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THE POLITICAL AND ECONOMIC SITUATION OF  
SERBIA-MONTENEGRO AND ITS RELATIONS  
WITH THE EUROPEAN UNION

*This paper was prepared for the Members of the European Parliament. The opinions expressed are the author's and do not necessarily reflect the European Parliament's views.*

Sources:      Agence Europe  
                  European Commission  
                  Economist International Unit  
                  Oxford Analytica  
                  Reuters  
                  World Markets Analysis

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## I. POLITICAL SITUATION

### 1. *Historical background*

#### 1.1. Serbia

Serbia opens to the great Danubian plain to the north and extends to the heart of the Balkan peninsula to the south. It shares borders with almost all the Balkan states. It has a total area of 102 173 sq. km<sup>1</sup> and a population of over 10 million<sup>2</sup>.

The Serbs and Montenegrins are Southern Slavs, who settled in the Balkan peninsula in the seventh century. In the ninth and tenth centuries there was no Serbian state as such but states based on a union of Slav tribes, often dependent on the Byzantine empire. The Serbian state emerged at the time of the Nemanjid dynasty (1170-1371). This became a short-lived empire in the reign of Tsar Dusan (1331-1355), who controlled the greater part of the Balkan peninsula<sup>3</sup>.

After Tsar Dusan's death, his empire broke up into about ten rival principalities, which facilitated the incursion of Ottoman armies into the Balkans. The Ottoman victory over the Serbs at the Battle of Kosovo, the Field of the Blackbirds<sup>4</sup>, in 1389 led to Serbian territory being completely occupied until the nineteenth century.

The autonomy of the principality of Serbia was recognised by agreement with the Ottoman empire in 1830. However, Serbia remained a small enclave state and had to wait until the Congress of Berlin (1878) to obtain full independence, at the same time as the Kingdom of Montenegro.

The idea of forming a Southern Slav union in the form of a nation state emerged in the 19th century, inspired by the universalist ideas of the Enlightenment philosophers. In the same way that German unity was created around Prussia, the Southern Slav union was led by Serbia.

Between 1914 and 1918, the Kingdom of Serbia was the only one in the region to side against the Austro-Hungarian empire. The Serbs thought all these efforts merited a moral recompense. In 1918 they obtained the creation of the Kingdom of the Serbs, Croats and Slovenes (the first Yugoslavia) as a reward to the liberators of the Southern Slavs. However this was not a federal state but a centralised state on French lines, which displeased the Croats and Slovenes and other peoples in the kingdom.

When external threats were added to the internal divisions, the country was not able to resist for very long. The Second World War hostilities exacerbated the antagonism between the various peoples.

Socialist Yugoslavia (the Second Yugoslavia), created in 1945, was the product of the ideals of the Tito's Partisans and the geopolitical situation of the time. The Communist League (the only party) never had any real strategy to deal with the nationalist issue. Referring to Serb hegemony

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<sup>1</sup> This figure includes Montenegro, Kosovo and Vojvodina.

<sup>2</sup> Idem.

<sup>3</sup> This empire is at the origin of Serb nationalist territorial claims.

<sup>4</sup> The Field of Blackbirds lies 5 km from Pristina, hence the importance of Kosovo for the Serbs.

during the First Yugoslavia, Tito advocated 'a strong Yugoslavia with a weak Serbia'. The Serbs felt that the Titoist federation prevented them from developing their national aspirations.

Slobodan Milosevic, whose nationalist and populist views enabled him to take control of the Serbian wing of the single party in 1987, succeeded in obtaining a revision of the Serbian constitution in March 1989, which deprived the provinces of Kosovo and Vojvodina of any autonomy<sup>1</sup>, thus initiating a dictatorial and repressive movement that became entrenched in the next few years. Slovenia, Croatia and Macedonia responded to the Serbs' change in attitude by announcing in June 1991 that they were withdrawing from the Yugoslav Federation, which thus came to an end.

The third Yugoslavia was founded in April 1992 on the ruins of the preceding Yugoslavia. It was an association of two republics, Montenegro and Serbia, the latter flanked by two former autonomous provinces, Kosovo and Vojvodina, and structured as a federation. It was even more ephemeral than its predecessors as it lasted only 11 years. The federation was the victim of the enormous demographic imbalance between the two component entities (10 million inhabitants of Serbia compared with about 600 000 inhabitants of Montenegro), and above all the crushing political weight of the personality of Slobodan Milosevic<sup>2</sup>, who dominated Serbia for more than a decade. The conflicts in Slovenia (1991), Croatia (1991), Bosnia-Herzegovina (1992-1995) and Kosovo (1999) isolated the country and even led to intervention by the international community. After a 78-day bombardment by NATO's forces in 1991, the government in Belgrade had to accept the peace plan and withdraw its army from Kosovo.

## 1.2. Montenegro

Although Serbian-speaking and Orthodox in faith, the Montenegrin nation is distinct from the Serbian nation. Montenegro emerged in the 11th century. In 1516 it was placed under the theoretical suzerainty of the Ottoman empire. At its head was a prince-bishop, the Bishop of Cetinje, who was also Prince of Montenegro. Its independence was recognised at the Congress of Berlin (1878) and it became a kingdom in 1912. At the end of the First World War, the Montenegrins were the most fervent partisans of union with the Serbs. In November 1918 a national assembly deposed King Nikola and voted for incorporation in the Kingdom of Serbs, Croats and Slovenes. In 1945 Montenegro became one of the six republics of the Yugoslav Federation (the smallest at 13 812 sq. km) and the Montenegrins one of the peoples making up Yugoslavia. Podgorica (called Titograd until 1992) then replaced Cetinje as capital. Following the implosion of the Republic of Yugoslavia, Montenegro, remained faithful to Serbia and the two formed the third Federal Republic of Yugoslavia (1992-2003). Nevertheless it had very little influence in the republic's government and suffered a great deal from the sanctions against Serbia. The election in October 1997 as President of Montenegro of Milo Djukanovic, who had clearly spoken out in favour of increased autonomy with regard to Serbia further soured relations between the two partners in the Federation.

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<sup>1</sup> These provinces had had a large measure of autonomy since 1974.

<sup>2</sup> As a nationalist, Mr Milosevic had been influenced by the 'Memorandum', written in 1986 by members of the Serb intelligentsia, who denounced the injustices suffered by and the sacrifices made by the Serb people, who had no right to their own state. He thought the Serbs should again become a subject of history and control their own nation state.

### 1.3. Kosovo

The territory of the present province of Kosovo remains very dear to the hearts of Serbs as it was the cradle of their nation (end of the 12th to the end of the 14th centuries). For five centuries Kosovo was a dependency of the Ottoman empire. It was during this period that the Albanians<sup>1</sup> were massively converted to Islam. The first Balkan war permitted the emergence of an independent Albania but Kosovo remained in Serbia's orbit. The Yugoslav constitution of 1974 granted Kosovo (and Vojvodina) prerogatives almost equal to those of a republic. In 1989 the Serbian Government restored its authority over the autonomous provinces. A year after its official abolition by the authorities in Belgrade, the Kosovan Parliament met clandestinely to proclaim a 'Republic of Kosovo'. Legislative and presidential elections were held in May 1992. The Democratic League of Kosovo won a majority and its leader, Ibrahim Rugova, assumed the presidency of the 'Republic'. The same majority and leader were again approved by the Albanian voters of Kosovo in March 1998. The Belgrade authorities did not recognise the validity of these elections and rejected the idea of a 'Republic of Kosovo'. At the same time they began stringent clamp-down on any hint of free expression by the Albanian community. Certain analysts have even described the situation in the province as a form of apartheid.

