the Poverty Reduction Strategy.

5.1.8. One of the main qualities of this Committee is that its members represent poor and vulnerable social groups, and that they are regionally distributed throughout the whole of Serbia.

5.1.9. During 2004 the Civil Society Advisory Committee continued to actively promote the PRS as a national development document. In January 2005 it organized nine round tables⁸⁶ on the territory of Serbia to promote the PRS and mobilize all actors toward an active approach in solving the problem of poverty, using the PRS as a basis for their activities. As a result of these round tables, the Civil Society Advisory Committee published a brochure on opportunities for the participation of civil society in poverty reduction in Serbia.

⁸⁶ In cooperation with the Deputy Prime Minister's PRS Implementation Focal Point and with financial support from DFID.

LOCAL SELF-GOVERNMENTS ADVISORY COMMITTEE

5.1.10. The Local Self-Governments Advisory Committee coordinates between the Government of the Republic of Serbia and representatives of towns and municipalities in the process of PRS preparation and implementation. This Advisory Committee was established with the support of the Committee on Social Policy of the Standing Conference of Towns and Municipalities (SCTM)⁸⁷. Through the work of the Local Self-Governments Advisory Committee, towns and municipalities in Serbia have been given the opportunity to raise relevant questions or influence changes in the attitudes of the central government towards key issues in the daily activities of local self-governments.

5.1.11. In January 2005, the SCTM⁸⁸ published a brochure entitled “Poverty Reduction Strategy—challenges and opportunities at the local level.” This brochure points to the most important elements of the national PRS document and proposes activities that can be included in strategies at the local level. Within the Program for Environmental Protection and Sustainable Development in Serbian Towns and Municipalities, the SCTM has prepared the Strategy on Local Sustainable Development. This document was introduced to the representatives of towns and municipalities of Serbia at the National Conference on Local Sustainable Development on May 26, 2005. The recommendations have been integrated into this document.

INTERNATIONAL DEVELOPMENT PARTNERS ADVISORY COMMITTEE

5.1.12. The International Development Partners Advisory Committee, which gathers multilateral and bilateral donors as well as international NGOs, participated actively in the PRSp preparation process. After the adoption of the document, donor organizations supported the integration of measures envisaged by the PRS into their respective plans, as well as the coordination of their activities targeting poverty reduction with the Deputy Prime Minister’s PRS Implementation Focal Point and the Ministry of International Economic Relations. International NGOs started to coordinate their poverty reduction activities with the efforts of the Government of the Republic of Serbia. Towards this end, international NGOs in Serbia have created a database on their current and planned programs, which contains PRS-related programs of different international NGOs together with their regional distribution in Serbia. By ascertaining this information, better targeting of support to sectors and regions in Serbia where needs are the most considerable is enabled.

⁸⁷ The Standing Conference of Towns and Municipalities (SCTM) is a national association of local authorities in Serbia. The Committee on Social Issues (one of the SCTM’s 10 line committees) deals with issues of social policy and employment at the local government level.

⁸⁸ In cooperation with the Deputy Prime Minister’s PRS Implementation Focal Point and with financial support from DFID.

6. ANNEXES

6.1. Analysis of budgetary allocations: absolute amounts of expenditures directed at the priority PRS- related areas

The budget of the Republic of Serbia and other levels of authority (the provincial and local level), represent a **line type of budget** according to the manner in which they show the allocation of funds. It is characterized by the distribution of funds according to budget beneficiaries⁸⁹ (organizational classification) and the type of expense⁹⁰ (economic classification). Reviewing the distribution of funds is united by the functional classification, which is identical for different budget beneficiaries whose activities, by their nature, belong to the same state function⁹¹ (functional classification). For each budget beneficiary it shows the expenditures according to the type of expenses (salaries, material costs, the purchase of fixed assets and so on), i.e. expenditures presented according to the economic classification.

The tables below represent expenditures according to the functional classification from different type of sources – budgetary resources and other sources of financing (budget beneficiaries' own incomes, donations and borrowings).

⁸⁹ The distribution of funds according to budget beneficiaries represents the **organizational classification of budget**.

⁹⁰ The distribution of funds according to the type of expenditure represents the **economic classification**.

⁹¹ The IMF's functional classification of state functions according to the type of service which a Government institution provides for the citizens (economic affairs, public services, social welfare, health care, public order and security, etc.).

Table 6.1.a.: Expenditures according to priority functions—budget resources

		Budget resources (Currency USD)		
		2003	2004	2005
Function	Economy, Labor and Employment	853.520.125,50	960.833.323,66	1.037.232.325,02
410	General Economic and Commercial Affairs and Labor Affairs	233.409.045,47	213.369.096,35	250.869.090,91
420	Agriculture, Forestry, Fishing and Hunting	131.170.256,80	264.059.441,16	241.048.189,86
450	Transport	306.123.666,54	227.355.242,90	242.565.953,34
620	Community Development	13.369.335,89	6.722.718,99	10.320.884,96
	<i>National Employment Service</i>	<i>169.447.820,80</i>	<i>249.326.824,25</i>	<i>292.428.205,95</i>
	Social Protection	3.299.302.625,62	4.065.670.311,51	4.338.761.078,04
010	Illness and Disability	113.008.095,80	148.921.130,62	164.958.165,73
040	Family and Children	246.257.687,39	253.393.897,16	278.443.121,48
070	Social Welfare for Most Vulnerable Groups	98.488.770,75	116.025.386,22	155.833.081,26
090	Social Welfare Unclassified Elsewhere	119.568.435,30	125.971.544,93	137.174.658,09
	<i>Pension and Disability Insurance Funds</i>	<i>2.721.979.636,38</i>	<i>3.421.358.352,59</i>	<i>3.602.352.051,49</i>
	Of employees	2.539.823.927,77	3.150.017.300,45	3.307.092.067,58
	Of agricultural producers	83.517.439,02	161.028.153,75	177.205.229,28
	Of the self-employed	98.638.269,60	110.312.898,39	118.054.754,63
	Health Care	1.211.860.331,56	1.513.974.290,66	1.605.274.432,82
760	Health Care Unclassified Elsewhere	54.696.708,29	78.796.633,50	83.694.384,55
	<i>Republic Health Insurance Institute</i>	<i>1.157.163.623,27</i>	<i>1.435.177.657,16</i>	<i>1.521.580.048,27</i>
	Education	712.227.791,74	785.128.677,91	930.297.940,47
910	Preschool and Primary Education	353.724.277,94	393.483.115,84	468.082.783,59
920	Secondary Education	178.382.899,79	191.946.697,10	229.630.136,77
940	Higher and University Education	112.046.413,37	128.161.072,92	150.076.958,97
960	Additional Services to Education	59.364.368,32	65.633.260,23	71.989.557,52
980	Education unclassified elsewhere	8.709.832,32	5.904.531,83	10.518.503,62
	Environment	9.090.244,40	6.624.618,55	9.757.827,84
510	Waste Management	397.781,61	263.738,77	457.988,74
560	Environmental Protection unclassified elsewhere	8.692.462,79	6.360.879,78	9.299.839,10
	Total	6.086.001.118,82	7.332.231.222,29	7.921.323.604,18

**Table 6.1.b.: Expenditures according to priority functions –other sources
(own income, donations, domestic and foreign borrowing; in USD)**

		Other sources		
		2003	2004	2005
Function	Economy, Labor and Employment	793.024.948,92	272.454.854,47	377.398.364,18
410	General Economic and Commercial Affairs and Labor Affairs	255.714.304,20	8.227.277,19	4.798.558,44
420	Agriculture, Forestry, Fishing and Hunting	134.667.250,63	6.231.625,98	6.148.833,47
450	Transport	389.014.004,63	257.476.146,92	365.804.150,07
620	Community Development	13.629.389,46	519.804,37	646.822,20
	<i>National Employment Service</i>	0	0	0
	Social Protection	580.277.633,93	8.695.905,35	10.157.181,22
010	Illness and Disability	113.008.095,80	0	0
040	Family and Children	246.257.687,39	72.156,31	160.901,05
070	Social Welfare for Most Vulnerable Groups	99.728.008,68	7.913.941,25	4.411.131,34
090	Social Welfare Unclassified Elsewhere	121.283.842,06	709.807,80	5.585.148,83
	<i>Pension and Disability Insurance Funds</i>	0	0	0
	Of employees	0	0	0
	Of agricultural producers	0	0	0
	Of the self-employed	0	0	0
	Health Care	56.547.832,36	4.503.287,51	54.002.221,24
760	Health Care Unclassified Elsewhere	56.547.832,36	4.503.287,51	54.002.221,24
	<i>Republic Health Insurance Institute</i>			
	Education	712.227.791,74	2.771.995,58	209.612.967,53
910	Preschool and Primary Education	353.724.277,94	287.853,25	66.394.078,84
920	Secondary Education	178.382.899,79	28.871,93	34.845.100,56
940	Higher and University Education	112.046.413,37	0	83.843.732,90
960	Additional Services to Education	59.364.368,32	0	20.822.622,69
980	Education unclassified elsewhere	8.709.832,32	2.455.270,40	3.707.432,53
	Environment	9.090.244,40	1.151.706,55	3.055.195,09
510	Waste Management	397.781,61	0	0
560	Environmental Protection unclassified elsewhere	8.692.462,79	1.151.706,55	3.055.195,09
	Total	2.151.168.451,35	289.577.749,46	654.225.929,26

Table 6.1.c.: Expenditures according to priority functions – Own incomes

		Own incomes of budgetary recipients (Currency USD)		
		2003	2004	2005
Function	Economy, Labor and Employment	86.776.332,70	187.459.456,21	182.455.349,96
410	General Economic and Commercial Affairs and Labor Affairs	128.947,21	0	707.964,60
420	Agriculture, Forestry, Fishing and Hunting	3.496.993,83	6.231.625,98	6.148.833,47
450	Transport	82.890.338,09	180.708.025,86	174.951.729,69
620	Community Development	260.053,57	519.804,37	646.822,20
	<i>National Employment Service</i>	0	0	0
	Social Protection	2.947.632,56	2.927.263,02	6.752.019,31
010	Illness and Disability	0	0	0
040	Family and Children	0	72.156,31	160.901,05
070	Social Protection for Most Vulnerable Groups	1.232.225,80	2.145.298,91	1.005.969,43
090	Social Protection Unclassified Elsewhere	1.715.406,75	709.807,80	5.585.148,83
	<i>Pension and Disability Insurance Funds</i>	0	0	0
	Of employees	0	0	0
	Of agricultural producers	0	0	0
	Of the self-employed	0	0	0
	Health Care	1.851.124,07	2.573.673,47	1.541.230,49
760	Health Care Unclassified Elsewhere	1.851.124,07	2.573.673,47	1.541.230,49
	<i>Republic Health Insurance Institute</i>	0	0	0
	Education	0	0	102.410.876,91
910	Preschool and Primary Education	0	0	6.518.938,05
920	Secondary Education	0	0	7.125.374,09
940	Higher and University Education	0	0	71.137.827,84
960	Additional Services to Education	0	0	17.604.601,77
980	Education unclassified elsewhere	0	0	24.135,16
	Environment	0	1.097.619,55	314.457,32
510	Waste Management	0	0	0
560	Environmental Protection unclassified elsewhere	0	1.097.619,55	314.457,32
	Total	91.575.089,33	194.058.012,26	293.473.933,99

Table 6.1.d.: Expenditures according to priority functions - **Donations**

		Donation resources (Currency USD)		
		2003	2004	2005
Function	Economy, Labor and Employment	22.176.311,52	7.829.138,68	4.090.593,84
410	General Economic and Commercial Affairs and Labor Affairs	22.176.311,52	7.720.564,82	4.090.593,84
420	Agriculture, Forestry, Fishing and Hunting	0	0	0
450	Transport	0	108.573,86	0
620	Community Development	0	0	0
	<i>National Employment Service</i>	0	0	0
	Social Protection	7.012,13	5.768.642,33	3.405.161,91
010	Illness and Disability	0	0	0
040	Family and Children	0	0	0
070	Social Protection for Most Vulnerable Groups	7.012,13	5.768.642,33	3.405.161,91
090	Social Protection Unclassified Elsewhere	0	0	0
	<i>Pension and Disability Insurance Funds</i>	0	0	0
	Of employees	0	0	0
	Of agricultural producers	0	0	
	Of the self-employed	0	0	0
	Health Care	0	1.068.287,79	356.002,82
760	Health Care Unclassified Elsewhere	0	1.068.287,79	356.002,82
	<i>Republic Health Insurance Institute</i>	0	0	0
	Education	0	1.224.296,02	99.028.237,04
910	Preschool and Primary Education	0	0	57.776.991,15
920	Secondary Education	0	0	27.381.834,27
940	Higher and University Education	0	0	12.554.384,55
960	Additional Services to Education	0	0	0
980	Education unclassified elsewhere	0	1.224.296,02	1.315.027,06
	Environment	0	54.087,00	2.740.737,77
510	Waste Management	0	0	0
560	Environmental Protection unclassified elsewhere	0	54.087,00	2.740.737,77
	Total	22.183.323,65	15.944.451,83	109.620.733,38

Table 6.1.e.: Expenditures according to priority functions - **Borrowing**

		Domestic and foreign borrowing (Currency USD)		
		2003	2004	2005
Function	Economy, Labor and Employment	684.072.304,70	77.166.259,57	190.852.420,38
410	General Economic and Commercial Affairs and Labor Affairs	233.409.045,47	506.712,37	0
420	Agriculture, Forestry, Fishing and Hunting	131.170.256,80	0	0
450	Transport	306.123.666,54	76.659.547,20	190.852.420,38
620	Community Development	13.369.335,89	0	0
	<i>National Employment Service</i>	0	0	0
	Social Protection	577.322.989,25	0	0
010	Illness and Disability	113.008.095,80	0	0
040	Family and Children	246.257.687,39	0	0
070	Social Welfare for Most Vulnerable Groups	98.488.770,75	0	0
090	Social Welfare Unclassified Elsewhere	119.568.435,30	0	0
	<i>Pension and Disability Insurance Funds</i>	0	0	0
	Of employees	0	0	0
	Of agricultural producers	0	0	0
	Of the self-employed	0	0	0
	Health Care	54.696.708,29	861.326,25	52.104.987,93
760	Health Care Unclassified Elsewhere	54.696.708,29	861.326,25	52.104.987,93
	<i>Republic Health Insurance Institute</i>	0	0	0
	Education	712.227.791,74	1.547.699,56	8.173.853,58
910	Preschool and Primary Education	353.724.277,94	287.853,25	2.098.149,64
920	Secondary Education	178.382.899,79	28.871,93	337.892,20
940	Higher and University Education	112.046.413,37	0	151.520,51
960	Additional Services to Education	59.364.368,32	0	3.218.020,92
980	Education unclassified elsewhere	8.709.832,32	1.230.974,38	2.368.270,31
	Environment	9.090.244,40	0	0
510	Waste Management	397.781,61	0	0
560	Environmental Protection unclassified elsewhere	8.692.462,79	0	0
	Total	2.037.410.038,37	79.575.285,38	251.131.261,89

6.2 ANALYSIS OF THE STATUS OF PRS RELATED LAWS⁹²

Table 6.2.a.: Adopted laws, envisaged by the Poverty Reduction Strategy in Serbia

Law	Relevant Ministry	Date of enforcement
Law on Mandatory Social Insurance Contributions (PRS envisages the Law on Mandatory Social Insurance Contribution Bases and Rates)	Ministry of Finance	Official Gazette of the Republic of Serbia No. 84/04 and 61/05
Law on Free Access to Public Information	Ministry of Culture	Official Gazette of the Republic of Serbia No. 120/04
Law on Drugs and Medical Items	Ministry of Health	Official Gazette of the Republic of Serbia No. 84/04
Bankruptcy Law	Ministry of Economy	Official Gazette of the Republic of Serbia No. 84/04
Law on Registration of Commercial Entities	Serbian Agency for the Development of Small and Medium Sized Enterprises and Entrepreneurship	Official Gazette of the Republic of Serbia No. 55/04 and 61/05
Law on Value Added Tax	Ministry of Finance	Official Gazette of the Republic of Serbia No. 84/04, 86/04 and 61/05
Law on Tourism	Ministry of Trade, Tourism and Services	Official Gazette of the Republic of Serbia No. 45/05
Law on Energy	Ministry of Mining and Energy	Official Gazette of the Republic of Serbia No. 84/04
Law on National Housing Credit Corporation	Ministry of Finance	Official Gazette of the Republic of Serbia No. 55/04
Law on Business and Entrepreneurship Registration	Ministry of Economy	Official Gazette of the Republic of Serbia No. 55/04
Law on Electronic Signature (envisaged as the Law on Electronic Business Transactions and Digital Signature + bylaws)	Ministry of Science and Environmental Protection	Official Gazette of the Republic of Serbia No. 135/04
Law on the Amendments to the Law on the National Bank of Serbia	Ministry of Finance	Official Gazette of the Republic of Serbia No. 55/04
Law on the Republic of Serbia's Budget for 2004	Ministry of Finance	Official Gazette of the Republic of Serbia No. 33/04 and 115/04
Law on the Level of Funding and the Shares in Payroll Tax and Sales Tax by Municipalities and Towns and the City of Belgrade for 2004	Ministry of Finance	Official Gazette of the Republic of Serbia No. 33/04
Law on Insurance	Ministry of Finance	Official Gazette of the Republic of Serbia No. 55/04, 70/04 and 61/05
Law on the Amendments and Additions to the Law on Payment System	Ministry of Finance	Official Gazette of the Republic of Serbia No. 43/04
Law on the Amendments and Additions to the Law on Excise	Ministry of Finance	Official Gazette of the Republic of Serbia No. 43/04, 55/04, 135/04 and 46/05
Law on the Amendments and Additions to the Law on the Rights of Veterans, Military Invalids, Civilian War Victims and their Survivors	Ministry of Labor, Employment and Social Affairs	Official Gazette of the Republic of Serbia No. 137/04

⁹² The Annex was prepared in cooperation with the Parliamentary Committee for Poverty Reduction

Law on the Amendments to the Law on Publications (PRSp envisages the Law on Publishing)	Ministry of Culture	Official Gazette of the Republic of Serbia No. 135/04
Law on the Prevention of the Conflict of Interest in Performance of Public Functions	Ministry of Finance and Economy was envisaged in PRSp	Official Gazette of the Republic of Serbia No. 43/04
Law on Forest Trees Reproductive Material	Ministry of Science and Environmental Protection	Official Gazette of the Republic of Serbia No. 135/04 and 8/05
Law on the Amendments to the Law on Health Insurance	Ministry of Health	Official Gazette of the Republic of Serbia No. 45/05
Law on Postal Services	Ministry of Capital Investment	Official Gazette of the Republic of Serbia No. 18/05
Serbian Investment and Export Promotion Agency of the Republic of Serbia was founded by the Law on Ministries as a separate organization (PRS envisages the Law on Serbian Investment and Export Promotion Agency-SIEPA)	Ministry of International Economic Relations	Official Gazette of the Republic of Serbia No. 84/04
Law on the Annulment of the Law on the Foundation of Public Air Transport Company	Ministry of Capital Investment	Official Gazette of the Republic of Serbia No. 18/05
Law on Rail	Ministry of Capital Investment	Official Gazette of the Republic of Serbia No. 18/05
Family Law	Ministry of Labor, Employment and Social Affairs	Official Gazette of the Republic of Serbia No. 18/05
Law on Economic Societies		Official Gazette of the Republic of Serbia No. 125/04
Law on the Amendments to the Law on Social Protection and Provision of Citizens' Social Security	Ministry of Labor, Employment and Social Affairs	Official Gazette of the Republic of Serbia No. 84/04
Law on Prices	Ministry of Trade, Tourism and Services	Official Gazette of the Republic of Serbia No. 79/05
Law on Tertiary Education	Ministry of Education and Sport	Official Gazette of the Republic of Serbia No. 76/05
Law on Consumer Protection	Ministry of Trade, Tourism and Services	Official Gazette of the Republic of Serbia No. 79/05
Law on Advertising	Ministry of Trade, Tourism and Services	Official Gazette of the Republic of Serbia No. 79/05
Law on Bank Rehabilitation Agency	Ministry of Finance	Official Gazette No. 61/05
Law on Bankruptcy and Liquidation of Banks and Insurance Societies	Ministry of Finance	Official Gazette No. 61/05
Law on the Amendments and Additions to the Law on Banks and Other Financial Institutions	Ministry of Finance	Official Gazette No. 61/05
Law on Public Debt	Ministry of Finance	Official Gazette No. 61/05
Law on Amendments and Additions to the Law on Passenger Road Transfer		Official Gazette of the Republic of Serbia No. 61/05
Law on Amendments and Additions to the Law on Pledge on Registered Movables		Official Gazette of the Republic of Serbia No. 61/05
Law on the Protection of Competition (Antimonopoly Law)	Ministry of Trade, Tourism and Services	Official Gazette of the Republic of Serbia No. 79/05

