

# Serbia-Montenegro

<b>Status Index</b> (Democracy: 3.6 / Market Economy: 2.9)		<b>6.5</b>	<b>Management Index</b>		<b>6.6</b>
<b>System of government</b>	Parliamentary-presidential democracy		<b>Population</b>		8.6 mill. <sup>b</sup>
<b>Voter turnout</b>	70.5 % (2002)		<b>GDP p. c. (\$, PPP)</b>		-
<b>Women in Parliament</b>	12.8 % (Serbien)		<b>Unemployment rate</b>		27.9 % <sup>b</sup>
	10.6 % (Montenegro)		<b>HDI</b>		0.728 (1996)
<b>Population growth</b>	0.6 %		<b>UN-Education Index</b>		-
<b>Largest ethnic minority</b>	16.4 % (1991)		<b>Gini-Index</b>		33.5

Figures for 2001 – if not indicated otherwise. <sup>a)</sup> Annual growth between 1975 and 2001. <sup>b</sup> not including Kosovo. Sources: Wiener Institut für Internationale Wirtschaftsvergleiche, Juli 2002. Transition Report update Mai 2003. Economic Survey of Europe, 2002. UNDP: Yugoslavia 1997. UNDP: Human Development Report 2003. The Economist Intelligence Unit.

## 1. Introduction

The key to understanding the political, social and economic processes in the Federal Republic of Yugoslavia (FRY), the two-member federation of Serbia and Montenegro, lies in the dissolution of the Socialist Federal Republic of Yugoslavia (SFRY) in June 1991. The break-up was caused more by internal rather than external forces. It was closely linked with policies of the Communist elite in the Yugoslav republics and autonomous provinces who were willing to do anything to remain in power, including committing acts of war. The SFRY's modernization crisis came to light in the late 1980s. At the same time, political oligarchies of the component republics wanted to avoid democratization and replace it with nationalism. The state of Yugoslavia broke up after Slovenia and Croatia declared their independence and were recognized by the European Union. The Federal Republic of Yugoslavia, consisting of Serbia and Montenegro, was proclaimed in April 1992.

On October 5, 2000, Slobodan Milosevic was forced to resign as President of the FRY following democratic federal elections. After initially trying to manipulate and defy the results, Milosevic was forced to submit to the rules of democracy after days of mass protests. These were nothing short of a national uprising, which security forces did not take action against. New leaders, who had united to create the Democratic Opposition of Serbia (DOS), took control and replaced the parties that supported Milosevic. The DOS was led by Vojislav Kostunica, the newly elected president of the FRY, and Zoran Djindjic, who became prime minister of Serbia after the DOS won a sweeping victory in parliamentary elections in Serbia on December 23, 2000.

To a large extent, the evaluation period covers the legislative period of Prime Minister Djindjic, which ended prematurely with his assassination on March 12, 2003. It also covers Kostunica's term as president of the FRY, which ended when he resigned from office on March 3, 2003 after the State Union of Serbia and Montenegro was declared on February 4, 2003.

## **2. History and characteristics of transformation**

Politicians in the former Yugoslavia (the SFRY) had been constantly promising political reforms since 1984, but delivered none. The last government (1989–1991) also failed in this, because there were very few political leaders at all the levels of government who would have been interested in reform and would have been convinced enough to be willing to institute it. The introduction of the multi-party system in 1990 can also be viewed in this context. This occurred in each of Yugoslavia's republics independent from and actually against the federal state. There were no elections at the federal level in 1990. This contributed to the momentum for dissolution of the SFRY by depriving citizens a chance to express their political wishes as members of the Yugoslav political community.

The FRY's political, economic and social transformation was decided by the fact that the dissolution of the SFRY raised the Serbian national question without offering conditions for solving the Albanian national question at the same time. Approximately one-third to one-fourth of the ethnic Serb population remain internally displaced in Croatia and Bosnia-Herzegovina, while government ties to Serbia, which had existed since 1918, were severed. On the other hand, the population in Serbia reflected the problematic structure of the SFRY in its national composition. More than one-third of Serbia's citizens belonged to minority communities until June 1999. The most important minority was the ethnic Albanian community in Kosovo.

Those factions of the Communist oligarchy in Serbia that came to power in 1987 under the leadership of Slobodan Milosevic took advantage of this complex situation by manipulating the Serbian national question to achieve their goals. Instead of converting the state-controlled economy into a market economy and the authoritarian system into a democratic, pluralistic political system, the FRY's entire post-Communist development was limited to the national question. The country's policies and society were influenced by Milosevic and his rules of the game, even though political protests were continually being organized (for example, in the winter of 1996/1997). That is what shaped the Serbian and Yugoslav politics and continues to shape them today. The FRY, unlike other former Communist countries in Central and Eastern Europe, had not begun the structural transformation of the authoritarian political system and controlled economy before the Milosevic government's downfall in the fall of 2000. The fact that there was no fundamental consensus in either Serbia or Montenegro about the

government or about the set of values on which society and the political community should be based was also crucial. In addition, there were many gaps in constitutional and legal arrangements between the republics and the federal government. Constitutional institutions did not have actual power. Instead, power was concentrated in the hands of informal groups. The relative importance of constitutional competences is reflected in the fact that until October 2000, power simply rested with Milosevic. Until 1997, the Serb presidency was the most powerful position in all of Yugoslavia because Milosevic was the president of Serbia. After 1997, power shifted to federal presidency without a constitutional amendment because Milosevic held this office.

