

Republic of Serbia

Rating report

Rating rationale

Robust medium-term growth, favourable FDI prospects, and strengthened external metrics: Serbia's economy has demonstrated improved resilience to external shocks, bolstered by a well-established macroeconomic policy framework. The medium-term growth outlook for Serbia's small, open economy is supported by significant FDI in tradable sectors and expanded public investments in infrastructure projects. This trend facilitates continued reserve accumulation, despite structural current account deficits.

Moderate public debt and effective fiscal policies: Serbia's budget performance is characterised by effective budget management, combined with high capital spending. We expect moderate primary deficits, structural reform progress in the state-owned entities sector, and a gradual downward debt trajectory.

Political and governance challenges: The EU accession negotiations for Serbia have encountered obstacles due to legislative inefficiencies and durable tensions with Kosovo. Challenges surrounding the early parliamentary elections in December 2023 underscore the necessity for further reforms in governance. However, the recently signed lithium deal with the EU will not only boost FDI inflows but can also support the overall relationship with the EU.

Rating challenges: i) elevated external vulnerabilities due to high external debt and a prevalence of foreign currency in the financial sector, encompassing public and private debt; and ii) institutional weaknesses and geopolitical complexities associated with Serbia's EU membership aspirations.

Figure 1: Serbia's sovereign rating drivers

| Risk pillars | Quantitative | | Reserve currency* | Political risk** | Qualitative*** | Final rating | |
|-------------------------------------|-----------------------|-------------------|-------------------|------------------|----------------|--------------|---|
| | Weight | Indicative rating | Notches | Notches | Notches | | |
| Domestic economic risk | 35% | bbb | RSD [+0] | Serbia [-1] | 1/3 | BB+ | |
| Public finance risk | 20% | aaa | | | 0 | | |
| External economic risk | 10% | cc | | | - 1/3 | | |
| Financial stability risk | 10% | aaa | | | - 1/3 | | |
| ESG risk | Environmental factors | 5% | | | b- | | 0 |
| | Social factors | 7.5% | | | bb- | | 0 |
| | Governance factors | 12.5% | b+ | -1/3 | | | |
| Sovereign Quantitative Model | bbb- | | | -1 | | | |
| Additional considerations | | | | 0 | | | |

*The reserve-currency quantitative adjustment applies to currencies in the IMF's Special Drawing Rights (SDR) basket.

**The political-risk quantitative adjustment is based on the World Bank's Political Stability & Absence of Violence/Terrorism index.

***The qualitative scorecard analyst adjustments, capped at one notch per rating pillar, are weighted equally with an aggregate adjustment rounded to the nearest integer. For details, please see Scope's [Sovereign Rating Methodology](#). Source: Scope Ratings.

Foreign currency

Long-term issuer rating/Outlook

BB+/Positive

Senior unsecured debt

BB+/ Positive

Short-term issuer rating/Outlook

S-3/ Positive

Local currency

Long-term issuer rating/Outlook

BB+/ Positive

Senior unsecured debt

BB+/ Positive

Short-term issuer rating/Outlook

S-3/ Positive

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Credit strengths and challenges

