



Investment Series 2008

Serbia

A country on fast forward



Serbia has always benefited from its strategic position between East and West. As it shrugs off the stigma of the Milošević era and drives through a program of political and economic reform, more and more Western companies are waking up to the advantages of investing in the republic.

Is Serbia Europe's latest investment treasure trove?

When the blue-chip retailer Marks & Spencer opened the doors of its new store in the Serbian capital of Belgrade last November, the queue of customers waiting to snap up packs of underwear, cashmere jumpers and the other products that have made St. Michael such an iconic brand went round the block.



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Sitting on the banks of the Danube, Belgrade has long been a gateway from Europe to the East.

Marks & Spencer is not the only organization to have spotted the untapped potential of Serbia's consumer market or to have been attracted to its overall business environment. In recent months, long-established companies such as processing and packaging giant Tetra Pak have been joined in the Serbian marketplace by a number of other far-sighted businesses, including Merrill Lynch, which recently agreed to a strategic partnership with Serbian property developer MPC Properties; bus and rail group Arriva; and on the private investment side the Guernsey-based Argyll Investment Services, which has launched the Belgrade Pioneer Fund, one of the first funds to invest in Serbian real estate. The Fund was oversubscribed in a matter of days.

As a result of such initiatives, foreign direct investment into Serbia is forecast to grow from \$3.2 billion in 2007 to \$4.5 billion in 2008, according to the *World Investment Prospects to 2011* report from the Economist Intelligence Unit (EIU) and the Columbia Program on International Investment. This represents a jump of 41%, which far outstrips the report's predictions for any of Serbia's Balkan or East European neighbors; by this yardstick, only oil-rich Kazakhstan enters 2008 with a greater degree of optimism on the Serbian side of the Atlantic.

Serbia may also be about to receive an unexpected filip from the current credit crunch as—according to one fund manager, at least—emerging markets may offer shelter to funds fleeing the

problems associated with defaults on subprime loans in the U.S. "Our best performance is coming from parts of the world with no subprime exposure," says New Star Global Financials manager Guy de Blonay. "I am seeing good growth from peripheral markets like Russia, Montenegro, and Serbia."

There are, however, more fundamental and durable reasons to invest in Serbia—principally its size, strategic location, the success of its reform program and its highly educated population. With eight million citizens, Serbia's internal market is among the largest in Southeast Europe, and all major road, rail, water, and even air routes traverse Serbia, connecting Europe with Southeast Europe, Turkey, Greece, and the Middle East. A major upgrade of the country's transport infrastructure is currently in progress, principally focused on Corridor X. Due to be completed by 2010, this international initiative will link Salzburg in Austria to Thessaloniki in Greece, and will take in 800 kilometers of Serbian road and 767 kilometers of its rail network.

As a consequence, Serbia has now begun to reclaim its role as a strategic staging post for any business wanting to expand into Central and Eastern Europe. It has the added advantage of being in the middle of the proposed Southeast Europe Free Trade area, which will give duty-free access to a market of 60 million people; and it is the only country outside the CIS (Commonwealth of Independent States) that has a Free Trade Agreement with the Russian Federation, giving it potential access to an additional 150 million people.

Serbia has enjoyed an extensive program of political and economic reform that has seen it develop into a stable democracy with a fast-growing market economy.

Serbia also has great potential as a market in its own right. Over the past six years it has enjoyed an extensive program of political and economic reform that has seen the country develop into a stable democracy with a fast-growing market economy. Western-oriented, democratic political parties have a clear majority among its citizens, and there are now whole-hearted attempts to bring the legal framework in line with EU regulations.

The country's progress has the support of the World Bank and the EBRD (European Bank for Reconstruction and Development), and investment projects in Serbia can now be insured by all major and international investment export agencies. The protection of foreign capital is further safeguarded by bilateral investment treaties between Serbia and 34 other countries, including the U.S., the U.K., Germany, France, Austria, Italy, and Greece.