### 1.4. Vojvodina

Vojvodina is a multinational region in the north of Serbia proper, which was formerly dependent on the Kingdom of Hungary. At the creation of Yugoslavia in 1918 it was incorporated into the new country. In 1946, to take account of the ethnic mosaic that has been a characteristic of this territory since the 18th century, an autonomous region of Vojvodina<sup>2</sup> was created in the Republic of Serbia.

The rise of nationalism at the end of the 1980s and the outbreak of conflict in Yugoslavia in the following decade seriously affected the region's multinational balance. In 1989 Vojvodina was deprived of its autonomous status. Since then the authorities have undermined minority rights (especially since Mr Milosevic was in power) to the benefit of the Serb majority (57.3% of the population of the province according to the 1991 census).

## 2. *Internal policy*

### 2.1. Institutional system

On 4 February 2003 the new common state of Serbia and Montenegro replaced the Federal Republic of Yugoslavia (FRY). The republics share a titular president, and run joint policies on defence and foreign affairs, but little more. Moreover, both republics have the option of declaring independence after an initial three-year period.

The **federal Parliament** (Federal Assembly – Skupstina) is unicameral and was established on 4 March 2003. The assembly has 126 seats, with 91 allocated to Serbia and 35 to Montenegro. Members of the new Federal Assembly were chosen by the parliaments of the two republics and will serve for two years. A direct election is scheduled for 2005.

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<sup>1</sup> Today the largest minority in the region (82.2 % according to the 1991 census).

<sup>2</sup> The territory was called Vojvodina between 1848 and 1860.

The **President**, currently Svetozar Marovic from Montenegro, is the head of state and was elected by the Federal Assembly on 7 March 2003 for a four-year term.

The **Council of Ministers** is headed by the President and answers to the Federal Assembly. In addition to the President, there are five ministers (defence, foreign affairs, foreign economic relations, domestic economy and human rights): three nominated by Serbia and two from Montenegro.

The **judicial system** consists of communal courts, county courts, republican supreme courts, the Federal Constitutional Court and the Federal Court. The Federal Court is the highest court in the common state of Serbia and Montenegro and rules on disputes between Serbia and Montenegro, and between the common state and the republics. The independence of the judiciary is formally guaranteed by laws in both Serbia and Montenegro. Yet, particularly in Serbia, judges complain of excessive interference of the executive power and of media campaigns aimed at discrediting the judiciary through allegations of corruption and links with organised crime.

The Republics of Serbia and Montenegro have their own parliaments, governments, and presidents. The Constitutional Charter that brought the common state into being also requires **Serbia** to draft a new constitution. The drafting and approval (by both parliament and a public referendum) were scheduled to have been completed by late summer 2003, but will stretch into 2004. The current institutional system is based on the Serbian constitution of 1989. Serbia has a unicameral parliament, with 250 seats. The President is elected by universal suffrage. Natasa Micic, the parliamentary speaker, has served as acting president from January 2003 till July 2004.

**Kosovo's** status remains uncertain. Since 1999, it has been governed by a UN interim administration.

**Montenegro's** institutional system is based on the constitution of 1992. The parliament is unicameral and comprises 75 seats. The head of state is the President (currently Filip Vujanovic), who was elected by universal suffrage.

## **2.2. Recent events**

### *2.2.1 Serbia*

#### (a) The end of Milosevic's regime and the DOS coalition

Yugoslav politics underwent a major change in October 2000 following Mr Milosevic's defeat in the presidential election on 24 September by Vojislav Kostunica, the candidate of the Democratic Opposition of Serbia (DOS). Although Mr Milosevic at first refused to accept the result of the vote, a wave of popular protests forced him to concede defeat. The DOS followed up its triumph by winning an early general election in Serbia in December, obtaining 176 seats out of the total of 250. The DOS went on to form a government and Zoran Djindjic, leader of the Democratic Party (DS), the largest in the DOS coalition, became Prime Minister of Serbia.

The DOS, originally a coalition of 18 political parties, came together to prevent Slobodan Milosevic from regaining power after the September 2000 elections. It did not have a broad ideological basis in common. The two leading parties were President Kostunica's Democratic Party of Serbia (DSS) and Serbian Prime Minister Djindjic's Democratic Party (DS). Already in 2001, the coalition effectively split into two factions, one around Kostunica, the other around Djindjic. A major disagreement arose concerning the extradition of former President Slobodan Milosevic to the International Criminal Tribunal for the former Yugoslavia (ICTY): while President Kostunica and his DSS were opposed and considered his extradition to be against the Constitution, the Serbian Prime Minister Djindjic and his cabinet reacted to international pressure and turned Milosevic over on 28 June 2001. The decision caused serious tensions in Yugoslavia, but the success of the donors' conference following Milosevic's extradition calmed political outrage. However, all DSS cabinet ministers resigned following this move<sup>1</sup>.

Kostunica and Djindjic argued constantly over the pace of reforms and western integration as well as cooperation with the ICTY. The continuing conflict between the two and their respective parties culminated in June 2002 with the withdrawal of the DSS from the coalition.

(b) The assassination of Zoran Djindjic and the subsequent state of emergency

On 12 March 2003, Zoran Djindjic, the Serbian Prime Minister, was assassinated outside of the main government building in Belgrade. The government immediately declared a state of emergency that lasted until 22 April 2003. On 19 March 2003, parliament approved the nomination of Zoran Zivkovic, then Interior Minister, as new Prime Minister.

During the 42-day state of emergency the government embarked on 'Operation Sword', a wide-ranging crackdown against organised crime and its supporters. Criminal charges were filed against more than 3.000 people, including several members of the so-called Zemun clan, a Belgrade-based criminal gang that has close ties to elements of the state security services, which was identified as the organiser and perpetrator of the killing. At the end of April 2003 the authorities declared that the murder of Mr Djindjic was part of a far-reaching conspiracy to overthrow the government. On 21 August, the Serbian government issued indictments against 44 people suspected of conspiring or taking part in the killing of Zoran Djindjic.

After the assassination, the government was also quick to disband the 'Red Berets'<sup>2</sup>, a paramilitary special forces unit that had close links with the criminal underworld<sup>3</sup>. Milorad Lukovic, the leader of the Zemun clan and prime suspect of the killing of Djindjic, had been the leader of the Red Berets until 2002.

(c) The parliamentary elections in December 2003 and the political scene

On 13 November 2003, parliamentary speaker and acting President Natasa Micic, announced early parliamentary elections for 28 December 2003 and dissolved the parliament. The decision

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<sup>1</sup> Reuters Business Briefing, 21 June 2002, 'Yugoslavia: The Disintegrating Coalition' by Transitions Online.

<sup>2</sup> Created by Mr Milosevic in 1991, the Red Berets included known criminals and members of various paramilitary militias.

<sup>3</sup> According to Serbian judicial reports, Red Berets associated with the Zemun Mafia clan was responsible for over 50 homicides in Belgrade, organised drug trafficking and the creation of a trafficking network in the former Yugoslavia and elsewhere in Europe.

came after some smaller parties in the DOS coalition had withdrawn their support from the government, leading to the loss of its majority in parliament. The government also faced a no-confidence vote. The weeks before, the opposition had accused the government of incompetence and rampant corruption and both the DSS and the Radical Party had submitted motions of no-confidence in the government. On 18 November, the DOS presidency officially concluded that the DOS coalition had ceased to exist with the call for early elections.