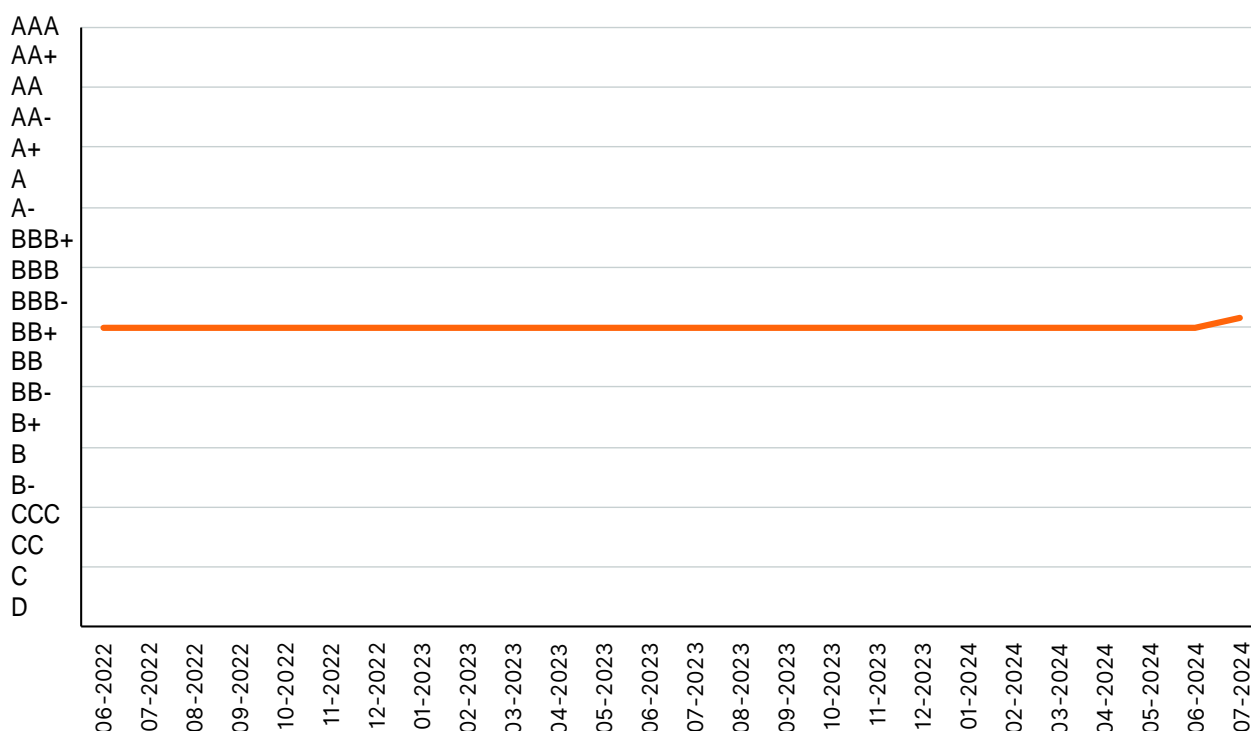
| Credit strengths | Credit challenges |
|--|--|
| <ul style="list-style-type: none"> Well-established macroeconomic policy framework with a good record of sustained and balanced growth rates Moderate public debt, efficient budget management | <ul style="list-style-type: none"> Elevated external vulnerabilities due to high external debt and high FX share of debt Institutional weaknesses, slow progress on structural reforms |

Outlook and rating triggers

The Positive Outlook reflects Scope’s view that risks to the ratings are skewed to the upside over the coming 12 to 18 months.

| Positive rating-change drivers | Negative rating-change drivers |
|---|---|
| <ul style="list-style-type: none"> Debt/GDP ratio set on a firm downward trajectory over the medium run External position further strengthened, due to robust exports or increased net FDI inflows Governance and/or political risks eased, resulting in material progress towards accession to the EU | <ul style="list-style-type: none"> Steady increase in debt/GDP ratio in the medium run Increase in external vulnerabilities weighing on reserve adequacy Governance and/or political risks increased, affecting the quality and predictability of policymaking |

Figure 2: Rating history¹



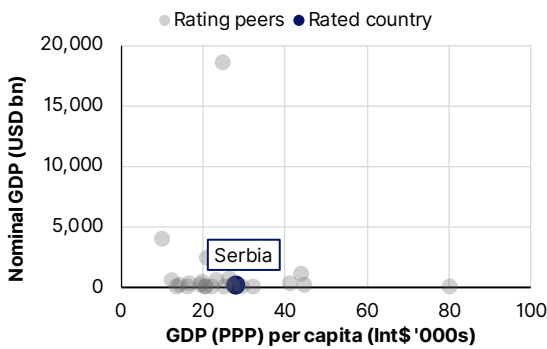
¹Foreign-currency long-term issuer rating. Positive/Negative Outlooks are treated with a +/-0.33-notch adjustment. Credit Watch positive/negative with a +/-0.67-notch adjustment. Source: Scope Ratings.