Law on Amendments and Additions on the Law on Financial Leasing	National Bank of Serbia	Official Gazette of the Republic of Serbia No. 61/05
Law on the Strategic Environmental Impact Assessment	Ministry of Science and Environmental Protection	Official Gazette of the Republic of Serbia No. 135/04
Law on Reporting and Keeping Record of Confiscated Property (PRS envisages the Law on Confiscated Land and Restitution and Compensation)	Ministry of Finance	Official Gazette of the Republic of Serbia No.45/05
Law on Political Parties Financing	Ministry of Finance	Official Gazette of the Republic of Serbia No. 72/03
Local Self-Governance Infrastructure Development Agency was established as a separate organization in the Law on Ministries (PRS envisages the Law on Local Self-Governance Infrastructure Development Agency)		Official Gazette of the Republic of Serbia No.19/04 and 84/04
Law on Public Administration	Republic Secretariat for Legislation	Official Gazette of the Republic of Serbia No. 79/05
Law on Civil Servants	Republic Secretariat for Legislation	Official Gazette of the Republic of Serbia No. 79/05
Law on Ombudsman	Ministry of Public Administration and Local Self-Government	Official Gazette of the Republic of Serbia No. 79/05

Table 6.2.b.: PRS related draft laws that are in the Parliamentary procedure

Law	Relevant Ministry	Date of the beginning of the Parliament procedure
Law on Health and Safety Regulations at Work	Ministry of Labor, Employment and Social Affairs	Draft Law in the Parliament procedure since December 24, 2004
Law on Health Protection	Ministry of Health	Draft Law in the Parliament procedure since May 20, 2005 (adoption envisaged for the second half 2003)
Law on Public Skiing Venues	Ministry of Trade, Tourism and Services	Draft Law in the Parliament procedure since January 11, 2005 (adoption envisaged for the middle of 2003)
Law on Roads	Ministry of Transport and Telecommunication	Draft Law in the Parliament procedure since February 18, 2005 (adoption envisaged for the middle of 2003)
Anti Money Laundering Law	Ministry of Finance	Draft Law in the Parliament procedure since November 29, 2004 (adoption envisaged for September 2003)
Law on Amendments and Additions to the Customs Law	Ministry of Finance	Draft Law in the Parliament procedure since June 2, 2005
Law on Prevention of Doping in Sport	Ministry of Education and Sport	Draft Law in the Parliament procedure since November 19, 2005
Law on the Amendments and Additions to the Law on Artistic and Other Activities in the Area of Culture	Ministry of Culture	Draft Law in the Parliament procedure since March, 24, 2005 (Draft Law was submitted to the Parliament on November 15, 2002)
Law on the Amendments to the Law on Misdemeanour Penalties	Ministry of Justice	Draft Law in the Parliament procedure since January 31, 2005 (planned for the second half of 2003)

Draft Law on Amendments and Additions to the Law on the Registration of Commercial Entities		Draft Law in the Parliament procedure since February 16, 2005
Draft Law on Medial Workers' Chambers		Draft Law in the Parliament procedure since May 20, 2005
Draft Law on Substances that are used in Illegal Production of Narcotics and Psychotropic Substances		Draft Law in the Parliament procedure since May 20, 2005
Law on Goods and Services Market Inspection	Ministry of Trade, Tourism and Services	Draft Law in the Parliament procedure since July 22, 2005
Law on Veterinary Medicine	Ministry of Agriculture, Forestry and Water Management	Draft Law in the Parliament procedure since July 22, 2005
Law on the Amendments and Additions to the Law on Employment and Unemployment Insurance	Ministry of Labor, Employment and Social Affairs	Draft Law in the Parliament procedure since July 22, 2005

Table 6.2.c.: Laws envisaged by the PRS that are in the preparation process

Law	Relevant ministry	Law status
Law on Foreign Trade	Ministry of International Economic Relations	In the preparation phase
Law on Special Anticorruption Institution	Ministry of Justice (instead of the envisaged Ministry of Finance and Economy)	In the preparation phase
Law on Trade	Ministry of Trade, Tourism and Services	On a public debate (planned for the end of 2003)
Law on Sports	Ministry of Education and Sport	Draft has been prepared
Law on Waste Management	Ministry of Science and Environmental Protection	Draft has been prepared
Law on Professional Associations (Chambers)	Ministry of Health	In the preparation phase
Law on Protection against Non-Ionic Radiation	Ministry of Science and Environmental Protection	In the preparation phase
Law on Fisheries	Ministry of Science and Environmental Protection	Draft has been prepared
Geology Law	Ministry of Science and Environmental Protection	In the preparation phase
Law on Preprimary Education	Ministry of Education and Sport	In the preparation phase (envisaged for mid 2003)
Law on Student Associations	Ministry of Education and Sport	In the preparation phase (envisaged for mid 2003)
Law on Voluntary Pension and Disability Insurance	Ministry of Social Affairs	In the preparation phase (adoption envisaged until the end of 2003)

Table 6.2.d.: Other laws envisaged by the PRS

Law	Relevant ministry	Envisaged adoption period
Law on Administrative Proceedings	Ministry of Public Administration and Local Self-Government	
Law on Administrative Procedure	Ministry of Public Administration and Local Self-Government	
Law on Citizen Associations	Ministry of Public Administration and Local Self-Government	
Law on Public Defence		
Law on Judicial Budget		
Law on Non-Governmental Organizations		Draft Law has been prepared. On a public debate.
Law on Conditions for Employing a Foreign Citizen		
Law on Trade Societies		
Law on Contributions		
Law on Underdeveloped Regions		
Law on Resources for Stimulating the Development of Underdeveloped Regions		
Law on Gender Equality		In Parliamentary procedure in September 2005
Anti Discrimination Law		On a public debate
Law on Mortgage	Ministry of International Economic Relations	Adoption envisaged by the end of 2003
Law on Passenger Road Transport	Ministry of Transport and Telecommunications	Adoption envisaged by the end of 2003
Law on International Trade Arbitration	Ministry of International Economic Relations	Adoption envisaged by the end of 2003
Law on Transport and Road Safety	Ministry of Transport and Telecommunications	Adoption envisaged by the end of 2003
Law on Cargo Road Transport	Ministry of Transport and Telecommunications	Adoption envisaged by the end of 2003
Law on Hazardous Substances Transport	Ministry of Transport and Telecommunications	Adoption envisaged by the end of 2003
Law on Internal Navigation	Ministry of Transport and Telecommunications	Adoption envisaged by the end of 2003
Law on Physical and Technical Security	Ministry of Internal Affairs	Adoption envisaged by the end of 2003 (in the Parliament procedure)
Law on Amendments and Additions to the Law on Mining	Ministry of Mining and Energy	Adoption envisaged by the end of 2003
Law on Sanitary Inspection	Ministry of Health	
Law on the RS Aviation	Ministry of Transport and Telecommunications	Preparation being finalized during September 2003
Law on Agriculture	Ministry of Agriculture, Forestry and Water Management	
Law on Amendments and Additions to the Law on Primary Education	Ministry of Education and Sport	

Law on Amendments and Additions to the Law on Secondary Education	Ministry of Education and Sport	
Law on Privatization in Sport Industry	Ministry of Education and Sport	Adoption envisaged by the end of 2003
Law on Police	Ministry of Internal Affairs	Being prepared during 2003
Law on Police Education Institutions	Ministry of Internal Affairs	Preparation being finalized during September 2003
Law on Social Protection System	Ministry for the Protection of Natural Resources and Environment	Government of the Republic of Serbia adopted the Draft Law on May 15, 2002
Law on Academic Research	Ministry of Science, Technology and Development	Adoption envisaged by the end of 2003
Law on Innovation System	Ministry of Science, Technology and Development	Adoption envisaged by the end of 2003
Law on Amendments and Additions to the Law on Foreign Currency Transactions	Ministry of Finance and Economy	Proposal submitted to the Parliament in September 2003
Law on Biomedical Artificial Insemination	Ministry of Health	Draft Law submitted to the Government of the Republic of Serbia at the end of 2003
Law on Harvesting and Transplantation of Human Organs	Ministry of Health	Draft Law submitted to the Government of the Republic of Serbia at the end of 2003
Law on Health Safety of Food Products and General Goods	Ministry of Health	
Law on Records, Development and Maintenance of Memorial Cities and Serbian Veteran Cemeteries in the Country and Abroad and Foreign Soldiers Cemeteries in the Territory of the Republic of Serbia	Ministry of Labour, Employment and Social Affairs	
Law on the Protection of the Family Members of the Military Service Conscripts	Ministry of Labour, Employment and Social Affairs	
Law on Cultural Heritage	Ministry of Culture and Public Information	Draft Law developed during 2003
Law on Cinematography/ Law on Cinematography Fund	Ministry of Culture and Public Information	Adoption envisaged by the end of 2003
Law on Libraries	Ministry of Culture and Public Information	
Law on Inspection Supervision and Administrative Inspection	Ministry of Public Administration and Local Self-Government	
Law on Spas	Ministry of Trade, Tourism and Services	Adoption envisaged by the end of 2003
Law on Amendments and Additions to the Law on Terms and Conditions of Approving Rights and Restituting Land Transferred in Social Ownership on the Basis of Agricultural Land Fund and Confiscated on the Basis of Unfulfilled Obligations of Mandatory Buyout of Agricultural Production	Ministry of Finance and Economy	Draft Law developed during 2003
Law on Agency for Rural Development	Ministry of Agriculture, Forestry and Water Management	
Law on Agency for Serbian Academic Computer Network	Ministry of Science, Technology and Development	Adoption envisaged by the end of 2003

Law on Rehabilitation of Political Convicts and Prisoners	Ministry of Justice	Adoption envisaged by the end of 2003
Law on Terms and Conditions for Performance of Court Expertise	Ministry of Justice	Adoption envisaged by the end of 2003
Law on Narcotic Precursors	Ministry of Health	Adoption envisaged by the end of 2003
Law on the Production and Trading of Narcotics	Ministry of Health	Adoption envisaged by the end of 2003

Table 6.2.e.: Laws that are not envisaged by the PRS, but have been recognized by the line ministries of the Republic of Serbia as relevant for the PRS

Law	Relevant Ministry	Status of the Law
Law on Environmental Protection	Ministry of Science and Environmental Protection	Official Gazette of the Republic of Serbia No. 135/04
Law on the Strategic Environmental Impact Assessment	Ministry of Science and Environmental Protection	Official Gazette of the Republic of Serbia No. 135/04
Law on Integrated Pollution, Prevention and Control	Ministry of Science and Environmental Protection	Official Gazette of the Republic of Serbia No. 135/04
Law on Amendments to the Law on Local Self-Government		Official Gazette of the Republic of Serbia No. 33/04
Law on the Amendments and Additions to the Law on Local Self-Government		Official Gazette of the Republic of Serbia No. 135/04
Law on Amendments and Additions to the Law on Public Income and Expenditures		Official Gazette of the Republic of Serbia No. 33/04
Law on Regulating Duties of the Republic of Serbia regarding the Borrowings for Economic Development		Official Gazette of the Republic of Serbia No. 43/04
Law on Amendments and Additions to the Law on Guarantee Fund		Official Gazette of the Republic of Serbia No. 43/04 and 61/05
Law on Amendments to the Law on Taxes for Using, Keeping and Carrying Goods		Official Gazette of the Republic of Serbia No. 43/04 and 132/04
Law on Addition to the Law on Securities and Other Financial Instruments Markets		Official Gazette of the Republic of Serbia No. 55/04 and 45/05
Law on Amendments and Additions to the Law on Public Procurement		Official Gazette of the Republic of Serbia No. 55/04
Law on Amendments and Additions to the Law on Tax Procedure and Tax Administration		Official Gazette of the Republic of Serbia No. 55/04 and 61/05
Law on the Serbian Business Registration Agency		Official Gazette of the Republic of Serbia No. 55/04
Law on Amendments and Additions to the Law on Sales Tax		Official Gazette of the Republic of Serbia No. 84/04
Law on Amendments and Additions to the Law on Corporate Income Tax		Official Gazette of the Republic of Serbia No. 84/04
Law on Games of Chance		Official Gazette of the Republic of Serbia No. 84/04
Law on Amendments and Additions to the Law on		Official Gazette of the Republic of Serbia No. 42/02 и 97/04

Broadcasting		
Law on Mediation in Labour - Related Disputes	Ministry of Labor, Employment and Social Affairs	Official Gazette of the Republic of Serbia No. 125/04
Law on the Budget of the Republic of Serbia for 2005		Official Gazette of the Republic of Serbia No. 127/04
Law on the Citizenship of the Republic of Serbia		Official Gazette of the Republic of Serbia No. 135/04
Law on Amendments and Additions to the Law on Income Tax		Official Gazette of the Republic of Serbia No. 135/04
Law on Amendments and Additions to the Law on Property Tax		Official Gazette of the Republic of Serbia No. 135/04
Law on Fiscal Cash Registers		Official Gazette of the Republic of Serbia No. 135/04
Law on Fulfilling the Duties of the Republic of Serbia towards the National Bank		Official Gazette of the Republic of Serbia No. 135/04
Law on Non-life Insurance Premium Tax		Official Gazette of the Republic of Serbia No. 135/04
Law on the Distribution of Transfer Resources from the Budget of the RS and the Share of Towns and the City of Belgrade in the Payroll Tax in 2005		Official Gazette of the Republic of Serbia No. 135/04
Law on Amendments to the Law on the Privatization Agency		Official Gazette of the Republic of Serbia No. 135/04
Framework Law on Education System		Official Gazette of the Republic of Serbia No. 62/03
Law on Amendments and Additions to the Framework Law on Education System		Official Gazette of the Republic of Serbia No. 58/04
Law on Amendments and Additions to the Law on Criminal Procedure	Ministry of Justice	Official Gazette of the Republic of Serbia No. 58/04
Law on Civil Proceedings	Ministry of Justice	Official Gazette of the Republic of Serbia No. 125/04
Law on Extra-Judicial Proceeding		Official Gazette of the Republic of Serbia No. 18/05
Law on Mediation	Ministry of Justice	Official Gazette of the Republic of Serbia No. 18/05
Law on Executive Procedure	Ministry of Justice	Official Gazette of the Republic of Serbia No. 125/04
Law on Agency for Licencing of Bankruptcy Trustees	Ministry of Justice	Official Gazette of the Republic of Serbia No. 84/04
Law on Prosecutor's Office	Ministry of Justice	Official Gazette of the Republic of Serbia No. 51/04
Court Organisation Bill	Ministry of Justice	Official Gazette of the Republic of Serbia No. 29/04
Law on Public Agencies	Serbian Agency for the Development of Small and Medium Sized Enterprises and Entrepreneurship	Official Gazette of the Republic of Serbia No. 18/05
Law on Amendments and Additions to the Law on Financial Transactions Tax	Ministry of Finance	Official Gazette of the Republic of Serbia No. 43/04
Law on the Cessation of the Law on Income Fund Tax	Ministry of Finance	Official Gazette of the Republic of Serbia No. 33/04

Law on the Amendments to the Law on the Action Plan of Serbia and Montenegro for the Harmonization of Economic Systems of Member States in order to Prevent and Remove Obstacles to Unimpeded Flow of People, Merchandise, Services and Capital	Ministry of International Economic Relations	Official Gazette of the Republic of Serbia No. 18/05
Law on Amendments and Additions to the Law on Privatization	Privatization Agency	Official Gazette of the Republic of Serbia No. 45/05
Labour Law	Ministry of Labor, Employment and Social Affairs	Official Gazette of the Republic of Serbia No. 24/05 and 61/05
Law on Socio-Economic Council	Ministry of Labor, Employment and Social Affairs	Official Gazette of the Republic of Serbia No. 125/04
Competitiveness Law	Ministry of International Economic Relations	Law Proposal in the Parliamentary procedure since May 30, 2005
Law on Red Cross	Ministry of Health	Law Proposal in the Parliamentary procedure since May 6, 2005
Law on Precursors	Ministry of Health	Law Proposal prepared
Law on Insufficiently Developed Regions	Republic Development Bureau	Draft prepared
Law on Protection against Non-ionic Radiation and Nuclear Safety	Ministry of Science and Environmental Protection	Draft prepared
Law on Chemicals	Ministry of Science and Environmental Protection	Draft prepared
Law on Legal Assistance	Ministry of Justice	In the preparation phase
Law on Public Notaries	Ministry of Justice	In the Parliament procedure
Social Residence Law	Ministry of Capital Investment	In the preparation phase
Law on Amendments and Additions to the Planning and Constructing Law	Ministry of Capital Investment	In the preparation phase
Arbitration Law	Ministry of International Economic Relations	In the preparation phase
Law on Industrial Parks	Ministry of International Economic Relations	In the preparation phase
Law on Even Regional Development	Republic Development Bureau	In the preparation phase
Refugees Law	Comissariat for Refugees of the Republic of Serbia	In the preparation phase
Strike Law	Ministry of Labor, Employment and Social Affairs	In the preparation phase
Law on the Protection of Citizens of the Republic of Serbia Working Abroad	Ministry of Labor, Employment and Social Affairs	In the preparation phase
Law on Employing Disabled Persons	Ministry of Labor, Employment and Social Affairs	In the preparation phase
Law on Record Keeping within the Field of Labor and Employment	Ministry of Labor, Employment and Social Affairs	In the preparation phase
Antidiscrimination Law against Disabled Persons	Ministry of Labor, Employment and Social Affairs	In the preparation phase

Law on Package and Package Waste Material	Ministry of Science and Environmental Protection	In the preparation phase
Law on Nature Protection	Ministry of Science and Environmental Protection	In the preparation phase
Law on Air Protection	Ministry of Science and Environmental Protection	In the preparation phase
Law on Schoolbooks and Other Teaching Equipment and Methodology	Ministry of Education and Sport	In the preparation phase
Law on Pupil and Student Standard	Ministry of Education and Sport	In the preparation phase
Law on Financing Water Management	Ministry of Agriculture, Forestry and Water Management	In the preparation phase
Standardization Law	Ministry of Trade, Tourism and Services	
Law on Unions and Employers Society	Ministry of Labor, Employment and Social Affairs	In the preparation phase

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Government of the Republic of Montenegro
Ministry of Labor and Social Welfare



Poverty Reduction Strategy Paper
Strategija razvoja i redukcije siromaštva
Montenegro / Crna Gora

The First Progress Report 2003 – 2004

Podgorica, July 2005.

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Introduction

The Government of the Republic of Montenegro adopted the Development and Poverty Reduction Strategy in November 2003. The preparatory work on Strategy development started in May 2002 when the Government of Montenegro adopted the Interim Poverty Reduction Strategy in July 2002. Apart from the government officials, a wide range of stakeholders took part into the drafting process including NGOs, trade unions, academics, and donors. The Development and Poverty Reduction Strategy was adopted for the period 2003-2006.

In May 2002, the Government of the Republic of Montenegro adopted a strategic country development agenda called The Economic Reform Agenda in Montenegro 2002-2007. The Economic Reform Agenda and the Development and Poverty Reduction Strategy are completely complementary documents.

A strong emphasis in the Economic Reform Agenda is given to economic reform, based on sustainable macroeconomic stability and rapid growth of private sector, while in the Development and Poverty Reduction Strategy development of the country is parallel with poverty reduction. For that reason, the priorities set in the Economic Reform Agenda were taken into account during the preparation of the Strategy, while poverty reduction priorities were especially treated in the fields of social protection, health and education.

Work on the Development and Poverty Reduction Strategy has built the capacities of government institutions in charge for strategic planning. In addition, the partnership with NGO sector, which showed a great interest to participate in strategy drafting process, was developed. This partnership made a good framework for preparation of strategic documents, which in perspective should be prepared in the same way and thus reflect the priority of the whole society.

Donors also took part in preparation of the Strategy. Support for preparatory process itself was obtained by WB, DFID and UNDP. The implementation of the Strategy will be supported by the share of domestic resources, but also it will be necessary to provide international assistance. The Board of the World Bank and International Monetary Fund discussed the Development and Poverty Reduction Strategy and it was assessed as a good basis for encouraging economic growth and poverty reduction in Montenegro.

In November 2003 the Development and Poverty Reduction Strategy was presented to the Donor Conference in Bruxelles, where international donors promised to provide a part of the funds for implementation of the Development and Poverty Reduction Strategy in Montenegro.

Regional experiences played an important role in the drafting process. Considering that Montenegro tends to EU membership, special emphasis was put on regional development and so as to priority actions for rapid integration into European Union.

I CHAPTER: LIVING STANDARDS AND POVERTY IN MONTENEGRO

1.1 Living Standards and Poverty in Montenegro in 2004

The Poverty Assessment for Montenegro was produced in 2003 and used data from two rounds of 2002 ISSP¹ household surveys. Together with this source, a focused survey of the poorest strata conducted by ISSP in 2003 (with UNDP support) was used to produce poverty diagnostics for PRSP.²

The newest and the latest data on poverty in Montenegro can be obtained from the 2004 ISSP survey supported by the World Bank. ISSP 2004 survey was implemented in April, only four months after the start of the implementation of PRSP. There is no way how changes induced by PRSP could be reflected in that data set.

The 2004 ISSP survey confirmed and validated the poverty diagnostics on which PRSP is based. It proved that all major diagnostics on which the PRSP action plan is based are correct:

- Absolute poverty in Montenegro affects a relatively small percentage of the population (between 8.4 and 13.6 percent), with the poor concentrated in Center and North and in rural areas;
- There are some groups which are extremely poor and socially excluded, for these groups poverty is severe and multi-dimensional, spanning housing, access to and quality of education, and health (Roma, IDPs, some rural poor);
- A significant fraction of the population is vulnerable to poverty, regardless of how many people are poor in a given period of time, many more are subject to shocks that will make them poor. One source of such shocks and uncertainty are unreformed systems of public service provision.

Poverty reduction strategy targets these various facets of poverty:

- Focuses on economic growth through private sector development to reduce the number of people close to poverty line (vulnerable to poverty);
- Reforms of the social sectors to provide safety nets for the poor, vulnerable and at the same time reduce risks coming from poorly functioning infrastructure, health and education;
- Addresses pockets of severe poverty and social exclusion of marginalized groups.