This rehabilitation has helped more than double the country's GDP per capita between 2002 and 2006, and the EIU predicts a further 10% increase in 2008, with steady improvement set to continue through to 2011. This is good news for companies like Tetra Pak, which has been operating out of Serbia for nearly 40 years. "At the moment we have marginally more exports than local sales," says the Brazilian-born Managing Director Nelson Falavina, "but that is not to say that the local market isn't growing. On the contrary, the local market is good but we are also able to export to 30 markets from our base here, so it's like two businesses operating from the same factory."

Falavina believes the future is bright. "Serbia is becoming more stable and predictable—not just in our sector but in other industries as well. Every year, we see more international companies coming here and local ones also springing up." The reforms that have been implemented since the Milošević era have triggered exponential growth in the Serbian private sector, and there are now around 270,000 entrepreneurs and 90,000 small to medium-sized enterprises (SMEs) operating in Serbia; experts expect this number to increase to more than 400,000 over the next five years.



Tetra Pak is one of many international companies that now call Serbia home.

Foreign direct investment into Serbia is forecast to grow from \$3.2 billion in 2007 to \$4.5 billion in 2008.



Tourism is once again blooming in historic Belgrade.

If the experience of coffee specialists Doncafé is anything to go by, this SME sector should include some rich pickings for potential investors. Established in 1992, the company was acquired by the Israeli Strauss Group in 2005. Under the newly appointed CEO Milan Petrović, the company immediately moved "from domestic standards to international standards" and, significantly, moved into profit within six months. It now competes for domination of the domestic espresso market with Lavazza. "Serbian consumers are very educated," says Petrović. "They love brands, communication, and quality."

One enduring legacy from the era of Tito's Yugoslavia is an extremely high level of education, and it is a mantle that has been taken up by the private sector, which has developed an appetite for MBAs.

Singidunum University, for example, was founded by a group of professors who used to work at state universities "but who realized that a new kind of education was needed for the changing times," according to one of its founders, Dr. Milovan Stanišić. New curricula and degree formats were drawn up, modeled on European faculties and in accordance with the principles of the Bologna Declaration.

Like Stanišić, Professor Mića Jovanović, Rector at Megatrend University, sees the training of Serbian management for a European business environment as a key mission. "We have to prepare them for the EU," he says, "because we can't say that they are familiar with all the things that happen abroad—but they are very capable."

Though both foreign direct investment into Serbia and the country's GDP are set to grow rapidly over the next few years, there is no disguising the fact that the country is starting from a low base: GDP per head in 2007 was, for example, one-third of that in the Czech Republic. Is this an opportunity or a threat? Maybe Doncafé's Petrović should have the last word: "This country is the center of the region and it is still very cheap to enter the market—but land and real estate prices are going up every day. We bought the land for our new coffee factory 18 months ago, and now it's worth five times what we paid for it. Hurry up!" ■

New privatization policy rings in the changes

The latest outcome of Serbia's privatization program will see telecommunications giant Telecom Serbia put up for sale. As the technologies behind terrestrial, wireless, and the Internet continue to converge at a staggering rate, the privatization promises to trigger a flurry of activity in the ICT sector.



Investment potential exists in every sector, especially infrastructure.

In January this year, Serbia's Deputy Finance Minister Nebojša Čirić told a conference in Vienna that his government was planning the partial privatization of a whole raft of state-owned companies—including the country's leading telecommunications organization, Telecom Serbia—by the end of 2008.

There should be no lack of interest from the global business community. "The telecommunications sector in Serbia is very impressive," says Aleksandra Smiljanić, Minister of Telecommunications. "We already use it to offer a wide variety of e-government services to our citizens to give them more control over their lives." Potential investors will be buying into a company that has installed some 3.45 million lines with a 90% level of digitalization and 20% annual profit rate.

