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Country Report

MEASURES IN THE FIRST PHASE OF BANKING HARMONIZATION WITH EU LEGISLATION - CASE OF SERBIA[1]

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Abstract
Measures in the first phase of banking harmonization are regulated by the following four main EU Directives: First Banking Directive (77/780/EEC), Directive on own funds (89/299/EEC), Directive on a solvency ratio (89/647/EEC) and Directive on deposit-guarantee schemes (94/19/EEC). This article discusses measures undertaken in the first phase of banking harmonization with EU Legislation in Serbia and the results accomplished by these measures and proposes some further steps that have to be implemented in order to accelerate harmonization of the domestic financial system with EU standards. The article analyses banking reform processes in Serbia so far, describes the requirements of the four EU directives mentioned and compares domestic legislation with them. The conclusion is that in Serbia's financial reform the initial positive results have been achieved, but the process has not yet been completed and there are still various problems both at the level of the financial system and at the level of specified financial institutions.

JEL Classification: E44, G34, P31

Keywords: financial system, banking sector, restructuring, harmonization, EU directives

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1. Introduction

The Yugoslav banking system was transformed into a two-tier system as early as the mid-1960s. In other words, commercial banking was separated from the central bank, as opposed to most eastern European countries in transition, which initiated this process in the late 1980s and the early 1990s. With the reforms carried out in 1989, state banks ("old banks") were transformed into joint-stock companies and many new private banks were established.

However, the decade of sanctions, isolation and wars brought about a lagging behind of the overall economy and the degradation of the financial system. At the beginning of its reform, the banking system was characterized by general illiquidity, an oligopolic structure, a heavy burden of non-performing assets, frozen old foreign currency savings, lack of responsibility for the operation of banks, etc.

After the formation of the new Government in 2001, the aims of a thoroughgoing economic and legal reform of society were set and the process of economic stabilization was initiated. One of the priorities of economic policy was the strengthening of the financial system through the restructuring of the banking sector and the revival of the financial market. In the initial phases, the results of this reform were most evident in the field of banking: insolvent banks were liquidated, while the preparations for bank privatization are now under way. Progress has also been made in the development of the financial market, including specifically the adoption of necessary legislation, and thanks to the implementation of the process of privatization through the stock exchange, which contributed to a revival in activity on the capital market.

2. An Analysis of the Banking Reform

Banking reform in Serbia started with the adoption of the Bank Restructuring Strategy, in May 2001. In the first phase, banks were classified into four groups on the basis of a detailed financial analysis of the overall banking sector, aimed at determining the actual state of banks' assets: a) sound banks; b) banks that are solvent, but have been given a deadline for recapitalization; c) insolvent banks of strategic significance and d) insolvent banks without strategic significance. At the same time, it was decided to increase the minimum capital requirement to €5 million.

In the next phase, after it was determined that financial rehabilitation would not be possible, four state banks (Beogradska Banka, Beobanka, Investbanka and Jugobanka) and 19 minor banks, in which 66% of the balance of the overall banking system was concentrated, were liquidated. The remaining banks were classified into: a) banks that can operate autonomously on the market, or A and B category banks; b) banks managed by the Agency for Deposit Insurance and Bank Rehabilitation, or C category banks (3 banks), and c) banks against which liquidation or bankruptcy proceedings have been initiated, or D category banks (23 banks).

To restore confidence in domestic banks and enhance banking efficiency and competitiveness, the minimum required amount of capital was doubled under the Law on Banks and Other Financial Institutions (*Official Gazette of the FRY,* No. 36/2002), thus reaching €10 million. In addition, to reinforce legislation, the current laws and related decisions were amended. A certain number of "greenfield" licences was issued, thus enabling the flow of foreign capital into the domestic banking sector (domestic banks with foreign capital).[2]

3. Privatization in Banking Sector

Bank privatization, as the next phase of the banking reform, started with the adoption of the Bank Privatization Strategy, whereby the privatization method, competent institutions and the schedule of the privatization process were presented in detail. The Bank Privatization Strategy anticipates that before initiating the privatization process banks must clear their balance sheets of old bad debts and potential risks, including the liabilities arising from old foreign currency savings, as well as the liabilities vis-à-vis the Paris and London Clubs. To that end, in 2002, the Law on the Regulation of Relations Between the FRY and Legal Entities and Banks from the FRY Territory Being the Original Debtors or Guarantors vis-à-vis the Paris and London Clubs (*Official Gazette of the FRY,* Nos. 36/2002 and 7/2003) and the Law on the Regulation of the FRY Public Debt Arising from Household Foreign Currency Savings (*Official Gazette of the FRY,* No. 36/2002) were adopted.