Comparing data from 2002, 2003 and 2004 surveys is difficult. However, one can nevertheless observe that poverty **remained stable in Montenegro** between 2002, 2003 and 2004. The lack of progress in reducing poverty is not surprising given that in the period 2002-2003:

- The economic growth remained anemic, about 2.5 percent per year. Such low rates of growth are shown to have minimum impact on poverty.³

¹ ISSP – The Institute for Strategic Studies and Prognosis, www.isspm.org

² Radevic D. and Beegle K. (2003) Living Standards and Poverty in Montenegro. Background paper for Serbia and Montenegro: Poverty Assessment. ISSP and The World Bank, June, 2003 and ISSP-UNDP (2003). Household Survey of Roma, Ashkaelia and Egyptians, Refugees and IDPs in Montenegro. Podgorica, 2003.

³ Alam A., Murthi M., Yemtsov R et al. Growth, Poverty and Inequality in Eastern Europe and the Former Soviet Union. World Bank, 2005. Available for download: www.worldbank.org/eca/ecapovertyreport.

- Prior to the adoption of PRSP the Government policies were not intentionally pro-poor and were not targeted to the poor.

The new ISSP data containing panel component (same household re-interviewed in 2002-03 and 2004 surveys) revealed that **chronic and extreme poverty outside the group of socially excluded** (such as Roma and IDPs) is **minimal** with only a negligible share (about one percent) of non-Roma and non-IDP household staying chronically poor between 2002 and 2004. **Economic vulnerability, i.e. elevated risk to become poor, on the other hand**, is by far the largest social problem, and affects about one third of the population. Vulnerability to poverty, especially among farmers and families outside the regular employment remained large throughout this period.

1.2 How many poor?

In the period between two households' data collection⁴, **no changes are reflected in the overall poverty figures**. Between 8.4 and 13.6 percent (with best approximation of 10.9%) of the population live in absolute material poverty. Poverty pockets exist among subpopulations like Roma (48%) and recipients of social assistance (39.3%). It is confirmed that one third of the population can be classified as economically vulnerable, living below 150% of the poverty threshold. Thus, vulnerability to poverty, especially among farmers and families outside the regular employment remains significant.

Chronic and extreme poverty outside the group of socially excluded is minimal with negligible share (about one percent) of non-Roma and non-IDP household staying chronically poor between 2002 and 2004.

Stability of poverty is due to limited changes in the employment situation, concentration of gains among those already employed, and to the increased gap between those with jobs and those without. As expected, employment status is associated with poverty risk. However, poverty profile by employment status has not changed, suggesting that households headed by those who are non-working, non-retired have the highest risk of poverty, while having a household head employed is associated with lower poverty. The position of pensioners remained stable (poverty risk around average).

Social protection net (including pensions) is wide but analysis shows that **poor are not well covered** (only 20 percent of the poor receive targeted benefits).

Regional differences remain large and are changing, despite overall stability of poverty. North continues to have higher poverty rate, although it has somewhat receded by 2004. South, initially the richest region, has benefited most from the economic growth with poverty falling to almost zero by 2004.

Inequality, as measured by Gini index for consumption per capita is estimated at 0.28, suggesting that overall the distribution has hardly changed compared to 2002 or 2003. But as reflected is the

⁴ July 2003 when Household Survey of Roma, Ashkaelia and Egyptians, Refugees and Internally Displaced Persons was undertaken, and May 2004 when last survey round occurred.

poverty gap and poverty severity the gap between the poor and the rest of the population did not change, reflecting negative distributional changes for the poor.

1.3 Material Poverty in Montenegro

As a multidimensional concept encompassing various aspects of well-being, poverty in practice cannot be explained with single indicator that captures all of its dimensions. Material well-being is measured based on the consumption poverty, while additional indicators are calculated using the best practice in explaining living standards of a population. The consumption indicator is compared to a poverty threshold which is a minimum living standards (in Euros) calculated based on the actual consumption patterns and minimum caloric needs, applying methodologies based on international best-practices, making the results internationally comparable. This analysis is not fully comparable to so far existed since differences in preparing and conducting the survey influence the results. However, it offers an updated poverty profile and the most detailed set of both material and non-material living standard indicators.

Table 1 represents results as they are from various sources of data for the period 2002-2004.

Table 1: Poverty Rates in Montenegro

2002 data (rounds 5 and 6 of ISSP survey)*	
Poverty rate: Head Count	9.4 (7.5-11.3)
Poverty gap	1.3
Severity of Poverty	0.3
2003 ISSP household survey	
Poverty rate: Head Count	12.2* (6.8-17.6)
2004 ISSP household survey	
Poverty rate: Head Count	10.9 (8.4-13.6)
Poverty gap	2.1
Severity of Poverty	0.7

Source: Radevic and Beegle (2003) ISSP Household Survey 5 and 6, ISSP&UNDP report "Household Survey on RAE, refugees and internally displaced persons", 2003 for 2003 data and Staff estimates using 2004 data; 95% confidence intervals provided for poverty rates in brackets

* Note: 2002 data are not fully representative of the population for the reasons mentioned.

Despite difference across results and variants of methods used, all estimates show a remarkable consistency in terms of poverty profile, its statistical precision (lack of thereof) and its dynamics over time. They are also broadly consistent with the structure of poverty revealed by the Poverty Assessment.

One of the conclusions of the poverty assessment in Montenegro is that significant share of population is vulnerable to the smallest either positive or negative shocks. **Economic vulnerability** between 2003 and 2004 has been reduced marginally confirming that one third of the population is highly sensitive to what is going on in the economic scene of the country. However, vulnerability to

poverty, especially among farmers and families outside the regular employment remains significant.

Regarding other dimensions of poverty, it is important to assess the result of the **panel experiment** which consisted of tracing the evolution of living standards of 100 households from the 2002/03 surveys to 2004. It is important to note that since there was a bias in the pre-2004 ISSP survey samples towards the middle class, the panel will assess the dynamics of living standards for such group. Indeed, out of 100 households only one remained poor in both rounds, while 7 household which were poor in 2002 moved out of poverty, and 5 originally non-poor households fell in poverty. Thus, for the small panel sub group, there was some reduction in the overall poverty and clearly only a minimal risk of chronic poverty. But this sample is too small to allow for any precise assessment of the extent of vulnerability and chronic poverty as well as their profile.

Non-monetary poverty indicators are adding important flavor to the poverty picture in Montenegro, underlining significant employment poverty meaning that there are persons not working but ready to work if given a job opportunity.

Table 2: Multidimensional Poverty Indicators

Indicators	% of population	% of poor
<i>Consumption poverty</i>		
absolute poverty	10.9	
economically vulnerable	31.6	
<i>Education poverty</i>		
16-24 years: not in school and did not attend secondary school	13.8	39.6
<i>Health poverty</i>		
any illness/injury in last 30 days that precluded usual activities or disabled	5.7	9.0
<i>Employment poverty</i>		
ages 20-65: not working but ready to work if given a job opportunity	23.7	46.5
<i>Housing poverty</i>		
drinking source for dwelling is not piped water (ex: pump well) or dwelling has no bathroom*	18.3	22.8
Dwelling has less than 10m ² per person	22.6	57.3

1.4 Poverty and environment

The new 2004 ISSP survey found a striking link between poverty and environment. The survey found that staggering 51.3% of Montenegrin households are using fuel wood for heating, with clear consequences for the environment and their own health. Percentage of households using fuel wood is higher in rural areas (86.6) and northern part of the country (88.3%). Also, more households living in the environmentally hot spot areas (87.6%) and more Roma households (88.0%) are using fuel wood. As much as 85.7% of the poor rely on fuel wood for heating. Monitoring the use of fuel wood for heating will directly link poverty with the environment and will supplement the set of environment indicators proposed in the PRSP.

1.5 Poverty monitoring

This short summary of the joint analysis of data shows that critically important elements of poverty profile established using 2002-03 ISSP survey data are confirmed. But it also shows that there is a significant agenda to improve the poverty monitoring.

It is expected that PRSP monitoring system will switch to the HBS data as main monitoring tool as soon as they will become available.

As HBS survey data for 2005 will become available for the analysis in early 2006 **it will be necessary to carry out the comparative analysis of HBS and ISSP survey data** to calibrate poverty estimates. To complement gaps in HBS data it will also be needed to continue for some time ISSP surveys. In particular **it will be needed to carry out a panel element of the ISSP survey** that would allow measurement of chronic poverty and changes in the economic vulnerability. It will also serve as the best possible data source to evaluate the impact of reforms and specific programs on the poor and the population at large.

**II CHAPTER: GOALS AND IMPLEMENTATION OF THE
DEVELOPMENT AND POVERTY REDUCTION STRATEGY**

1.1 The objectives of the development and poverty reduction strategy (DPRS)

The Development and Poverty Reduction Strategy defined its main objectives. Disaggregation of the objectives in each sector was provided into the Action Plan for the DPRS implementation.

Table 1: Objectives of the Development and Poverty Reduction Strategy

	OBJECTIVES	STRATEGIC DIRECTIONS / ACTIVITIES	INDICATORS
1.	Create the conditions for self-sustainable and equitable economic growth, which will reduce the rate of the economically vulnerable population	<ul style="list-style-type: none"> ▪ Create a stable macro-economic environment for dynamic economic growth, while ensuring the private sector plays a crucial role. ▪ Harmonization of legislation and policy with the EU ▪ The promotion of Montenegrin potential, especially in areas where Montenegro holds a comparative advantage ▪ Pro-active policies in creating employment opportunities ▪ The protection of the environment and the sustainable management of resources. 	<ul style="list-style-type: none"> ▪ The GDP growth rate ▪ The employment growth rate ▪ The growth in exports ▪ A reduction in imports ▪ A growth in foreign direct investment ▪ Progress on SAP ▪ A reduction in the economically vulnerable population rate
2.	Ensure social stability and reduce the poverty rate	<ul style="list-style-type: none"> ▪ Improved targeting of social welfare measures especially those directed at children, older people and the disabled. ▪ Improved access to and quality of education ▪ Improved access to and quality of health services ▪ Improved quality of environmental protection ▪ Development of infrastructure in the function of poverty reduction ▪ Implementation of regional development policies for poverty reduction in least development and rural areas ▪ Implementation of activities for enabling the realization of the Strategy for repatriation of persons who wish to return to their former homes. ▪ Improved quality of social integration and poverty reduction of refugees, IDPs and 	<ul style="list-style-type: none"> ▪ A reduction in the poverty rate ▪ Improved multi-dimensional poverty indicators ▪ A reduction in regional development gaps ▪ The level of social integration of marginal groups.

		RAE, for those persons who wish to remain in Montenegro.	
		<ul style="list-style-type: none"> ▪ Achieving gender equality and human rights 	
3.	Define key poverty indicators, in line with the Millennium Development Goals (MDGs) and assess them through an integral system of monitoring and evaluation, during the DPRS implementation period.	<ul style="list-style-type: none"> ▪ Develop an integrated monitoring system ▪ The quality of change to be measured through key indicators, that is, through their gradual reduction, as the proposed measures are implemented. 	<ul style="list-style-type: none"> ▪ MDG indicators

Source: *Development and Poverty Reduction Strategy*

Apart from defining objectives, the Development and Poverty Reduction Strategy also defined basic indicators to measure the implementation performance.

Table 2: *Implementation performance indicators of the Development and Poverty Reduction Strategy*

	Indicator	Goal	2002	2006
1.	GDP/pc	Economic growth (GDP/pc growth)	1832	2379
2.	Share of public expenditure of GDP (Consolidated public expenditures)	Macro-management quality (Reduce the share of)	42.3%	40.7%
3.	Rate of debt return	Loan sustainability	4.8	4.5
4.	Unemployment rate	Reduce	30.4	19%
5.	Grey economy	Reduce	30%	11%
6.	Time needed to register a company	Reduce bureaucracy		
7.	Agriculture production growth rate	Strengthen domestic production and export growth, regional development (Increase rate)	6	8
8.	Population below the poverty line	Reduce percentage of population living below the poverty line	12.2	11.2
9.	Infant mortality rate	Reduce	14.7	Under 10
10	Maternal mortality rate	Eradicate	2 women	0.00
11	Percentage of the newborn under 2.5 kg	Introduce as an obligatory indicator, reduce		
12	Net enrolment ratio in primary school	100%	96.93%	100%
13	Coverage of organized preschool education	Increase	22%	30%

14	GDP per energy consumption unit (USD per kg of oil equivalent)	Increase	1.29	1.42
15	Part of population whose sewage is treated by processing plants before these are released in to natural receptors	Increase	11%	25%
16	Share of the private sector in GDP	Increase	(37% in 2001)	55%

These indicators are mostly harmonized with implementation performance indicators from the Economic Reform Agenda in Montenegro 2002–2007. The Emphasis was put on those indicators whose achievement would sustain macroeconomic stability through further fiscal deficit reduction along with stable economic growth rate. On the other side, there are indicators which point out whether economic growth is followed by an adequate allocation of newly obtained values and whether the growth contributes to poverty alleviation. These indicators are harmonized with commitment of Montenegro towards the achievement of the Millennium Development Goals.

1.2 Implementation of the Development and Poverty Reduction Strategy

Implementation of the Development and Poverty Reduction Strategy has started by the end of 2003. The Government of the Republic of Montenegro has appointed the Ministry of Labor and Social Welfare to be the coordinating ministry for monitoring realization of the Development and Poverty Reduction Strategy. Within this Ministry, Monitoring and Evaluation Unit is operating, which is in day-to-day contacts with government authorities, NGO sector, local community representatives, social partners, media and international development partners. Thus, this is the place where all information are collected and disseminated to stakeholders. This Unit is in charge of preparation of information regarding DPRS implementation, submission of concrete projects to donors, all in purpose of establishing high quality monitoring and evaluation system. The Unit also collects information on the status of projects realized within each sector. Thus, there is a close cooperation among line ministries in charge for realization of the concrete projects.

Inter-ministerial Steering Committee for monitoring implementation of the Development and Poverty Reduction is comprised of the following representatives from: Ministry of Labor and Social Welfare, Ministry of Education, Ministry of Health, Ministry of Finance, Ministry for International Economic Relations and European Integrations, Ministry of Agriculture, Forestry and Water Management, Ministry of Environment Protection and Urban Planning, Employment Agency, Secretariat for Development as well as experts – working group leaders who participated in the DPRS preparation, Parliament representatives, local community, NGO sector, social partners and media.

This body is in charge of monitoring project implementation, considering information made by Monitoring and Evaluation Unit prior to their submission to Government consideration and relevant international partners when necessary, as well as providing all needed suggestions aiming at high quality implementation.

In each line ministry there is a contact – the so-called *focal point*, to monitor realization of the DPRS projects in respective ministry and provide information to DPRS Monitoring Unit. By the end of 2004, Inter-ministerial Steering Committee for monitoring implementation of the Development and Poverty Reduction Strategy made a conclusion in purpose of more quality monitoring: that each ministry involved in implementation of the Development and Poverty Reduction Strategy should form a monitoring unit to follow realization and collect information on development documents (Development and Poverty Reduction Strategy, Economic Reform Agenda, Stabilization and Association Process for EU integration), whose realization is a part of the competence of respective ministry.

Monitoring of the achieved results and evaluation of the realized projects will be carried out in permanent cooperation with Central bank, MONSTAT, Institute for Strategic Studies and Prognosis, Economic and Social Council and so as with all other relevant institutions and organizations capable of providing quality and verified data.

Thus, monitoring of poverty over the poverty rate remains a great challenge for Montenegro, yet with a limited data comparability. So far researches on poverty were carried out by the ISSP and were based on the household consumption surveys that had certain sampling limitations, seasonal effects etc. More precise poverty assessment will be obtained only upon the completion of the Household Budget Survey performed by MONSTAT on the basis of new methodological approach in order to ensure improved statistical indicators.

Development and Poverty Reduction Strategy Progress Report for 2003 – 2004 (Report) is the first report on Strategy implementation and is related to 2004. It is based on the achieved outcomes of the activities set in the Strategy Action Plan. Also, the activities taken place during 2005, supported by UNDP are considered. These activities are related to rapid prioritization process. This process contributed to building capacities for monitoring implementation and is a good basis for innovation of the document in accordance with the outcomes of its implementation.

Additional element taken into consideration while drafting the Report is monitoring performance indicators set in the Development and Poverty Reduction Strategy. Ministry of Labor and Social Welfare, while monitoring implementation of the Strategy, could analyze progress made in the implementation using most of the set indicators. However, line ministries have not still developed some of the set indicators, or there is no adequate method to monitor them. This primarily relates to indicators from 9 to 15 (see above). Therefore, apart from monitoring Strategy implementation, permanent responsibility of the line ministries is to develop these indicators and thus enable the evaluation of the progress made in implementation of the Strategy, especially when it comes to the part related to poverty alleviation.

As it was mentioned previously, the Economic Reform Agenda in Montenegro 2002 – 2007 and the Development and Poverty Reduction Strategy are complementary documents. The Government of Montenegro adopted a biennial Report on the Agenda implementation. Taking this into consideration, Ministry of Labor and Social welfare, while preparing this Report relied on outcomes made so far in the implementation of the Agenda, as well as on monitoring of poverty reduction policies that are not defined in the Agenda.

Finally, it can be said that the first year of implementation of the Development and Poverty Reduction Strategy was rather successful. A great number of planned measures were realized, in spite of the fact that promised foreign assistance to support realization of the concrete projects has failed. Montenegro has managed to sustain macroeconomic stability, ensure rapid growth of private sector, reduce unemployment and informal economy, and provide increase in wages and pensions, as well as pro-poor social protection allowances.

In the next chapter of the Report, there are the outcomes of so far implementation of the Development and Poverty Reduction Strategy within macroeconomic reforms, employment growth and the following sectoral priorities: social protection and poverty reduction, labor market, anticorruption and transparency, agriculture, regional, rural and urban development, housing, tourism, transport, energy, water supply and sewage, environment, water and forest management, education and health.

**III CHAPTER:
MACROECONOMIC FRAMEWORK AND NEW JOB CREATION**

1.1 Introduction

Maintaining macroeconomic stability, accelerated growth of private sector and new job creation are the top priorities of the Development and Poverty Reduction Strategy. By the beginning of 2005 the Government of the Republic of Montenegro adopted a refreshed Economic Reform Agenda 2002 – 2007.

T1. Basic macroeconomic indicators with projections up to 2007

	2002.	2003.	2004.	2005.	2006.	2007.
Real economy*	<i>In mil. €</i>					
GDP in current prices	1.301,5	1.433,0	1.535,0	1.644,0	1.759,0	1.873,3
GDP per capita	2.109,1	2.317,9	2.473,0	2.635,6	2.808,8	2.979,5
	<i>% Change</i>					
Real GDP growth	1,7	2,3	3,7	4,1	4,5	4,5
Nominal GDP growth	19,1	10,1	7,1	7,1	7,0	6,5
Poverty	-	12,2				
Agriculture	6,0	1,0				
Industrial production	0,7	2,2	13,8	-	-	-
Retail price index	9,4	6,7	4,3	3,0	2,5	2,0
Unemployment rate	30,45	25,82	22,6	21,6	20,6	19,3
Informal economy	30	20	15	15	15	15
Number of the employed	140.100	142.679	143.479			
Number of the unemployed	76.293	68.625	59.002			
Retirees	88.835	90.183	93.033			
Average wage	193,0	271,0	302,8			
Average pension	108,8	113,0	122,0			
Financial sector*	<i>% In GDP</i>					
Total deposit	1,7	3,1	5,3	26,8	31,3	33,2
Total credit	9,6	14,0	18,5			
Annual active interest rate	15,16%	14,07%	13,50%			
Annual passive interest rate	0,50%	1,84%	3,39%			
Consolidated government finance^{5**}						
Consolidated public revenues	36,5	37,1	38,0	38,3	37,0	36,1
Current revenues	n.a	37,1	37,8	38,0	36,7	35,8
Tax revenues	34,2	34,5	35,5	35,4	34,2	33,4
Capital revenues	n.a	-	0,2	0,3	0,3	0,3
Consolidated public expenditures	40,6	41,0	40,6	40,4	38,5	37,1
Current expenditures	38,3	38,1	38,5	37,8	36,1	34,8
Capital expenditures	1,60	1,0	0,9	1,9	1,9	1,8
Reserves and net credit	n.a	1,9	1,2	0,7	0,5	0,5
Corrective fiscal measures	n.a	1,3	-	-	-	-
Total balance prior to grants	-4,0	-4,1	-2,6	-2,1	-1,5	-1,0
Foreign support	2,2	0,9	0,5	0,2	0,3	0,2
Local financing	-3,5	-0,2	1,5	0,6	0,5	0,4
Foreign financing	0,6	0,8	1,3	0,9	0,3	0,2
Privatization revenues	5,1	1,8	0,5	0,4	0,4	0,4
Investments *	14,1	14,9	7,2			
Local savings	1,7	3,1	5,2			
Foreign direct investments	6,7	2,7	3,3	9,1	10,2	10,7
Balance of payments^{***}	<i>In mil €</i>					
Current account in mil €	-176,00	-101,98	-142,97	-160,0	-170,0	-190,0
Foreign debt in mil €		-498,8	-582,4	-650,0	-700,0	-730,0
Trade balance in mil €	-334	-247,7	-291,0	-280,0	-260,0	-250,0
	<i>In % GDP</i>					
Foreign debt in % GDP		-36,28	-39,48	-39,5	-39,8	-39,0
Current account in % GDP	13,5	-7,1	-9,3	-9,73	-9,67	-10,14
Trade balance in % GDP	-25,7	-17,3	-19,0	-17,03	-14,78	-13,34

Sources: Economic Reform Agenda 2005, ** Ministry of Finance 2005, *** Economic Reform Agenda and projections of the Central Bank of Montenegro.