The dominant force in the former DOS coalition, the Democratic Party (*DS*) initially announced that it would contest the elections on its own, but agreed later to run joint lists with smaller parties. The party was founded by Zoran Djindjic and others following the collapse of single-party rule in the late 1980s.

The *G17 Plus* is a former think-tank that transformed itself into a political party in December 2002. The new party is led by Miroljub Labus, a former federal deputy prime minister who ran unsuccessfully for the Serbian presidency in 2002. There are relatively few ideological differences between the former DOS coalition and the G17 Plus; however, the G17 Plus is now competing for the same segment of pro-reform voters.

The *DSS* was formed in the early 1990s by Vojislav Kostunica following a dispute with Mr Djindjic's DS. The DSS is more conservative and nationalistic than most of the governing parties and favours a more gradual pace of reform, not only of the economy but also of institutions such as the army.

The Socialist Party of Serbia (*SPS*), the party of the former Yugoslav president Slobodan Milosevic, became the largest opposition force in the Serbian parliament after the 2000 election, with 37 seats. However, the SPS has since seen its popularity decline, owing to the absence of Mr Milosevic from the domestic political scene and a series of internal arguments.

The Serbian Radical Party (*SRS*) is an extreme nationalist party led by Vojislav Seselj. It won 23 seats in the 2000 election. The strong electoral support for the SRS was confirmed in the first round of the Serbian presidential election in late September 2002, when Mr Seselj came third with 23.2% of the vote, and again in the November 2003 presidential elections, when the SRS's candidate Tomislav Nikolic won 46.2 % of the votes.

In the extraordinary parliamentary elections on December 28, Vojislav Seselj's Serbian Radical Party (SRS) won 82 seats and former Yugoslav President Slobodan Milosevic's Serbian Socialist Party (SPS) 22 seats. More moderate parties, the Democratic Party of Serbia (DSS), Democratic Party (DS), G17 Plus and a coalition of the Serbian Renewal Movement (SPO) and Velimir Ilic's New Serbia (NS) between them won 146 of the 250 seats in the Serbian Assembly.

According to observers, the SRS victory was not the result of a resurrection of Serb nationalism. Some of those who voted for the Radicals did so because of their extreme nationalistic attitudes, but some wanted to vote against the former ruling Democratic opposition of Serbia (DOS) coalition and its leading party, the DS, as a reaction against its record over the past three years. There were several reasons for the SRS success, apart from the poor and unconvincing election campaign fought by the two main moderate parties, the DS and DSS: the economic and social



difficulties, the allegations of corruption and misconduct within the government, the quarrels between the more democratically oriented parties and the foreign interference<sup>1</sup>.

The current Serbian Cabinet was finally sworn in on 2 March 2004, two months after the parliamentary elections of 28 December 2003. These saw a major increase in support for the ultra-nationalist Radicals, to the detriment of reformist parties.

Although reformist parties of various hues did win a majority of seats, it proved impossible for them to form a majority coalition, mainly because of the differences between the DS and DSS. A minority coalition of the DSS, the economically liberal G17 Plus and the monarchist SPO-NS will balance between the socialists and the DS parliamentary support.

#### (d) Presidential elections in Serbia

Presidential elections were again held on 16 November 2003. Two previous attempts to elect a president (in September/October and December 2002) failed owing to low voter turnout, leading Natasa Micic, the speaker of the Serbian Parliament, to take over as acting president in January 2003, when the term of Milan Milutinovic expired. Since a new Serbian constitution has not yet been adopted, the November election also took place under the existing rules, requiring a turnout exceeding 50 % in the first round for the vote to be valid.

Dragoljub Micunovic, the speaker of the federal parliament, contested the elections as the candidate of the DOS coalition. The G17 Plus and the DSS boycotted the vote. On election day, voter turnout stood below 39 %, leading to yet another annulment of a presidential election. Micunovic, the DOS candidate obtained only 35.4 % of the votes cast, while Tomislav Nikolic, the candidate of the ultra-nationalist Serbian Radical Party, won 46.2 % of votes. Four other candidates shared the rest of the votes. This result was considered a major blow to the reformist forces in the country.

Finally, on 27 June 2004, Boris Tadic, the reformist, pro-European Union, head of the Democratic Party (DS) was elected Serbian President, beating the ultra-nationalist Serbian Radical Party's Tomislav Nikolic by 54% to 45%. The election was a crucial juncture for Serbia, which reform could have been jeopardised if the populist Nikolic had been elected. The DS also performed well in the September 2004 local elections, confirming that it and the SRS are now Serbia's most popular parties. By contrast, support for the moderately nationalist Democratic Party of Serbia (DSS), which heads the governing coalition, has fallen. The reformist vote appears to be consolidating under the DS banner and the nationalist under that of the SRS. According to observers, after Tadic's elections, a cohabitation between the government and the new president may continue for at least the next six months, during which a new constitution should be adopted, to be followed by parliamentary elections.

#### (e) Serbia and ICTY<sup>2</sup>

The compliance with the country's obligations under the statute of the ICTY is stagnating, and even deteriorating. A public campaign against the Tribunal, conducted virtually since October

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<sup>1</sup> According to observers the declarations of some European leaders instructing people how they should vote encouraged people to vote for the other parties.

<sup>2</sup> International Criminal Tribunal for the Former Yugoslavia.

2000 by some leading Serbian politicians, resulted in overwhelming public hostility against the ICTY and a practical refusal to proceed with new extraditions. The DS and the two junior coalition number parties, G17 Plus and SPO-NS, want cooperation, but the DSS, which leads the government coalition, continues to resist it, although Serbian Prime Minister, Vojislav Kostunica visiting Brussels on 4 November 2004 for meetings with the EU High Representative for CFSP, Javier Solana, provided assurances that his country is going to cooperate with the ICTY<sup>1</sup>. Cooperation with The Hague Tribunal is crucial for the country's progress towards a Stabilisation and Association Agreement (SAA) with the EU and NATO's Partnership for peace. Furthermore, Secretary of State Colin Powell refused on the 31 March 2004 to certify that Belgrade is cooperating with ICTY. Washington has suspended the rest of the 100 million dollars in aid for the financial year, apart from humanitarian aid. Belgrade may regret the loss of US support, not only at such institutions as the IMF, but also in finding a solution to the Kosovo problem.

### 2.2.2 Montenegro

In the parliamentary *election of 22 April 2001*, the major political parties were split into two blocs: those favouring a constitutional link with Serbia, albeit redefined (the coalition 'For Yugoslavia'), and those preferring a looser relationship eventually leading to full independence (the coalition 'Victory for Montenegro' and the Liberal Alliance of Montenegro (LSCG) running independently in the elections). Following the elections, the 'Victory for Montenegro' coalition, which won the largest number of seats, formed a minority government with the parliamentary support of the LSCG. In April 2002, however, the LSCG and the Social Democratic Party (SDP), both supporting Montenegro's independence, withdrew their support from the government. This move came in protest of parliament's approval of the Belgrade agreement on the future union of 'Serbia and Montenegro', which implies postponing a referendum on independence for three years. A vote of confidence on 23 May 2002 led to the dismissal of Prime Minister Filip Vujanovic and his cabinet.<sup>2</sup> When Vujanovic failed to form a new government in July, early elections were called.

The early *parliamentary elections* took place on **20 October 2002** with high voter's participation (74.6 %)<sup>3</sup>. The two major opponents were the re-named continuations of the political coalitions of the 2001 elections. President Djukanovic's Democratic Party of Socialists (DPS) and its Social Democrat allies won the elections, gaining 39 seats in the 75 seat parliament. Djukanovic resigned from the Presidency to become Prime Minister. The speaker of the Parliament, Filip Vujanovic, became acting president.

