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# Onshore, Nearshore, Offshore: Unsure?

**A 2012 Serbian Perspective >**



## Today - emerging market, Tomorrow - potential BPO/SSC hub of CEE

### Executive Summary

#### Economics

- Serbian economy contracts in 2012 due to effects of global and Eurozone crisis; recovery is estimated over the next two years
- Serbia granted EU candidate status
- High unemployment rate offers low labour costs

#### Business Environment

- Belgrade – administrative, economic, cultural and educational centre, totalling 1.6 million people
- Very favourable business climate offering numerous tax, financial and other incentives
- At 10%, Serbia has one of the lowest Corporate Tax rates

#### Labour Markets

- Highly educated, skilled and multilingual labour pool
- Among the lowest labour costs in CEE
- High unemployment rate

#### Real Estate

- Tenant favourable market
- Good supply of office space according to international standards
- Increasing supply of office space

### Introduction

Business Process Outsourcing (BPO) is a form of business services provided to companies located in different markets. A Shared Service Centre (SSC) can also be operated by a company itself but, often shored (On-, Near- or Off-) to a lower cost destination. The Serbian BPO market is emerging, but is recognized as having high potential and being a future hot spot for hosting shared service centres once other CEE markets reach saturation.

## The Republic of Serbia

Foreign investors in Serbia benefit from the extremely convenient geographic and strategic position, low operating costs, numerous state incentives for foreign investment and a skilled and highly motivated workforce.

In March 2012, Serbia was granted EU candidate status, as recognition of its consistent efforts in implementing reforms in the field of democracy.

Serbia has the same time zone as many countries in continental Europe (GMT+1) and most major European capitals are not more than three hours flying distance from Belgrade.

The successful business stories of FIAT, Gazprom, Michelin, Delhaize, Telenor, Yura and many others ranked Serbia among the top investment destinations in Central and Southeastern Europe.

### Demographics and Economics

The Republic of Serbia has a population of 7.1 million people (2011 Census official data), with the capital city of Belgrade totalling 1.6 million inhabitants. The other three largest regional cities are Novi Sad (335,701), Niš (257,867) and Kragujevac (177,468).

The following table shows the key economic indicators of the Republic of Serbia:

Indicators	2009	2010	2011	2012E	2013F	2014F
Gross Domestic Product*	-3.5	1.0	1.6	-0.2	2.0	3.7
Consumer Price Index*	8.1	6.1	11.1	5.7	7.6	5.2
Nominal Wage Growth*	0.2	0.7	0.2	n/a	n/a	n/a
Unemployment Rate (%)	16.9	20.0	23.7	26.1	24.7	23.5

Source: IHS Global Insight, Ministry of Finance and Economy, September 2012

\* Change Year on Year, E=Estimate, F=Forecast

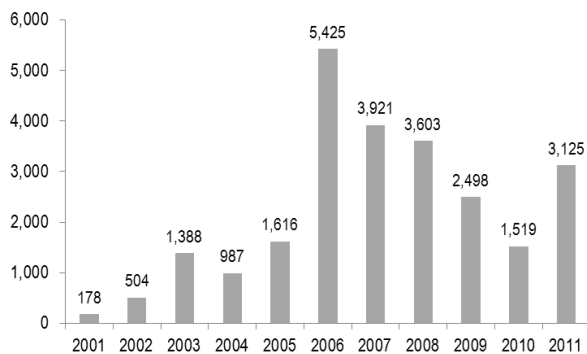
Between 2004 and 2008, Serbia experienced an economic boom with an average annual GDP growth rate at 5.5%. Although the Serbian economy contracted by 3.5% in 2009, due to the global economic crisis, the country has continued to improve its business environment and has attracted foreign direct investments that have brought moderate economic recovery in 2010 and 2011.

The Serbian economic outlook is highly positive due to its persistent determination to continue implementing economic and legal reforms. The business climate will continue to be supported and strengthened by an educated and skilled labour pool.

## Business Environment

Recognized as an Investment hotspot of SEE, over the last ten years Serbia showed great performance in attracting foreign direct investment. Since 2001, Serbia and its investor friendly environment have attracted \$25 billion of FDI inflow. Over the last six years, the most targeted was the services sector, particularly financial intermediation.