⁵ Without public expenditures of municipalities

Macroeconomic projections have been revised on that very occasion. The DPRS experts took part in revising new projections, which maintain compatibility with those set in the Development and Poverty Reduction Strategy as well as with plans for achieving Millennium Development Goals.

The Economic Reform Agenda is focused on achieving the same macroeconomic goals as the ones in the Development and Poverty Reduction Strategy. Based on this fact, a revised macroeconomic projection from the Economic Reform Agenda will also be a macroeconomic framework for reaching goals defined in the Development and Poverty Reduction Strategy.

1.2 Priority actions defined in the Development and Poverty Reduction Strategy

1.2.1 Macro-economic framework

Maintaining macroeconomic stability along with achieving a stable economic growth rate, which leads to the decrease of unemployment is one of the main priorities of the Development and Poverty Reduction Strategy. Projected real economic growth rate in 2004 is 3.7 % of GDP, while in 2006 it is projected to reach 4.5% of GDP. A significant drop of inflation rate is also projected, from approximately 6.7 % to around 2.5 % in 2006.

It is envisaged that stable economic growth rates are mostly supported by greater inflow of foreign investments that should grow from 3% of GDP in 2003 up to 10 % of GDP in 2006.

Planned economic growth is based on the development of export-oriented private sector, which would lead to trade balance drop from 17 % of GDP to 14 % of GDP in 2006. The drop of the trade balance would have an impact on sustaining current account deficit right below 10% of GDP.

Export-oriented growth assumed greater investments. Investment share in GDP is envisaged to grow from 18 % in 2003 to 19.5 % of GDP in 2006. Investment rise will be supported by the rise in domestic savings, which should grow from 3 % of GDP in 2003 up to 4.3 % of GDP in 2006.

In 2006 the share of public revenues in GDP should grow by 1% of GDP (38% of GDP), while the share of public expenditures is anticipated to fall by 3 % of GDP, thus reaching around 38,5 % of GDP. Important priorities within fiscal consolidation have been defined aiming at decreasing total fiscal deficit (prior to grants) from 4 % of GDP in 2003 to 1 % of GDP in 2006. The most important among them are further decrease in public administration costs and increase in the so-called projected financing. It is envisaged that the share of capital expenditures in GDP grows from 1 % of GDP in 2003 to 2 % in 2006.

1.2.2 New job creation

Stable economic growth rate should lead to decrease in unemployment rate, which was 30 % in 2002 and should fall to 20 % in 2006. Private sector i.e. small and medium-sized enterprises should be responsible for new employment, especially within tourism, agriculture, transport and wood industry.

Apart from maintaining macroeconomic stability, the growth of private sector should be supported by the improvement of business climate, escalation of the process of privatization as well as by

maintaining stability of financial (banking) sector. Jurisdiction and state administration reform should lead to the improvement of business climate and lower commercial tax burdens.

Increase in employment rate should be followed by the unemployment rate decrease, especially when it comes to the young labor force mainly employed in informal economy. Reduction of informal economy is also defined as priority action. In 2002 the level of informal economy compared to GDP was 30 %, and it is planned to be halved in 2006, thus reaching 15 % of GDP.

Reduction of informal economy is also defined as the priority action. In 2002 the level of informal economy related to GDP was 30%, while it is envisaged to be halved and thus amount to 15% in 2006.

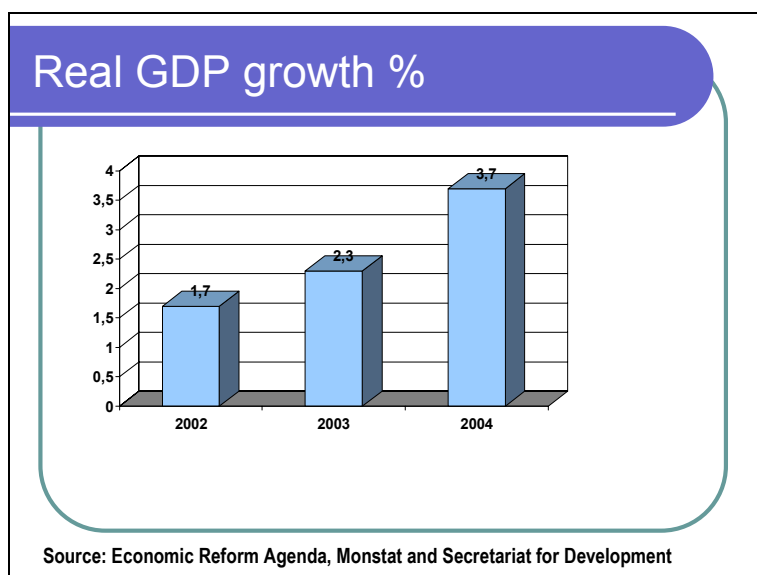
Restructuring of companies is also assessed as a high priority, which should lead to the increase in employment, while escalation of the bankruptcy proceedings is stressed as an important step to improve business climate.

To encourage employment of the poor, a full support was given to micro financing.

The Development and Poverty Reduction Strategy provided support to collective bargaining and also to work of Economic and Social Council.

1.3 Implementation of the priorities of the Development and Poverty Reduction Strategy in macroeconomic reforms and new job creation

In 2000-2004 series of reforms were implemented leading to the recovery of GDP and sustainable macroeconomic stability. In 2001-2003, there was a slight economic growth ranging between 1-2 % of GDP. However, in 2004, real GDP growth was 3.7 %. Estimated level of GDP and so as the growth rate (for 0.7% of GDP) is greater than it was projected in the Development and Poverty Reduction Strategy.

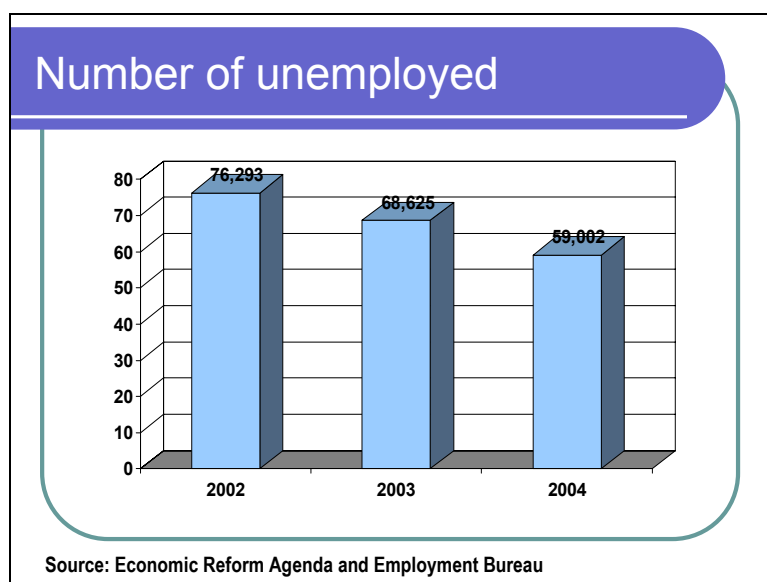


Graph 1: Growth of real GDP in 2002-2004.

In 2004 light industry made a growth, which is greater by 13 % than in 2003, contributing to economic growth of the country of about 1.5%. Electricity and gas production have been increased by 21 %, which also contribute to economic growth of the country of about 1.5% in relation to GDP.

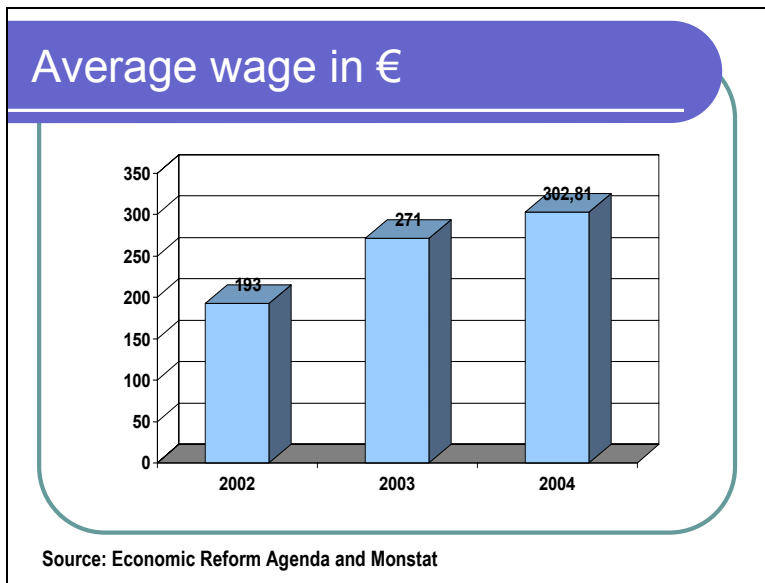
In addition, progress has been made in relation to other performance indicators (see Table 3). Foreign debt of Montenegro has been increased from 438 mil EUR in 2003 to 502 mil EUR in 2004. However, servicing of foreign debt remained on the level below 4 % of total import of goods (3.7%), in compliance with projections made in the Development and Poverty Reduction Strategy.

Unemployment rate is gradually decreased, but is still high, reaching 22.6% in 2004, which is slightly higher than it was projected in the Development and Poverty Reduction Strategy. However, in 2004 the number of unemployed people was reduced by 11.000 people compared to 2003. It should be stressed that there are some methodological problems while measuring unemployment.



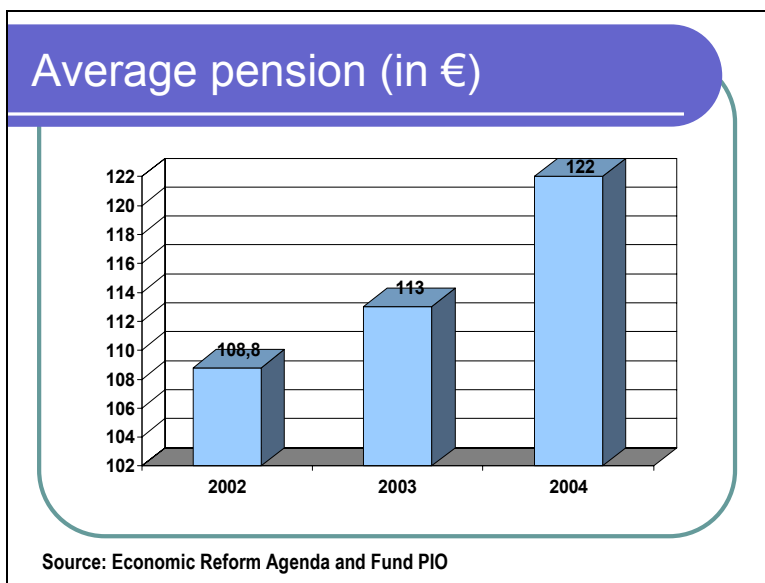
Graph 2: Number of the unemployed and unemployment rate in 2002-2004.

Apart from decrease in unemployment, there is also an increase in wages, as one of the basic criteria to measure living standards of the population.



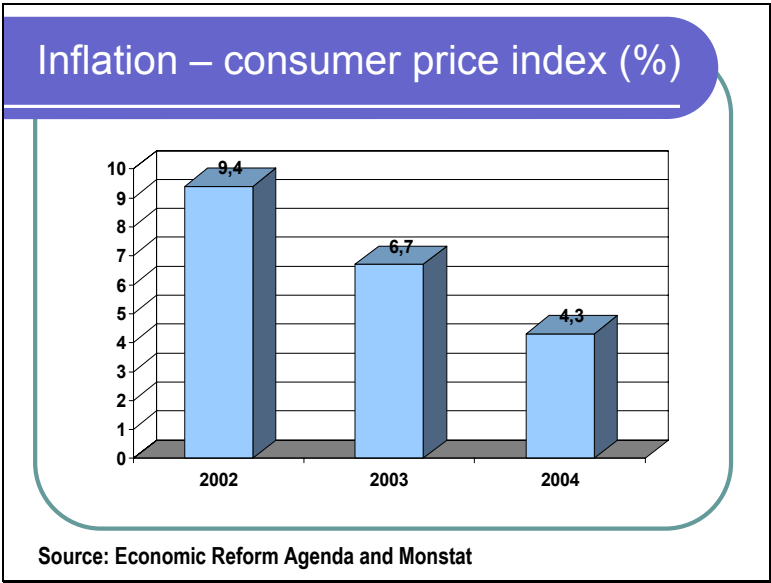
Graph 3: Average wage in Montenegro in 2002-2004.

Decrease of unemployment and increase in wages have also been followed by the increase in pension.



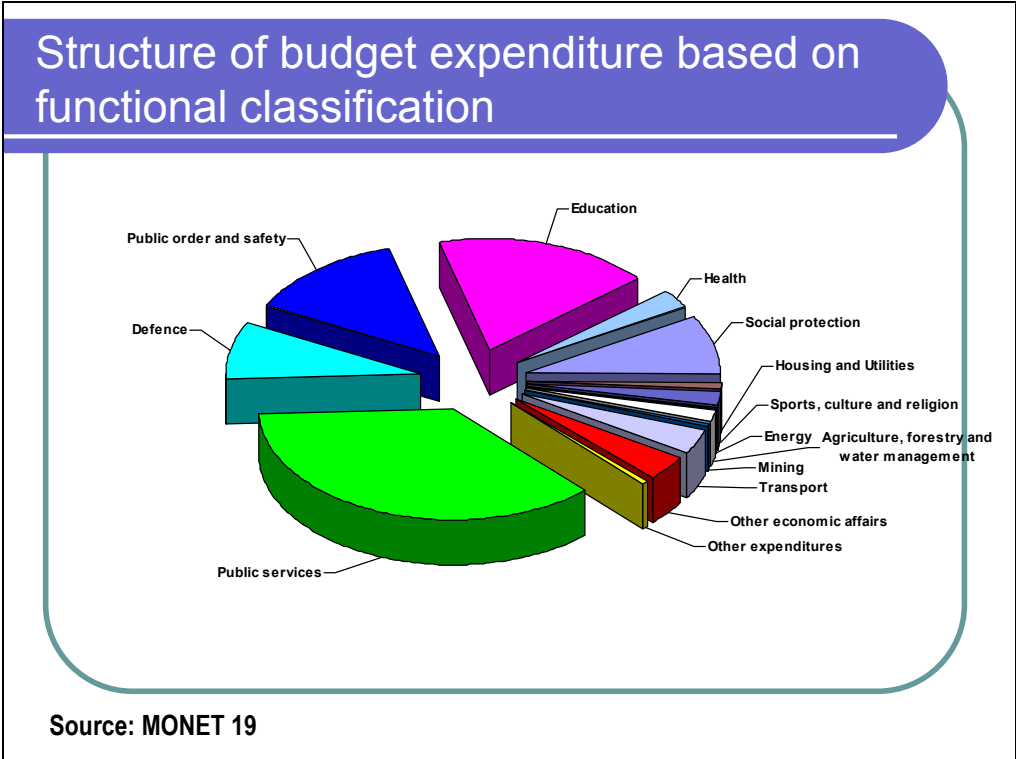
Graph 4: Average pension in Montenegro in 2002-2004.

The inflation rate has a decreasing tendency still more, especially since monetary reform and EURO as a legal tender (23.8% in 2001) have been introduced. Measured by the retail price index, the inflation rate was 4,3 % in 2004, while measured by consumer price index, it was 1.5 %. Level of inflation rate is coming closer to the level of EMU inflation rate, which is a long-term goal in Montenegro. The inflation rate in the first three quarters in 2004 was on the EMU level while considerable increase in the forth quarter was caused by local factors and the increase in price of telecommunication services. Further reduction of the inflation rate will depend on limiting power of monopolistic and oligopolistic suppliers by accelerated adoption of anti-monopolistic legislation.



Graph 5: Inflation rate in 2002-2004.

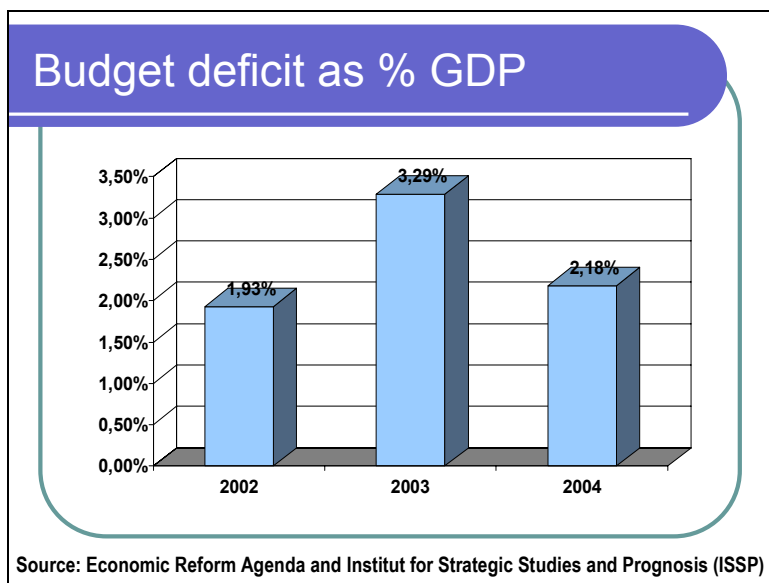
Apart from significant limitations, fiscal policy should be a kind of support for development and poverty reduction programs. Public expenditures in 2003 and 2004 were based on the objectives of the economic policy of the Government of Montenegro and consistent with frameworks and goals of the IMF and World Bank.



Graph 6: Share of the categories of budget beneficiaries per functional classification in total expenditures in 2002-2004.

Main results within the fiscal system are fiscal balance, tax rate decrease and creation of favorable conditions for economic entities and their operation and so as for foreign investment. The Law on income tax rate and the Law on profit have successfully been implemented.

Fiscal deficit is decreased from year to year, as well as its share in GDP. Thus, the fiscal deficit in 2004 was 2.6 % of GDP, which is lower compared to the fiscal deficit projected in the Development and Poverty Reduction Strategy (4.7% of GDP).



Graph 7: Fiscal deficit as GDP percentage in 2002-2004.

The share of public expenditures in GDP has a decreasing trend and is projected to fall from 41.0% of GDP in 2003 to 37.1% of GDP in 2007. Deficit decrease and financing of the public expenditures from real resources are also evident.

In 2004, the number of employees in state administration was reduced, which was also one of the objectives of the Development and poverty Reduction Strategy. At the same time, relative share of the resources allocated for salaries disbursed from the state budget are constantly reduced (from 11.28 % of GDP in 2004 to 9.3% of GDP projected for 2007, based on Ministry of Finance data).

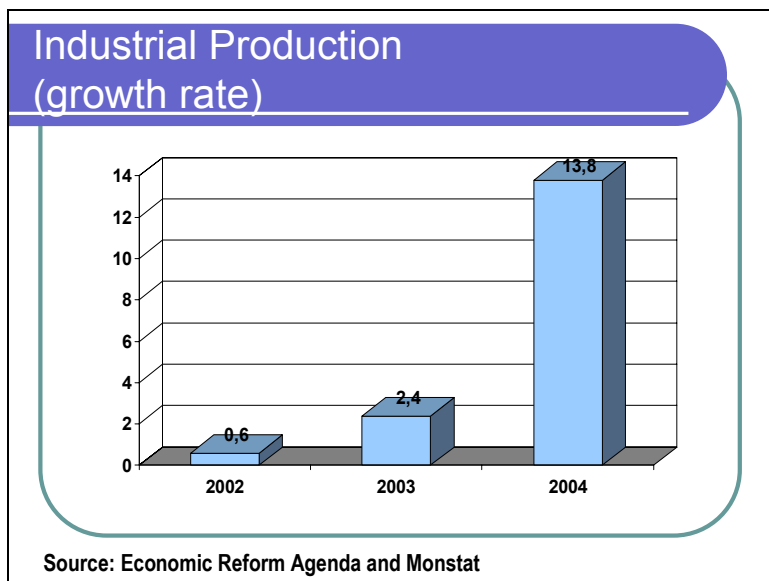
In the short run, this measure will have a negative effect on the poverty reduction policy, but in the medium-long term, there will be some savings in the budget to finance domestic and foreign obligations as well as investments a little bit later. In purpose of reducing social consequences of such a policy, the Government of Montenegro passed the decision that attending social programs should be financed from privatization revenues.

Establishment of the Department for internal auditing in the Ministry of Finance, as well as introduction of the provision on financial reporting is a step forward in ensuring transparency when it comes to public revenues allocation and will contribute to greater efficiency of the Government institutions.

1.4 Implementation of the priorities of the Development and Poverty Reduction Strategy in structural reforms

1.4.1 Private sector as a basic generator of the employment growth

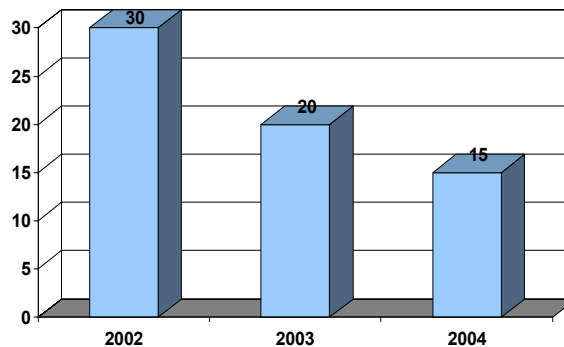
The structure of new employers is changed more and more in favor of private sector. The share of private sector in GDP is increased compared to 2002 when it was around 37% of GDP. In 2004 it was 44 % of GDP (Agenda, 2005). Private sector is more and more proved as the generator of economic and employment growth. In that term the growth rate of industrial production has suddenly been raised from 3.4 % in 2003 to 13.8% in 2004.