Domestic economic risk

Overview of Scope's assessments of Serbia's Domestic Economic Risk

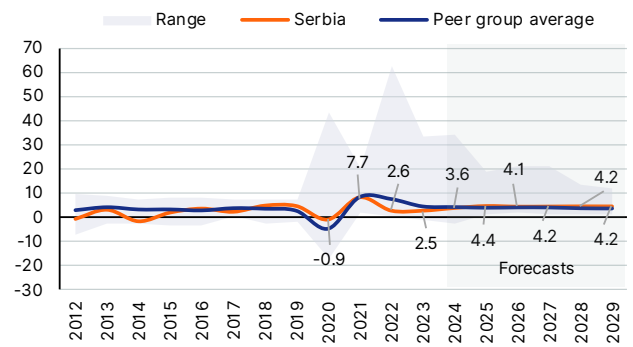
| SQM* indicative rating | Analytical component | Assessment | Notch adjustment | Rationale |
|------------------------|--|------------|------------------|--|
| bbb | Growth potential and outlook | Strong | +1/3 | Solid medium-run growth potential of 4.0%, supported by steady net FDI |
| | Monetary policy framework | Neutral | 0 | Pre-crisis record of managed inflation, adequate monetary policy |
| | Macroeconomic stability and sustainability | Neutral | 0 | Improved macro-economic stability, but relatively low domestic savings |

Figure 3: Nominal GDP and GDP per capita



Source: IMF World Economic Outlook (WEO), Scope Ratings

Figure 4: Real GDP growth, %



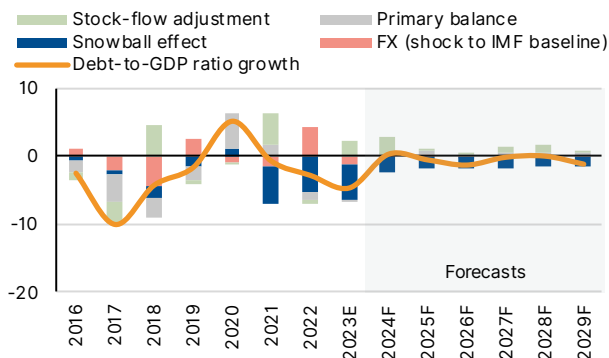
Source: IMF WEO, Scope Ratings forecasts

Public Finance Risk

Overview of Scope's assessments of Serbia's Public Finance Risk

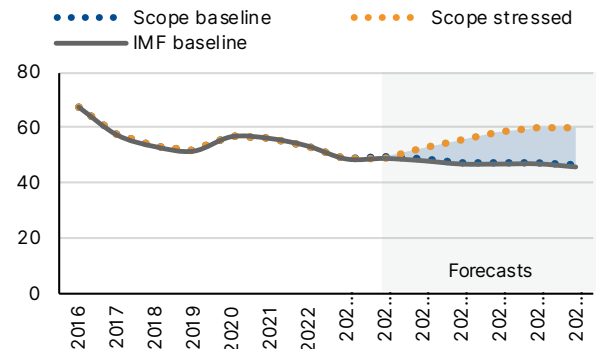
| SQM indicative rating | Analytical component | Assessment | Notch adjustment | Rationale |
|-----------------------|--------------------------------|------------|------------------|--|
| aaa | Fiscal policy framework | Neutral | 0 | Pre-crisis record of fiscal prudence; development of new fiscal-rules framework and ongoing IMF policy support anchor fiscal discipline; high public investments |
| | Long-term debt trajectory | Neutral | 0 | Stable debt trajectory over medium run, but exposure to significant exchange-rate risk |
| | Debt profile and market access | Neutral | 0 | Long maturities and high share of multilateral, institutional debtholders but elevated share of FX debt |