**FDI Inflow in USD millions**



Source: National Bank of Serbia

Strong foreign investment and continuous improvement of the business climate put Serbia among the fastest growing European economies between 2004 and 2008. The main contributors to the favourable business climate were numerous financial, tax and other incentives set up by the government.

<b>Financial Incentives</b>	For large scale projects, grants up to 25% of the investment amount
	For standard-scale projects, grants from €2,000 up to €10,000 per new job created
<b>Tax incentives</b>	Support schemes offered by the National Employment Service
	10-year Corporate Income Tax holiday for large investments
	5-year Corporate Income Tax holiday for investments in underdeveloped regions
	Corporate Income Tax credits up to 80% of the investments in fixed assets
	5-year Corporate Income Tax holiday for concessions
	Carrying forward of losses over a period up to 5 years
	Avoiding double taxation
	Salary tax and Social Insurance charges exemptions
	Annual Income Tax deductions up to 50% of the taxable income
Value Added Tax exemption in Free Zones	
<b>Other Incentives</b>	Customs-free import
	Regional and local incentives

Source: SIEPA

Employment incentives offered by the National Employment Service for creating new jobs can be particularly alluring for companies that see Serbia as their next shoring location. National Employment Service grants depend on the number of new jobs created and the municipality where the business starts up. Furthermore, grants are also offered for employing the disabled. The range of grants is shown in table below:

Program	Grant per employee
Employment Subsidies Program	€850 - €1,700
Apprentice Program	€170 - €210
Re-training Program	€850

Source: SIEPA

### Setting up a Business and Related Conditions

#### Grants and Incentive Possibilities in Serbia

Tax incentives are generally available for Serbian tax payers under specific conditions prescribed by the tax rules (no specifically tailored tax incentives for BPO/SSC industry):

- Ten years tax holiday for investing approximately €7 million and employing at least 100 new employees
- Tax credit of 20% to 40% of the value of investment made in own fixed assets

#### Corporate Profit Tax

- Resident entities are subject to tax on their worldwide income. Non-resident companies are subject to tax on their Serbian-sourced income only.
- Serbian corporate profit tax rate is currently set at 10%.
- The taxable basis is accounting result of the taxpayer, adjusted for tax purposes for non-taxable revenues, partly or whole non-deductible expenses, thin capitalization and any transfer pricing adjustments.
- The fiscal year coincides with the calendar year.
- Tax losses may be carried forward over five years. The carry back of losses is not permitted.
- Capital gains of resident entities are taxed in the same way as corporate profits at the standard rate of 10%. Capital gains can be realized from the sale of immovable, industrial property rights and the sale participations. Serbia applies a basket limitation with respect to capital gains.
- Accelerated depreciation is available for assets used for the protections of the environment, recycling equipment, research and development, and education of employees.

### Withholding Tax

- Income realized by non-residents from resident entities with respect to dividends, bankruptcy surplus, interest, royalties, lease of movable and immovable is subject to 20% Serbian WHT unless otherwise stipulated in applicable DTT.
- Capital gains realized by non-resident from both residents and non-residents, on the territory of Serbia, are subject to 20% capital gains.

### Value Added Tax

- The Serbian VAT system is modelled loosely on the 6th EU Directive.
- Standard VAT rate is currently 18% (announced to change on 20%), while 8% applies for specific supplies of goods.
- If the input VAT exceeds the output VAT, the recoverable balance VAT can be either carried forward to the subsequent VAT period or compensated/refunded by the tax authorities, based on the option clicked by the taxpayer in the VAT return.

### Personal income tax and SSCs

- Serbian residents are taxed in Serbia on their worldwide income. Non-residents are subject to taxation in Serbia on Serbian sourced income.
- Personal income tax rate is 12%.
- SSC are currently set at 17.9% (burden for both employer and employee 35.8%).
- The taxable base is gross income consisting of net income, related tax and contributions (if applicable). Serbian tax residents are obliged to pay an annual tax on their worldwide income earned in the year, if the total sum of the income (reduced by paid income tax and obligatory social contributions, and excluding certain types of income such as dividends and interest) exceeds prescribed thresholds.
- Annual tax is levied at progressive rates of 10% and 15%.