In the direct *presidential elections* on 11 May 2003, Montenegrin voters elected Filip Vujanovic as president. Mr Vujanovic, the candidate of the ruling DPS, easily topped the poll with around 64% of the vote. Mr Vujanovic had also won the presidential elections held in December 2002

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<sup>1</sup> The previous government cooperated with the tribunal, albeit not always easily, extraditing Slobodan Milosevic and several other notable figures. Recently, however, cooperation has stalled. Former Bosnian Serb General Ratko Mladic remains at large and four Serbian generals have not been extradited. Following a negative public reaction, the government has postponed the handover of the indictees.

<sup>2</sup> OSCE/ODIHR Election Observation Mission Report on Municipal Elections in the Republic of Montenegro, 21 June 2002 and World Markets Country Analysis: 'Montenegro heads for Early Election', 11 July 2002, and 'Controversy over 6 October Montenegro Elections', 22 July 2002.

<sup>3</sup> OSCE/ODIHR Election Observation, Final Report, 28 November 2002.

and February 2003, but these were declared invalid because turnout was below the legal minimum of 50%.

In May 2003, the main opposition parties – the Socialist People’s Party (SNP), the Liberal Alliance of Montenegro (LSCG), the People’s Party (NS) and the Serb People’s Party (SNS) – walked out of the legislature in protest against a decision by Radio Televizija Crne Gore, the state-controlled broadcaster, to stop broadcasting parliamentary sessions in full. The parties continue their boycott, but Mr Djukanovic’s DPS and the Social Democratic Party (SDP), the two members of the ruling coalition, can continue to govern since they have enough MPs between them for parliament to be quorate. However, analysts consider that a long-term boycott of the legislature could seriously damage the government's credibility and hinder the implementation of laws at local level.

A looser union between the Republics of Serbia and Montenegro was encouraged by the EU in 2002, but it was not until its ratification by the federal and republic parliaments in February 2003 that Serbia and Montenegro officially came into being, replacing Federal Republic of Yugoslavia. No referenda on independence can be held by either side until 2006. In practice, however, Prime Minister Milo Djukanovic is coming under pressure to push for one before that date. In August 2004, he announced that he was planning to mount a referendum, but after the European Union made it clear that it would not countenance that, he backtracked but said that he would continue to push for an agreement that will see the union dissolved earlier than 2006. Opinion polls show that in any case, voters would actually be unlikely to approved Montenegro independence in a referendum at present.

### 2.2.3 Kosovo

Since 10 June 1999, Kosovo is under temporary international (UN) administration, according to United Nations Security Council Resolution 1244. While being effectively governed by the UN Interim Administration (UNMIK), Kosovo officially remains part of Serbia. Its final status remains undecided. Finding a solution between the Albanians' desire for independence and the Serbs' wish, supported by Belgrade, to restore Serbian sovereignty (albeit with extensive political autonomy) is one of the major challenges of the region.

**UNMIK** is currently headed by Soren Jessen-Petersen. He is the successor of Harri Holkeri who resigned in the wake of March 2004 riots. The violence in March was a heavy blow to the slow improvement in inter-ethnic relations. To implement its mandate, UNMIK has established 4 pillars, integrating the UN, the OSCE and the EU. Pillars I and II (Police and Justice, Civil Administration) are directly led by the UN, while pillar III (Democratisation and Institution building) is led by the OSCE and Pillar IV (Reconstruction and Economic Development) by the European Union. In line with Resolution 1244, UNMIK is responsible for the transitional administration of Kosovo as well as for organising and overseeing the development of provisional institutions for democratic and autonomous self-government pending a political settlement, including the holding of elections.

Legislative *elections* to provide an interim assembly and government in Kosovo on 17 November 2001 were won by Ibrahim Rugova and his Democratic League of Kosovo (LDK).

Local elections were held in Kosovo on 26 October 2002. Ibrahim Rugova's LDK secured the most councillors in the 30 municipalities of Kosovo, the Democratic Party of Kosovo came second and third place was secured by the Serb parties and associations.<sup>1</sup> The Kosovo-Serbs had only participated in the elections in the five municipalities where they are the majority and boycotted the elections in the others.

The first *high-level talks* between Serbian and Kosovo officials since the war in 1999 took place on 14 October 2003. Discussion focused on four areas: the return of refugees, missing people, transport and communications and energy. Working groups of officials from Serbia and the local Kosovo Albanian authorities will continue discussions on these issues. However, the meeting also highlighted the persisting differences, with Kosovan President Rugova insisting on independence for Kosovo and Serbian Deputy Prime Minister Nebojsa Covic on Kosovo being a part of Serbia. In expectation of the dialogue, the Serbian parliament (followed by the joint Serbia-Montenegro parliament) had already adopted a declaration in August 2003, asserting that Kosovo should remain a province of Serbia, with wide autonomy.

The results of the legislative elections in Kosovo on 23 October 2004 set the seal of victory on the Democratic League of Kosovo, the party of the current President, Ibrahim Rugova, who won 47 seats out of the 120 in parliament. A coalition government thus had to be formed. The Serb minority massively boycotted the elections, despite conflicting messages from ntradictoires de Belgrade<sup>2</sup>, mais devrait néanmoins disposer des dix sièges qui lui étaient, d'avance, réservés<sup>3</sup>.

Talks on Kosovo's final status had already been preliminarily scheduled for mid-2005. In the wake of the wave of violence that swept the province in March 2004, the UN reiterated its 'standards before status' stance, but put forward a revised programme of eight key standards that have to be met. These cover the rule of law, institutions, freedom of movement, the return of refugees, the economy, property, rights, dialogue between Pristina and Belgrade on practical issues, and an increase in professionalism in the Kosovo Protection Corps (KPC). However, although some talks on practical issues had been progressing, the challenge of meeting these standards by mid-2005 appears almost insurmountable, especially after the March 2004 events and the recent parliamentary elections boycott.

#### 2.2.4 *Vojvodina*

Recently, there have been reports of an increase in the number of incidents against members of the Hungarian and other minority communities in Vojvodina. According to the Serbian police, more than 50 ethnically base incidents have occurred in the last 20 months. These incidents have included fights, attacks, the desecration of cemeteries and anti-Hungarian graffiti. Ethnic Hungarian politicians in Vojvodina and politicians from Hungary itself complain that the Serbian police had not arrested or prosecuted any violence against Hungarians in Vojvodina. On September 16, the European Parliament adopted a resolution calling for an investigative mission to Vojvodina and for the Council and Commission to raise the issue of minority rights in Vojvodina with the Serbian authorities and press for measures to prevent more incidents.

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<sup>1</sup> Reuters Business Briefing, 3 November 2002.

<sup>2</sup> Boris Tadic, the President of Serbia, called on the Kosovan Serbs to vote but numerous Serbian leaders, including the Prime Minister, Vojislav Kostunica, supported the Serbian Orthodox Church in calling for a boycott.

<sup>3</sup> Fewer than 1 % of the Serbs in Kosovo voted.

### 2.3. External policy

The new common state of Serbia and Montenegro has continued to pursue the broadly pro-Western foreign policy taken by the former Yugoslavia since the downfall of Slobodan Milosevic in October 2000. After the death in March 2003 of Mr Djindjic, the Serbian authorities stepped up their efforts to hand over war crimes suspects to the ICTY in The Hague, which improved their relations with the European Union and the United States.

