

NATIONAL BANK OF SERBIA

GOVERNMENT OF THE REPUBLIC OF SERBIA

MEMORANDUM

ON THE STRATEGY OF DINARISATION OF THE SERBIAN FINANCIAL SYSTEM

MARCH 2012

Recognising the need to increase the use of the dinar in the financial system in order to strengthen the country's financial stability, lessen the risk of currency changes to the most vulnerable sectors of the economy, reinforce the efficiency of monetary policy, and by extension, create preconditions for strong and durable economic growth, the Government of the Republic of Serbia (hereinafter: Government) and the National Bank of Serbia (hereinafter: National Bank) have made this

MEMORANDUM ON THE STRATEGY OF DINARISATION

OF THE SERBIAN FINANCIAL SYSTEM

The Memorandum on the Strategy of Dinarisation of the Serbian Financial System (hereinafter: Memorandum) defines the objectives, measures and activities to be taken with a view to strengthening confidence in the national currency and promoting its use in the financial system (hereinafter: dinarisation).

DINARISATION STRATEGY, OBJECTIVES AND MONITORING

The National Bank and the Government agree to jointly determine and implement the dinarisation strategy. The aim of the dinarisation strategy and process is the achievement of a satisfactory level of use of the dinar in the financial system without threatening the country's financial and macroeconomic stability. The National Bank and the Government will regularly monitor and analyse the level of dinarisation based on the technical guidelines set out in the Annex to the Memorandum.

The National Bank and the Government agree to classify the activities related to the implementation of dinarisation strategy into three groups, in accordance with the different objectives of the process.

The first group comprises monetary and fiscal policy measures geared at strengthening the macroeconomic environment by delivering low and stable inflation through a managed floating exchange rate, alongside durable economic growth.

The second group comprises activities to promote the development of the market of dinar securities and create conditions for the introduction of new dinar instruments.

The third group comprises activities to promote the development of foreign exchange hedging instruments.

The current financial and macroeconomic developments permitting, the National Bank and the Government agree to also use other measures within their respective scopes of authority for the purpose of implementing the dinarisation strategy.

The National Bank and the Government agree to express all prices, procurements and invoices in the country exclusively in dinars, and abroad when possible, in all stages of the

implementation of the dinarisation strategy. Conditions permitting, the National Bank and the Government also agree to express in dinars all claims and liabilities arising from contractual relations. If the nature of claims and liabilities arising from contractual relations requires their denomination in foreign currency, the National Bank and the Government agree to also state their dinar equivalent whenever the conditions permit.

Representatives of the National Bank and the Government agree to express financial amounts in their public communications in dinars, whenever possible.

MEASURES AND ACTIVITIES OF THE NATIONAL BANK

The instruments and monetary policy measures supporting the process of dinarisation will be selected and applied based on the analysis of current financial and overall macroeconomic developments.

The National Bank will continue to support the process of dinarisation through reserve requirements. The National Bank will also continue to support the process of dinarisation through prudential and other measures.

In the event of a structural dinar liquidity shortage, the National Bank stands ready to use all monetary policy instruments at its disposal to supply dinars at the key policy rate which ensures the achievement of inflation target.

Together with representatives of competent institutions, the National Bank will make every effort to create an institutional and regulatory environment which will contribute to the development of primary and secondary markets of dinar securities. To achieve this, and in particular, to bolster the liquidity of the secondary market of dinar securities, in cooperation with other competent institutions, the National Bank will set up a working group. The National Bank will also closely cooperate with international financial institutions in order to create regulatory and market conditions conducive to issuing of long-term dinar securities and dinar loans by these institutions.

In collaboration with competent institutions, the National Bank will work on the creation of conditions for further development of existing and introduction of new foreign exchange hedging instruments.

The National Bank will continue to implement educational activities targeting financial services consumers in order to increase their understanding of potential risks and of the instruments they may use to hedge against those risks.

The National Bank will undertake periodic comparative analysis of dinar products available in the domestic market and present the results of that analysis on its website.

MEASURES AND ACTIVITIES OF THE GOVERNMENT

The Government will support dinarisation particularly by investing further effort in raising the share of pure dinar debt in total public debt.

The Government will engage in subsidised loan financing provided these loans are dinar-denominated.

Through stimulative tax policy, the Government will continue to support saving in dinars.

Together with representatives of competent institutions, the Government will make every effort to create an institutional and regulatory environment which will contribute to the development of primary and secondary markets of pure dinar securities, simplification of procedures and a reduction in costs of secondary trading in government securities.

Whenever market and overall macroeconomic conditions permit, the Government will favour borrowing in dinars without any form of currency clause. This will imply exerting an active influence on activities of local governments and public enterprises. If the Government, local governments and public enterprises borrow in foreign currency, they will endeavour to use market instruments to hedge against the foreign exchange risk whenever possible and economically justified. By improving the regulatory environment in Serbia, the Government will support local government borrowing through the issue of dinar-denominated municipal bonds.

To finance budgetary needs, the Government will develop and implement a medium-term public debt management strategy. The aim of the future strategy will be to reduce public sector exposure to exchange rate risk. In line with the strategy and market trends, the Government will issue longer-term dinar bonds, both in the domestic and international financial markets, and thus contribute to the development of primary and secondary markets of dinar securities.

COMMUNICATION WITH THE PUBLIC

The National Bank and the Government agree to disclose to the public data on dinarisation of the Serbian financial system measured by defined criteria, on a quarterly basis.

The National Bank and the Government also agree to disclose all essential and relevant information and data relating to the process of dinarisation on their websites and through other means of communication.

The National Bank and the Government agree to regularly inform the public of measures and activities and their effects in relation to the process of dinarisation which are taken to strengthen confidence in the domestic currency.

When needed, representatives of the National Bank and the Government may also organise meetings with representatives of the banking and corporate sectors with a view to exchanging information about the introduction of additional measures to support the process of dinarisation. At public events, conferences or working group meetings, representatives of the National Bank and the Government may propose and promote activities to be taken by the banking and corporate sectors to raise the degree of dinarisation.

The National Bank and the Government will make sure that the public is timely informed about the changes in monetary and fiscal policies which may affect the degree of dinarisation. Any proposal of measures which is contrary to the process of dinarisation must be clearly justified.

ANNEX: MEASUREMENT AND MONITORING OF DINARISATION

The National Bank and the Government will regularly monitor and analyse the trends in the degree of dinarisation.

The National Bank and the Government agree that dinar deposits, dinar loans and dinar securities mean only pure dinar categories, i.e. deposits, loans and securities without any form of currency clause, enabling their indexation to inflation.

The National Bank and the Government agree to measure the degree of dinarisation of the financial system by the share of dinar in total loans. As supplementary criteria for the measurement of the degree of dinarisation, the National Bank and the Government may use in particular: the share of dinar household and corporate deposits in total deposits, the maturity structure of dinar loans and deposits, the currency structure of public debt, liquidity in primary and secondary markets of pure dinar securities, the maturity structure of dinar securities.

The National Bank and the Government agree that the National Bank will conduct a quarterly analysis of the degree of dinarisation of the Serbian financial system and of the effects of measures taken. The National Bank will submit the analysis to the Government and will publish it.

FOR
THE NATIONAL BANK OF SERBIA

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