### BPO/SSC sector in Serbia

In Serbia, the BPO/SSC sector is an emerging market with excellent potential. The eventual saturation of the leading markets in CEE will likely make Serbia the next outsourcing hotspot in the near future.

Due to the immaturity of the market, the statistics and exact figures of past investment in this sector cannot be quoted. However, the sector of business activities experienced a constant growth of number of new investment projects. The most active were Sales, Marketing and Support and Business Services sectors.

Number of Projects by Activity					
Business Activities	2009	2010	2011	Total	Average Annual Growth
Sales, Marketing & Support	5	11	18	34	91.8%
Business Services	4	6	8	18	41.7%
Customer Contact Centre		1	1	2	n/a
ICT & Internet Infrastructure		1		1	n/a
<b>Overall Total</b>	<b>9</b>	<b>19</b>	<b>27</b>	<b>55</b>	<b>76.6%</b>

Source: Jones Lang LaSalle Location Consulting Services

The general impression is that the shoring market in Serbia is in an early stage with very few big market players. The first market entrants appeared after the political changes in 2001. However, until recently, the investments in this market were quite sporadic with no more than 90 jobs created per project. The first big market player was Trizma, the first Independent Call Centre, that currently employs 211 people. Last year, the market experienced a real boom when Sitel and NCR opened their offices in Belgrade. Sitel employed 300 people and NCR opened their office and employed 200 people, with a plan to expand the businesses and team in 2013.

IT companies are taking the largest share in the current BPO/SSC industry in Serbia. Other services are relatively new to the market but we see a great potential for their development in this region. BPO and SSC investors have often chosen proven locations for their businesses over Serbia. Therefore, the success stories of Sitel and NCR will certainly help put Serbia back on the radar.

The following are examples of major local and foreign companies offering BPO / SSC services in Serbia:

Company	City	Project Started	No. of Employees*
Sitel	Belgrade	2011	300
NCR	Belgrade	2012	200
Trizma	Belgrade	2002	211
PSTech	Belgrade	1996	180
BDO	Belgrade	2004	90
ConsulTeam	Beograd	2002	83
Euronet	Belgrade	2002	70
Mellon	Belgrade	2001	60
Execom	Novi Sad	1997	57
Intens	Novi Sad	2003	48
Embedded (IMPT)	Belgrade	1997	42
Prozone	Novi Sad	2002	34
Amrop Adria	Belgrade	2007	20
Omnicom Solutions	Belgrade	2005	19
Iron Mountain	Belgrade	2006	14
NTH Group	Belgrade	2006	13
Intentcall	Belgrade	2011	n/a

Source: SIEPA and companies websites; \*figures are taken from companies' websites and internet portals and JLL is not responsible for their accuracy

## Labour Market

Although the impact of the global crisis continued through 2011 and into 2012, a slight recovery on the labour market was seen, despite a rising unemployment rate. According to research by Infostud, an employment Internet portal, the number of job advertisements increased by 17% in 2011 compared to 2010. The highest demand from employers was registered in the IT sector which experienced an incredible expansion with a 70% increase of job advertisements y-o-y in 2011. Employers mainly seek database administrators, PHP programmers and IS Project Managers. In 2011, most of the vacant job positions were for salesmen, PA, cashiers, administrative workers, PR and Marketing managers and financial managers.

In terms of the professional profile and skills, employers who advertised vacant positions on Infostud in 2011, mainly searched for employees with high school education, English language and computer competences. The number of job seekers are also increasing, especially young graduates who, in current times, are having more difficulty to find a job due to a lack of work experience.

The general sentiment is that Serbia is an employers market. Due to the high level of redundancies that companies were constrained to make over the last few years, employees approach to work has changed. Aware of the very low supply of good and steady job positions and the inconvenient economic conditions, employees are somewhat discouraged to change their existing jobs, as was more common before the crisis. Higher redundancy potential has therefore brought higher professional loyalty. Furthermore, the higher levels of competition on the labour market necessitates further education and qualification in the field of language competence, computing and other professional skills.

According to a survey done by "Nabolji poslodavac" ("The Best Employer") in 2012, the sample of 8,100 employees in 57 companies in Serbia would be happier if their performance was better financially and non-financially remunerated, if they had more feedback for the work performed and more opportunities for professional progress.