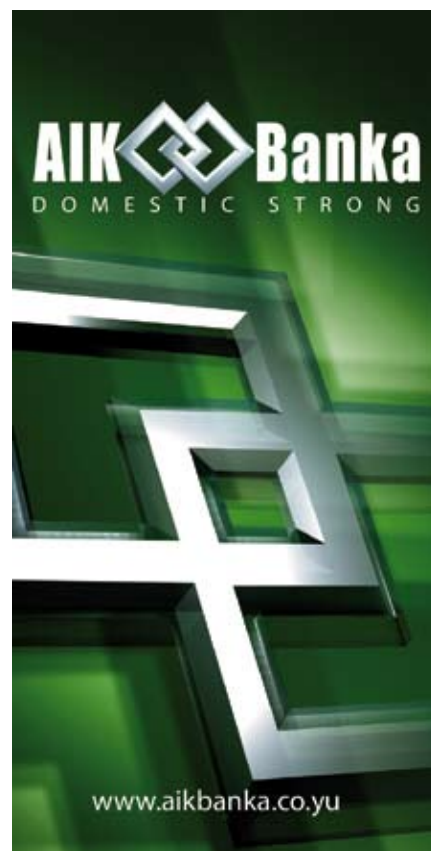
Serbia's wireless networks have already been deregulated to some extent, and whoever acquires Telecom Serbia will find themselves competing with Norway's Telenor and Austria's Mobikom, which launched its Vip mobile service last June. Mobile telephony penetration is 73%, with Telecom Serbia boasting over 4 million and Telenor some 2.5 million users at the time of the Vip launch.

But as Minister Smiljanić's acknowledgement of the Internet's importance suggests, the significance of this announcement will not be lost on Serbia's incumbent private-sector telecommunications companies, many of which have also positioned themselves as Internet service providers. One such company is Telefonija, among the first companies to be privatized post-Tito back in 1991 and still going strong. As the technology has progressed and the political climate has unwound, Telefonija has diversified into gas as well as telephone infrastructure construction; electronic payment; and information communication technology, where they count IBM and Cisco among their partners.

Telefonija also owns BeotelNet, which stakes a claim to being the first ISP in former Yugoslavia, let alone modern Serbia, and is therefore well positioned to benefit from one of Serbia's fastest-growing consumer markets. Since Telecom Serbia introduced ADSL, broadband Internet has rapidly developed and services around 200,000 users—a 500% increase year on year. ADSL now has a larger penetration than Internet dialup

services, and at 15% enjoys a higher percentage of customers per capita than comparable services in either Hungary or the Czech Republic.

There are now around 780,000 Internet users in Serbia and some 40 ISPs like Telefonija fighting for market share. With the upcoming privatization program, life is about to get even more interesting. "We're paying Telecom two or three times what we would pay some foreign international operator," says Telefonija CEO Branimir Bošković, "which is why the Internet is more expensive than in many other countries. This should change soon and we should also be in a position to use our own—or lease somebody else's—fiber optic network." It sounds like whatever happens post-privatization, it is the Serbian consumer who is going to be the ultimate winner. ■



Megatrend University

“Testimony to the high caliber of the learning at Megatrend University is that of the 362 full-time members of the teaching staff, 315 have PhDs.” Rector Mića Jovanović expects that within five years it will be the largest university in the region. And with Megatrend alumni already occupying leading positions in Serbia’s political and commercial seats of power, it’s easy to see why the Rector is confident about the legacy that he is creating through his graduates.

A conversation with Mića Jovanović, Rector of Megatrend University.

Q: What are the origins of the Megatrend University, the third largest university in Serbia?

MJ: The origins of Megatrend University date back to 1989 when changes in legislation of former Yugoslavia meant that for the first time since the Second World War everyone had the right to start some private company or entrepreneurial private initiative. Returning from England with a PhD from the London School of Economics, I was inspired to try to establish the type of business school that could prepare dynamic young minds for this changing business environment and capitalize on the flourishing commercial opportunities. It was a revolutionary idea and the first time in the history of Yugoslavia that someone had started a private business school.