Graph 8: Growth rate of industrial production in 2002-2004.

Informal economy has been halved compared to 2002, when it was 30%. In 2004 it was around 15 %, which is also close to the projected goal planned for 2006. (11%).

Informal economy



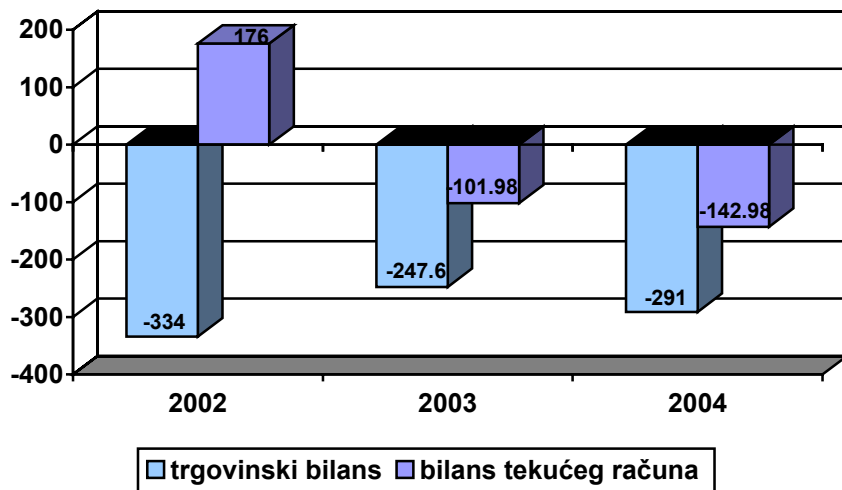
Source: Economic Reform Agenda

Graph 9: Share of informal economy in GDP in 2002-2004.

Stimulation of real growth in Montenegro has to be based on **export-oriented private sector** development, having in mind a small domestic market. In last couple of years, export of raw aluminum prevails and makes 60-70% of total export of goods in Montenegro, while in 2004 export of raw aluminum was 60,7% of total export of goods. Apart from raw aluminum, export-oriented sectors in Montenegro are drinks (wine, beer and brandy) making a share of 1.85%, than wood processing sector with a share of 1,3% of total export in 2004. Furthermore, a great significance in total export of goods belongs to agricultural products such as fruits and vegetables, medical herbs, mushrooms and some food products (cereals, smoked meat and the like).

By the end of 2004, current account deficit of the balance of payment has been increased in relation to previous year; in addition that there is a dilemma if this is a result of deterioration or bad statistics. Foreign trade exchange has registered a dynamic growth, with permanent growth of GDP share, reaching 81% in 2004, while together with services it reached 104%. However, export/import ratio is still low (47% in 2004), but is improved related to previous year, while export of services/goods ratio according to GDP higher by 2% than it was in 2003 (42.4% in 2004).

Problems of foreign trade exchange are reflected in permanent goods exchange deficit, which is however, lower by 1% in 2004 compared to the level projected in the Development and Poverty Reduction Strategy, pointing out that economy depends on import to a significant extent. Insufficient competence of domestic products, low capacity exploitation, technological backwardness, excessive domestic demands for consumers' goods, as well as the rise in oil price are the main causes for deficit in good balance. Consumers' goods prevail in import structure with 69%. The share of the goods planned for reproduction is 25%, while the import of equipment is only 5.4% in 2004.



Graph 10: Trade balance and current account balance in 2002-2004.

Sector of services in Montenegro is of special importance when it comes to development of export-oriented private sector. Namely, Montenegro should tend to be developed as service-oriented country, with special emphasis on tourism and transport. Profit made by tourism in 2004 was 67.8 % of total service profit, while transport made 19% of total service profit in 2004. Therefore, development of the activities in these sectors where Montenegro has comparative advantages will stimulate economic growth, increase employment and reduce poverty.

More effective export-oriented growth should be stipulated by considerable **investment activity**. Domestic investments are insufficient, i.e. inconsiderable, so the strong export-oriented production primarily depends on foreign investments.

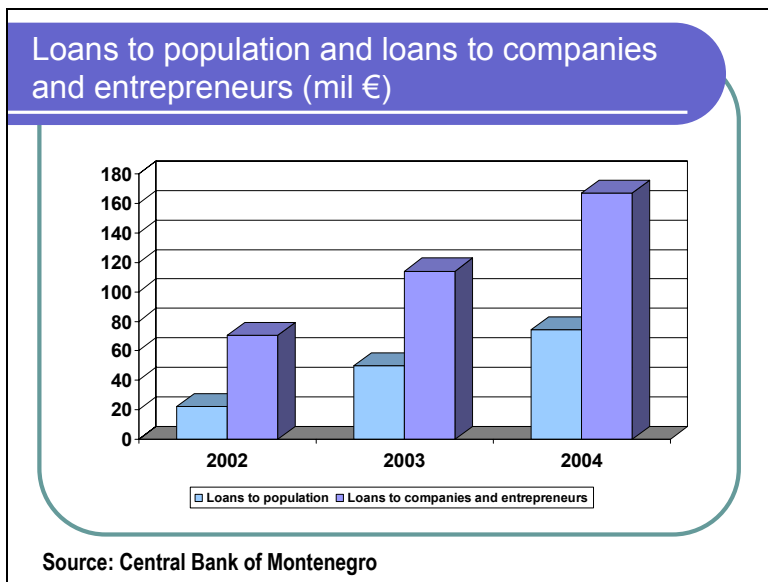
Since the banking sector reform was launched in 2000, the most significant progress has been made within banking sector recovery and restructuring. There are ten banks operating in Montenegro. Out of that number eight banks are private, while foreign investors are majority shareholders in three of them.

Privatization of Podgoricka and Niksicka bank (the last two banks in state ownership), as well as further privatization of the part of the state property is expected to take place in 2005. However, financial system efficiency is low, and still banks are the most important bearers of this sector, while there is a small share of other participants.

Main success achieved through the banking sector reform also implies: regulation and resolution of the banks in accordance with Basel principles and EU Directives, further privatization of banks, adoption of provisions for money laundering prevention and payment system reform.

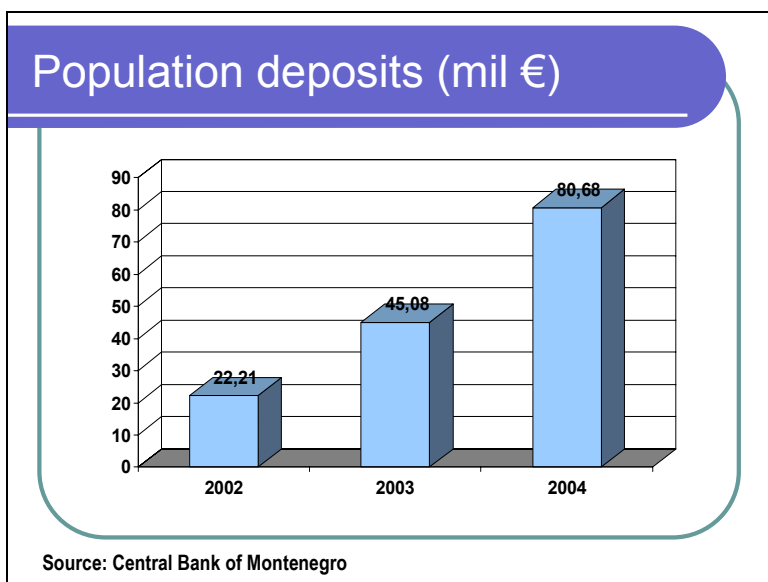
Significant lending of the economy and population is continued, with an annual growth of 42% in 2004, (Central Bank, 2005). Loan expansion did not jeopardize banking sector liquidity, and the potential of the banks was increased by 27% in 2004. Although, banking system liquidity was not

jeopardized in 2004, a credit risk for the banks can be a significant problem in the forthcoming period. Excessive credit expansion can imperil macro stability, through the increase of domestic demands, deficit of current balance and pressure on fiscal sustainability.



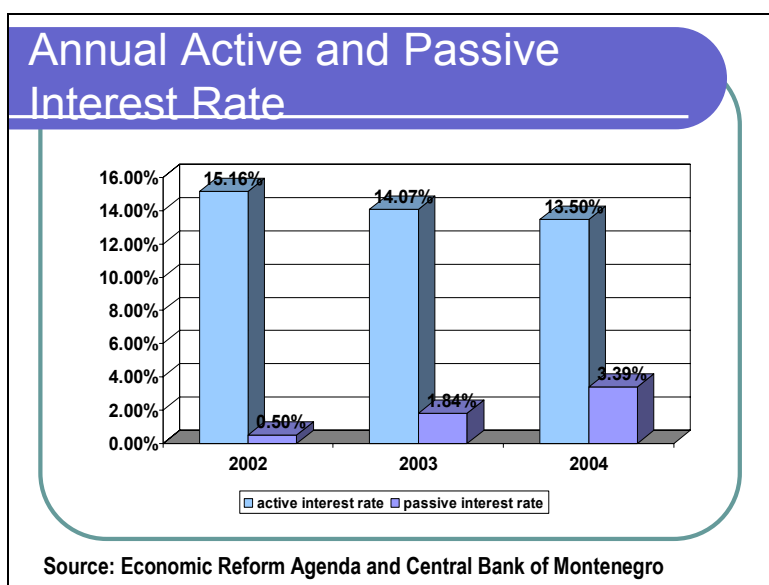
Graph 11: Loans given to population and companies and entrepreneurs in 2002-2004.

Timeframe credit structure is improved but still is not satisfactory for the share of the short-term credits was 60% in 2004. Most credits are given to citizens and service sector companies. During 2004, recorded deposit growth was 30%, but the dynamics of deposit growth in domestic banking system should be better. Deposit structure is improving, but sight deposits make 55%, while time deposits make 45% of total deposits. The growth of citizens' savings is an indicator that their confidence in banking sector is gradually returned. In 2004 domestic savings amounted to 80 mil €, which is an increase of approx. 80% related to 2003, meaning that one of important goals of the Development and Poverty Reduction Strategy has been achieved.



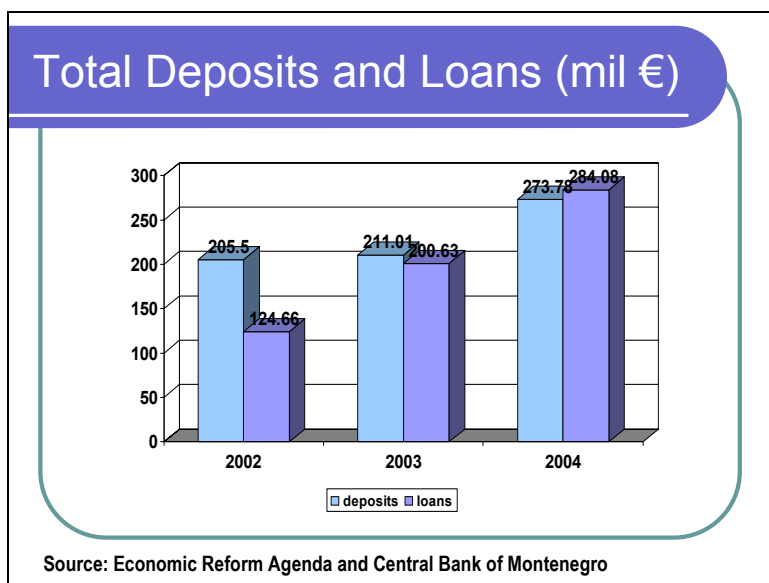
Graph 12: Population deposits in 2002-2004.

Apart from the improved credit and deposit structure and an evident return of confidence in banking sector, interest rates are still double-digit numbers, which burden economy and point out that risk exists. Introduction of risk decreasing measures, increase of the competence in banking system, further strengthening of bank supervision aiming at better risk management, future banking sector privatization are measures which should impact the decrease of active interest rate in the forthcoming period.



Graph 13: Annual active and passive interest rate in 2002-2004.

A series of measures were taken in 2004 aiming at increasing confidence in the banking system: the Agency for money-laundering prevention was established, bond issuance was taken place on the basis of old foreign currency savings and the Central Bank of Montenegro is now carrying out a severe bank supervision. By the end of 2004, deposit of the Government was transferred in the Central Bank, which leads to centralization and easier deposit management. As of January 1, 2005 commercial banks completely took over the system of payment while the Deposit Protection Fund is anticipated to start operating during the year.



Graph 14: Total deposits and credits in 2002-2004.

International economic relations is characterized by strategic determination of the Government of Montenegro in terms of further economic development and removal of trade barriers, as the main source of growth of the small country such as Montenegro. Last years a great progress has been made through the liberalization and deregulation of external trade and investments, which is incorporated in the Tax Law and the Law on Foreign Trade, both completely harmonized with WTO rules, which contributed to further liberalization of trade regime, abolition of licenses, prohibitions and quotas⁶. Regardless of the removal of import barriers emerging from the adoption of the new foreign trade legislation and in spite of the growth of economic activity, the level of import and foreign trade deficit of goods and services have an increasing tendency and is rather high. Increasing productivity and competence will impact the foreign trade dynamics and attraction of direct foreign investments, which also have an influence on export growth and further rise in productivity in other countries.

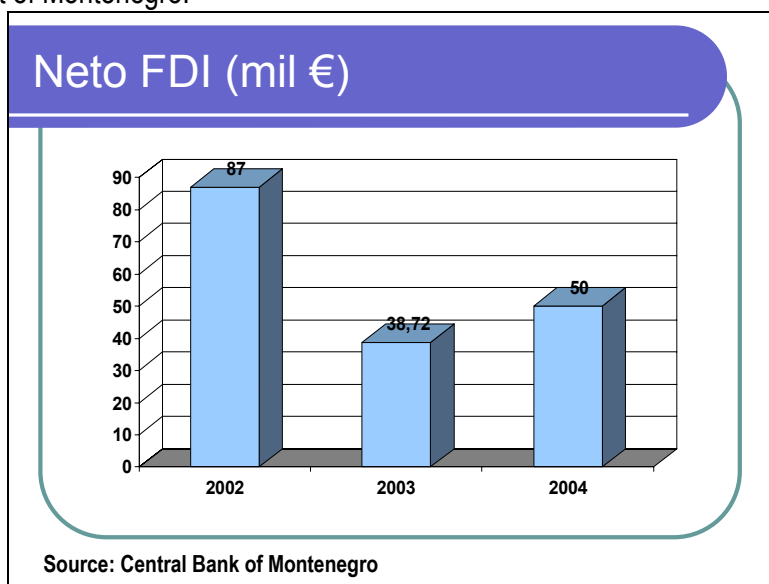
Creation of favorable business environment is one of important prerequisite for economic recovery and private sector development. Barriers imposed by rules, licensing procedures, taxes, waiting time and disharmony with new procedures and rules obstruct the establishment of new companies and development of existing ones. In last four years, a great progress has been made through liberalization and deregulation of foreign trade and investments, simplification of tax system, modernization of the employment legislation, improvement of legislation for commercial companies.

More competent tax rates have been introduced: income and contribution tax rate have been decreased by 10%, while profit tax rate have been decreased from 20% and 15% to 9%. It is especially worth mentioning that the process of establishing companies have been deregulated to great extent and now it takes two days.

⁶ Harmonization with Serbia led to the increase of the average tax rate from 2.8% up to 7.1% in 2003.

Small and Medium-sized Enterprise Development Agency as well as some non-governmental organizations such as Center for entrepreneurship and economic development is a successful catalyst in efficient resource management and stimulation of small and medium-sized business. Series of laws have been passed, which should improve business environment such as the Law on bankruptcy, ensuring unsustainable enterprises to be closed, the Law on private sector participation in delivering public services, the Law on electronic trade and the like. In addition, the Law on Mortgage, the Law on insolvency of the companies and the Law on Pledges have been passed.

Direct investment inflow has an increasing tendency although not as anticipated and is mostly related to privatization process. Attracting Foreign Direct Investments is one of the top priorities of the Government of Montenegro.



Graph 15: Net foreign direct investment in 2002-2004.

Privatization and reconstruction of companies is a base for accelerated economic growth, fiscal and external sustainability. New **privatization** framework was adopted 1998/99 in Montenegro. It envisages various methods, including mass voucher privatization (MVP), direct tender sale and auctions. Upon the mass voucher privatization and series of tenders, a great deal of share capital in Montenegro is possessed by private owners (around 70%). Restructuring and privatization of 16 large industrial companies, making 45% of industrial property, including KAP (Aluminum Company) are coming to an end.

Although the funds possess significant percentage of capital in some companies, more often it is the case that the capital structure is disaggregated and in most of them there is no outstanding majority of shares, though centralization process has already been started.

New legal procedures, which hasten bankruptcy and liquidation of companies, with low fiscal resource to finance subsidies, will contribute to the acceleration of the restructuring process taken in the sector of companies.

1.4.2 Reform of state administration and judicial system

Good and efficient state administration providing reliable services to their clients leads to a great confidence of citizens and investors and encourages entrepreneurship activities. To implement successful reforms it is necessary to modernize structure of the state administration. At the same time, the integration process into European Union also requires new organization and concept of state administration.

Greatest achievements within the reform of state administration were made by: adoption of the Law on civil servants and its initial implementation phase, establishment of the Human Resource Directorate, adoption of the Law on civil servants' salaries and so as the Law on inspection and all accompanying by-laws.

Montenegrin judicial system makes great efforts to meet the requirements of modern jurisdiction in compliance with the EU standards. All legislations passed within the area of jurisdiction are harmonized with EU standards and they are provided with a high independence degree – permanence of the function of judge, competence and structure of judicial council, which took over legal authorities, belonging to executive authorities until the adoption of the Law on courts.

Greatest achievements within jurisdiction reform imply: adoption of new legislation on civil suits and executive proceedings, which considerably contributed to the improvement of business climate through prompt solution of commercial disputes, as well as adoption of the Law on mediation and the Law on notary. Besides, new Administrative and Appellate Court was established, which should disburden work of the Supreme Court. The Commission for testing bankruptcy managers, Center for training judges and Judicial Council have been set up. New financing model and other solutions providing high degree of independence and sovereignty have also been established.

1.4.3 Stabilization and Association Process

Final strategic determination of the Government is a gradual harmonization with EU standards and systems, i.e. **EU Stabilization and Association Process. (SAP)**. Action plan for creation of unique foreign trade policy and concept of free internal market was adopted by the Parliament of Serbia and Montenegro in summer 2003, half a year upon the constitution of the state union and adoption of the Constitutional Charter. Adoption of these basic documents made possible for the Commission to start drafting the Feasibility Study. Nevertheless, an attempt for reaching minimum level of joint trade policy and integration of internal market did not bring the desired results.

To exceed permanent constitutional stagnation and to stimulate SAM integration in EU, the Commission proposed the approach of »dual track« in July 2004, which was approved by the EU Council of Ministry and politicians of Serbia and Montenegro.

Negotiations and implementation of the requested obligations from SAP Agreement will be a great challenge. Having in mind a considerable size of bilateral trade, SAP Agreement will require significant dedication of Montenegro in political, administrative and financing terms. The process of liberalization of bilateral trade with Economic Community will require further efforts to be taken within structural reforms, for building capacities of both republics to resist from the pressure of the

competence imposed by SAP Agreement, improve export and decrease current account deficit. In that term, one of the key elements to be considered is the possession of necessary standards and certificated capacity for trade with EU. Republic will also be obliged to ensure that local economic stakeholders will understand and accept the objective of trade liberalization.

According to the assessment of the Commission, Montenegro made considerable progress in implementing European partnership priorities and should provide the liberalization of movement of goods, labor force, services and capital with EU, possible with different liberalization schedule. In that purpose the liberalization process with neighboring countries has already started, and so as the dedication to reforms and further regional trade liberalization.

1.5 Priority actions for the forthcoming period

Maintaining macroeconomic stability and stimulating development of export-oriented private sector remain the priorities whose realization will be the basis for employment growth and reduction of poverty.

To realize planned goals defined in the Development and Poverty Reduction Strategy, real economic growth rate should reach the level above 4 % of GDP while inflation rate should fall to 3%. Fiscal deficit (prior to grants) should be decreased to 1,5% of GDP by the end of 2006, trade balance should reach 15% of GDP while current account deficit should be sustained below 10% of GDP.

Still more the fiscal reform will be based on reducing of total public expenditures, increasing taxes, improving efficiency in collection of public revenues, more efficient management of foreign debt, building transparency and state auditing.

Beside the focus on low deficit level, the attention should be paid to the quality of the government lending. Commercial banks' lending should be reduced. Practice of domestic lending in the state records is a very expensive source of domestic financing. Undoubtedly, emersion into international capital market would enable supply of cheaper resources, which is possible with receiving credit rating, a little higher than in other countries in the region. External funding has its limitations in terms of the level of indebt ness.

Fiscal balance is imposed as an imperative in the medium term. Further rationalization of the budget expenditures remains a priority goal in the medium-term, implying more solid discipline on the expenditure side and improving conditions related to wages and subsidies. As far as the revenues are concerned, it is necessary to work on further legalization of informal economy, constant improvement of tax collection, tax policy to increase tax basis and decrease tax burdens, which would allow strong private sector development. Certain public function should be entrusted to private sector. Fiscal discipline imposed a delay of the announced tax decrease, lest fiscal position of Montenegro will be more deteriorated. Increasing fiscal sustainability is closely related to the necessity to accelerate structural reforms, especially when it comes to public conglomerates in energy, telecommunication and railway sectors.