As far as economic reforms and social economic development are concerned, a change in property ownership rules began in the late 1980s, before solidifying in the early 1990s. In the course of the SFRY's disintegration process, each republic later passed its own laws regarding privatization (Serbia in August 1991 and Montenegro in January 1992). At first, development leaned toward the privatization of state-owned companies and the establishment of private companies in both republics. However, political processes changed the transformation and privatization processes dramatically in the early 1990s. The dissolution of the country, civil war and UN sanctions led to a drastic deterioration in economic conditions. Meanwhile, the old elite clung to power and blocked the entire transformation process. It is true that there was a large increase in the number of private companies, but at the same time there was also counter-development. Political leaders nationalized the most important economic areas and brought a majority of the remaining big companies and banks under their control. This ensured their control of the economy and the continued existence of the most important characteristic features of the socialist system.

Studies conducted in the FRY show support for democratic values had doubled between 1993 and 1998. In 1998, twice as many Serbians and Montenegrins had no confidence in their president, the government and the political system than in the other former Communist countries. Nevertheless, in the fall of 2000 the country had not begun its transformation from an authoritarian system and a controlled economy. The baseline situation for this was extremely unfavorable. The economy was in a deep slump, the people were impoverished and there were hardly any concrete starting points for the introduction of democratic, constitutional conditions.

### **3. Examination of criteria for democracy and a market economy**

#### **3.1 Democracy**

The FRY has made progress in transforming the political regime in some of the evaluated areas. However, it is still a defective democratic system with

transformation deficits in the areas of state identity, political participation and rule of law.

### **3.1.1 Political regime**

(1) *Stateness*: The issue of national state identity remains unclear. Power structures have not been sufficiently established and developed. The constitutional and legal arrangement between the republics and the federal government is full of gaps. The state's monopoly on the use of force has prevailed in the central areas of the country, but the southern province of Kosovo remains under the interim administration of the United Nations Resolution 1244. A multinational peacekeeping operation (Kosovo Force or KFOR), established under the Kumanovo agreement, is the chief force for maintaining law and order.

There is no fundamental agreement on who qualifies as a citizen of the state. However, there is consensus in both partial republics on the inclusion of the republic population. With the exception of Kosovo, whose citizens enjoy their own status, all Yugoslav citizens enjoy the same civic rights (including ethnic, religious or other minorities). As a result of military hostilities in Croatia, Bosnia and Herzegovina and finally in Kosovo in 1999, Serbia (and in some cases Montenegro) was forced to accept approximately 900,000 refugees whose status remains unclear.

For the most part, there is separation of church and religion from the state. Religious dogmas do not have any significant influence worth mentioning on political policies and the law.

The federal government is present throughout the state territory with a fundamental infrastructure (with the exception of Kosovo), but in some cases this infrastructure is ineffective.

(2) *Political participation*: There is effective universal suffrage and the right to campaign for office, and elections are properly conducted. The citizens, therefore, determine their representatives and have other political freedoms. Until just recently, presidential elections in the republics (the elections in the first round are modeled after the French presidential system) operated with a regulatory quorum in which at least a 50 % turnout of eligible voters was required by law to render the result valid. However, after three unsuccessful attempts to elect a president from October to December 2002, the country's institutional crisis was heightened by the fact that the Serbian presidency remains vacant. The Serbian election law was modified in November 2002. In the future, a run-off election for the Serbian presidency will be considered valid if less than half of eligible voters participate.

In view of the splintered political power relationships and increased weariness of politics, this decision will help the political clarification of the elections, even though the first round of voting will still require a quorum. The effective power to rule lies with the elected government; however, there are some limitations. In order to bring about the fall of Slobodan Milosevic and bring about political change, Zoran Djindjic had to form ties with certain organized criminal groups. The alternative power groups formed by Milosevic, which practically acted as an illegal parallel state while he was in office, kept a relatively low profile during Djindjic's first two years in office, only to reemerge in society and politics and use their power to work against the elected officials' policies (blocking reforms). After the assassination of the incumbent Prime Minister of Serbia, the government began to destroy the symbiosis between the state security forces and organized crime.

In late 2000, one of the first steps of the new Serbian government was to abolish the repressive Public Information Act and close the Ministry of Information, which controlled the media. Public information and opinion-making, therefore, exist. The new media laws in Serbia and Montenegro are the foundations for independent private and public media and put an end to monopolies. Nevertheless, political and economic lobbies and government circles still have selective influence on some of the media so that the old and new media cultures coexist in both republics. Political and civic organizations can form freely.

The situation for minorities in Serbia has improved considerably since Milosevic's fall from power. Hungarian and Muslim political parties are part of the DOS and have representation in the government. The minorities themselves are able to advocate their demands in a more open fashion, and they are much more present in public discussions. New measures taken by the federal government include the Law on the Protection of Rights and Freedoms of National Minorities, which came into force in March 2002. This law contains all of the rights that are guaranteed by the Council of Europe's General Convention on the Protection of National Minorities. However, many ethnic Albanians from the Presevo region that borders Kosovo refused to participate in the Serbian presidential election of 2002.

(3) *Rule of law*: The system of checks and balances between the executive, legislative and judicial branches shows transformation problems. As the party leaders, Zoran Djindjic and Vojislav Kostunica, have immediate influence on their party's 45 members of Serbian Parliament and allowed themselves to get involved in an unproductive power struggle, which was based on personal animosity, a quest for power as well as very different visions of the country's past and future. The Serbian prime minister risked his reputation as a politician obligated to constitutional principles at the end of 2002 when he expelled parliamentary deputies representing Kostunica's Democratic Party of Serbia (DSS) from the

Serbian parliament because they would not support some of his draft laws and repeatedly boycotted sessions of parliament.