Figure 5: Contributions to change in debt levels, pps of GDP



Source: IMF WEO, Scope Ratings forecasts

Figure 6: Debt-to-GDP forecasts, % of GDP



Source: IMF WEO, Scope Ratings forecasts

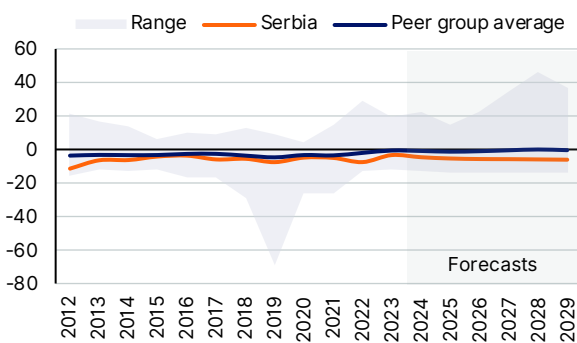
*Sovereign Quantitative Model.

External economic risk

Overview of Scope's assessments of Serbia's External Economic Risk

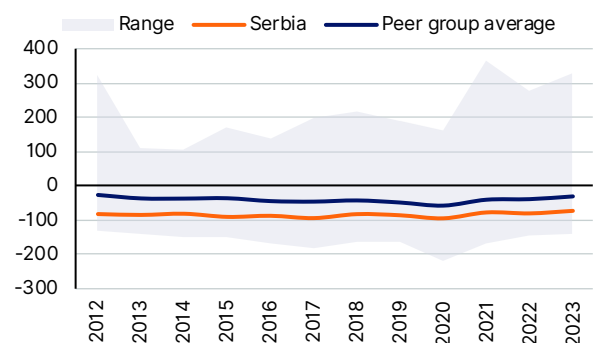
| SQM indicative rating | Analytical component | Assessment | Notch adjustment | Rationale |
|-----------------------|--|------------|------------------|--|
| CC | Current account resilience | Neutral | 0 | High investment needs with low domestic savings |
| | External debt structure | Neutral | 0 | Current account deficits are largely financed by FDI inflows |
| | Resilience to short-term external shocks | Weak | -1/3 | Good reserve adequacy; small, open economy |

Figure 7: Current-account balance, % of GDP



Source: IMF WEO, Scope Ratings

Figure 8: Net international investment position (NIIP), % GDP



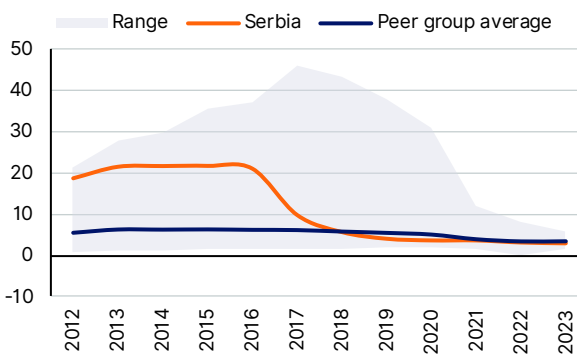
Source: IMF, Scope Ratings

Financial stability risk

Overview of Scope's assessments of Serbia's Financial Stability Risk

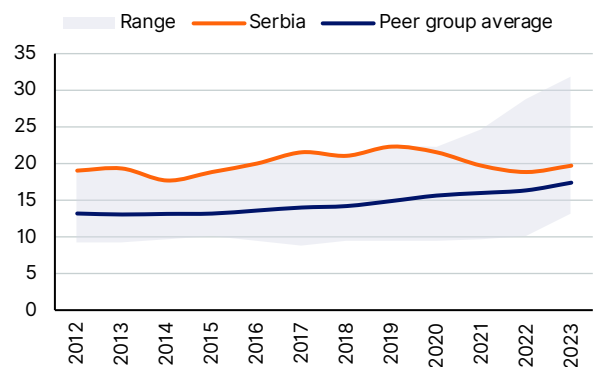
| SQM indicative rating | Analytical component | Assessment | Notch adjustment | Rationale |
|-----------------------|---|------------|------------------|--|
| aaa | Banking sector performance | Neutral | 0 | Mostly foreign-owned, well-capitalised and liquid banking sector; low contingent liability risk to the sovereign balance sheet |
| | Financial sector oversight and governance | Neutral | 0 | Conservative banking framework, macroprudential tools framework regarded as 'equivalent' to the EU one |
| | Financial imbalances | Weak | -1/3 | High euroization of deposits and loans (at around 50% of the total) represents a financial stability concern |