With the adoption of these Laws, the government was able to take on banks' liabilities and convert them to public debt. In this way, the government acquired

2. A foreign bank may set up its affiliation only with the status of a legal entity, which practically means that the affiliation has its own share capital and current account, that it may keep its accounts abroad and conclude contracts and that it is subject to all legal procedures. To obtain an operating licence for its affiliation, the parent foreign bank must apply to the NBS, enclosing all necessary documents. In addition, its minimum cash capital must be €10 million. According to Serbia's regulations, it is not allowed to set up a foreign bank's operating unit, i.e. its branch, without the status of a legal entity. The opening of representative offices is regulated by the Law on Banks and Other Financial Institutions and the Decision on the Granting of a Licence for Opening a Foreign Bank's Representative Office in the Territory of the FRY (*Official Gazette of the FRY,* Nos. 55/93, 24/96 and 9/97). A foreign bank may open its representative office so as to conduct market research in the field of banking and financial transactions, as well as to perform preliminary activities relating to the conclusion of a contract and its presentation.

majority interest in some banks, which gave it the right – and the Laws oblige it to do this – to find strategic investors to which it would sell the acquired shares and, thus, carry out the privatization of these banks within a specified period of time. Otherwise, any acquisition of a bank's shares with controlling interest, whereby one acquires 15% of that bank's share capital, as well as any increase in that share, regardless of whether it was acquired on the primary or secondary market, will be subject to the prior approval of the NBS.

Of the 16 banks in which the Republic has the ownership share arising from the debt vis-à-vis the Paris and London Clubs, as well as the debt stemming from old foreign currency savings, the Republic of Serbia has temporarily acquired a majority shareholding in 11 banks (of which three are undergoing the process of rehabilitation) and a minority shareholding in 5 banks. The ultimate aim of debt conversion is to accelerate the privatization process in the banking sector by offering shares of these banks owned by the state for sale. In addition to this model (the sale of the government's ownership share acquired through debt conversion), bank privatization may be carried out by recapitalization or, in other words, by the share issue on the part of banks for the purpose of recapitalization. After the completion of the privatization process, only 3 banks should remain in state ownership: the Post-Office Savings Bank, JUBMES (which will specialize in export insurance) and Ju Garant Banka (which will specialize in the armament industry).

After the government's conversion of debt to an ownership share in banks, the ownership structure of Serbia's banking sector changed significantly (graph 1). According to the 2002 annual report, of a total of 50 banks (including two from northern Kosovo), in 7 banks majority shareholders are foreign banks; in 6 banks majority shareholders are other foreign entities; 15 banks are with dominant private capital; in 8 banks the dominant share is held by socially-owned enterprises; 11 banks (with majority interest held by the Republic of Serbia and 3 of them undergoing the process of rehabilitation) are being privatized, and in 4 banks there is a significant share of state capital. In 2003, another two foreign banks were established (domestic banks with foreign capital), so that in Serbia today there are 9 foreign banks and 12 foreign banks' representative offices.

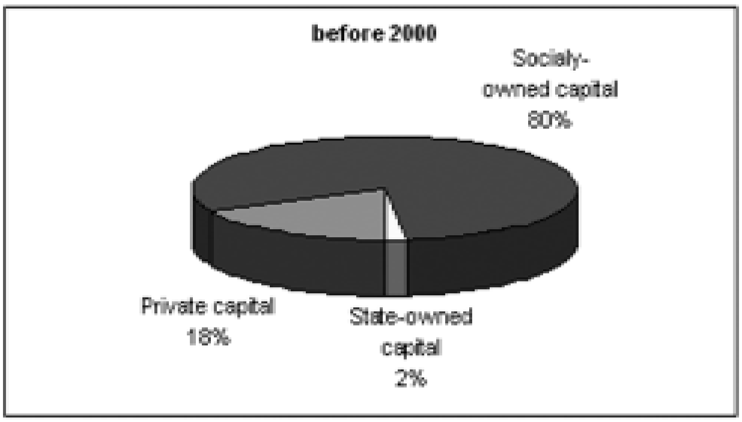
Until the beginning of 2001, the ownership structure of the banking sector was dominated by socially-owned capital. The situation changed after the reforms were initiated, so that in 2003 private capital constituted 49% of the ownership structure of the banking sector.