After Communism and the Milosevic regime, the government's central reform tasks—in terms of developing conditions based on the rule of law—lay in making the judiciary and the police independent from political influence and establishing democratic civilian control of the army. However, the government failed to destroy the symbiosis between government security forces and organized crime, as well as between corrupt politicians in nearly all parties and businessmen who had risen from the ranks of war profiteers to become the new economic elite. Initially, a few of the leading positions in the judiciary were filled with qualified lawyers who had been fired during the Milosevic era. However, attempts to exclude high-ranking officials and partisans of the Milosevic regime from public office and the judiciary within the framework of a lustration law failed to find a majority in parliament.

Subsequently, the government adopted five laws on the reform of the judiciary. One of the most important legislative improvements was the establishment of the High Judicial Council, which is based on the French system in which the minister of justice is influential in appointing judges and public prosecutors. Representatives of the judiciary and the legal profession, instead of politicians, form a majority on the Council. In the interest of maintaining the independence and impartiality of the judiciary, the government increased salaries of judicial personnel to the pay level of ministers.

Corrupt politicians often go unpunished or are insufficiently prosecuted. They are, nonetheless, criticized openly in public. The government has yet to determine who was behind the political assassinations committed in the last years. Apart from top positions of authority, the police force staff has stayed more or less the same. Corruption appears to be less of a problem with the uniformed police than with the Serbian state security police, who were one of the most important instruments of the Milosevic regime as the secret police. Legislation adopted in July 2002 removed the state security police from the control of the Ministry of the Interior, placed it under the direct control of the Serbian government and required it to report to parliament. The duties of the security force are defined as classic intelligence services, and the law draws the line at interfering with a citizen's basic rights. Civil freedoms are protected and enforceable by law, but they are still limited due to the state's lack of commitment to legal standards despite the efforts of some NGOs (such as the Humanitarian Law Center). The State Union of Serbia and Montenegro joined the Council of Europe on April 3, 2003.

### 3.1.2 Political patterns of behavior and attitudes

(1) *Institutional stability*: Democratic institutions essentially operate according to their functional purpose; however, there are inefficiencies in the institutional interaction. The issues of constitutional federalism were the focus of the political structural reforms, primarily the definition of the relationship between the two members of the former federal state of Yugoslavia. Serbia's political and economic development has been impeded by the fact that the government's relationship with Montenegro had not been clarified until only recently. In order for reforms to proceed, the government urgently needs to definitively clarify the competences of the state and the republics.

A newly defined "federal state" was created in March 2002 by the Belgrade Agreement. The structures and institutions of the federal state were set down in a Constitutional Charter in late January 2003. The State Union of Serbia and Montenegro, which formally came into being in February 2003, is not a federation. This is illustrated in the fact that it has a unicameral Parliament. There is no second chamber to represent the state constituents, but simply a Parliament that is made up of nominees of the two state Parliaments with a total of 126 representatives (91 from Serbia and 35 from Montenegro) with a four-year term. The State Union does not show many signs of domestic cohesion, and its organs are unable to balance this lack of cohesion. Not enough time has passed in order to evaluate the working capacity of the State Union; however, it has allowed the government to start working on the upcoming constitutional reforms in both republics.

The country's institutional stability during the evaluation period was largely determined by the rivalry between the two leaders of the DOS coalition, Vojislav Kostunica and Zoran Djindjic. The relevant civil and political actors (with the exception of Vojislav Seselj's Serbian Radical Party) fundamentally accept the democratic institutions and consider them legitimate.

(2) *Political and social integration*: There was no stable representation pattern for mediating between the state and society during the evaluation period. The party system is fragile, highly fragmented and not well anchored in society. The party responsible for the overthrow of the Milosevic government in the fall of 2000 was the DOS, a coalition of 18 parties and one labor union that has remained extremely heterogeneous. It is a broad-based alliance that includes nationwide and regional parties as well as parties that represent various minority groups, parties with relations to the current European party system and parties ranging from strongly nationalist to liberal.

The party system is characterized by a low degree of organizational stability, poor ability to develop programs, a barely existent anchoring in society and strong foundations in individual personalities. The DOS has shown strong signs of erosion since October 2000, which could lead to the dissolution of the Serbian government. The comparative strengths of the political forces are extremely fragmented. As a result, the party system inhibits stability and does not meet with wide approval among the population. One of the dangers facing the country that should not be ignored is that the “dark side” of civil society—the organization of social, media and political powers with anti-democratic intentions—is gaining power.

The approval rate for democracy is fair to high, but the population has very little faith in the political institutions. This also applies to civic organizations. Serbia and Montenegro do not have a well-differentiated landscape of interest groups. However, there is a heterogeneous network of autonomous, self-organized groups, associations and organizations even though the dynamics of organization are not very progressive.

Voter turnout was low in the Serbian presidential elections in late 2002. Citizens are increasingly apathetic about politics.

## **3.2 Market economy**

The downfall of former Yugoslav President Milosevic marked the beginning of a change in Serbia, especially in the area of economic policy. The country has begun to move toward a free market economy under the coalition government of Zoran Djindjic. The move was accompanied at the federal level by a reform package, which was comprised of measures to liberalize foreign trade, negotiations, and the country’s entry into the International Monetary Fund, the World Bank, and the World Trade Organization.

However, there are transformation problems in every area. Those problems are more about the implementation of the transformation rather than the status of the reforms. It should be pointed out here again that Serbia and Montenegro have two different economic systems. The two republics have two separate currencies and two separate customs and tax systems.