Serbian president Boris Tadic embarked on a week-long visit to the US almost immediately after his inauguration, holding talks with leading officials. However, Serbia and Montenegro did not sign an agreement not to extradite US citizens to the International Criminal Court (*ICC*) and therefore stands to lose several million dollars of US military assistance in 2003-04. Apart from pressure from the EU, the main reason why Serbia and Montenegro has not yet signed the agreement is a domestic issue. Mr. Zivkovic said that he would find it hard to explain to the Serbian people why the government should help to protect US nationals from possible prosecution in the ICC when the US is simultaneously putting pressure on Serbia to send war crimes suspects to the ICTY.

Relations with Russia continue to be good, bolstered by the fact that Russian investors have taken an interest in investing in the country, particularly in Montenegro. Serbia appreciated the fact that Russia sent a substantial amount of aid after the March 2004 violence in Kosovo.

At the beginning of April 2003, Serbia and Montenegro officially became the 45th member of the *Council of Europe*. In June 2003, Serbia and Montenegro formally applied for membership of *NATO's Partnership for Peace* (PfP) programme, which is regarded as a stepping-stone towards eventual membership of the alliance. NATO officials, however, have said that Serbia must first arrest (or help to arrest) General Ratko Mladic, the former commander of the Bosnian Serb army and the main ICTY war crimes indictee still at large, and fulfil several other conditions.

Serbia and Montenegro has made substantial progress in improving its bilateral relations with *neighbouring countries*, especially the successor states of former Yugoslavia. On 25 May 2001, an agreement was concluded on the division of the assets of the former Socialist Federal Republic of Yugoslavia (SFRY) between the successor states. The final signature came on 29 June 2001. In June 2001, Albania, Bulgaria, Bosnia and Herzegovina, Croatia, FYROM, Moldova, Romania and Serbia and Montenegro signed a Memorandum of Understanding for liberalising trade in the region, which provides for the establishment of a network of *Trade Agreements* by the end of 2002 aimed at liberalising at least 90% of trade among the parties within a transitional period of six years.<sup>1</sup>

Serbia and Montenegro's relations with *Croatia* improved further on 10 September 2003, when Stipe Mesic, the Croatian president, made the first official visit to Belgrade by a Croatian head of state since 1991. Mr Mesic and Mr Marovic, the president of the common state, exchanged apologies for the crimes carried out during the 1991-95 war. Relations with *Albania* have improved substantially, with the re-establishment of full diplomatic relations in September 2002 and increased dialogue at political level. However, the resolution of the Serbian Parliament

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<sup>1</sup> For details see: <http://www.stabilitypact.org/regional.html>.

declaring the Kosovo province an integral part of Serbia, has caused some tensions between the two countries. The Albanian government also recently signed a free-trade agreement with Kosovo, which led to protests from Serbia and Montenegro.

## **II. ECONOMIC SITUATION**

### **1. *Introduction***

Serbia and Montenegro came into being in early 2003 as a new, looser union between the two republics. Their economies are fairly different, and although the European Union, in particular, is urging harmonisation as a precondition of closer integration with the EU, this is proving difficult to achieve.

Regional wars, the imposition of international sanctions, the loss of the former Yugoslav market left GDP in the late 1990s at around one-half of its 1989 level and prevented radical reform of the Serbian economy during the 1990s. However, the post-Milosevic government, reformist and pro-western, made rapid progress and the country is no longer a pariah within the international economic and political community.

Montenegro's population and economy are much smaller than Serbia's; it accounts for around 7% of Serbia's economy. In its quest for greater independence from Serbia, the republic has introduced divergent legislation and has its own monetary, tax, and customs regimes. Its macro-economic goals, however, are largely similar to Serbia's. Podgorica has made faster progress than Belgrade to date on the introduction of business-friendly legislation. It has also progressed further on administrative reform. Still, the country is plagued by concerns over a lack of transparency, and therefore of competitiveness.

### **2. *Economic policy***

While the first post-Milosevic government was successful in bringing the country towards fragile macro-economic stabilisation, the passage of key legislation suffered as a result of political frictions or by general fear of social discontent. The Kostunica government contains some notable reformist economic liberals but their overall room for manoeuvre is limited by the populist tendencies of other government members and the fact that the government does not have enough parliamentary support.

On the macro-economic side, the government's strategy focuses on maintaining monetary stability and further reducing inflation, as well as on the reform of state spending. In terms of stimulating production and growth, the main accent is on attracting foreign investment by legislative improvements to the business climate, such as new laws on company registration and bankruptcy. These reforms essentially build on initiatives that were launched by the Djindjic government, but were not brought to fruition. The privatisation programme accelerated markedly in 2003, when the Serbian authorities concluded a series of major sales<sup>1</sup>. However, differences within the government over privatisation have caused the restructuring and sale of state-owned

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<sup>1</sup> Aleksandar Vlahovic, the economy and privatisation minister said that 1,117 companies were privatised from the beginning of 2001 until the end of February 2004. These sales generated €1.3 bn in revenue for the budget, €775 m in new investment and €280 m for social programmes.

assets to slow down in 2004. In Montenegro, according to the Commission, privatisation has not yet brought satisfactory results and 40% of industry remains in public hands.

Economic re-integration of Serbia and Montenegro remains a major challenge. At the end of August 2003, the parliament of Serbia and Montenegro finally adopted the action plan for trade and the internal market. This action plan implies the harmonisation of import tariffs on more than 8.500 products. The two republics pledge to enforce unified tariffs on 93% of these goods immediately.

### **3. Key sectors**

#### **3.1. Agriculture**

Agriculture is a significant sector in Serbia, and much less so in Montenegro. In Serbia, it employs some 17% of the population, and accounts for around the same percentage of the economy, which in the short term is dependent on a good level of exports from the sector. The plains in the north of the country produce wheat, maize, sunflower oil, sugar beets and tobacco. Fruit farming also occupies a prominent place, and livestock productions are also important. The private sector owns about 85% of the cultivable land area, and produced 83% of gross agricultural output in 2001.

#### **3.2. Manufacturing**

By 1999 the loss of links with other Yugoslav republics and international isolation had already taken their toll on important sectors. At present, manufacturing industries are once again providing an increasing source of export earnings. Food processing accounts for around 20% of industrial production. Other key sectors include vehicle manufacture, capital machinery, chemicals, cement, steel and textiles.

#### **3.3. Mining**

Serbia and Montenegro have deposits of lead, zinc, iron, nickel, silver, magnesium, aluminium (in Montenegro), bauxite (also mainly in Montenegro), although the mining of many of these has declined. There are also lignite, oil, and gas deposits. However, 30% of lignite deposits are in the province of Kosovo, whose future status remains uncertain.

#### **3.4. Financial services**

Confidence in Serbia's banking system was destroyed following what amounted to the sequestration by the state of the population's hard-currency savings during the wars of 1991-92. The governments' post-Milosevic era has seen the closure of a total of 24 banks in the past three years in an attempt to clean up the sector, but much remains to be done. The experience of other transition countries suggests that the common state's banking sector problems will be resolved only through large-scale foreign investment in this sector.

### 3.5. Tourism

The tourism industry in Serbia and Montenegro began to decline in the late 1980s, before the break-up of former Yugoslavia, and continued to do so in the 1990s owing to war and international sanctions. Although Serbia has not been a favoured tourist destination for foreigners, with the exception of special sites such as medieval monasteries, the development of the tourism industry is much more important for Montenegro, which has spectacular beaches.