Today, Megatrend has over 25,000 students, and is the third largest university in Serbia behind the state-run universities of Belgrade and Novi Sad.

Q: How is Megatrend unique as an institution for higher learning?

MJ: Megatrend’s biggest and most popular courses are within the School of Business Studies and the Faculty of Culture and Media. Yet what makes the university unique are the varied courses that cannot be found anywhere else in Europe, such as the National Graduate School for Geoeconomics, where students can specialize in the history of civilization, politics, economics, culture, and the language of just about every region in the world. We pride ourselves as an institution that encourages the fostering of language skills. Everybody has to learn English,



Dr. Mića Jovanović receiving the Socrates International Award from the Europe Business Assembly.

“I am proud to say that our graduates are placed in top management positions in some of the top banks in Serbia.”

no matter their specialty, in addition to an option of learning a second language like French, German, or Spanish in smaller groups.

The university excels in a number of other fields and also enjoys a strong reputation in sciences with its Graduate Bio Farming School recognized as a leader in its field on a global level.

The Bora Stanković Basketball Academy is another example of a unique program where it’s not basketball as a sport that is taught but rather the



management, coaching, and media relations skills that make up the curriculum. This idea came to us directly from Bora Stanković and his assistant from FIBA, Mr. Lakumović, who got his PhD here in sports management. In fact, the two of them created the first program.

Q: How does Megatrend cooperate with the business community to help graduates integrate smoothly into the professional realm?

MJ: Our close contact with the Chambers of Commerce around the country ensures that Megatrend is no ivory tower, and the university prides itself on turning out students ready to thrive in a real business environment. In this respect, we plan to use our relationship with the Belgrade Chamber of Commerce in offering an Executive MBA course in 2008. We also have close ties with embassies and international companies, especially in the banking sector. I am proud to say that our graduates are placed in top management positions in some of the top banks in Serbia, and many are also working in the government and the various municipalities across the country.

Q: Where do you see Megatrend University in the near future?

MJ: Over the past five years Megatrend has expanded extensively. We have two locations, with our third and newest complex opened on December 27, in conjunction with our 18th anniversary. This building will not only help us accommodate our growth—because of its modern architecture, it will add to New Belgrade’s contemporary facelift. We also plan to build a new campus, near the airport, to help us reach our objective of becoming the second largest university in Serbia. ■

Serbian consumers get the banking bug

Under the watchful eye of the National Bank of Serbia, the country's financial services sector has begun to win a name for transparency and integrity in its dealing with businesses and consumers alike. This can only help attract more businesses and investors into the republic.

Following the collapse of the Milošević regime in 2000, the Serbian authorities were quick to grasp one of the golden rules of the global economy—that a competitive, credible, and transparent financial sector is as critical to the country's ability to attract overseas investment as a pluralist democratic system. It should come as no surprise, therefore, that two of the National Bank of Serbia's (NBS's) proudest achievements are firstly that it has persuaded 85% of the country's banks to open up call centers for their customers, and secondly that in its second year of existence the NBS's own Center for Financial Services Consumer Protection and Market Supervision received over 20,000 calls in the first nine months of 2007—well on course to double the figure for 2006.

The growth in enquiries is a sure indication both of the rapid growth of Serbia's retail banking market and consumer faith in its transparency. This has seen the number of Serbian citizens abandoning 'mattress' economics (storing cash under the bed) in favor of bank accounts soar from 47.8% of the population in 2002 to 65.7% by the end of 2006. Serbia has now overtaken Poland in terms of per capita use of credit cards.

The modernization of the Serbian banking system over the past eight years is a significant achievement. Milošević's regime had disastrously frozen depositors' foreign currency accounts, fed hyperinflation by printing cash, plundered state coffers, and treated cash from state-owned banks as easy credit for troubled industries. The incoming authorities' response was to force doomed banks to close and try to save those in peril.