### **3.2.1 Level of socioeconomic development**

There are many shortcomings in the statistical apparatus, and it lacks several key indicators. There is no data on the GDI or the HDI. According to the Gini index, Yugoslavia (Serbia) is the least stable compared with other Eastern and Central European transition countries. Macroeconomic data show a low level of

development. Social exclusions are quantitatively and qualitatively pronounced, and in some cases are structurally entrenched. Social disparities have increased, and poverty has become more prevalent during the evaluation period. Corporate restructuring has resulted in high social costs.

The development status does not allow all citizens sufficient freedom of choice. In Serbia, GDP in 2000 stood at 55 % of the 1990 level and per capita income was 60 % of the 1990 level. One-third of the Serbian population live in relative poverty (less than \$60 per month, per person), and almost one-fifth live in absolute poverty (less than \$20). A large group lives just above the poverty line. The poverty rate in Serbia has therefore increased dramatically between 1990 and 2000. In Montenegro, where the decline in GDP was slightly less, 27 % of the population lives below the relative poverty line (45 euros per month and per person) and 31 % of families earn less than 75 euros a month.

The average income of the citizens of Serbia and Montenegro dropped from \$125 in 1996 to \$48 in 1999 and was around \$135 in 2002. Unlike in the past, the state now pays salaries and pensions on time.

### **3.2.2 Market structures and competition**

Free market competition only exists in certain segments. The country adopted an anti-monopoly law in 1997 that regulates free market competition; however, it was not implemented. The law was recently revised. The country has an anti-monopoly commission. It has not been possible to remedy the lack of even the most basic prerequisites for corporate governance. Structural reform measures were aimed at bringing about the introduction of real income taxation, more efficient privatization of state-owned property, banking system reform and a certain liberalization of the labor market. Of these measures, bank reform is considered to have been the most successful. A large number of insolvent banks were liquidated, including four large banks in Belgrade. In connection with this, the repayment of old foreign currency holdings and savings accounts, as well as assets from pyramid schemes, was regulated in a binding manner, and should be carried out by 2016. At the same time, laws were passed that make it more difficult to launder money, and the general supervision of banks was improved.

Foreign trade was liberalized. An unavoidable concomitant effect of the transitional period is a decrease in industrial production and a stronger increase in imports compared with exports.

### **3.2.3 Stability of currency and prices**

One of the main goals of the reforms was to curb inflation. Another goal was to reopen the country for international financial and economic institutions. Trade and prices were liberalized in order to open the economy to the global market. A stable currency and a continuous inflow of international funding should make room for restructuring the economy. The federal government was able to lower the inflation rate from 120 % in late 2000 to 40 % in late 2001 to less than 15 % at the end of 2002. The dinar has been convertible since May 13, 2002. Foreign currency reserves have increased more than fivefold. The International Monetary Fund guaranteed a total of \$1.5 billion in financial aid in three separate loan agreements. The Paris Club of sovereign creditors agreed to forgive 66 % of the country's debt. Policies on inflation and the currency are accepted economic and political goals that are rigorously implemented by the central bank, even when it resulted in friction between the governor of the central bank, Mladjan Dinkic, and Serbian Prime Minister Zoran Djindjic. The political and institutional elements of a state stabilization policy therefore exist.

Tax reform in the spring of 2001 expanded the tax base, lowered the nominal rate and closed some loopholes designed under the Milosevic regime for politically connected companies that led to billions of dollars in lost revenues. As a result, there was an increase in tax revenue, though not as much as the government had hoped for.

### **3.2.4 Private property**

There has been substantial progress in the privatization of smaller companies, which began even before the political changeover because of several different laws. A privatization law adopted by the Serbian Parliament in June 2001 should make it to sell the approximately 7,000 state companies. The new law sufficiently defines property rights and the acquisition of property and represents a clean break with the privatization laws of the past. On the one hand, the old laws tried to implement another property model, but on the other hand they were also abused by dubious machinations.

The government privatized a total of 250 companies using accelerated auctions, and it plans to sell another 1,000 companies this way in 2003. However, this method of privatization is also susceptible to criminal manipulation (for example, there have been accusations of money laundering) and other dishonest acts such as high bids that were retracted at the last minute in order to enable partners to be able to buy the company for considerably less during the second round of bidding. An amendment that was passed in February 2003 is supposed to put a stop to this practice. One problem is former owners of companies that were sold this way who demand a refund or reimbursement for their losses.

The Serbian Ministry of Privatization and Kosovo authorities have agreed to postpone all privatizations until all of potential creditors in Serbia have registered with the relevant institutions.

### **3.2.5 Welfare regime**

The social networks for welfare, pensions, health insurance, unemployment benefits and disability payments, which by and large covered these risks were included in the SFRY's economy, and are now only rudimentary. The two republics worked together to draft an interim strategy paper on reducing poverty, and the final paper should be released by the middle of 2003. The government has taken some steps towards social reconciliation. When the Montenegrin government decided to liberalize the prices of milk and bread in 2001, it provided families with financial compensation and also increased child benefits.

Public health care is traditionally the responsibility of the republics. There are three health care systems, two at the republic level and one for the military at the federal level. Large portions of the population lack sufficient health care. The health care system in both republics is in very bad shape with regard to equipment, buildings and daily provisions. Medicines and basic medical supplies are often unavailable. Spending on health care in Serbia dropped in the last ten years from approximately \$200 per person in 1990 to approximately \$30 in 2001. The Serbian government adopted a new health care program in early 2002.