Additional capacity development in this field should support future MTEF development aimed at better usage of the key macroeconomic indicators, projection of the revenues and expenditure plans, as well as further development of the programming budget in phases to be completed up to

2007. Currently programming budget exists only in three ministries: Ministry of Education, Ministry of Maritime and Transport and Ministry of Tourism.

Further encouragement of entrepreneurship and improvement of business climate remained important priorities. It will be especially important to implement the Law on mortgage, as well as a legislation framework for intellectual property protection, and so as to improve work of courts in purpose of efficient settlement of commercial disputes.

Complete realization of privatization annual plans should also contribute to rapid private sector development. Acceleration of the bankruptcy proceedings and so as restructuring of companies will significantly improve the business climate for domestic and foreign investors. Establishment of the Agency for Foreign Direct Investments Promotion should provide increase in attraction but also removal of obstacles for external capital. Besides, in the forthcoming period the emphasis will be focused on future development of Montenegro and its concepts of national treatment of foreigners and adjustment of legislation, which will strengthen the competence of certain fields of Montenegrin economy.

Within the financial system the priority will be the follow-up of the privatization of banking sector as well as strengthening its supervision. The accent will be put on further development of the market of capital by improving legislation for insurance sector, reorganization of investment funds and legal framework for trade with securities.

Liberalization of foreign trade and so as the implementation of customs reform remains great priorities. Conclusion of the Agreement on free trade in the region will be a significant incentive to these processes for it ensures the emersion of 55 million of people into the market. However, liberalization of trade is not sufficient for itself to contribute to economic development. It should be provided through structural changes, macroeconomic policy support, development of infrastructure, increasing investment, human resources development, rapid restructuring of enterprises and various program on the increased competence of domestic products, which would altogether result in growth of productivity competence.

Improvement of these policies with permanent emphasis on foreign trade, as a development factor, creates prerequisites for further transition and integration in world trade system. Negotiations for WTO membership, and so as regional EU integration and signing of bilateral trade agreement give new aspects to trade reform.

Within the reform of state administration there will be undertaken follow-up activities on its cost-effectiveness, strengthening of professional capability and increase in work efficiency. Jurisdiction reform will be more streamlined towards implementation of adopted legal provisions and realization of administrative reform aiming at raising court efficiency to strengthen business atmosphere and confidence of businessmen and citizens in judicial system of the country.

IV SECTORAL PRIORITIES

1 SOCIAL PROTECTION AND POVERTY REDUCTION

1.1 DPRS Priority Activities

Introduction

According to the survey done by the Institute for Strategic Studies and Prognosis (ISSP), which was basic for DPRS development, **12.2% of the population of Montenegro is poor**⁷⁸. The survey comprised domicile population, refugees and IDPs and RAE. The absolute poverty line is defined as the total expenditure below the expenses of the minimal consumer basket for a standard household (€ 116. 2 per consumer unit) and the line of defining the economically vulnerable population is set 50% above the poverty line (€ 173.4).

Assessments of poverty are sensitive to the poverty line: **more than one third of the population is classified as economically vulnerable** or without access to sufficient resources, because they live below the level of 150% of the poverty line. Therefore, a significant part of the population living in the zone immediately above the poverty line is vulnerable in the sense that it is sensitive to any form of economic instability or drop of personal income.

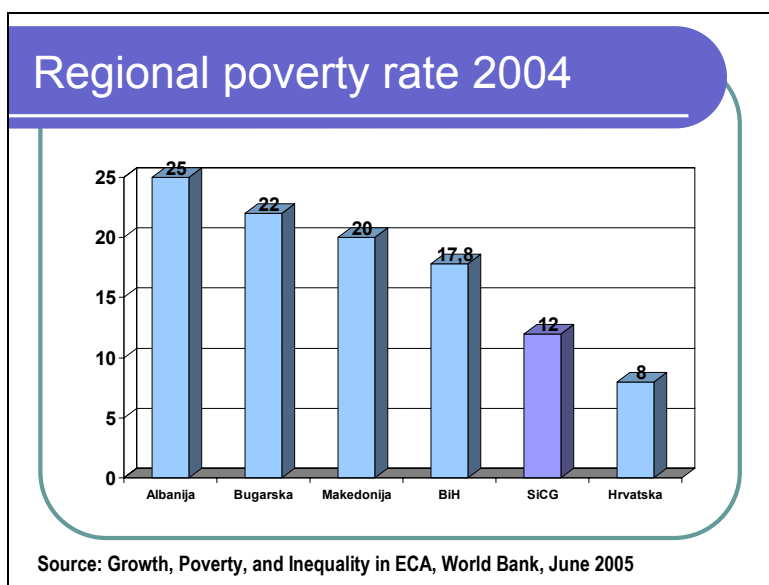


Chart 16: Regional poverty rate in 2004

⁷ Poverty Assesment and Social Protection, Ministry of Labor and Social Welfare, 2004

⁸ Northern region consists of 11 municipalities: Andrijeвица, Berane, Bijelo Polje, Kolašin, Mojkovac, Plav, Plužine, Pljevlja, Rožaje, Šavnik, Žabljak.

Vulnerable Groups

DPRS and later developed documents for the purpose of prioritization⁹, defined the following vulnerable groups:

- Persons in the state of social need,
- Pensioners and elderly without personal income
- Children and youth,
- Persons with disability,
- Unemployed,
- Refugees and IDPs,
- Roma, Ashkealia and Egyptians.

Poverty Causes

DPRS defined the main causes of poverty:

- Economic activity setback,
- Unemployment,
- Low level of education,
- Inequality (refugees, IDPs, Roma, Ashkealia and Egyptians).

Regional and population poverty dispersion

The population of Northern Montenegro¹⁰, where 45% of poor live, is greatly affected with poverty. In the central part of Montenegro live around 35% of poor, while on the south this percentage goes up to 19.

The poverty rate is highest among RAE population and it is around 52%, and it is also high among the refugees and IDPs (around 40%), while it is lowest among domicile population (around 10%). Nevertheless, the greatest part of poor within the total population living in Montenegro consists of the domicile population and that percentage amounts to 72%.

Risks for falling into poverty

As it was previously mentioned 30 % of the population in Montenegro is concentrated close to the poverty line, therefore there is a risk of falling into poverty. The DPRS cites the following main risks of falling into poverty:

- Increasing number of household members
- Setback of country economic development
- Job loss

⁹ Poverty Assessment and Social Protection, Ministry of Labor and Social Welfare, 2004

¹⁰ Northern region consists of 11 municipalities: Andrijevica, Berane, Bijelo Polje, Kolašin, Mojkovac, Plav, Plužine, Pljevlja, Rožaje, Šavnik, Žabljak.

Priority Activities on Poverty Reduction within the Area of Social and Child Protection

The Government of Montenegro adopted the strategic document, Economic Reform Agenda in Montenegro 2002-2007. The Agenda comprises the Social Protection System Reform Plan. The DPRS (adopted six months after the Agenda by the Government of Montenegro) follows the social protection sector priorities defined within the Economic Reform Agenda, while the special accent is placed on poverty reduction. The aim of both documents is the establishment of social protection system, for especially vulnerable groups, so as for those in the state of social need.

The main priorities are:

- To elaborate the National Employment Strategy including regional, municipality and local-level Employment Action Plans;
- To adopt the National program on social protection of the elderly,
- To define policies and key principles towards the family and children, especially those without parental care,
- To define the Strategy on population development; (Nativity policy),
- To define the Strategy for resolving the status and problems of refugees and IDPs;
- To define the Strategy on social protection of people with special needs,
- To define Programs for Roma protection
- To develop a unique information system within the Ministry of labor and Social welfare
- To continue the pension system reform.

Social protection system in Montenegro

Social protection system in Montenegro has two main components: social protection based on insurance and social protection. The third component consists of active policy measures within the labor market and war veteran protection.

Social protection comprise a wide range of benefits offered to Montenegrin population. Apart from the visible benefits there is a set of policies and measures undertaken by the Government of Montenegro, aimed to decreasing vulnerability and providing assistance to Montenegrin families. Those measures consist of subsidized price of certain services and different programs and one-time allowance for workers in weak enterprises, for example payment of outstanding wages, severances and similar measures.

Furthermore, the system of informal social protection, ei. family solidarity is rather strong in Montenegro. According to household survey conducted by ISSP, over 10% of the total household income is made by other households income (family and friends).

Within the child protection sector the following priority activities are defined:

- Define a national level approach on supporting children and youth at state level, but also design regional and local strategies which should be based on respect of human and child rights

- Realize the decentralization of functions and responsibilities for social and child protection financing,
- Strengthen the personal responsibility of citizens for family social protection,
- Develop competitiveness among different service providers within child protection and stimulate the introduction of market criteria in financing programs and services within this area.

Within the pension insurance sector the following priority activities are defined:

- Restructuring the existing obligatory insurance system on the basis of generational solidarity,
- Introduction of obligatory insurance on the basis of capitalized savings,
- Introduction of voluntary insurance,
- Implementing stricter criteria for access to age-based, disability and family pensions,
- Reduction of gray economy and increasing the number of social insurance contributions.

Within the elderly protection sector the following priority activities are defined:

- Strengthening the system of non-institutional protection,
- Building of additional facilities for elderly accommodation,
- Building of day rehabilitation centers.

Within the refugees and IDPs social protection sector (including RAE) the following priority activities are defined:

- Strengthen the process of repatriation of refugees and return of displaced people,
- Create programs for employment and accommodation of refugees and IDPs.

1.2 Implementation of priority activities within the social protection sector for the period 2003-2004

According to DPRS Plan for realization (matrix) the Government of Montenegro has adopted several strategic documents and laws within the first phase of realization of the Strategy (end 2003 – 2004). The most important are:

- National Strategy for Permanent Resolving of issue of refugees and IDPs in Montenegro (prepared in 2004, but adopted in 2005)
- Action plan for poverty reduction among Roma people (Roma Inclusion Decade 2005-2015),
- National Action Plan for Children,
- Action Plan for Substance Abuse Prevention among Children and Youth,
- Housing Policy Action Plan (prepared in 2004, and adopted in 2005)
- Law on Pension and Disability Insurance
- Law on War Veterans Disability Protection
- Law on social and child protection
- By-laws for legislation appliance of the above mentioned laws.

In addition, an educative campaign for women health protection and gender equality promotion was conducted.

Social and Child Protection Reform

Particularly important activity was the adoption of the new Law on Social and Child Protection, which should help realize one of the main goals set in the DPRS – better targeting of the social protection beneficiaries.

According to this law some of the rights were restricted in order to introduce more effective assistance to the poor (personal disability allowance, foster-family allowance). Conditions for exercising certain rights have been altered in order to achieve more effective use of the funds (child allowance, allowance for care/assistant services).

The basic rights of social protection, have been outlined in the Law and include the following: access to family support, access to accommodation in a social protection institution or in a family environment, support for covering costs of in-home care, access to health care, coverage of funeral expenses, access to services of social welfare centers, and one-time financial support disbursements.

Special novelty represents the introduction of subsidies for guardian family and this is aimed at providing incentives to families to accept children or other persons into their environment, which would be more favorable type of social care for beneficiaries of social care.

Basic rights arising from the child protection defined by the Law on Social and Child Protection are: outfit for newly born child; child allowance, compensation based on childbirth; wage compensation for part time work hours and rest and recreation of children.

Change of conditions for exercise of right based on child protection and aid and care of other persons is aimed at better targeting and/or to enable that this right is used only by those persons that are in social need which represents break with the previous general principle for exercise of this right. This is the way to implement an important goal of the Development and Poverty Reduction Strategy that refers to rationalization of public revenues use. Special novelty is the change of methodology according to which the amount of right is set and indexed. For example, the right based on family financial support will be set not with regard to net wage but with regard to possibilities of the state budget.

Important step forward in implementation of goals set under the DPRS represents the fact that the new Law enabled participation of private sector in providing of services of social protection. According to this Law, private sector can apply for use of concessions in providing of accommodation, recreation and rest for all beneficiaries of social protection.

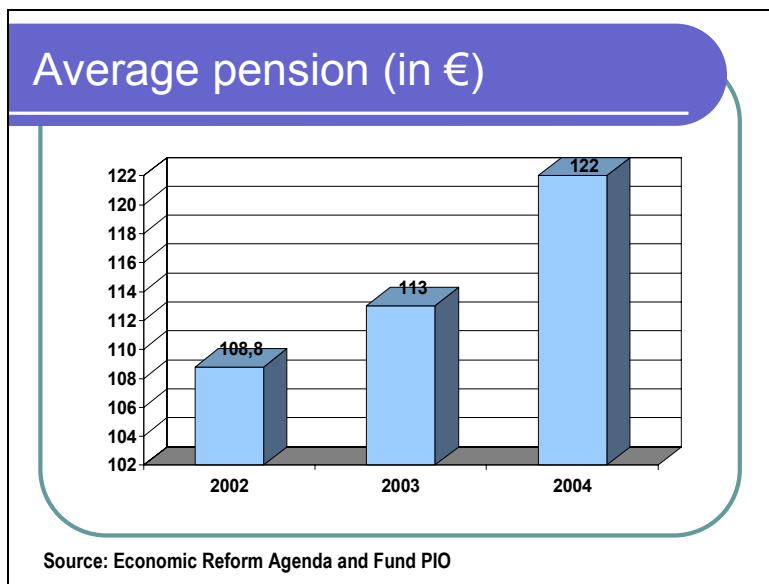
Reforms in the Pension System Area

Pension reform represents an important priority in DPRS. In the first stage of its implementation the emphasis was on continuation of reforms initiated in 2004 when pension system transition process was defined from the so called generational solidarity system (PAY-GO) to so-called three-pillar system.

In accordance with the goals set in the Strategy, reform of the first pillar was implemented in 2004 through implementation of the following measures:

- Increase of retirement age to 60 years for women and 65 years for men,
- Introduction of so-called Swiss indexation, and
- New pension formula based on individual coefficients and increased number of years for pension calculation.

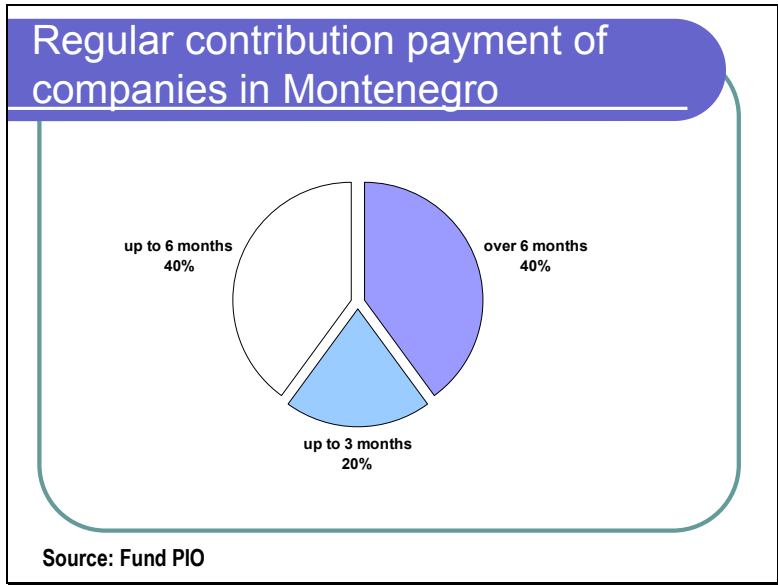
It is particularly important to mention that pension deficit was reduced from 1.1% of GDP in 2002 to 0.9% of GDP in 2004. Preparations of legal framework for introduction of the third pillar of reforms started in 2004.



Graph 17: Average pension in Montenegro in the period 2002-2004.

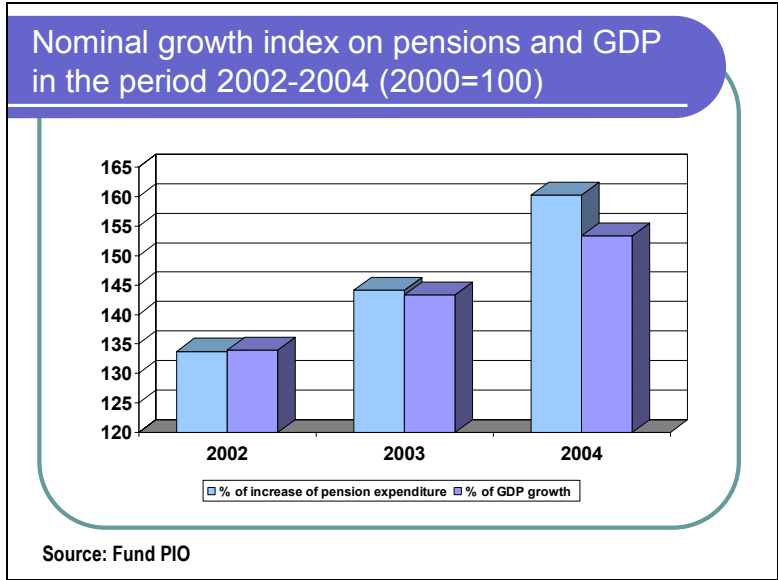
In 2004 contribution rate for pension insurance was reduced from 24% to 21.6%. At the same time, control of payment of contributions was strengthened. As the result, revenues of the Fund PIO increased for 24% in 2004 compared to 2002.¹¹

¹¹ Agenda ekonomskih reformi u Crnoj Gori 2002.-2007.



Graph 18: Regularity of payment of contribution by companies

Administrative and structural reform of the Fund PIO has been initiated. The role of the Fund PIO has been reduced to pension administration and Tax Administration has become the central register of insured persons. The World Bank granted loan (6.5 million US\$) meant for reform of the Fund PIO to make preparations for introduction of the II and III pillar of the pension reform.



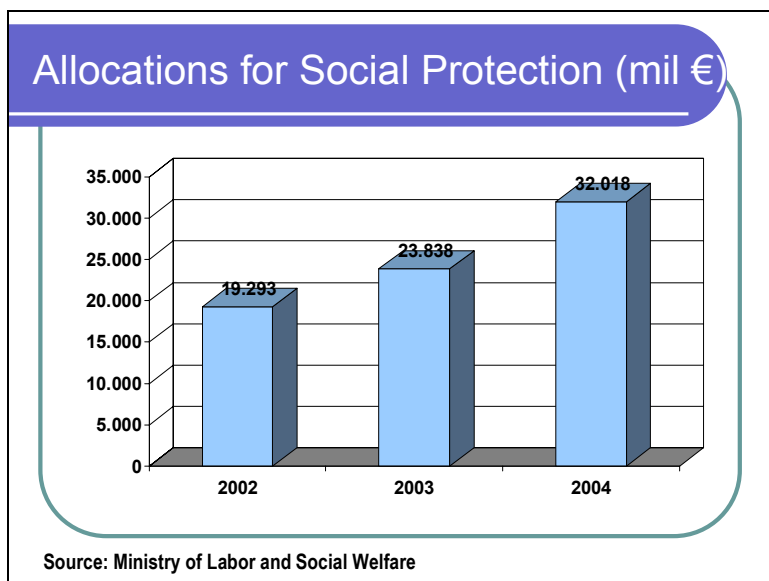
Graph 19: Nominal growth of expenses for pensions as percentage of GDP in the period 2002-2004

Allocations for Social Protection

Payment of social-protection entitlements was the priority for the Government of RM in 2004 and 12 monthly payments were provided. In this manner the Government decided to continue with activities for strengthening of social protection system and placing of the same in the poverty reduction function.

Implementation of the new Law on Social and Child Protection will enable better targeting and higher rationalization of social protection system. It is particularly important in the situation of implementation of transition reforms when the success of all reforms requires efficient functioning of the social protection system and assistance to the poor. Further to this it can be said that the Government of the Republic of Montenegro, in the situation of modest budget resources, presented necessary susceptibility to support poor categories. In the last three years budget funds meant for social and child protection were significantly increased. For example, allocations for social protection in 2002 amounted to about 19 mil € to exceed the amount of 30 mil € in 2004.

It is important to mention that in order to have better targeting of beneficiaries and increase of efficiency of protection and in accordance with priorities of the Development and Poverty Reduction Strategy, in 2004 compared to 2003, there were more budget allocations on behalf of child allowance and family financial support (these are deemed to be the most efficient forms of social protection).



Graph 20: Total allocations for social protection in the period 2002-2004.

Taking into consideration that poverty is more spread out in the northern region of Montenegro, about 40 percent of payments on behalf of child allowance (about 1 million euros) were realized in this area in 2004, and payments on behalf of family financial support were realized in the same percentage (about 3., 4 mil €).

Table 4: Total public consumption on child allowance and family financial support in the period 2003-2004.