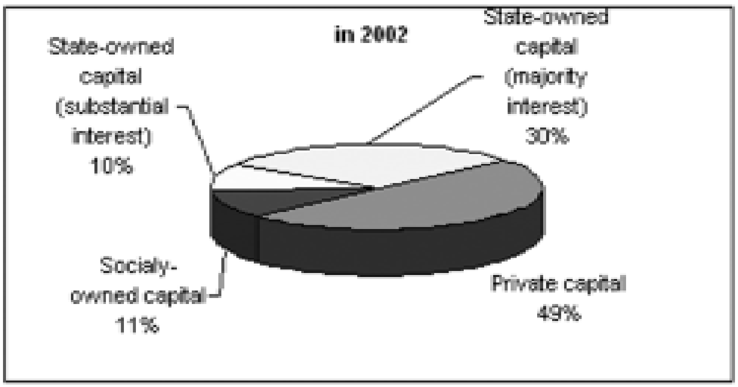
Table 1. Ownership structure of the banking sector in 2003 (in mil. SCD.).

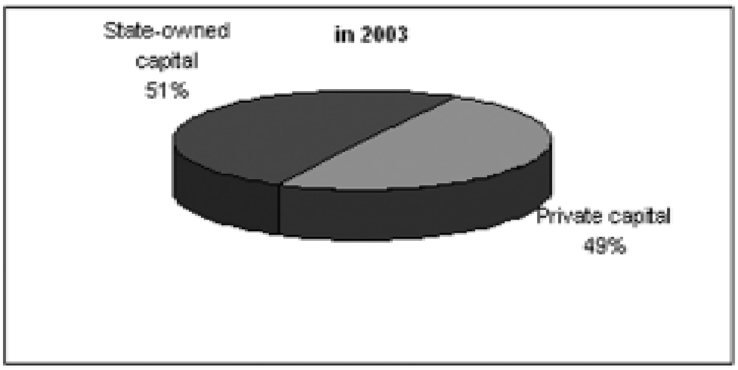
	Balance sum	Share(%)	Capital	Share (%)
Domestic banks	226,351	61.6	63,612	73.7
- state – owned	125,477	34.1	32,330	37.5
- private	100,874	27.5	31,282	36.2
Foreign banks	141,135	38.4	22,691	26.3
Total	**367,486**	**100.0**	**86,303**	**100.0**

Source: Annual report, 2003, NBS

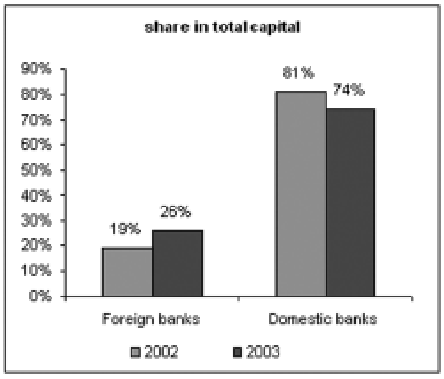
Graph 1. Ownership structure of domestic banks