#### 4. *The common-state and the international financial institutions*

In May 2002, the IMF approved an Extended Arrangement worth SDR 650 million (about US \$ 929 million) to support the economic programme in 2002-2005. The Fund's executive board completed the second review of Serbia and Montenegro's performance under the arrangement in July 2003, enabling the country to draw about US \$ 147 million immediately. The Fund concluded that macro-economic policy is on track, and that the authorities' economic objectives for the remainder of 2003 were sound. However, it also pointed out that the large current-account deficit leaves the external position vulnerable to shocks and that the authorities' intention to press ahead with structural reforms is critical to attracting direct foreign investment. In April 2004, the IMF approved US \$ 137 million credit disbursement under the Extended Arrangement with Serbia and Montenegro.

On 8 May 2001, the *World Bank* announced that Yugoslavia had become a member of the financial institution. At the same time, a plan was approved for settling the country's outstanding US \$ 1.9 billion debt owed to the World Bank. The World Bank had already re-engaged in the Federal Republic of Yugoslavia after the change of government in September 2000. The World Bank currently assists Serbia and Montenegro through a Transition Support Strategy, which allows the country to receive up to US \$ 540 million over three years for up to six loans in support of the government's programme.

The European Bank for Reconstruction and Development (*EBRD*) also responded rapidly to the democratic changes in Yugoslavia in 2000. The country's application for membership was approved and became effective in January 2001. On 31 December 2002, the Bank had a net cumulative business volume in Serbia and Montenegro of €366.4 million. Investments have been made in energy, transport (railway), municipal infrastructure, the financial sector and local private enterprise.

#### 5. *Current trends*

##### 5.1. Economic growth

After reaching a revised 4.0 % growth in 2002, GDP was up an estimated 3.0 % in 2003. According to observers<sup>1</sup> GDP growth was driven by gross fixed investment. By sector, GDP was brought down last year by the poor performance of industry and agriculture. The industry recovery was slower and the hot summer 2003 brought weak results in the agricultural sector.

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<sup>1</sup> World Markets Analysis



At the start of the year, the government was forecasting that GDP would rise 4.0 % in 2004; however, finance Minister Dinkic announced in August that thanks to the strong performance of industry, the forecast was being raised to 6.0 %.

## **5.2. Inflation**

The removal of some price controls following the fall of Slobodan Milosevic in October 2000 led to Serbia recording average annual retail price inflation of 91% in 2001. Inflation was one of the primary concerns of the Serbian authorities in 2003, and the country achieved major success in that realm last year, with a sharp deceleration of growth in retail prices. In Serbia alone, the year-end rate fell to 7.8 % down from 14.8 % a year earlier. In Montenegro, prices were even lower. The government and the National Bank of Serbia (NBS) are working hard to limit average annual inflation in 2004, which the government forecasts at 8.5%. In addition, the managed float of the dinar should help to keep inflation under control.

## **5.3. Monetary policy**

Serbia's current-account deficit reached US \$ 1.93 bn in 2003, more than three times the deficit recorded in 2001. According to observers<sup>1</sup>, the current-account deficit of the common state is set to rise further in 2004, to about US \$ 3 bn. The sharp increase in the external gap in 2002-2004 reflects the widening trade deficit. The IMF has become increasingly concerned with the common state's large external deficit, which reflects a lack of competitiveness among exporters (a situation reinforced by the real appreciation of the dinar in 2001-2002), and a weak external environment<sup>2</sup>. Larger current-account deficits may put greater pressure on the Serbian government to introduce measures to protect domestic producers, and to contemplate allowing the dinar to depreciate more rapidly in nominal terms against the euro.

Serbia and Montenegro have covered much of their current-account deficits in recent years with external aid and foreign direct investment (FDK). However, external assistance is likely to decrease over the medium term, and FDI alone will not be enough to cover current-account deficits.

At the end of July 2004, Serbia's total foreign debt stood at US \$ 12.16 bn, according to the NBS, including US \$ 1.15 bn in relation to liabilities located in Kosovo.

In 2001-2002, the NBY's policy was to keep the dinar stable in nominal terms against the euro at a rate of around YUD 60: €1. This caused the local currency to appreciate strongly in real terms, leading to concerns that the dinar was becoming overvalued and harming the competitiveness of Serbian exporters. The 'hard dinar' policy of 2001-2002 was relaxed in 2003 and by September 2004, the dinar fell to about YUD 74.5: €1, reflecting concern over the uncertain political situation in Serbia and the sharp increase in the trade deficit.

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<sup>1</sup> Economist International Unit (EIU).

<sup>2</sup> Serbian Deputy Prime Minister Miroljub Labus said on 28 September 2004 that the IMF was asking for the impossible in urging a budget deficit in 2005 of just 1% of the GDP.

## 5.4. Trade

Trade data showed that import growth continued to outrun export growth in 2003 for the third consecutive year. Imports jumped 18.8 % in dollar terms last year, while exports rose 11.5 %. The foreign trade deficit reached \$ 4,974 million (36.8 % of GDP), up from \$ 4,045 million in 2002<sup>1</sup>.

Serbia's most important export category last year was fruit and vegetables, which accounted for 9.2% of the total. Iron and steel was second, followed by clothing, rubber products, and non-ferrous metals. Serbia's most important import was oil and oil products, accounting for 9.6% of the total. Serbia and Montenegro conducted about 40% of its two-way trade in 2003 with EU countries, especially Germany, Italy and France. Russia remains one of the common state's most important trading partners, accounting for 13.7% of imports and 5% of exports in 2003; it is also the country with which Serbia and Montenegro has its greatest bilateral deficit. The common state continues to record large bilateral surpluses with Bosnia and Herzegovina (BiH) and FYROM, its main partners in the Balkan region.

Serbia and Montenegro signed free-trade agreements with Albania, Bulgaria, Croatia, FYROM, Moldova and Romania. These agreements form part of the programme backed by the EU Stability Pact for South-Eastern Europe to establish a free-trade zone for industrial products in the region by January 1st 2007.

## 5.5. Unemployment and poverty

*Unemployment* is still very high with official figures between 25 % in Serbia and 30 % in Montenegro. However, official data is incomplete and, according to the Commission, unemployment may in fact be considerably lower. Survey data for Serbia suggests levels at 15 % if the non-measured official economy and the grey economy are included.

*Poverty* rose dramatically in the FRY during the 1990s and continues to be an important problem in Serbia and Montenegro. In Serbia, one third of the population live in relative poverty (less than €30 per month per person), and almost a fifth are estimated to live in absolute poverty (less than €20). In Montenegro, 27 % of the population live below the relative poverty line (less than €45).<sup>2</sup>

## III. RELATIONS BETWEEN THE EU AND SERBIA AND MONTENEGRO

### 1. *The Stabilisation and Association Process*

After the change of regime in October 2000, the European Union immediately re-established relations with the Belgrade administration at both federal and republican levels and quickly lifted most sanctions<sup>3</sup> against the Federal Republic of Yugoslavia. With effect from 1 December 2000, the EU included the FRY in the liberalised EC preferential trade regime for the region. The FRY also became a full participant in the *Stabilisation and Association Process* (SAP), participating

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<sup>1</sup> World Markets Analysis.

<sup>2</sup> European Commission, Serbia and Montenegro Stabilisation and Association Report, 26.3.2003, SEC(2003) 343

<sup>3</sup> Except those Sanctions directed at ex-President Milosevic and his associates.

already in the first summit (Zagreb, November 2000) between the EU and the SAP states. The SAP for the countries of the Western Balkans (Albania, Bosnia-Herzegovina, Croatia, FRY and FYROM) had been initiated in 1999 as the EU's main contribution to the Stability Pact. It establishes a strategic framework for their relations with the EU, combining new contractual relationships (Stabilisation and Association Agreements) and an assistance programme (CARDS). It is not simply a bilateral process between each country and the EU, but places considerable emphasis on regional cooperation. The European Councils in Feira and Nice (June and December 2000) explicitly recognised the vocation of the countries included in the SAP as potential candidates for accession and spoke of a clear prospect of accession once the relevant conditions had been met. The European Council in Copenhagen in December 2002 reaffirmed the European perspective of the countries of the Western Balkans and underlined its determination to support their efforts to move closer to the EU.