### Educated and Skilled Labour

According to Ministry of Education, Serbia has 8 public and 11 private universities, with a total of 136 faculties. With the exception of one, all other public faculties are accredited. Among the private ones, there are many in the process of accreditation. The University of Belgrade is the most important educational centre in Serbia. Currently, there are 89,481 enrolled students at the public faculties in Belgrade.

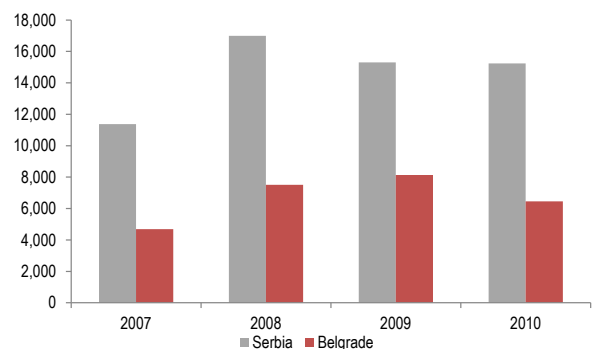
Belgrade University	Nr. of enrolled students
Faculty of Electrical Engineering	4,138
Faculty of Organizational Sciences	5,515
Faculty of Economics	7,905
Faculty of Law	8,632
Faculty of Philology	8,029

Source: University of Belgrade, September 2012

Traditionally, students in Serbia show the highest interest for studying law, economics and foreign languages. Over the past few years, IT sciences have rapidly gained popularity, as people with good IT skills have less difficulties in finding a proper job position upon graduation.

The Serbs have always been talented for foreign languages. The education system, particularly over the past ten years, has encouraged the learning of English and other foreign languages. Nowadays, at least two foreign languages are studied in Serbia, starting in primary schools, with a second language being introduced at the upper levels.

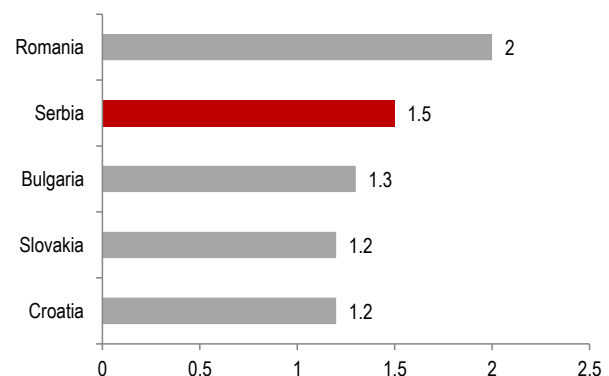
### Number of Graduated Students in Serbia and Belgrade



Source: Statistical Office of Serbia, September 2012

English language is studied during the whole education process in Serbia. Apart from compulsory education, English language lessons can be taken in private schools for languages. All Serbian universities have philology faculties or foreign language departments. At the Faculty of Philology in Belgrade, except the mother language, students are able to choose from English, German, French, Russian, Italian, Spanish, Polish, Czech, Ukrainian, Slovak, Scandinavian, Dutch, Hungarian, Turkish, Arabian, Chinese and Japanese.

### Number of Foreign Languages Learned



Source: Manpower Serbia, September 2012

## The Cost of Labour

Not only does Serbia have a skilled, effective and multi-lingual labour force, but it offers convenient labour costs as well. After the saturation of other BPO/SSC markets, Serbia can be considered the next outsourcing hotspot for its low salaries, which are ranked among the lowest in CEE. Average net salary in Serbia in 2011 amounted to €372/month and €461/month in Belgrade.

A company employing the workforce in Serbia needs to know that total labour costs include net salary, income tax and contributions paid by the employee and employer. Income tax does not apply to public transport allowance, meal allowances on business trips in Serbia and daily allowances on business trips abroad, accommodation and transport allowances, as well as solidarity relief in the event of sickness.