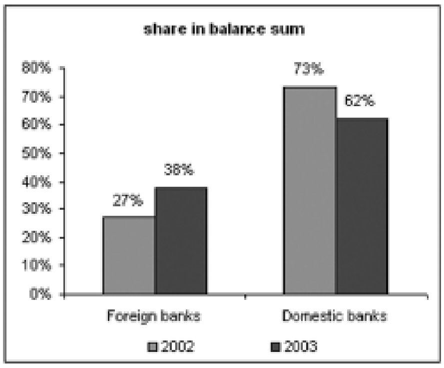


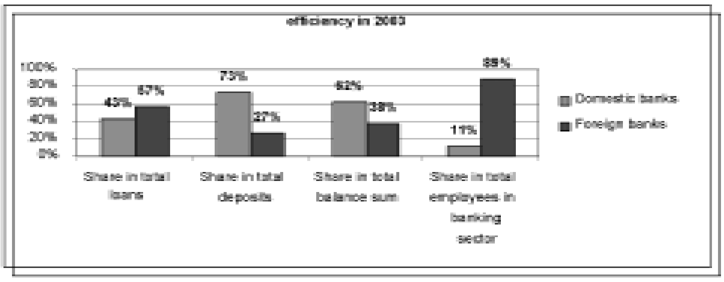




The government's share in commercial banking is declining due to the entry of foreign banks and the beginning of the privatization of state banks. This enhances the efficiency of the banking system in large measure, although it still leaves much to be desired. An analysis of the efficiency of banks in foreign private ownership and banks in dominant domestic, that is, state ownership is especially interesting. Measured by the balance, foreign-owned banks constitute more than one-third of the national banking system (38% in 2003). Their share in the total number of persons employed in the banking sector is much lower (about 11%). Over the past three years, they have increased their credit portfolio, starting virtually from zero. Their current credit supply is also increasing much faster than that of banks in dominant domestic ownership. On the other hand, their share in deposits is nowhere near so high (Graph 2).







It can easily be concluded that banks with dominant foreign capital are more efficient than the rest of the banking sector. With a relatively smaller amount of funds, they manage to increase their yield much faster and to a greater extent in the situation where the credit risk is still high. However, foreign banks are focused primarily on the government bond market and household customer services. They have displayed a marked aversion to risky investments, thus increasing the cost of bank capital, which is granted to the economy through credits. The efficiency ratio may also have other consequences. The advantages of foreign-owned banks will make them dominant on the domestic banking market. This may affect the efficiency of the privatization of state banks, because their selling price will depend, in large measure, on their current and potential market share.

So far, tenders have been invited for the privatization of three banks – Jubanka, Novosadska Banka and Kontinental Banka, offering 88% of government ownership in Jubanka, 82% of government-held shares in Novosadska Banka and 98% of government-held shares in Kontinental Banka. From publicly accessible information it can be observed that the government offers these banks to strategic partners. Those partners must have «... satisfactory experience in the provision of banking services to the population in at least one European country, outside their parent country...» This definition points to the government's preference for bringing a European bank group into the national market by selling these banks. Indirect evidence is also provided by the other tender requirement: the required size of the potential strategic partner – €3 billion of own or consolidated funds– which is relatively large and hardly attainable in local circumstances. There are a sufficient number of banks in the EU which meet these requirements. The only uncertain issue is the selling price. The effects on banking sector development are predictable: a wider range of banking services, increased competition, lower operating costs, as well as the further lowering of interest rates. It can be expected that these effects will also contribute to the creation of a healthier climate in Serbia's financial sector.

4. EU Banking Legislation

Bearing in mind the great significance of the financial system, the EU rules call for gradual harmonization. When the EU initiated[3] the process of coordination of the financial system, its member countries had developed financial systems, so that the basic task of this coordination was not to develop a completely new financial system, but to upgrade the existing national financial systems by adjusting the basic conditions for certain types of financial institutions so as to establish the minimum common standards and create a single market for financial services. Therefore, the harmonization of supervision over the institutions providing financial services has become a priority for the EU member countries. This enabled the mutual recognition of the authority and system of prudent supervision over financial institutions among the EU member countries. On the other hand, financial services in the centrally planned economies were developed on different foundations from those in market economies. As the process of their inclusion in European integration was becoming increasingly more realistic - after the beginning of the transformation of these economies into market-based ones – it proved to be necessary that financial services in these countries should also meet the minimum conditions, thus lessening significant global differences in the structure, operation and supervision of the financial services sector.