Figure 9: Non-performing loans, % of total loans



Source: World Bank (WB), Scope Ratings

Figure 10: Tier 1 capital, % of risk-weighted assets



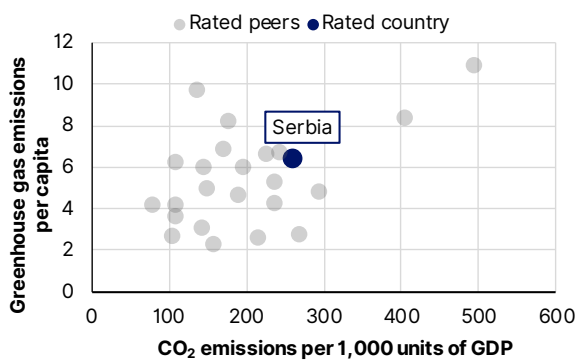
Source: IMF, Scope Ratings

Environmental, Social and Governance (ESG) risk

Overview of Scope's assessments of Serbia's ESG risk

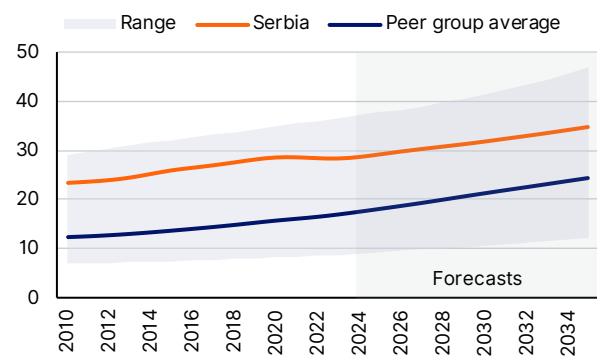
| SQM indicative rating | Analytical component | Assessment | Notch adjustment | Rationale |
|-----------------------|-----------------------|------------|------------------|---|
| b+ | Environmental factors | Neutral | 0 | Increasing reliance on renewable energy sources; still elevated energy reliance on coal |
| | Social factors | Neutral | 0 | An ageing population and elevated youth unemployment constrain labour supply |
| | Governance factors | Weak | -1/3 | Serbia advances slowly EU accession reforms; lack of tangible progress towards a sustainable settlement with Kosovo |