CHILD ALLOWANCE					
2003.			2004.		
No. of families	No. of children	Total disbursements	No. of families	No. of children	Total disbursements
6896	12.956	2.452.324,24	7.299	13.919	2.627.542,70
FAMILY FINANCIAL SUPPORT					
2003.			2004.		
No. of families	No. of members	Total disbursements	No. of families	No. of members	Total disbursements
10.117	29.132	7.674.640,28	10.423	30.541	7.982.695,20

RECAPITULATION FOR 2004

CSR	MUNICIPALITY	Child Allowance			Family Financial Support			Aid and Care Allowance					Family Accommodation		
		No. of holders of the right	No of children	Amount	No of families	No of members	Amount	No 60%	Amount	No 100%	Amount	Total number	Total amount	Num ber	Amount
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
Podgorica	1. Podgorica	1.969	3.816	718.140,20	2.452	8.078	2.065.441,88	644	221.790,00	75	59.810	719,1667	281.600,00	86	132.736,00
	2. Cetinje	316	582	110.120,00	388	1.191	266.318,76	167	60.830,00	35	20.780	202,0833	81.610,00	12	18.432,00
	3. Danilov	198	405	75.405,00	302	924	243.100,92	75	27.720,00	11	6.500	85,75	34.220,00	5	7.936,00
	4. Kolašin	97	174	32.675,00	218	478	149.913,11	94	34.200,00	36	22.280	129,75	56.480,00	9	14.336,00
Nikšić	1. Nikšić	1106	2.053	396.247,50	1.372	4.260	1.086.440,42	397	142.800,00	114	68.450	510,75	211.250,00	38	67.450,00
	2. Plužine	42	81	15.490,00	119	267	76.697,38	48	17.280,00	31	18.550	78,91667	35.830,00	0	-
	3. Savnik	28	50	10.000,00	99	180	65.234,70	30	10.860,00	14	8.500	44,33333	19.360,00	2	3.072,00
Bar	1. Bar	209	363	68.615,00	274	742	195.079,00	280	100.950,00	29	17.000	309,4167	117.950,00	13	22.669,00
	2. Ulcinj	173	322	59.665,00	227	541	157.580,90	159	57.210,00	18	10.550	176,5	67.760,00	6	6.000,28
Kotor	1. Kotor	117	213	40.630,00	143	423	112.928,40	134	40.350,00	5	3.000	138,75	43.350,00	4	7.665,21
	2. Tivat	95	167	32.080,00	138	357	103.790,60	87	31.410,00	10	6.000	96,66667	37.410,00	4	7.421,00
	3. Budva	66	104	19.805,00	81	217	63.583,70	46	18.780,00	2	1.200	48,16667	19.980,00	7	10.651,00
Herceg Novi	1. Herceg Novi	250	431	83.070,00	367	866	241.534,54.	114	41.160,00	97	58.050	211,0833	99.210,00	14	21.504,00
Berane	1. Berane	587	1.234	224.095,00	947	2.889	743.376,81	367	132.710,00	17	11.400	383,3333	144.110,00	13	19.456,00
	2. Andriji	57	116	21.790,00	115	294	80.982,90	81	29.070,00	5	3.030	85,75	32.100,00	1	1.536,00
Plav	1. Plav	242	510	93.265,00	473	1.304	356.826,45	126	45.420,00	0	0	126,1667	45.420,00	8	11.385,00
Rožaje	1. Rožaje	416	854	162.295,00	740	2.059	562.992,90	252	90.780,00	36	21.800	288,5	112.580,00	17	26.624,00
B. Polje	1. B. Polje	831	1.612	307.090,00	1.171	3.528	867.823,80	540	195.810,00	141	86.550	680,6667	282.360,00	11	16.256,00
	2. Mojkovac	155	271	50.865,00	229	620	167.917,60	107	38.490,00	22	13.250	129	51.740,00	5	7.296,00
Pijevlja	1. Pijevlja	322	518	98.135,00	468	1.166	311.413,03	501	186.760,00	29	17.350	539,0833	204.110,00	2	3.146,00
	2. Zabljak	26	42	8.065,00	102	160	63.737,40	37	14.460,00	18	10.800	55,41667	25.260,00	0	-
TOTAL		7.299	13.919	2.627.542,70	10.423	30.541	7.982.695,20	4.295	1.538.840,00	744	464.850,00	5.039,00	2.003.690,00	257	405.571,49

Note: Number of beneficiaries of all rights is shown on the average level for 2004

Refugees and internally displaced persons and RAE are included in the social and child protection system. Commissariat for Displaced Persons developed a program of support to these categories. It usually refers to aid for those that are in collective centers. In 2004, the Government of the Republic of Montenegro doubled allocations for these programs (77.923 €) compared to the budget in 2003. In 2003, total support (approved in the balance and off-balance) for these categories amounted to about 162,000 €, and in 2004 it was significantly increased to about 900,000 €. It is for concern that UNHCR significantly reduced its support to these categories - in 2003 it amounted to about 1 mil €, and in 2004 it fell down to about 730.000 €. Support of other international partners for these purposes has also been significantly reduced.¹²

Total amount of compensations to the unemployed persons was also increased. In 2002 it amounted to about 960.000 €, to record an increase in 2004 to about 1.5 million euros.

Indirect Privileges

It is important to emphasize that the system of functioning of public companies recognizes so-called indirect privileges targeted at living cost reduction. Prices of electricity, telephone services and water were subsidized by the economic sector and the budget. For example, the price of electricity for households is twice lower than the price of electricity for the economy and the same applies for prices of telephone services. Although the price of water varies from municipality to municipality, households in average pay 0,37 €/m³ for water and drainage of wastewaters while legal entities pay almost three times more (1,07 €/m³).

1.3 Actions to be Taken in the Forthcoming Period

Continue with Improvement of Efficiency in Provisioning Social Protection

In the period 2000-2005 total expenditures for social protection and insurance (pensions) amounted to about 15% of GDP, which significantly exceeds the average of countries in transition. About 8% of GDP was in average allocated only for social protection (without pensions). This does not include privileges that citizens get through subsidies for prices of electricity, water and telephone. If these privileges are shown in numbers as the system of social protection than total allocations of Montenegro for social protection and insurance would amount to about 20% of GDP which is almost twice more than in developed countries. For that reason it would be necessary to additionally rationalize social protection system by eliminating all types of social payments to unsuccessful companies.

Further to this it is also necessary to:

- Establish system of monitoring and research in social protection system,
- Continuously assess efficiency of social rights,
- Create data base of social protection beneficiaries,
- Promote system of self-support,

¹² Commissariat for Displaced Persons

- Ensure additional tax relieves for private sector and non-government organizations engaged in the sphere of social protection provisioning.

Provide Subsidized Prices of Electricity and Water for the Poorest Categories

Taking into consideration the need to balance fiscal deficit and improve business climate through further reduction of taxes, it will be necessary to continue with rational use of funds meant for social assistance through additional improvement of targeting of beneficiaries. Without bringing into question the need to balance the price of electricity, water and telephone calls in favor of the economy, it will be necessary to develop programs for subsidizing prices of electricity and water for the poorest categories.

Reduce Delays in Payments and Debs Based on Social Transfers

One of the largest problems in functioning of social protection system is delay in carrying out of social transfers. Delays depend on type of right. For example, social transfers for child allowance and family financial support are delayed even for six months and delays are even longer with regard to social transfers for aid and care of other persons. Compensations for maternity leave are delayed for 12 months and pensioners are owed one and a half pension. .

Table 5: Unpaid obligations based on social payments in the period 2003-2004

UNPAID OBLIGATIONS	
2003.	2004.
Child allowance	Child allowance
€ 1.652.478,34	€ 1.772.449,20

UNPAID OBLIGATIONS	
2003.	2004.
Aid and Care Allowance	Aid and Care Allowance
€ 1.508.871,90	€ 1.520.318,80

UNPAID OBLIGATIONS	
2003.	2004.
Family Financial Support	Family Financial Support
€ 3.103.564,71	€ 3.384.622,23

The Government of the Republic of Montenegro adopted a decision that funds received from privatization are primarily used for social protection needs.

Continue Activities on Pension Reform

Further to this it is necessary to:

- Adopt and prepare legal framework for implementation of the II and III pillar of pension reforms,
- Continue with the reform of the Fund PIO,

- Strengthen conditions for obtaining of disability pensions.

Establish the Unit for Poverty Analysis and Monitoring of Policies for its Reduction

Montenegro Economic Reform Agenda 2002-2007 and Development and Poverty Reduction Strategy are two mutually reconciled documents. In view of this, it is necessary that the emphasis in the future implementation of the Development and Poverty Reduction Strategy is put on implementation of measures referring to poverty reduction, particularly to monitoring of implementation of sectoral policies in the area of social protection, health and education.

Further to this it is necessary to transform the current DPRS unit for monitoring and evaluation into the Unit for Poverty Analysis and Monitoring of Policies for its Reduction. The Unit would have the mandate to coordinate defining of policies for reduction of poverty and perform monitoring of implementation.

The Unit would play an important role in the implementation of obligations based on the so-called Millennium Developmental Goals (MDGs). Special task of this Unit would be to develop indicators for poverty reduction. The current indicators are not developed and are based on measuring of consumption and not income.

2 LABOR MARKET

2.1 DPRS Priority Activities

The goals of the labor market strategy are defined through the program “Stimulation of New Employment” adopted by the Government on March 24, 2005 and innovated version of Economic Reform Agenda in Montenegro¹³. The program “Stimulation of New Employment” represents new version of the program “Legalization of Existing Jobs and Job Creation”, which is specified in the Economic Reform Agenda and adopted by the Government in March 20, 2003.

Key goals of the Development and Poverty Reduction Strategy within the area of labor market are:

- Labor legislation reform,
- Stimulation of new employment and
- Development and strengthening of the small and medium-sized enterprises sector.

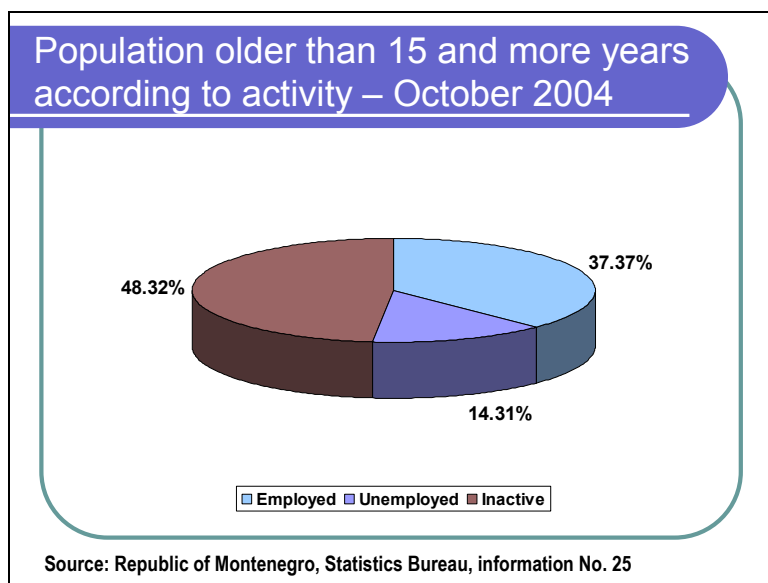
1. Labor Legislation Reform. Reform of the labor market legislation framework (Labor Law, Law on Supervision, Law on Labor Supervision, Law on Employment Record, Law on Strike and Law on Protection on Work) is necessary in order to create preconditions for dynamic growth of employment and greater mobility of labor force, so as to adapt the legal regulations within the labor market area to ILO standards and EU regulations.

2. Encourage new employment. Consistent with the program “Encouraging New Employment” the main goal of inciting employment in Montenegro is to influence the creation of environment that would stimulate new employment, development of entrepreneurship and increase competitiveness of companies and products and raising exports.

Special attention will be given to:

- Stimulating entrepreneurship,
- Increasing the number of work places in Montenegro, primarily in the private sector and
- Enabling new, primarily foreign investments.

¹³ Government of Montenegro 2004. *Economic Reform Agenda in Montenegro 2002-07 – report and recommendation*. Podgorica



Graph 21: Population of Montenegro - 15 and over 15 years of age - according to the activity

The development and strengthening of small and medium-sized enterprises, SMEs should become the leading force in economic development of Montenegro, and thereby in the reduction of poverty through programs that encourage establishing of new enterprises and create new employment, as one of the fundamental generators of economic growth and development.

The Government of the Republic of Montenegro has adopted the “Strategy for Development of Small and Medium-sized Enterprises”. The main strategic courses of development of SMEs are to:

- Increase the number of small and medium-sized enterprises registered in the private sector that officially operate.
- Achieve greater diversity and integration of economic activity by increasing the share of small and medium-sized enterprises that are based on production and non-trading services.
- Significantly increase the share of small and medium-sized enterprises with respect to micro-enterprises in the overall structure of enterprises.
- Increase the competitive activities of small and medium-sized enterprises in the economic sectors in which the Republic of Montenegro depends on imported goods
- Increase the share of small and medium-sized enterprises in the foreign strategic alliances and joint venture arrangements.
- Increase the share of small and medium-sized enterprises in the Gross Domestic Product.
- Increase the share of small and medium-sized enterprises in overall employment.

2.2 Implementation of Priority Activities for the Period 2003 - 2004

In accordance with DPRS priorities, preparations for adoption of important laws regulating labor market (Labor Law, Law on Inspection Control, Law on Labor Inspection, Law on Labor Records (registration), Law on Strike and Law on Protection at Work) are in progress.

Achievement of the set up goals in the labor market that will contribute to higher level of employment and consequently lead to poverty reduction will be accomplished through measures of fiscal and credit policy defined by the Government programs in the labor market and whose implementation has yielded positive results.

Incentives to employment based on Government measures for steering and development of labor market is a successful project that is still in progress. This project will create incentives for tax and administration framework,¹⁴ (with the emphasis on relieves for pension and disability insurance of farmers), for development of entrepreneurship and increase of employment, and/or more efficient legalization of work in “informal sector” both with regard to non-residents and residents. Over the period of implementation of DPRS this project resulted in legalization of about 42.000 jobs.¹⁵ It is likely that this is one of the reasons for fall of unemployment from 24% in 2002 to 22.3% in 2004. Project “Incentives to Employment of Unemployed Persons” is already yielding results in employment of interns with participation of the Employment Fund in financing and professional training of interns. Programs of training, additional training and re-training in several training centers have encompassed over 9.000 unemployed persons since 1999. Within the Program of public works, 57 projects were implemented and 785 unemployed persons recruited since 2004.

Incentives to self-employment and entrepreneurship and development of small and medium size enterprises are implemented through the Program for continuous incentives to employment and entrepreneurship that is being implemented since 1999. Special attention in this program is paid to redundancies and persons that lost their job due to company bankruptcy. These loans are granted to the period of three years with the “grace” period of one year and the amount of loan is €3,000 for every newly opened job. The Program of Banking Support provides loans to unemployed persons, redundancies, small companies and entrepreneurs in order to encourage employment, develop entrepreneurship and improve priority industries.

Project „Incentives to Dynamic Entrepreneurship“ supports the sector of small and medium size enterprises to purchase new technology and create products with the trade mark »Made in Montenegro«, and provide credit lines for financing fast growing companies with purpose to increase exports, development and new employment of labor force.

Government support to activities for increase of competitiveness of domestic products on Montenegrin and foreign market is targeted to increase exports, reduce imports, connect sectors, introduce standards and increase number of jobs. This project is directed to companies in the sector of agriculture (meat industry, bee keeping, collection of plants and forest fruits, fishing and farm establishing), tourism (support to small private hotels and motels and support to development of rural tourism) and wood processing (support to companies dealing with manufacturing of furniture).

Project of establishing of entrepreneurship clubs in primary schools, that is being implemented, represents the beginning of creation of entrepreneurship society. In these clubs students in primary schools are taught to be creative and their entrepreneurship spirit and capacities for teamwork developed.

¹⁴ It implies gradual and complete removal of barriers that create obstacles to employment and business development in Montenegro.

¹⁵ Montenegro Economic Reform Agenda, pg. 36.

2.3 Actions to be Taken in the Forthcoming Period

Adoption of the Employment Strategy in Montenegro is planned with purpose to successfully resolve the unemployment problem.¹⁶ Adoption of the National Program of Protection at Work is also anticipated. Opening of new jobs and increase of company flexibility is the project that is being prepared and is primarily targeted towards resolution of problems of redundancies through measures and activities developed by the Employment Fund. This project also encompasses activities related to business incubators, industry parks, free zones and incentives to investments.

With incentive measures for employers when employing persons with disabilities, by granting micro loans under favorable conditions and construction of protective workshops for persons with disabilities, the Government will encourage increase of employment of these persons and their faster inclusion in social processes.

The goal of establishing of the Fund for Diaspora is strengthening of business cooperation with Montenegrin Diaspora, based on mutual economic interest and establishing of conditions for activation of huge potential of Diaspora in the form of ideas, knowledge and capital and to attract more investments of Diaspora in Montenegro. This activity is being prepared.

Within the project "Incentives to the Successful", two complementary activities are being prepared and/or two forms of promotion of successful companies and entrepreneurs in Montenegro by compiling a list of the most successful companies and proclamation of the entrepreneur of the year on the national and regional level.

Establishing of industrial zones will encourage the opening of new companies that will be offered with modern integral support. Similar activity is the opening of Internet Park and business incubators that would facilitate development of ICT sector. Both of these activities are being prepared.

On the occasion of implementation of all projects, special attention will be given to equal gender treatment, employment of youth and employment of people in undeveloped regions of Montenegro.

¹⁶ Montenegro Economic Reform Agenda, pg. 95.

3 ANTICORRUPTION AND TRANSPARENCY

3.1 DPRS Priority Activities

General goal of all who deal with fight against corruption in Montenegro is to reduce the corruption to the least possible level, to constantly monitor the process and to prevent negative influence of the corruption on social development. Another important goal is creation of conditions for full implementation of standards included in international documents of the Council of Europe and EU in the field of anticorruption, conflict of interests and prevention of money laundering.

This goal can be achieved by:

- Strengthening capacities of bodies competent for fight against corruption. A set of laws and regulations has been lately adopted in Montenegro that is largely reconciled with the international practice and standards. However, full and proper implementation of these regulations requires training of officers and furnishing of institutions in adequate manner, which requires substantial financial resources that are not currently available.
- Increasing the level of information and education of citizens of Montenegro on this problem. Successful resolution of the problem such as corruption requires creation of assumptions for its clear identification and for establishing of appropriate attitude of citizens that corruption is a criminal act both for the one taking bribe and for the one giving it and harmful to the entire social and economic development. In order to improve the situation, constant and strong education campaigns should be carried out whose target group would be all citizens of Montenegro. In addition to public campaigns this problem should be treated through all types of formal and informal education.
- Establishing of solid partnership between public, private and NGO sector in the society. Although all these sectors are willing to cooperate, the cooperation requires establishing of appropriate normative and institutional environment.
- Continuation and strengthening of international cooperation in fight against corruption.

3.2 Implementation of Priority Activities in the Period 2003-2004

In the previous activities on creation of legal framework for fight against corruption, the following laws have been adopted or amended: Law on Public Procurement, Law on Prevention of Money Laundering and Financing of Terrorism, Law on Accounting and Audit – working version, Law on Conflict of Interest, Law on Financing Political Parties, Criminal Code, Law on Criminal Procedure, Law on State Prosecutor, Law on State Employees and Officials, Law on Wages of State Employees and Officials and Law on Witness Protection.

With regard to creation of institutional environment for fight against corruption and organized crime, the following bodies have been established: Administration for Anticorruption Initiative, Administration for Prevention of Money Laundering, Commission for Public Procurement, Commission for Establishing Conflict of Interest and the institute of the Special Prosecutor for Fight Against Organized Crime was established.

In the field of international cooperation excellent cooperation has been achieved with a significant number of relevant international institutions:

- Administration for Anticorruption Initiative is a full member of SPAI initiative for South Eastern Europe,
- Relevant state bodies actively participate in the work of the Third Round Table of the Stability Pact of South Eastern Europe.

Cooperation of the Government and Non Government Organizations has been established in the sphere of fight against corruption and increase of transparency, though those have usually been individual cases without existence of a strategy that would raise the cooperation to the level necessary for efficient fight against corruption and organized crime.

3.3 Actions to be Taken in the Forthcoming Period

Although the set of laws regulating the problem of corruption and organized crime has been significantly enhanced and elaborated, preparation and adoption of the Law on Free Access to Information and the Law on Criminal Responsibility of Legal Entities are still to be prepared and adopted. The need for amendments to already adopted Law on Conflict of Interest, Law on Prevention of Money Laundering and Law on Public Procurement is also recognized. Particularly important activity in the future period is adoption of the Strategy for Fight Against Corruption and Action Plan for its implementation with the necessity for maximum political consensus concerning their adoption.

It is necessary to implement public campaign for fight against corruption that should be implemented by the Government and NGO sector as partners with the objective to increase the level of information on the problem of corruption and increase of level of trust between institutions implementing the project (the Government and NGO sector).

It is necessary to ratify the UN Convention on Fight Against Corruption within the shortest possible period as one of the most significant international documents on which global approach to fight against corruption is based. Following the impending completion of activities for accession to Egmont Group, the Administration for Prevention of Money Laundering will become internationally recognized financial intelligence unit.¹⁷

Key activities, that are shortly to follow, include training of employees in the Administration and obligors that are responsible to report to the Administration as well as upgrade of the data base in accordance with the anticipated amendments to the Law on Prevention of Money Laundering. Complexity of this field also imposes urgent establishing of a coordination body to monitor activities in the field of money laundering, financing of terrorism and corruption.¹⁸

¹⁷ Montenegro Economic Reform Agenda, pg. 152.

¹⁸ Montenegro Economic Reform Agenda, pg. 153.

4 AGRICULTURE

4.1 DPRS Priority Activities

In the area of agriculture there are available resources of approximately 0.80 ha of agriculture or 0.29 ha of cultivable soil per capita, which are not adequately used and they represent one of the main preconditions for the faster development. Long tradition in agriculture business combined with large interest of young entrepreneurs to realize their entrepreneurship ideas exactly in the food production is an important circumstance for this sector. Running behind modern techniques and production technologies for decades, difficult economic situation in the country, fragmented ownership, negligence of the private sector during the previous period, low level of farmer's expert knowledge, poor infrastructure in villages and limitation of the processing capacities are seen to be the main obstacles for faster development of agriculture.