Therefore, coordination involved only the establishment of the minimum standards within the preparations for creating a single internal market, and was not an

3. The question of harmonization of the financial systems of the EU member countries and potential EU accession candidates was raised in 1970, when the idea of forming the European Monetary Union was presented in the so-called Warner Report.

attempt to improve and develop the financial sector. Therefore, in addition to the harmonization of their legislations, the candidate countries for accession to the EU must achieve the following aims:

• To establish an efficient banking system that will channel savings into loans to the economy under market conditions;
• To create an efficient payment system;
• To develop the capital market that should contribute to capital investment in industry through developed stock exchanges;
• To establish collective or common investment funds.[4]

Financial services are considered to be a heavily regulated area, in view of the fact that they are regulated by no fewer than 39 EU Council Directives. Harmonization of financial services is divided into five areas: credit institutions, securities, investment funds, money laundering and insurance.

In this paper we decided to point to the most significant aspects of banking harmonization in Serbia, but only to the measures of the first phase. Two factors exerted a decisive influence on such an approach: the fact that the first phase measures must be completely implemented as a matter of urgency, and the fact that the second phase measures are not obliged to be implemented within the next 3-5 years.

5. Harmonization of Serbia's Banking System with the EU Directives

The measures of the first phase of banking harmonization are regulated by the following four Directives:
• First Banking Directive (77/780/EEC),
• Directive on own funds (89/299/EEC),
• Directive on a solvency ratio (89/647/EEC)[5] and
• Directive on deposit-guarantee schemes (94/19/EEC).

The First Banking Directive regulates the establishment of credit institutions, freedom to provide services and minimum amount of initial capital; it defines the basic criteria for issuing an operating license to a credit institution, as well as the conditions under which an operating license can be revoked.

4. White Paper, p. 331.
5. As the result of modifications and additions, the first three Directives were replaced by Directive 200/12/EC. However, the structure of this paper is based on the previous three Directives for practical reasons, because that ensures a logical sequence of steps.

Domestic legislation and the First Banking Directive are not fully harmonized with respect to the establishment of financial companies. As a rule, the candidate countries are required to allow financial companies from the EU to operate in their territory by the end of the specified transitional period (it is recommended that they do this urgently, so as to acquire know-how). However, it is not clear whether the fulfillment of all legal conditions in Serbia entitles a foreign bank to obtain an operating license automatically, because the National Bank of Serbia has the discretionary right insofar as the final decision is concerned. At one time, the NBS held the opinion that, after September 2001, foreign banks should obtain an operating license only through the recapitalization or purchase of a domestic bank. The representatives of the new monetary authorities have not yet confirmed or abandoned this view, which is contrary to the First Banking Directive.

There is a significant problem relating to the mutual (non-)recognition of licenses for the establishment and operation of credit institutions throughout the state union, on which the EU particularly insists. The action plan for harmonization of Serbia and Montenegro anticipates that the banking license issued in one republic should also be recognized in the other republic by the end of 2004. However, it is still uncertain whether this provision will really be applied, owing to different control and supervision standards in the two republics.

There is also a departure from the EU standards with respect to the minimum capital required for bank establishment, which has been increased to €10 million in the dinar equivalent, as opposed to €5 million in the EU. A deviation from the minimum initial capital requirement for banks specified by the EU rules arises from the need for consolidation of the banking sector and the formation of fully capitalized banking groups, which will be able to pay out to their clients. After the full stabilization of the banking sector, this minimum capital is recommended to return the minimum initial capital requirement, or the level set by the EU.

Other provisions of the Law on Banks and Other Financial Institutions[6] have been harmonized with the First Banking Directive.

The Directive on own funds defines the own funds items that can be regarded as operating capital. These items are divided into two groups: original own funds (share capital, legal reserves and funds for general banking risks) and additional own funds (estimated reserves, securities of indeterminate duration, hidden reserves, commitments of the members of cooperative societies and subordinated loan capital). It is anticipated that additional own funds should not exceed original own funds.

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6. *Official Gazette,* Nos. 32/93, 41/93, 50/93, 24/94, 61/95, 28/96, 44/99 and 36/2002.

In respect of the structure of a bank's total capital as prescribed by EU Directive, i.e. original and additional capital, it can be stated that according to the Law on Banks and Other Financial Institutions and specifically pursuant to the Decision on Particular Conditions for the Implementation of Articles 26 and 27 of the Law on Banks and Other Financial Institutions (Official Gazette of the FRY, No. 39/02), the capital structure has been harmonized with the EU standards.