Figure 11: CO₂ emissions per GDP, mtCO₂e



Source: European Commission (EC), Scope Ratings

Figure 12: Old-age dependency ratio, %



Source: United Nations (UN), Scope Ratings

Reserve-currency adjustment

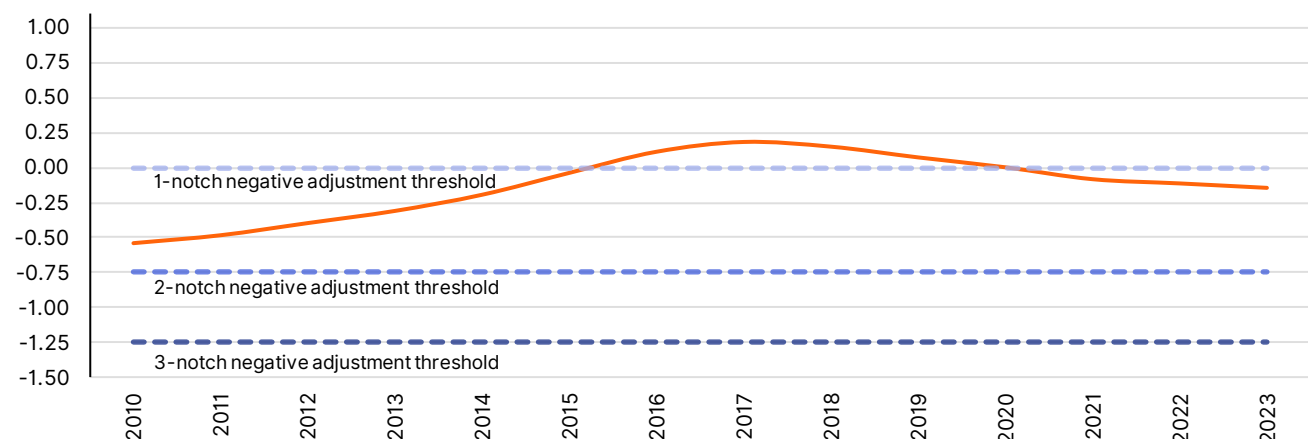
Figure 13: IMF SDR basket and Scope reserve-currency adjustment

| Currency | U.S. dollar | Euro | Chinese yuan | Japanese yen | Pound sterling | Other |
|------------------------------|-------------|------|--------------|--------------|----------------|-------|
| IMF SDR basket weights, % | 43.4 | 29.3 | 12.3 | 7.6 | 7.4 | 0.0 |
| Positive adjustment, notches | 3 | 1 | 1 | 1 | 1 | 0 |

Source: IMF, Scope Ratings

Political-risk adjustment

Figure 14: WB Political Stability & Absence of Violence/Terrorism index, Serbia, 3-year moving average



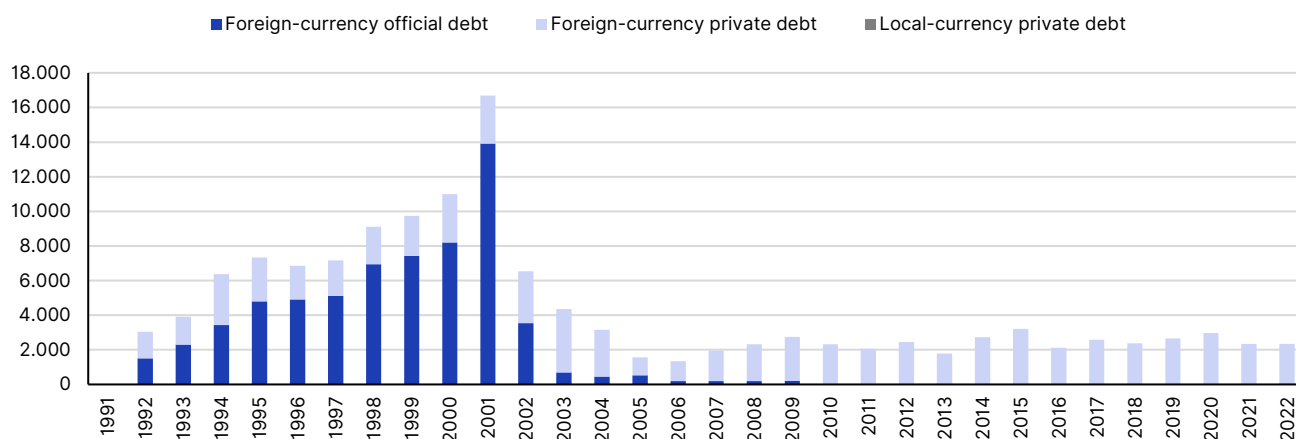
Source: WB, Scope Ratings

Additional considerations

No adjustment was applied to the rating from additional considerations.