The Thessaloniki Summit on 20/21 June 2003 gave a new impetus to the Stabilisation and Association Process. As a contribution to the Summit, the Commission had adopted a ***Communication on the Western Balkans and European Integration***<sup>1</sup> in May 2003. Herein it proposed to develop the Stabilisation and Association Process further by introducing certain elements inspired by the pre-accession process. The Commission has also suggested an increase in the CARDS budget of €200 million for the period 2004-2006.

Based on the Commission proposal, the Council of 16 June adopted the Thessaloniki Agenda for the Western Balkans. This agenda, which was endorsed by the Thessaloniki Summit, enriches the Stabilisation and Association Process with the following elements:

- Enhanced political dialogue and cooperation in the area of Common Foreign and Security Policy (including the EU-Western Balkans Forum, which will bring together periodically the heads of state or government of the SAP countries and their EU counterparts);
- The possible establishment of joint 'Stabilisation and Association Parliamentary Committees' with all SAP countries, even before the entry into force of the respective SAA;
- European Partnerships, inspired by the Accession Partnerships for candidate countries, to be drawn up for all SAP countries;
- Enhanced support for Institution Building, in particular extension of the twinning instrument to all SAP countries;
- Opening of community programmes to SAP countries along the lines established for the participation of candidate countries;
- Enhanced Community financial support.

The Commission produces ***annual reports*** on the Stabilisation and Association Process for South East Europe, accompanied by reports on each individual country. The **third annual report**, published in March 2004, reported that progress in Serbia and Montenegro has been mixed. It has successfully adopted the Constitution Charter but has yet to implement it. This is a result of continued disagreements about the interpretation and implementation of the new constitutional arrangements which reflect an overall lack of consensus in the country. This has weakened the joint institutions and policies necessary for progress and for developing relations with the EU. Furthermore, it went on to state that the specific, recurrent theme that has affected the country's efforts to strengthen its EU relations is the lack of a single, functioning trade

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<sup>1</sup> COM(2003) 285 final, 21.5.2003.

regime and of a single market which impacts on a great variety of policy areas. In addition, the political crisis in Serbia has stalled an important number of reform laws and policies. There are currently no contractual relations between the EU and Serbia and Montenegro.

**Serbia and Montenegro** re-launched the Feasibility Report on a Stabilisation and Association Agreement (SAA) in October 2004 after long delays due to internal disputes. This Report will assess the country's capacity to negotiate and implement the far-reaching political and economic obligations under a Stabilisation and Association Agreement. This decision follows the full endorsement of the EU's 'twin-track' approach by political leaders of Serbia and Montenegro. The 'twin-track' approach to SAA negotiations means dealing with the two republics on policies which they conduct separately, notably trade, economic and sectoral policies, while continuing to work with the State Union where it is the competent authority, for example on international political obligations and human rights. The Feasibility Study will consider Serbia and Montenegro's performance in upholding democratic standards, the state of play on its sectoral reforms, compliance with the EU's political and economic criteria such as the rule of law, human rights including media freedom, the fight against organised crime and cooperation with the ICTY, and of its administrative capacity to negotiate and fully implement the SAA. The Commission had indicated that the study was to be completed by March 2004 but was postponed in order to give the authorities more time to address the remaining key issues, including in particular political conditionality, constitutional issues and the Action Plan. In a meeting between Serbian prime minister, Vojislav Kostunica, and Javier Solana in November 2004, Mr. Kostunica expressed his hope to see the Commission submit its feasibility report in Spring 2005. A positive Report would see the Commission open SAA negotiations to EU Member States.

## 2. *Financial Aid*

Overall, between 1991 and 2002 (included), the state benefited from a total of more than €2.9 billion in EC assistance.

The main financial instrument for EU assistance to the Federal Republic of Yugoslavia since 2001 is the **CARDS-Programme**, which is designed to support the Stabilisation and Association process in the countries of South-East Europe. Its legal basis is Council Regulation (EC) No. 2666/2000, adopted on 5 December 2000<sup>1</sup>. Between 2000 and 2003, CARDS assistance totalled €898 million.

In accordance with the CARDS regulation, a **Country Strategy** defining the priorities for financial support for the period 2002-2006 has been adopted by the Commission on 27 December 2001. On this occasion, the Commission also announced that €960 million have been earmarked to finance this strategy during the three years 2002-2004 (for details see Annex 6). The Country strategy identifies three key areas for support:

1. *Good governance and institution building*, focusing on public administration reform, justice and home affairs and modernisation of customs and taxation.
2. *Economic recovery, regeneration and reform*, focusing on energy, transport, environment and economic development

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<sup>1</sup> OJ L 306 of 7.12.2000, p. 1.

3. *Social development and civil society*, focusing on university education via the TEMPUS programme, vocational education and training, employment generation and civil society.

During the year **2002**, some €359.6 million were allocated in the Federal Republic of Yugoslavia under the CARDS programme. The indicative financial allocation for CARDS assistance for Serbia and Montenegro for the period 2002-2004 was €933 million under the national programme and a share under the CARDS regional programme for measures which was implemented at state-level, republican level and in Kosovo. In Serbia and at federal level, the 2002 programme (€180 million) focussed on economic reconstruction and reform, civil society and media. The 2003 programme (€240 million) focuses, in addition to economic reform, mainly on good governance and institution-building, reinforcing public finance management at federal, republican and local levels. For Montenegro, the 2002 programme amounted to €15 million and focussed on institution building and transport. For 2003, the programme focuses on energy, judicial and border police reform and the environment. The 2002 programme in Kosovo (€147 million) focussed on public administration, economic reconstruction and reform, civil society and media. The 2003 programme (€53 million) focuses on energy, economic development, institution-building, education and refugee return. In addition, the state also benefited from the CARDS Regional Programme. The 2004 programme illustrated a gradual shift to longer-term development assistance and to continue to support institutional reform, with packages of €214 million for Serbia and at the state level and €15 million for Montenegro.

EC humanitarian assistance (ECHO) in 2002 amounted to €39.5 million (37.5 million for Serbia and 2 million for Kosovo).

On 5 November 2002, the Council adopted a decision providing for further **macro-financial assistance** to the FRY<sup>1</sup> of up to €130 million. The assistance will have a grant component of up to €75 million and a loan component of a maximum principal of €55 million. The objective of this assistance is to underpin economic policies in the context of the IMF Extended Arrangement, in particular to support the balance of payment and strengthen the country's foreign exchange position. The Commission proposed in August 2003 to amend the Council Decision, increasing the total amount of assistance by €70 million to €200 million (with €45 million as a grant and €25 million as a loan)<sup>2</sup>. The two tranches of this assistance amounting to €40 million and €65 million were disbursed in 2003. In October 2004, the Commission extended the assistance to June 2006 as it had yet to implement the remaining third tranche amounting to €25 million. In November 2003, the Council had decided to increase the amount of assistance by €70 million to €200 million to help address additional financing identified by the IMF. In addition, €45 million had been committed for 2004 and payment appropriations were made in the amount of €10 million and €45 million in 2005.

By the end of 2002, the European Investment Bank (**EIB**) had signed projects in the state for a total of €336 million, concentrating on the area of transport and financing of small and medium enterprises.