With regard to the continually increasing unemployment, the Serbian Ministry of Work and Social Care adopted a social program with both passive and active components, including severance pay and unemployment benefits or continuing education as well as help in starting a company. These measures were implemented as part of the corporate privatization process and bank liquidations.

In 2001, all regular social benefits were paid in full for the first time in 10 years. The pension scheme was reformed in late 2001. The new index is based on a combination of standard of living costs and salary. A new family law, which separated demographic and social measures, was adopted in 2002. The government also adopted a national strategy to help registered refugees in 2002. Despite the active role of women in NGOs and political networks of women in bringing about the democratic transformation, very few women are involved in political decision-making processes. There are no institutions to check legislation for the discrimination of women.

### 3.2.6 Strength of the economy

Per capita GDP growth is stagnant. After negative growth in almost all of the main macroeconomic indicators in 1999, the country is experiencing a slow upward trend. Industrial production is and will remain at a very low level due to the extremely weak industrial base. It can only recover in the medium term with the help of direct foreign investments. The agricultural sector has achieved only minimal results, and other economic sectors have not played a role in stimulating growth. Since the political changeover, economic development depends on foreign aid, which is primarily in the form of financial aid and not the transfers of technology that the country needs most. Many of the main economic problems in Montenegro are connected to fiscal adjustment, which has already begun but needs to be continued, and on an ever-decreasing amount of foreign aid.

### 3.2.7 Sustainability

The country has to cope with three challenges at once (economic transformation, reconstruction and development) even though the social category of “middle class” has practically disappeared over the last 10 years. Initial efforts to counteract poverty and social risks have been made. However, the country cannot systematically fight poverty on its own. There are educational as well as research and development facilities, but investments in these areas are quantitatively and qualitatively low.

Educational facilities are in poor condition in both republics, and there have been no new school materials for many years. Public spending for education dropped dramatically in Serbia. At the same time, there was a decline in the number of children with a diploma. There is no gender-specific discrimination of women in the legal system. While international economic and political sanctions were imposed on the country in the 1990s, the destruction of its natural resources intensified, having an extremely negative effect on the ecosystem. The bombing of the FRY in 1999 also had direct and indirect, as well as short-term and long-term economic consequences. Nine years after the SFRY signed Agenda 21 in Rio in 1992, the Serbian government announced in a 2001 report that the system in charge of environmental protection had done nothing for 10 years and was not even close to attaining sustainability. National priorities on environmental protection were defined in 2001.

## 4. Trend

(1) *Democracy*: The criteria of an unrestricted monopoly on power, a capable administrative system, a working court system, law and order and free elections were not guaranteed before the evaluation period. After the downfall of the former

autocratic ruler Slobodan Milosevic in fall 2000, there was a general sense that a new era was about to dawn, bringing with it improvements in the individual aspects of political participation and rule of law. The degree of democratic consolidation improved considerably in areas such as freedom of the press, free development in the landscape of civic interest groups and organizations, and progressive development in enforceability of civil rights. However, democratic development in the judiciary in both Serbia and Montenegro was stagnant. After the assassination of the Serbian Prime Minister, steps were taken to improve this area. The long-term effects of these steps remain to be seen. The armed forces, the police, the state security police, and the entire security apparatus were not subject to any effective civil controls. Organized crime had infiltrated the government structures.

During its first 18 months, the new Serbian government instituted many important reforms with the help of the Serbian parliament and the DOS. However, reforms have stagnated since the summer of 2002. This was a lost year for Serbia. A new constitution is the most important element in the country's development towards a democracy founded on the rule of law, but the government needs a two-thirds majority in the parliament to change the existing constitution, which dates back to the Milosevic era. The new constitution also needs to be approved by 50 % of eligible voters. However, political apathy is widespread among the population. Positions between the political camps are entrenched. The political and social integration of political parties remains slight. Citizens' conventional willingness to participate is diminished. They have become increasingly distrustful of the "new class" of democratic politicians, especially as a result of the volatile disagreements between Yugoslav President Vojislav Kostunica and Serbian Prime Minister Zoran Djindjic. Corruption and nepotism have undermined the public trust in government institutions. The standard of living for many citizens did not improve, and their struggle to survive in their materialistic society took all of their energy. The number of people wishing to emigrate has increased.

(2) *Market economy*: The institutional conditions have improved in several segments of the economic system, but the pace of reform slowed during 2002. Judged by the macroeconomic data, reforms have not yet precipitated macroeconomic recovery. However, the political decision-makers' stabilization policies scored noticeable successes. International economic integration has been successful, and household consumption increased significantly in 2001.

There are two economic consequences of the political crisis precipitated by the unsuccessful presidential elections in Serbia in the fall of 2002. First, the transformation process has slowed. The longer the crisis lasts, the greater the risk that some reform programs will go unimplemented. This applies especially to privatization, which is becoming increasingly controversial. Second, macroeconomic stability could be put at risk because a prolonged political crisis puts a heavy strain on public spending. The uncertainty regarding foreign inflow

of money (investments, loans, aid) can also have a negative effect on the exchange rate and monetary policy.