On the other side, the total amount of large and largest possible credits that a bank may grant at the EU level is 800%, whereas the domestic legislator set the limit of 400% of a bank's total capital. However, this more stringent requirement laid down by domestic law is considered to be justified, bearing in mind the widespread illiquidity of the banking system. Therefore, despite being contrary to the harmonization requirements, this indicator should not be changed before a satisfactory financial discipline is established in the domestic economy.

The Directive on a solvency ratio is aimed at coordinating auditing and protecting depositors and investors by defining a solvency ratio for credit institutions. The basic principle that should be observed is that the credit institution must have own funds to the amount of 8% of its unburdened assets and unbalanced securities. In essence, this requirement corresponds with the capital adequacy requirement[7] which should be met by all banks in Serbia. However, a problem may be posed by the fact that it is often disregarded; some banks do not meet this requirement in practice.

The Directive on deposit-guarantee schemes regulates the provision of guarantees to clients for their savings up to a certain amount in the case of a credit institution's insolvency. This Directive requires that each country should have at least one deposit insurance institution. It also requires that all depositors should be informed about the deposit-guarantee scheme. In addition, national supervisory authorities are required to impose sanctions against the banks failing to join the deposit-guarantee scheme.

The deposit guarantee system in Serbia is regulated by the Law on the Agency for Deposit Insurance and Bank Rehabilitation, Bankruptcy and Liquidation (*Official Gazette of the FRY,* No. 53/01). Under the Law, deposit insurance falls within the competence of the Agency, and all banks are obliged - pursuant to the still valid decision of the NBS about the types and amount of bank deposits insured by the Agency (*Official Gazette of the FRY,* No. 22/94) – to insure bank deposits of pri-

7. The Decision on Specific Conditions for the Implementation of Articles 26 and 27 of the Law on Banks and Other Financial Institutions, *Official Gazette,* No. 39/2002.

vate individuals up to the amount of 5,000 dinars per depositor, regardless of the type and number of deposits which a depositor may hold with a bank. Such a deposit insurance system deviates greatly from the EU standards, so that it would be good to make certain changes. As a very delicate and strategically significant activity, the deposit insurance procedure should be removed from the Agency for Deposit Insurance and Bank Rehabilitation, Bankruptcy and Liquidation, bearing in mind that this mechanism in the EU is operated by independent institutions engaged solely in this activity. It is not realistic to expect that one Agency can perform successfully so many significant activities at the same time.

The current deposit-guarantee scheme under which both dinar and foreign currency deposits are insured only up to 5,000 dinars is senseless. On the one hand, it does not provide any security to savers and, on the other, it only generates costs for banks. Therefore, the value of the deposit to be insured must be increased, but during the transitional period – for setting a new level – it will be necessary to take into account the current structure of credit institutions' deposit potential (in Montenegro, for instance, the level is €5,000). However, with the further strengthening of the financial sector, raising of the level of economic activity and the standard of living (which will, in turn, increase the volume of deposited funds), it will be necessary to achieve complete harmonization with the provisions of the EU Directive (in the EU, the deposit insurance level is €20,000).

The method of determining the premiums that banks should pay for the deposit insurance service is in conformity with the EU standards (the method of adjusting the amount of premium to the degree of risk to which the Agency is exposed in the bank in question). After the expiry of the transitional period, it will be necessary to prescribe the form of financing the Agency, which should be based solely on the collected premiums (i.e. to eliminate subsidies from the budget).

In order to surmount the problem of non-harmonization of the domestic deposit insurance system with the EU standards, two laws are being prepared. They have been drafted in accordance with the EU standards and are based on the EU countries' experience: the Law on Deposit Insurance and the Law on the Agency for Deposit Insurance. These laws stipulate: a) an increase in the level of the insured amount of deposit from 5,000 dinars to 230,000 dinars (around €2,800); b) a more efficient and faster collection of the insured amount for which the initial fund of €22 million will been established; c) formation of a modern and autonomous financial institution having deposit insurance as its basic function and d) the introduction of corporate governance into the Agency, that is, the formation of the managing board, supervisory board and the director of the Agency. Apart from harmonization with the EU regulations, the basic aim of these changes is to provide for better protection of depositors in the case of the bank's bankruptcy and further strengthening of confidence in the banking system.