The European Union, together with the World Bank, has played a leading role in ensuring mobilisation and **coordination of donors** via the organisation of international Donor's meetings

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<sup>1</sup> OJ L 308, 9 November 2002, p. 25.

<sup>2</sup> COM (2003) 506 final.

and Conferences. The second Donor Coordination Meeting was held in November 2003. The objective of the meeting was to assess the progress achieved in stabilising the political and economic situation and the challenges ahead in sustaining a viable reform path. It was announced that in 2004, overall donor commitments could reach €1.1 billion which would meet the overall target set in 2001.

***The European Union in Kosovo*** – The European Union is playing a prominent role in the reconstruction of Kosovo. It is, by far, the single largest donor providing assistance to Kosovo and the South Eastern European region as a whole and is at the forefront of the reconstruction effort. Between 2000 and 2003, CARDS assistance totalled €826 million. In 1999, the EU provided €378 million in emergency humanitarian assistance and a further €127 million for reconstruction programmes after the war. In 2000, it continued its support with €360 million and in 2001, up to €350 million was earmarked for further aid. The European Agency for Reconstruction took over the work of the Task Force for the Reconstruction of Kosovo in February 2000. It manages sustainable reconstruction and development programmes in Kosovo under the political guidance of the EU. Its main focus is on reconstruction and institution building. Funds for the reconstruction projects in 2000 amounted to €260 million and in 2001 to €285 million. In the 2003 programme, an additional €16.3 million was allocated bringing the total to €69.3 million. In 2004, the programme had a total allocation of €55 million. Exceptional Community financial assistance, in addition to CARDS assistance, was also provided for amounting to €30 million, of which the second and final €15 million tranche was disbursed in December 2002. From 1999 to the end of 2002, the EC contributed over €43 million to the running costs of the EU-led Pillar IV of UNMIK, which is in charge of creating the framework for the development of a modern market economy with stable institutions.

In a resolution adopted by the European Parliament on the situation in Kosovo in April 2004, it noted its alarm and condemned the March 2004 violent outbreak as the worst outbreak for five years. It called on the Kosovo Provisional Institutions of Self-Government (PISG) to condemn the violence and called for the Serb community to fully comply with UNMIK guidelines on security and local administration. The Parliament warned that these events are a setback on the road to integrating south-eastern European countries into European structures. It urged the Commission to continue with the Kosovo Stabilisation and Association process Tracking Mechanism, but stressed that it should be made clearly conditional on the PISG genuinely cooperating with UNMIK and on the Kosovo authorities showing complete respect for fundamental EU values.

### **3. *The European Parliament***

The European Parliament has supported EU aid to Yugoslavia via a number of resolutions and its budgetary responsibilities. In its resolution of 14 June 2001<sup>1</sup>, the European Parliament approved the disbursement of additional emergency funds to Kosovo at the amount of €30 million. In its resolution of 5 July 2001<sup>2</sup>, it approved a proposal for a decision to grant macro-financial assistance to the FRY of €300 million. On 29 November 2001, the EP adopted a resolution on

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<sup>1</sup> The full text of EP resolutions is available by date on the website:  
<http://www3.europarl.ep.ec/omk/omnsapir.so/calendar?APP=PV2&LANGUE=EN>

<sup>2</sup> Resolution on the proposal providing macro-financial assistance to the Federal Republic of Yugoslavia, 5 July 2001.

the proposal for a Council Regulation amending the regulation on assistance for Albania, Bosnia and Herzegovina, Croatia, the FRY and FYROM as well as a resolution on the proposal for a Council decision to amend the decision of 16 July providing macro-financial assistance to the FRY. On 10 October 2002, the Parliament approved a resolution on the proposal for a Council decision providing further macro-financial assistance to the FRY. The Commission's proposal for additional macro-financial assistance to Serbia and Montenegro was approved (with amendments) by Parliament on 23 October 2003. Furthermore, €45 million had been committed for 2004 and payment appropriations were made in the amount of €10 million and €45 million in 2005. In October 2004, the Commission extended its assistance to June 2006 to implement the remaining €25 million.

On **7 November 2002**, the European Parliament adopted a resolution *on the Stabilisation and Association Process* for South East Europe that gives a series of important recommendations for the whole region and each particular country.

One of the main general recommendations to the Council and the Commission is to ‘refrain from moving to a further stage of the SAP and/or consider the possibility of partly or totally suspending financial assistance to any of the five countries in the event of non-compliance with the following three political conditions,...’ The resolution then names the three conditions:

- full and effective cooperation with the International Criminal Tribunal for the Former Yugoslavia (ICTY);
- effective implementation of a policy in favour of the return of refugees;
- the effective implementation of an active policy against organised crime, corruption and trafficking in human beings, drugs and arms.

As regards the Federal Republic of Yugoslavia, the EP called on the Commission and the Council to make clear to the Serbian and Montenegrin authorities that effective cooperation with the ICTY is a pre-condition for any proposal for opening negotiations on an SAA.

In a resolution adopted on 5 June 2003 on the meeting of the Troika with the countries participating in the Stability Pact for South-Eastern Europe<sup>1</sup>, the EP asked for a clarification and reinforcement of the Stabilisation and Association Process. It also suggested further parliamentary cooperation between the EP, the national parliaments of the countries of South-Eastern Europe, the parliaments of the Member States and the candidate countries as well as the parliamentary assemblies of the Council of Europe and the OSCE.

In its *resolution of 20 November 2003* on the Stabilisation and Association Process for South-East Europe, Parliament reiterated the general recommendations on the SAP it had expressed in the resolution of 7 November 2002 (see above). Parliament further considered it undesirable that a SAP country become member of the EU, if it has entered into a bilateral agreement with the USA jeopardising the full effectiveness of the ICTY.

Regarding Serbia and Montenegro, the resolution points out, that the EU should be ready to assist Serbia and Montenegro in reaching a lasting arrangement. Parliament also expresses its concern about the deadlock resulting from the difficulties of the Serbian Government to secure a

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<sup>1</sup> Resolution of 5 June 2003, not yet published in the Official Journal.

parliamentary majority as well as about the standstill in the Parliament of the Republic of Montenegro. With the re-launch of the Feasibility Report on a Stabilisation and Association Agreement (SAA) in October 2004, it is hoped that a positive report will open further negotiations between Serbia and Montenegro and other EU Member States.





## PRESIDENT – GOVERNMENT – PARLIAMENT

Key Figures**Serbia e Montenegro**

<u>President</u>	Svetozar Marovic
Minister of Foreign Affairs	Vuk Draskovic
Deputy Minister of Foreign Affairs	Predrag Boskovic, M.A.
Minister of Defence	Vukasin Maras
Deputy of Defence	Prvoslav Davinic
Minister of International Economic Relations	Prof. Predrag Ivanovic
Minister of Internal Economic Relations	Amir Nurkovic
Minister of Human and Minority Rights	Rasim Ljajic
Assembly President	Zoran Sami

**Kosovo**

<u>President</u>	Ibrahim Rugova
Prime Minister	Ramush Haradinaj ?
Assembly President	Nexhat Daci

**Serbia**

<u>President</u>	Boris Tadic
Prime Minister	Vojislav Kostunica
Minister of International Economic Relations	Milan Parivodic
Minister of Diaspora	Vojislav Vukcevic
Minister of Interior	Dragan Jovic
Assembly President	Predrag Markovic

**Montenegro**

<u>President</u>	Filip Vujanovic
Prime Minister	Milo Djukanovic
Minister of Foreign Affairs	Miodrag Vlahovic
Assembly President	Ranko Krivokapic