**Table 2: Development of the macroeconomic fundamentals (1998–2002)**

	1998	1999	2000	2001	2002
GDP Growth	1,9	-18	5	5,5(1)	3,0(1)
Export growth	10 %	-44,6	14,7	4,16(1)	12,3(1)
Import growth	0,4	-32,0	12,6	30,2(1)	15,5(1)
Inflation	30.4 %	44.1 %	77.5 %	90.4 %	19,3 %
Unemployment in % (3)	27.2 %	27.4 %	26.6 %	27.9 %	-
Budget deficit as percentage of GDP (4)	-	-	-0,2	-1,7	-5,9
Current account balance, \$ billion	-7,4	-8,7	-4,9	-6,0	-14,0(2)

(1) estimated; (2) January-September; (3) since 1999, not including Kosovo (4) not including Montenegro.

## 5. Transformation management

### 5.1 Level of difficulty

At the start of the evaluation period, several factors made for extremely poor conditions for transformation, despite strong civic traditions. These included the country's low level of economic and social development, a lack of fundamental market-based structures, a falling level of education, growing poverty, a history of war, an inefficient state administration, tension between Serbia and Montenegro and the unresolved status of the Serbian province of Kosovo. Let's also not forget that the Federal Republic of Yugoslavia was bombed by NATO in 1999 and had economic sanctions imposed on them from 1992 to 2002 with only a few short interruptions (the "outer wall" of sanctions that cut off the country's access to international financial organizations was lifted in 2001). With regard to structural and socio-economic conditions that set the tone for the political process in the long-term, the transformation is extremely difficult, even against the background of the collapse of the SFRY. Before the evaluation period there was no fundamental consensus on democracy and the central democratic rules. The beginning and stabilization of the democratic transformation was impeded by the lack of democratic and constitutional experience and especially by the longstanding semi-authoritarian rule of the Milosevic regime. The fact that the FRY had not even started the transformation process until the Milosevic regime was overthrown in the fall of 2000 makes it even more difficult.

## **5.2 Reliable pursuit of goals**

In summer 2000, opposition parties agreed on a general program of democracy, rule of law, a market economy, and affiliation with the European integration process. The main goal was clearly to remove Milosevic from power. The Serbian government has ushered significant change, especially in the area of economic policy. It has pursued long-term goals with complete openness toward Western countries and movement to a market economy while trying to reconstruct the state's institutions. Decision-makers have generally maintained their commitment to the transformation goal of a consolidated, market-based democracy. The Serbian government did everything it could to fulfill foreign economic actors' expectations.

In the realm of democratic transformation, the choice of strategy was less convincing. There was a lack of willingness to cooperate within the government. The government's transformation strategy became increasingly restrained due to the unstable character of the DOS coalition and the approaching Serbian presidential elections (October 2002).

As far as the strategic approaches were concerned, there were differences between the economic and the democratic transformations, and especially between Serbian Prime Minister Zoran Djindjic and the Yugoslav President. While Djindjic's explicit goal was to integrate Serbia into Euro-Atlantic structures, Kostunica called for a qualitatively different transformation. This was especially true in regard to collective responsibility for the recent past within the territory of the SFRY. To Kostunica, this responsibility should fall upon on all the regional actors, as well as upon the international community. For example, the Serbian government under the leadership of Djindjic handed Milosevic over to the International Criminal Tribunal for the former Yugoslavia in The Hague on June 27, 2001 against the express will of President Kostunica. The United States had made it a requirement for their participation in the first international conference of donors for Yugoslavia two days later on June 29, 2001.

## **5.3 Effective use of resources**

The implementation of the Serbian government's economic transformation goals is dependent on the granting of foreign aid and privatization revenues. The government efficiently uses some of the personal, financial and organizational resources at its disposal. The IMF offered the country financial assistance in three agreements and confirmed the efficient and accurate use of public funds in view of structural reforms (increased company privatization, a strategy for bank

privatization, an improvement of the tax system). The government has reduced the budget deficit and implemented a policy for controlling loans and income.

The administration is overstaffed in many areas, while there is a lack of qualified personal in key sectors and the quality of the administration's services is insufficient. In the short term, the fiscal balance in Serbia is satisfactory. Transferring control of local spending from the central administration to the autonomous province of Voivodina reduced government spending. The tax reform process continued into 2002. The budget deficit for 2003 was set at 3.8 %, which is a realistic goal. Public spending should not exceed 47.6 % of the GDP. The high expenses are unavoidable, because the government has to cover the social costs of the transformation. Thus, the Serbian government did not deviate from its path of fiscal discipline in early 2003 (despite the fact that many employees staged strikes).

The government is not yet capable of successfully limiting corruption. The existing rules are not always used with determination and impartiality. The government has utilized the human resources it at its disposal, especially former dissidents and members of the opposition (G17Plus, etc.). All political actors are responsible for a somewhat regressive development in democratic stability and limited consolidation at the intermediate level. Overall, public services are generally suited for further economic progress. There are deficiencies in the area of social services.

#### **5.4 Governance capability**

One of the transformation's biggest problems during the evaluation period is the fact that Serbia still does not have a new constitution. Nevertheless, it is still apparent that a dynamic reform process has begun in almost all areas of social and economic life in Serbia and Montenegro, especially in Serbia. The Serbian government has been faced with many difficult problems. Out-of-date statutes needed amending as quickly as possible, but if they are passed too quickly, this could have a negative effect on the quality of the legislation being enacted.

Another question was also of immediate importance: To what extent must and should the passage of new laws be in line with Serbia and Montenegro's new Constitutional Charter, and which of the two republics and new state structure's competences should be regulated first? The economic reform policy was circumspect and intelligent, and a number of strategically important laws, especially in the area of fiscal policy and with direct foreign investments in mind, were passed. The reform of company law was slower than planned. A number of important laws in the area of social and family policy (labor laws, pension insurance fund, legal protection for children and youth, education law, university law) were passed. The democratic transformation is not as positive. New criminal

laws apply to the entire FRY and are an important step towards protecting human rights with regard to criminal proceedings and judicial inquiries. The government abolished the death penalty.