Other requirements - In addition to fulfilling the conditions set by the Directives mentioned, the countries in transition must meet several other conditions. The first condition involves the existence of the basic regulatory environment. It involves regulations governing company formation, accounting, supervision and auditing. In this category, there are some minor deviations from the EU Directives. There is a difference in the requirement set by the first Directive in the field of company law, which requires the disclosure of specified information on the enterprise's business operation. There is no such provision here except in the case of enterprise registration when the data on the establishment of an enterprise are disclosed. There is also a difference as to who issues the certificates and organizes the exams for registered auditors. Under the Law on the Audit of Accounting Records, this is done by the competent ministry in charge of finance, whereas the EU rules prescribe that this task should be performed by an independent association. There are also some differences in specified accounting items (in the chart of accounts).

The next requirement concerns the existence of supervisory authorities with a view to setting the rules for the issuing of operating licenses to credit institutions, auditing and supervision of the application of these rules by financial institutions. Insofar as this set of conditions is concerned, it can be stated that Serbia meets them in full, since all mentioned activities are performed by the NBS.

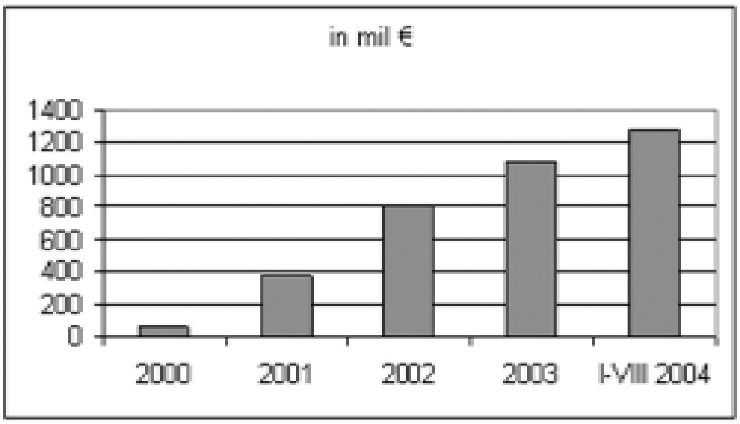
The next requirement concerns mortgage credit development, which anticipates clear ownership rights to land, accurate land registers and the development of qualified appraisers. Serbia does not meet these conditions, since the problem of nationalized property has not yet been solved, which means that ownership rights to land are not clear. There are no accurate land registers either. Although it has been announced that cadastral books will be prepared for the entire territory of Serbia, work has not yet started in earnest. As for the third requirement (the existence of qualified appraisers), it can be stated that there is a great number of agencies offering real-estate valuation services, but there is no evidence of their professional competence. In any case, it would be useful to set up an institution that would issue the certificates for a registered real estate appraiser.

6. The Effects of the Implemented Measures

The results of the activities carried out hitherto within the reform of Serbia's banking sector and harmonization with the EU banking standards are reflected in the recovery of the banking system and its ability once again to mobilize savings and ensure their allocation.

After the implementation of radical structural measures, the banks' capital base began gradually to get stronger, thus enabling the intensification of credit activity and the creation of conditions for the lowering of interest rates. The total balance-sheet amount of the banking sector, which was €4.9 billion in 2001, increased to €5.4 billion in 2003. Early in September of 2004, the deposit base of the banking sector amounted to €3.7 billion, thus increasing by almost 23% since the end of 2003. The strengthening of the banks' deposit base was mostly achieved through an increase in private savings, whose rate (Graph 3) is the best evidence of the extent to which confidence in the banking sector has been restored.