Their policy started to pay dividends in 2004 when Serbian Eurobonds were listed on the Luxembourg Stock Exchange for the first time. But 2005 was the real watershed year for the

banking sector when no fewer than four state-owned and a further six private banks were acquired by overseas interests who now have majority stakeholdings in 22 of the 37 commercial banks operating in the Serbian Republic. These include most of the republic's largest financial organizations, most notably Delta Bank that was acquired in February 2005 by Italy's Banca Intesta, and Jubanka, bought by the Greek Alpha Bank in the same month.

The arrival of foreign banks has helped raise standards, boost confidence, and increase competition. It also requires innovation, as Jelica Marjanović, President of the Executive Committee of AIK Banka Nis—one of the few independent domestic banks remaining—freely admits: "AIK Bank changed its business philosophy when the foreign banks came here," he says.

"We used to be a corporate bank, but because the new arrivals are oriented to retail banking, we had to move into that sector. This is a perfect example of how competition can influence quality and profit. It is very good that we have so many foreign companies in Serbia."

As a result, the sector is in better health than ever. By the end of 2006, according to the most recent figures from the NBS, licensed banks were managing funds amounting to 55% of Serbia's GDP; the sector's profits were up 127% on the previous year; and both corporate loans and household loans were up 20% and 54.5% respectively. Significantly in the context of the current global credit crunch crisis, corporate deposits also rose by 48% and household deposits by 39%.

And there is more to come. There are still a number of banks active with less than 1% market share. To put this in perspective, AIK Banka Nis is Serbia's tenth largest bank, with 4% of the market. Analysts predict that the twin trends of privatization and consolidation mean that inward investment into the banking sector is far from over. ■

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Telefonija
LEADING
SYSTEM INTEGRATOR

AD Telefonija

Kumodraška 241 | Belgrade
Phone: +381 11 34 04 000
E-mail: office@telefonija.co.yu
www.telefonija.co.yu



115 D, Blvd Mihajla Pupina
11070, New Belgrade, Serbia
Tel: + (381) 11 313 99 55
Fax: + (381) 11 313 99 58
serbia@colliers.com
www.colliers.com

Economic recovery starts property boom

The current surge of inward investment and Serbia's booming economy has created huge demand for both residential and commercial property, particularly in Belgrade. With the issue of land ownership due to be resolved soon, there are good times ahead for the property and construction sectors.

The number of construction cranes that currently make up the capital's skyline is clear evidence of Serbia's economic growth. Belgrade in particular is booming, as more and more private and commercial developments spring up to accommodate the needs of its increasingly affluent urban population and burgeoning business community.

largest residential area with a high population density means that Delta City has attracted some prestigious tenants, including Zara, Marks & Spencer, New Yorker and Esprit.

While this renaissance of the Serbian property sector—which is also beginning to take hold in the cities of Novi Sad and Nis as well as in the capital—is largely a logical consequence of national GDP



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Regarded as the country's cultural capital, Novi Sad is one of the many Serbian cities benefiting from a flourishing property market.

Last year will probably be remembered as the year Belgrade's property sector came of age. At the end of 2006 the Serbian capital's modern office stock stood at approximately 250,000 square meters. It had risen to 390,000 square meters by the beginning of 2008. Among the flagship developments was the expansion of Airport City Belgrade, a groundbreaking multi-use commercial complex that will ultimately boast 126,000 square meters of retail and office space.

The development is located in New Belgrade, which is becoming increasingly popular with both indigenous and foreign businesses. Around 65% of the capital's modern stock is now concentrated in this area; last year it attracted some significant tenants, including Norway's Telenor, PriceWaterhouseCoopers and Proctor & Gamble.

New Belgrade is also home to Delta City. When it opened for business last November, this 87,000-square-meter shopping mall became the biggest in the region and Serbia's first international-style shopping center. The fact that New Belgrade is also the city's

growth, it has also benefited from the lowest VAT rate in the region and the government's decision to halve property tax. Land ownership, however, remains problematic for foreign investors, who are

hesitant to buy land that, under current law, can be bought for 99 years with the risk of a rightful owner showing up to claim it. This obstacle should be removed once the Law on Restitution, currently in draft form, makes it to the statute books.