As for reform policies, the focus of the transformation has been the harmonization of the country's legislation with EU standards. The government has been able to avoid the misuse of the economic resources for the most part. In contrast, the government's ability to organize itself has been limited, especially due to the conflict between Djindjic and Kostunica, the erosion of the DOS, and the failed Serbian presidential elections in the fall of 2002. Even compromises that were made with certain powers within the security apparatus shortly before and after the fall of Milosevic in the fall of 2000 have had a negative effect on the political decision-making process and undermined the government's political authority. At the federal level, the government's ability to make decisions has been severely limited by the coexistence of the reform-minded DOS and the conservative socialist politicians from Montenegro in the federal government. This created a deadlock in regards to the political authority necessary for introducing and continuing reform.

As far as the political actors' ability to learn is concerned, the assassination of the Serbian Prime Minister may prove to be a catalyst for the necessary political reforms. As a result, many positive steps were taken within a very short time period (such as resolving who was behind the political assassination), but it remains to be seen whether this course will continue and how far it will go and whether the reformers can continue to expand their room to maneuver. There are some signs that the repercussions of the measures that were taken after the assassination could also have a contrary effect on human rights, freedom of the press, etc.

## **5.5 Consensus-building**

All of the substantial political and societal actors are in agreement on the goal of reform (market-based democracy); however, their ideas on how to achieve that goal vary considerably. The conflict between the Serbian prime minister and the Yugoslav president that continued within the DOS slowed down the reform process. The lines of conflict deepened. However, most of this occurred within the acceptable bounds of democracy. The Prime Minister Djindjic knew how to attract the loyalty of conservative democrats, as well as the pro-European organizations, but his expansion of power was dubious and came often at the cost of democratic procedures and institutions (especially Parliament).

The government failed to adequately promote solidarity among social groups and the general populace. The government has also barely begun coming to terms with the country's historic acts of injustice. The state's ability to move forward is

dependent on its attempts to come to terms with its past, including especially Serbia's responsibility in the Yugoslav wars of the 1990s. There appears to be no clear-cut course taken by political leaders, and the topic is still considered taboo by the media and intellectuals. Kostunica set up the State Commission for Truth and Reconciliation, which, thus far, appears to have dealt only with Serbia's role in World War II. Two non-governmental organizations in Belgrade, the Helsinki Committee for Human Rights in Serbia and the Humanitarian Law Center, are taking a firm stand in attempting to clarify the question of Serbia's responsibility. It appears that Serbian society is no longer blinded by the mythology of its own history. Instead, it appears to be extremely unnerved and disoriented.

The passage of laws about the military and the entire security apparatus, which needs to be placed under the control of civil society was especially slow. There were a number of suggestions from NGOs in this area that the government did not consider. Consensus building was hampered since the relationship and distribution of power between the republics of Serbia and Montenegro was not sufficiently settled. Some of the political elite in Montenegro pushed for the republic's sovereignty/independence during the evaluation period. The status of Kosovo is also unclear.

## **5.6 International cooperation**

Since the fall of Milosevic, relations between Belgrade and the other successor states of the SFRY have noticeably improved in various degrees. International relations exist between all of the previous Yugoslav partners. The lengthy discussion about socialist Yugoslavia's estate finally came to an end in June 2001. Economic and cultural connections are being rebuilt quickly. Serbia is actively participating in multilateral collaboration with other countries in the region under the Stability Pact for Southeastern Europe. Relations with Macedonia, which was Serbia's first trade partner, are the most developed so far. Both countries are irreplaceable transit countries for each other.

The relationship with Slovenia has experienced the most significant improvement since the downfall of Milosevic. Slovenia and the Serbia have signed several agreements including investment protection, cooperation in the areas of postal service and telecommunications, and on tourism. Slovenian companies comprise the largest group of foreign investors in Serbia. However, visitors still need to apply for a visa, since Slovenia is trying to become a Schengen country. Collaboration with Croatia has also improved, but there are still reservations, especially on the part of Croatia. Meetings with politicians that promised improvements in the plight of refugees and border traffic have not produced adequate results. There has been considerable improvement in negotiations over the provisional status of the Prevlaka peninsula, of which Croatia took possession

when a UN mission withdrew. Relations between Croatia and Serbia are still extremely strained by the recent past and the consequences of the war.

After the fall of Milosevic, the relationship with Bosnia and Herzegovina thawed somewhat, and diplomatic relations were established. The countries signed bilateral agreements on free trade, social security benefits and the possibility of dual citizenship. There are deeper problems that stem from the recent war, the unequivocal relationship between Serbia and the Serbian-Bosnian entity as well as the instability of the entire Bosnian state. Outside the borders of the former SFRY, Serbia has good traditional relations with its neighbors Hungary, Romania and Bulgaria. In view of the Kosovo problem, the positive new accents in relations with Albania are significant. The countries have signed three agreements about abolishing visas, establishing mutual investment protection and collaborating in the field of medicine. Serbia has been involved in multilateral cooperation among Balkan states since late 2000. However, the number and importance of concrete projects of multilateral cooperation is far below the number and importance of projects of bilateral cooperation.