Appendix I. Sovereign default history

Figure 15: Sovereign default history, USD m



Depicted private-debt defaults may not always constitute a credit event under [Scope's credit-rating definitions](#).
 Source: [Bank of Canada-Bank of England Sovereign Default Database](#), Scope Ratings

Appendix II. Rating peers

Rating peers are related to sovereigns with an indicative rating in the same rating category or adjacent categories, as assigned by Scope's sovereign quantitative model after accounting for methodological reserve-currency and political-risk adjustments.

| Peer group* |
|-------------|
| China |
| Georgia |
| Greece |
| Turkey |

*Publicly-rated sovereigns only; the full sample of sovereign-rating peers may be larger.

Appendix III. Economic development and default indicators

| | |
|---|--|
| IMF Development Classification | Emerging market and developing economy |
| 5y USD CDS spread (bp) as of 22 July 2024 | 207 |

Appendix IV. Statistical table for selected SQM indicators

This table presents a selection of the indicators (24 out of 30 – with the governance indicator reflecting a composite of five indicators) used in Scope's quantitative model, in line with Scope's Sovereign Rating Methodology. The metrics and sources for the data presented here ensure comparability across global country peers and may therefore differ from data from national and other select international statistical series.

| Pillar | Core variable | Source | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|---------------------|--|--------|-------|-------|-------|-------|-------|------|
| Domestic Economic | GDP per capita (PPP) , Int\$ '000s | IMF | 17.9 | 19.1 | 19.3 | 21.9 | 24.7 | 26.3 |
| | Nominal GDP , USD bn | IMF | 51 | 52 | 53 | 63 | 64 | 75 |
| | Real growth , % | IMF | 4.5 | 4.3 | -0.9 | 7.7 | 2.6 | 2.5 |
| | CPI inflation , % | IMF | 2.0 | 1.8 | 1.6 | 4.1 | 12.0 | 12.4 |
| | Unemployment rate , % | WB | 12.7 | 10.4 | 9.0 | 10.1 | 8.7 | 8.7 |
| Public Finance | Public debt , % of GDP | IMF | 53.3 | 51.7 | 56.9 | 56.2 | 53.5 | 48.9 |
| | Net interest payment , % of government revenue | IMF | 5.2 | 4.8 | 4.9 | 4.0 | 3.5 | 4.3 |
| | Primary balance , % of GDP | IMF | 3.0 | 2.0 | -5.2 | -1.6 | 1.4 | 0.5 |
| External Economic | Current-account balance , % of GDP | IMF | -4.8 | -6.9 | -4.1 | -4.3 | -6.9 | -2.6 |
| | Total reserves , months of imports | WB | 4.7 | 5.2 | 6.1 | 5.3 | 4.8 | 6.2 |
| | NIIP , % of GDP | IMF | -84.9 | -88.3 | -97.2 | -79.9 | -82.7 | - |
| Financial Stability | NPL ratio , % of total loans | IMF | 5.7 | 4.1 | 3.7 | 3.7 | 3.2 | 3.0 |
| | Tier 1 ratio , % of risk-weighted assets | IMF | 21.8 | 21.1 | 21.9 | 21.4 | 18.9 | 19.2 |
| | Credit to the private sector , % of GDP | WB | 41.4 | 42.0 | 45.5 | 43.4 | 40.3 | 35.8 |
| ESG | CO₂ per EUR 1,000 of GDP , mtCO ₂ e | EC | 360.6 | 350.9 | 348.8 | 330.4 | 320.3 | - |
| | Income share of bottom 50% , % | WID | 17.0 | 17.1 | 16.9 | 18.2 | 18.1 | - |
| | Labour-force participation rate , % | WB | 68.2 | 68.4 | 68.0 | 72.0 | 73.2 | - |
| | Old-age dependency ratio , % | UN | 27.5 | 28.1 | 28.5 | 28.5 | 28.4 | 28.3 |
| | Composite governance indicators* | WB | -0.1 | -0.1 | -0.1 | -0.1 | -0.1 | - |
| | Political stability , index | WB | 0.0 | -0.1 | -0.2 | -0.1 | -0.2 | - |

*Average of the following five World Bank Worldwide Governance Indicators: *Control of Corruption, Voice and Accountability, Rule of Law, Government Effectiveness, Regulatory Quality*.

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