Goals of the Strategy in the Agricultural Sector are to:

- Provide safety of food supply to Montenegrin citizens,
- Meet the needs of tourists in Montenegro,
- Increase exports,
- Increase competitiveness of domestic producers,
- Balanced regional development of Montenegro,
- Develop rural areas,

Inclusion in regional and European integration processes

4.2 Implementation of Priority Activities for the Period 2003-2004

In the set of activities directed towards implementation of DPRS goals particularly important is considered to be the adoption of the Law on Veterinary Practice in February 2004 that created assumptions for health-safe products of animal origin and introduction of their production according to the approach "from stable to table". New Law on Organic Agriculture was adopted and activities on preparation of the accompanying enabling regulations have almost been completed. Implementation of the Decree on Criteria and Manner of Payment of Crude Milk resulted in significant improvement of quality of purchased milk. Construction of the facility of veterinary laboratory¹⁹ is completed and activities for capacity strengthening of the Advisory Office for Plant Production and Office for Cattle Selection are in progress as well as furnishing of veterinary and agricultural inspection.

Reforms in the crediting policy of agriculture have already yielded noticeable results. Loan activity was transferred from the Ministry of Agriculture to banks. The most significant loan support to agriculture and food industry was through implementation of the program "Legalization of the Existing and Opening of New Jobs". Within the five credit lines (family farms in cattle- breeding, plant production, industrially produced chicken and production of poultry meat, blue fish fishing,

¹⁹ Montenegro Economic Reform Agenda 2002. – 2007., pg. 38.

and modernization of the existing and building of new capacities in agro-industry) 154 requests were selected, and banks approved the credit in the amount of over 3 million euros. These programs resulted in opening of 280 new jobs. Through the Directorate for Small and Medium Enterprises, credit support was approved to 5 entities in the amount of 2.3 million euros. Additionally, some Montenegrin commercial banks have started with provision of credit lines for agriculture.²⁰

Several projects for strengthening of capacities in cattle breeding, plant production and bee keeping are in progress. These activities are also followed by strengthening of manufacturing capacities: construction of small factories for drying, processing and packaging of fruit and medical herbs, construction of plant units for production of dairy products of high value, preparing of slaughtering capacities for export and completion of construction of the Distribution center.

Organic agriculture is recognized in Montenegro as important development chance. Education of producers is in progress along with the introduction of legal framework as well as training of inspectors for organic production.

Other important activities in implementation are construction and improvement of rural roads, programs „Young Farmer“ and „Young Marriage Couples in Village“. Particularly important are measures undertaken for improvement of market position of Montenegrin agriculture and providing of assistance for compensation of agricultural damages.

4.3 Actions to be Taken in the Forthcoming Period

Agricultural sector needs to carry out intensive activities on upgrade of legal and regulatory framework. Law on Health Protection of Plants, Law on Seeds, Law on Plants, Law on Wine, Brandy and other Alcohol Drinks will be in focus in the forthcoming period. Special priority is given to production of the Strategy of Agriculture Development and Strategy of Approaching Montenegrin Agriculture and rural Development to EU.²¹ Also important activities in this sphere are redefining of measures on protection of domestic agriculture, where the most important are: removal of non-customs barriers, reconciliation of customs rates with requests of domestic producers and special import tariffs. The goal is to reconcile protection of young Montenegrin agriculture with WTO requests.

With regard to strengthening of institutional framework, preparations for establishing of information system in agriculture are being carried out as well as establishing of Agency for Tobacco. The plan is to work on the reform of partnership and incentives to other types of association of farmers.

Important segment is support to strengthening of competition of Montenegrin agricultural products and exports including providing of subsidies for certain products. Special emphasis is put on production of fish and seafood. Certain activities are to be carried out in this sphere on education of producers on significance of international standards for increase of exports capacity and introduction of quality standards for all agricultural products.

²⁰ Montenegro Economic Reform Agenda 2002.–2007., pg. 38.

²¹ Montenegro Economic Reform Agenda 2002.–2007., pg. 193 i 195.

Innovation activities are prepared with purpose to build trademark for products of organic production: production of unique brand for Montenegrin organic products, establishing of Agency for Inspection Supervision and Certification of Organic Agriculture. Support to programs of organic agricultural production for the forthcoming period will be provided for in the Budget.

Defining and implementation of quality agricultural policy and meaningful implementation of incentive measures require providing of quality statistics. Improvement of statistics on trade is also key to successful negotiations for accession to WTO.

Package of statistical support to agriculture includes:

- Establishing of register of all agricultural producers that will represent the base for all other types of registration and implementation of incentive measures in agriculture,
- Implementation of identification and registration of animals and implementation of system “from stable to table”,
- Establishing of cadastre of agricultural plants, eg. vineyards, olives etc.
- Implementation of system of collection and analysis of market information in agriculture.

5 REGIONAL, RURAL AND URBAN DEVELOPMENT

5.1 DPRS Priority Activities

Goals of DPRS from the regional and rural aspect are reconciled with the document Montenegro Economic Reform Agenda and start from the goals defined under the “Strategy of Regional Development of Montenegro” adopted by the Government of the Republic of Montenegro on March 24, 2005.

Basic goals of DPRS from the aspect of regional and rural development are to:

- Accelerate overall economic development of the Republic through faster development of less developed sub-regions and/or undeveloped regions,
- Create conditions for more dynamic permanent development of less developed areas within their available developmental possibilities and with the support of the Republic. Policy of reducing regional differences in the development level should be kept within the framework.
- Preserve and balance the number of inhabitants in areas at risk, and
- Implement principles of sustainable development and preserve ecological balance.

The following areas have been established based on the existing resources and development level of the region as the basic strategic directions for development of the least developed northern region and reduction of poverty in it:

- Development of transportation, technical and municipal infrastructure that represent a serious cause of poverty in the region,
- Development of social activities (health, education and judicial and other social institutions) that are currently a factor that limits development and staying of population to live in the area and consequently represent the important priority of future development of the region,
- Development of agriculture (farming, cattle-breeding, fruit growing and soil cultivation: mini farms, milk processing, bee keeping, fishing) and revitalization of village based on significant resources of the area,
- Development of sustainable mountain tourism (winter and summer tourism, eco-tourism, sports tourism, agro-tourism, religious tourism, health tourism) and its linking with coastal tourism,
- Development of processing industry and in particular development of entrepreneurship through concept of small and medium enterprises (production of organic health –safe food - biological agriculture, processing of medical herbs and forest fruits, purchase and processing of fruits and vegetables),
- Ecological revitalization of environment and preservation of environment on ecological principles.

5.2 Implementation of Priority Activities in the Period 2003–2004

In line with DPRS, activities in the field of regional rural development targeted at reduction of poverty include policies and measures both on republic and the local level.

Solutions to large problems of road infrastructure are being sought both within development projects of construction of state roads²², and in projects for reconstruction and modernization of regional and main roads. Works on ensuring more reliable electricity supply are in progress with special emphasis on electricity supply to rural settlements that are inhabited throughout the year. Important aspect of regional development is ensuring of regular water supply of southern region and other rural areas of Montenegro, where significant results have been achieved and activities in this field will also continue in the future period. Several projects for improvement of the system in the Thermal Power Plant „Pljevlja“, that are being implemented, will also have positive impact on development in that part of the country.

Improvement of economic situation in rural areas is sought in projects of agricultural development and village revitalization. Specific projects that have already been implemented are as follows: strengthening of small and medium enterprises and organized purchase of agricultural surpluses. Projects of mountain tourism development are in progress and they will activate natural and other significant resources in mountain area (northern region) of Montenegro throughout the year. It is also important to ensure even higher respect for regional development criteria in elaboration and implementation of the overall and regional employment policy and key Government programs in the field.

Local bodies have large responsibilities for development of municipal area and consequently for poverty reduction in their area. Municipalities, primarily those recording negative demographic flows should bring programs for poverty reduction that will establish concept of measures under their competence for development of the area and creation of conditions to stop the process of population reduction. Projects for construction of local roads, construction and maintenance of local water supply and ensuring of more reliable supply with electricity, quality television transmission and telecommunication connections are carried out on local level. Further to this, it is necessary to have better coordination of activities of other sectors for improvement of quality and access to social, health, education and cultural institutions to inhabitants of urban and rural settlements.

5.3 Actions to be Taken in the Forthcoming Period

Institutionalization of problems of regional poor development will be carried out through adoption of the Law on Development of Undeveloped Areas and establishing of a special Fund for Development of Undeveloped Areas.

²² Construction of highway Podgorica - Mateševo has multiple significance:

a.) It represents one of the most significant parts on the future highway Bar - Belgrade that has the significance of the main road for integration of Montenegrin transportation space with the European one and b.) It connects the central part of Montenegro and/or Podgorica with the north of the country, creating assumptions for faster development of the north and at the same time takes off the burden from the road through Platije that, with regard to safety-security aspect and frequency, represents the bottleneck of the road network of Montenegro.

Implementation of economic policy according to sectors will be continued with the existing sources of funds for development enhancement. The policy of faster development of small and medium size companies in the area of less developed regions will be implemented within the framework.

Resolution of problems of transportation, technical, municipal and other infrastructure will remain in the long run the important requirement of regional and overall development and for that reason construction of regional roads will be continued, improvement of electricity supply and water supply, system of removal and disposal of waste etc.

Tax policy will provide for more favorable conditions for development of activity in undeveloped areas. Specific measures will include tax exemptions for a certain period of time to new businesses and newly employed workers, and a possibility will be reviewed to re-allocate a part of funds accrued based on VAT to local self-government on the territory of which it was accrued. Reform of local administration should enable decentralization of competencies in certain segments of development and implementation of regional development policy. Credit-monetary policy will support programs of employment and entrepreneurship in undeveloped regions.

Inclusion of Montenegro in flows of accession to EU will open new possibilities of access to instruments for support of regional development.

6 HOUSING

6.1 DPRS Priority Activities

Out of the principles on which the housing policy will be based, the following are especially important for development and poverty reduction issues: creation of appropriate stable and sustainable institutions and financing mechanisms; social safety net for households with low income, which in fact means existence of public rental (housing) sector; and creation of sustainable housing market.

Goals of the Strategy in the housing area are:

- Establishment of adequate institutional framework and of stable financing mechanisms;
- Development of social housing and of public rental sector;
- Integration of the existing informal settlements in the general urban system and prevention of future illegal construction; and
- Improving the living standard through improving the settlements and maintenance of the housing stock.

Activities regarding housing problems within urban development aiming at poverty alleviation have been defined in accordance with the goals from the “Action Plan on Housing Policy” adopted by the Government of Montenegro in March 31, 2005:

- Building capacities of local self-government to take over responsibilities for the overall social and economic development,
- Building social dialogue among all relevant partners, (NGOs, trade unions, association of employers and the poor) in purpose of improving management and decision-making system,
- Implementation of housing policy in order to ensure free selection of housing problem solution in compliance with financial capability and needs of the household;
- Social safety for the households with low incomes, implying the existence of public rental (housing) sector,
- Adjustment of urban and space planning of infrastructure taking into account problems and needs of the poor.

6.2 Implementation of the Priority Activities for 2003 - 2004

Though significant improvement in this sector requires mobilization of resources to the long run, the projects on social housing construction for the most vulnerable population categories, i.e. for those who cannot buy or rent a flat, have already been underway. The Law on the Condominium significantly contributed to the development of housing market.

Indicative investment plan of the Housing Policy Action Plan (the adoption of which is expected in the first half of 2005) for the period 2005 – 2008 estimated that around EUR 10 million was needed for temporary flats for socially vulnerable households (for app. 1,000 housing units). In addition,

funds needed for construction of around 2,000 new housing units were estimated at around EUR 50 million, and funds needed for improvements in illegal settlements at around EUR 46 million.

6.3 Actions to be Taken in the Forthcoming Period

Reform of legislation framework is underway aiming at ensuring housing facilities for socially marginalized categories and improving tenancy conditions. The Law on Social Housing, the Law on Housing Cooperatives and the Law on Tenancy are in preparation phase.

In this field, housing construction planned for the households with low incomes will be continuously carried out. Other important activity for improving housing conditions relates to prevention of illegal construction and legalization and integration of existing informal settlements into the whole urban system, implying infrastructural development of these settlement and improvement of utility services.

7 TOURISM

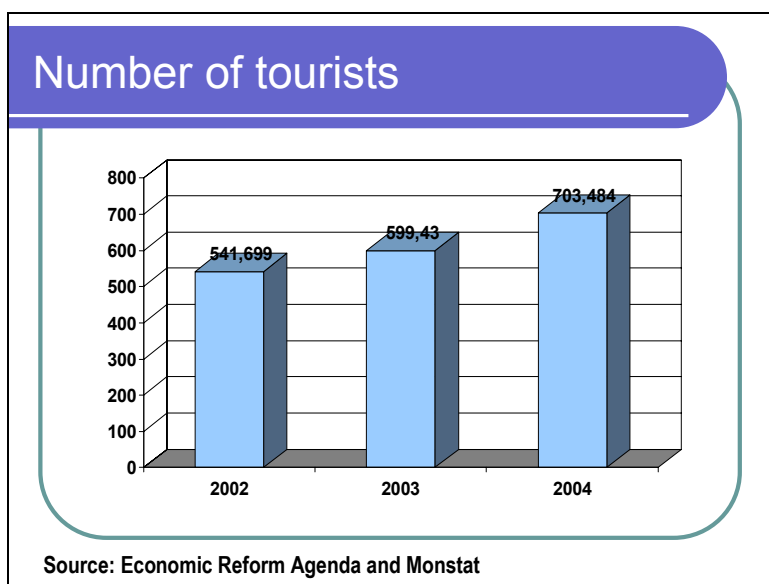
7.1 DPRS Priority Activities

Starting from the attitude that tourism is one of development priorities and pillar of developmental concept of Montenegrin economy, the Government of RM at the end of 2001 adopted the Strategy, and/or Master plan of tourism development by 2020. The Master Plan anticipates increase of hotel capacities from the current 26,000 to 50,000 beds in 2010 and 100,000 beds in 2020, striving to observe the international standards of hotel accommodation that will respond to complex requests of guests from the Western and Central Europe. The plan is to increase the number of overnights from the current 4.4 million to 11.4 million in 2010 and/or to 20.9 million overnights in 2020. Directly or indirectly, 75,000 new jobs will be opened based on tourism.

The assessment of the World Tourism and Travel Council (WTTC) is that the share of tourism in creation of gross domestic product in 2004 was 15% while the overall income was 214.7 million euros. WTTC estimated capital investments in 2004 into Montenegrin broader economy generated by tourism to 36.7 million euros or 19% of total investments. Furthermore, WTTC anticipates growth of 10.3% per annum in overall demand of travels and tourism, which, if realized, will make Montenegro the country with tourist economy developing at fastest rate in the entire world in the following decade.

The Government of the Republic of Montenegro and Ministry of Tourism are implementing regular activities on the plan of establishing business relations with foreign partners on permanent bases through investment of capital in tourist capacities. Basic priorities in the tourism development policy of Montenegro are fast privatization and creation of assumptions for direct foreign investments.

Basic goal of DPRS taken over from the Master Plan is creation of sustainable tourist product that would result in gradual increase of number of guests, accelerated increase of revenues and opening of new jobs.



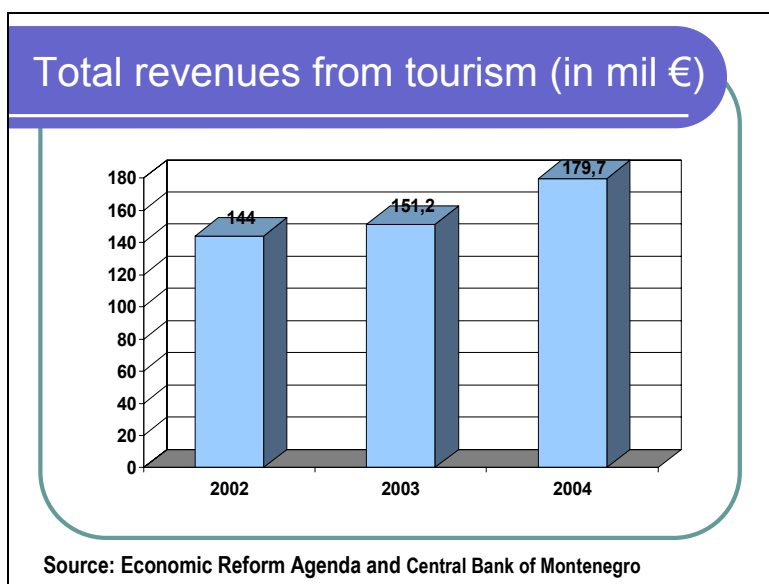
Graph 22: Number of tourists in Montenegro in 2002-2004.

7.2 Implementation of the Priority Activities for the Period 2003 – 2004

According to DPRS priorities, activities on preparation of the Strategy for integral management of coastal zone for Montenegro are in progress and preparation of the Strategy for development of nautical tourism is planned in 2005. Preparation of the remaining, more than 30 enabling regulations, rules and registries that should enable full implementation of the Law on Tourism adopted in 2002 continues. Law on Tourist Organizations and Law on Temporary Residence Fee were adopted in 2004. Preparations for adoption of amendments to this law are almost brought to the end. The Council for Tourism was established as the broadest institutional framework for running the tourism policy. Ministry of Tourism supports establishing of local tourist organizations - 12 have been established so far and in four municipalities the procedure of establishing is almost completed.

Privatization of a part of hotel capacities is already completed, several tenders have been announced and some are being prepared. Cooperation with the Employment Fund and Directorate for Small and Medium Size Enterprises on providing credit lines for tourist companies has been continued. The project of establishing and putting together quality offer in private accommodation will make this segment more interesting for the demanding foreign market.

Project of adoption of the World Tourist Organization (WTO) symbol system started with putting up of tourist signage on main roads and in main tourist municipalities and activities also continue in other cities. Measures for cleaning and space organization and campaign for improvement of beach quality are in progress in cooperation with local communities.



Graph 23: Total income obtained in tourism in 200-2004.

7.3 Actions to be Taken in the Forthcoming Period

Special Coastal Zone Plan is being prepared and it will make the problem of spatial development of coastal zone understandable. Adoption of Rules on Classification, minimum requirements and

categorization of hotels and restaurants is in progress. Activities for meeting of requirements for full membership to WTO continue.

Implementation of projects for strengthening of specific forms of tourism such as rural tourism, nautical tourism, health tourism, cultural tourism, construction of golf playground and eco tourism will contribute to diversification of tourist product.

Support to strengthening of sustainable tourism in the north of the country will be implemented in the following period by providing loans and donations and providing of technical assistance to small and micro companies and larger investments in preservation of protected areas. Promotion programs will be implemented for specialized activities such as rafting, mountain climbing, paragliding etc.²³ It is necessary to take into account the needs of tourism in the entire country when establishing priorities for infrastructure development.

Analysis of the possibility to amend the VAT Law is in progress in order to enable the sector of tourism to treat foreign turnover as exports, which is in accordance with practice of many countries and should result in removal or reduction of VAT rate on this category of tourism turnover

The ongoing marketing campaign for promotion of Montenegrin tourism should be continued and extended particularly to Western Europe markets and within these activities promotion of national trademark that would contribute to clearer image of Montenegro abroad should be developed and implemented.

Preparations for modernization of education programs at University and high schools educating staff to work in tourism are in progress.

²³ Montenegro Economic Reform Agenada 2002 – 2007, pg. 183.

8 TRANSPORT

8.1 DPRS Priority Activities

Fundamental principles of the new transport policy include efficiency, access to transport services and networks, and support to sustainable economic development. Moreover, the transport policy will be based on the principle of equal and equitable distribution of benefits from transport interventions among all segments of the society.

Strategic objectives of the transport sector:

- The integration in the European transport network (trans-European corridors V or X),
- Upgrading of links with countries in the region, and creating of an efficient transport system.

The Strategy objectives are:

- Create conditions for transport sector development and enhance transport efficiency and safety
- To upgrade the road infrastructure and its maintenance, primarily in the northern region and
- To start harmonizing domestic legislation and regulations with the EU one.

8.2 Implementation of Priority Activities for 2003 - 2004

According to the DPRS prioritization, in previous period a great attention has been paid to preparation of new legislations for all transport branches. The Law on Railway and the Law on Roads have been completed while the Law on Road Transport is in adoption procedure. In compliance with legislation the State Road Directorate has been established.²⁴ The Government has constituted The Maritime Safety Directorate. In addition, the reconstruction and modernization of the airport have started, while considerable, though insufficient, funds have been invested in the maintenance and reconstruction of roads.

8.3 A Actions to be Taken in the Forthcoming Period

Among projects related to sector policy, regulations and management, it was assessed that the following are of high priority: preparation of transport strategy, primarily preparation of the Road Infrastructure Development Strategy²⁵, Railway Infrastructure Development Strategy and the Strategy on the privatization of Railways of Montenegro.²⁶ Series of new legislations within railway and maritime transport as well as improvement of management and increase in efficiency in

²⁴ Economic Reform Agenda in Montenegro, 2002. – 2007, page 230.

²⁵ Economic Reform Agenda in Montenegro, 2002. – 2007, page 231.

²⁶ Economic Reform Agenda in Montenegro, 2002. – 2007, page 234.