Serbia has achieved nearly complete normalization of its international relations since the fall of Milosevic. Zoran Djindjic delivered Slobodan Milosevic to The Hague to stand trial before the International Criminal Tribunal for the former Yugoslavia (ICTY). The government passed a law governing its cooperation with the ICTY. International organizations of which the former Yugoslavia was member (especially the United Nations and the OSCE) immediately accepted the Serbia and Montenegro as a participating state after the new leaders applied for membership and submitted a thesis on the issue of automatic legal succession. Diplomatic relations with other countries were fully restored, insofar as they had been interrupted. The EU and the United States, which had supported the new leaders during the opposition period, continued this support in an even stronger manner. The new leaders consider them to be the country's most important international partners, followed by Russia. The disclosure that Serbian companies had sold arms to Iraq, which was a close ally of Yugoslavia during the reign of Milosevic, caused some irritation in Western countries.

Both Serbia and Montenegro feel that affiliation with the European alliances (mainly the EU) takes absolute precedence among international goals. Before it can enter into a long-term partnership with the country, the EU insisted that the identity of the union be clarified (by concluding negotiations about the future relationship between Serbia and Montenegro). The same applies to the question of Serbia and Montenegro joining NATO's Euro-Atlantic Partnership Council.

## 6. Overall evaluation

In view of the originating conditions, current status and evolution achieved, as well as the actors' political achievements (management), this assessment concludes the following:

(1) *Originating conditions*: The starting conditions for transformation can be rated as negative overall. Before the observation period, there was no market-based structure. The transformation of the authoritarian political system and controlled economy did not begin until the downfall of the Milosevic regime in the fall of 2000. The fact that there was no consensus in either Serbia or Montenegro about the government or the set of values on which the society and the political community should be based was also extremely important. Montenegrin President Milo Djukanovic's pro-Western orientation after 1997 and the isolation into which Milosevic was forced by the West provided the motivation for Milosevic to maintain political, social and economic power in the hands of informal power groups.

The policy of isolating the impoverished country that was destroyed by war in 1999 alone was not a prerequisite for deposing the authoritarian regime and the fundamental political and economic transformation. The baseline situation for this was extremely unfavorable. The economy was in a deep slump, the people were impoverished and there were no concrete starting points for the introduction of democratic, constitutional relations.

(2) *Current status and evolution*: Serbia and Montenegro has made progress in transforming the political regime in some of the evaluated areas. However, it is still a defective democratic system with transformation deficits in the areas of state identity, political participation and rule of law. In the area of legislation, Serbia has made quite a bit of progress in becoming a democracy based on the rule of law. However, in a society where for several years special interests and power constellations carried more weight than the law, it is not possible to secure enormous progress within three years.

The economy went a fairly long way along the path of transformation. Institutional conditions have improved in many segments of the economic system, but the pace of reform slowed in 2002. According to macroeconomic data, reforms have not yet precipitated recovery, but stabilization policies of the political decision-makers were able to register noticeable successes. International economic integration has been successful.

(3) *Management*: The verdict on the actors' relative management performance is mixed. During its first 18 months, the new Serbian government instituted important reform measures with the help of the parliament and the DOS, but reforms have stagnated since the summer of 2002.

In the summer of 2000, opposition parties agreed on a general program for democracy, rule of law, market economy and affiliation with the European integration processes. Their main goal was clearly to overthrow Milosevic. Yet, the Serbian/Yugoslavian government instituted a fundamental change, especially in the area of economics. It has pursued long-term goals, including openness towards the West and moving towards a free market economy while they tried to rebuild government institutions.

One of the transformation's biggest problems during the evaluation period is the fact that Serbia still does not have a new constitution. Nevertheless, it is still apparent that a dynamic reform process has begun in almost all areas of social and economic life in Yugoslavia and Serbia.

## **7. Outlook**

The former Yugoslav Minister of Interior Zoran Zivkovic was elected prime minister by the Serb Parliament following the March 12 assassination of Zoran Djindjic. Zivkovic was a close ally of Djindjic. He ruled out the possibility of new elections in his first official statement and announced that he intended to remain the head of the government until the next regular elections in late 2004. Many have doubts whether the government coalition (DOS) can maintain its unity and whether Zivkovic is capable of leading the country out of its current crisis. If the West wants to prevent further destabilization in Serbia and the region, it must continue its financial assistance. At the same time, the West should urge the government to stabilize weak democratic political institutions as quickly as possible.

The legacy is extremely difficult. Djindjic's death left a political vacuum. Democratic conservatives and pro-European liberal democrats must work together if reforms initiated by Djindjic are to succeed.

Important political institutions have been damaged, and vacant positions have yet to be filled. The country has not had an elected president since December 2002. The out-of-date constitution dates to the Milosevic era. The beginning of 2003 saw the formation of a new union with Montenegro, creating a number of important new institutions. For example, a five-person Council of Ministers constitutes the government of the union. Both republics have fallen behind with the necessary attendant legal adjustments. Moreover, no one knows whether or how the new entity, a unique experiment, will work.

Despite the splintering of democratic organizations, there is not much danger of the country returning to the conservative, nationalistic policies of the past. Doubts over whether the many small and rival opposition parties would be able to form a convincing alternative to the old regime prompted a group of 17 university

professors and other economic and financial experts to join the political process in 1999. As a new party, G17Plus (which stands for pro-European and liberal policies) immediately became one of the most popular political groups in Serbia, along with Zoran Djindjic's DOS and the Democratic Party of Serbia, in early 2003.

Zoran Djindjic paid for the Serbian government's biggest failure following the downfall of Slobodan Milosevic with his life. The government failed to destroy the symbiosis between state security forces and organized crime, and the connections between corrupt politicians from almost every political party and former war profiteers who had formed the new economic elite.