In the meantime there remain pitfalls for the inexperienced, according to Jovica Jakovac,

Managing Director of Colliers International—the first real estate specialists to open for business in Serbia after the regime change in 2000 and the only one to have stayed open for business in Belgrade since then. "Foreign investors should not expect red carpet treatment when they get here," he warns. "They should have done their homework in advance and should be in contact with a good consulting company which can save them time and money."

It is a question of fortune favoring the brave, he believes. "All the foreigners who have come here to do business are still here working on their second or third project; that says it all." ■

"All the foreigners who have come here to do business are still here working on their second or third project."

Singidunum University

At the forefront of Serbia's attempts to reintegrate with the rest of the world are universities such as Singidunum. The private higher learning institution was founded by teachers who used to work at state universities, who realized that new times called for a new type of education.

"After several decades of working at state universities, they realized that education of the student should not only be based on theory, but that we should combine theory and practice," says Singidunum Rector, Dr. Milovan Stanišić.

The university offers ordinary degree programs that comprise three or four years of full-time study, one-year master studies, and honors degree programs. Curricula and degree formats are modeled on the well-known European and American faculties and colleges, and on the best practices of Serbia's national faculties.

"We cooperate with George Washington University, University Balears from Mallorca, University Ca' Foscari from Venice, University Bologna from Rimini, University Bocconi from Milan and Treviso University, with Cambridge University, Central European University from Budapest, and Primorska from Slovenia."

Testimony to the high caliber of the courses and classes offered at Singidunum means that qualifications gained there are internationally recognized in accordance with the principles of the Bologna Declaration and the European Credit Transfer System (ECTS).

Indeed, what sets Singidunum apart from other universities in the country and region is the fact that it has close ties with other internationally renowned universities. As Rector Stanišić explains, "Singidunum cooperates with Lincoln University from Oakland, California, in the U.S. We offer MBA programs that run over three semesters. Students get double degrees, from both Lincoln and Singidunum, and everything is taught in English, both classes and exams. At present



Singidunum Rector Dr. Milovan Stanišić.

we are offering MBA programs, and the candidates choose one of the two areas of concentration: Financial Management and Investment Banking, and Human Resource Management."

"We also cooperate with George Washington University, University Balears from Mallorca, University Ca' Foscari from Venice, University Bologna from Rimini, University Bocconi from Milan and Treviso University, with Cambridge University, Central European University from Budapest, and Primorska from Slovenia. Another example of our international flavor is that we have 12 visiting professors from eight countries."



As well as insisting that students study two languages, the university also prides itself on the practical nature of its teaching. As Rector Stanišić explains, "Many of our professors own consulting companies where students can have hands-on practise. For example, I own an audit company which is a part of PKF International Company from Chicago. Our university encourages professors to open their own companies because in that way students can get practical knowledge."

At present, Singidunum University has 6,000 students, with 1,200 newcomers enrolled each year. However, it is quality rather than quantity that Rector Stanišić wants to focus on as he outlines his plans for the future growth of the university and aspirations for Serbia. "I definitely see Singidunum reaching higher levels of quality. We want to form a campus, but we need investors. The idea is to find an investor for a Belgrade suburb who would invest money in land and buildings that would be in

"We believe that in a very short period of two or three years we could attract 10,000 students from Asia and Africa."

their ownership, and we would organize education for foreign students from the Middle East, the Far East, and North Africa. Our security procedures are much easier to deal with, and professors from Great Britain, the U.S., and Germany, for example, would come here to teach. In that way all of us would gain, East and West. We believe that in a very short period of two or three years we could attract 10,000 students from Asia and Africa. Shanghai, for example, offered us 5,000 students. They are future friends of ours and friends of Western countries." ■