Graph 3. Savings of the population



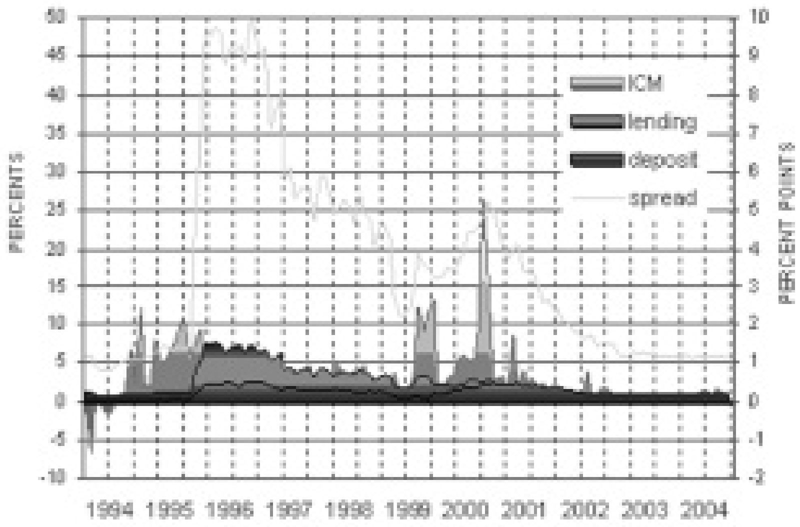
Source: Statistical Bulletin of NBS

Although the term structure of the absorbed private savings is dominated by short-term savings deposits, the increasing number of fixed-time deposits by private individuals is encouraging. This applies especially to foreign currency deposits. The currency structure is dominated by foreign currency saving, which accounts for more than 90% of savings deposits and where more than half of their value is accounted for by deposits between €3,000 and €25,000.

The strengthening of the deposit base has also enabled the intensification of banks' credit activity. Total bank placements in the non-monetary sector, observed since the end of 2001, through August 2004, increased 2.3 times. During the past three and a half years, banks have granted credit to the amount of over €3.1 billion. About half of them involve long-term placements (€1.5 billion). The currency structure of these placements points to the dominance of credits denominated in dinars – so far, 82% short-term and 63% of long-term dinar-denominated credits have been granted. When observing the structure of borrowers over the past three years, it can be concluded that there is an increasing share of the population in the distribution of bank funds, whereby long-term dinar-denominated credits, which are granted to the population, have a faster growth rate than short-term borrowings.

The intensification of credit activity has also been accompanied by a lowering of interest rates (Graph 4). The average annual weighted deposit interest rate, which had been 35.3% in December 2000, had fallen by 12.7% per year in September 2004, while the average weighted annual lending interest rate declined from 80% (December 2000) to 15.1% (September 2004).

Graph 4. Nominal interest rates (monthly), in %



Source: National bank of Serbia

However, interest rates are still relatively high and too expensive for most enterprises, and especially for the ordinary population. There are numerous reasons for this, ranging from a high political instability in the country, high investment risk and collection of invested funds, through an imbalance between the supply of and demand for credit and unregulated right of pledge over real estate, to the *sterilization* of a significant part of the banks' deposit potential through high legal reserve rates.

Therefore, the level and quality of credit supply are still far from being optimal, which, using the standard indicator of development (total credit/GDP ratio), means that the Serbian banking system ranks with those of Central Asian countries (this ratio in Serbia is 18.4, in Armenia and Azerbaijan 7.2, in Georgia 9.8 and in developed countries – higher than 100%)[8].

7. Final Considerations

Financial reform is one of the most important elements in the reform of Serbia's economic system. This reform is interrelated with, and conditioned by, the reform of the real estate sector. A developed financial sector provides efficient support to the real estate sector, but without a developed real estate sector the financial sector cannot ensure a profitable business operation. A delay in real estate sector restructuring in Serbia can be a limiting factor in the development of the financial system.

The financial reform is not a process that can be completed overnight, nor can shock therapy produce positive results automatically. To restore credibility, it is necessary to have a longer period of time and a well-conceived reform strategy.

In Serbia's financial reform the initial positive results have been achieved, but the process has not yet been completed and there are still various problems both at the level of the financial system and at the level of specified financial institutions. There is no doubt that the harmonization of the financial system with EU legislation should be a major priority for the immediate future.

8. IMF, WP No 3/179, page 27, and for Serbia National bank of Serbia.

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