Employment tax and contributions in Serbia are presented in the table below:

Taxes and Contributions		Rate %
Payable by Employee	Personal Income Tax	12.0
	Pension Contribution	11.0
	Health Contribution	6.15
	Unemployment Contribution	0.75
Payable by Employer	Pension Contribution	11.0
	Health Contribution	6.15
	Unemployment Contribution	0.75

Source: Ernst&Young

Since BPOs/SSCs are an emerging sector, the statistical authorities consider it as a integrated part of the wider range of financial, consultancy and administration services. Therefore, the table below contains typical salaries for typical BPO/SSC job positions in found on an internet portal.

Average Gross Monthly Wages 2012			
Job Position	RSD	EUR	USD
Accountant	43,500	371	480
Chief Accountant	54,700	467	603
Call Operator	28,800	246	318
IT Network Administrator	51,300	438	566
Data Entry Operator	33,500	286	370

Source: Infostud, September 2012

Exchange Rates: 1 EUR = 117.2132 RSD / 1 USD = 90.6519 RSD

(13 September 2012 Average FX rates published by the National Bank of Serbia)

## Real Estate

The Serbian office market is mainly focused in the Belgrade and totals 624,000 m<sup>2</sup> of A and B class office space. The regional Serbian cities lack modern office buildings constructed to Western standards, due to the fact that foreign companies choose Belgrade for their headquarters.

However, investment incentives offered by local authorities in the regional cities will certainly continue to attract foreign investments and increase the demand for office accommodation. Therefore, we expected to see future development of the office market in the regional and economic centres such as Novi Sad, Niš, Kragujevac.

Compared to other CEE cities, the city of Belgrade has a modest supply of office accommodation. The first modern office buildings that meet the requirements of the foreign companies appeared on the market after 2004. The development boom was driven by strong economic growth and the influx of foreign investors.

Except downtown that mainly hosts law firms, marketing and financial consultancy companies, New Belgrade has been establishing as a CBD of the capital city. New Belgrade became a centre of the city's business activities and the favourable destination of foreign companies.

Q2 Key Office Market Indicators			
City	Stock m <sup>2</sup>	Vacancy Rate	Prime Headline Monthly Rent EUR / m <sup>2</sup>
Belgrade	624,000	19%	€14 - €16

Source: Jones Lang LaSalle Q2 2012

### Supply

The most significant modern office projects constructed in New Belgrade over the last seven years are:

- **Ušće Business Centre** (21,000 m<sup>2</sup> GLA)
- **Airport City phase I,II,III,IV** (66,500 m<sup>2</sup> GLA)
- **Bluecenter** (33,000 m<sup>2</sup> GLA)
- **Sava Business Center** (20,000 m<sup>2</sup> GLA)
- **GTC 19<sup>th</sup> Avenue** (20,000 m<sup>2</sup> GLA)
- **GTC House** (12,000 m<sup>2</sup> GLA)
- **Belville I** (9,500 m<sup>2</sup> GLA)
- **Belville II** (17,500 m<sup>2</sup> GLA)
- **VIG Plaza** (13,500 m<sup>2</sup> GLA)

### Demand

Occupier demand is generally directed towards the modern office space in New Belgrade. However, law firms, financial and consultancy companies and marketing and advertising agencies, traditionally prefer downtown. In 2011, and the first half of 2012, the majority of office requests were for smaller floor plates up to 900 m<sup>2</sup>. There were a few larger lease transactions (over 2,000 m<sup>2</sup>), among which were the leases of Sitel and NCR with their SSCs.

## Rents

Prime headline office rents in Belgrade range from €14 to €16 m<sup>2</sup>/month whilst B class offices in prime locations, both downtown and in New Belgrade, are offered from €10 to €14 m<sup>2</sup>/month. Landlords offer typical incentives such as: rent free periods (usually three months), fit-out contributions and additional free parking spaces.

As the following chart suggests, today the market is tenant favourable and the same trend is expected to continue over the next year. Due to low new annual supply and increasing take up and demand for office space, in 2014 the market is estimated to be balanced between landlords' expectations and tenants' requirements.

Tenant- Landlord Market Conditions in Belgrade 2010-2013			
2012	2013	2014	2015
Tenant-favourable market conditions		Relatively balanced between landlord and tenant market conditions	
Landlord favourable market conditions			

## Summary

The objective of this report is to provide a better and greater understanding of the potential for the BPO/SSC market in Serbia, from a labour, economic and real estate prospective and the reasons for investing in this country.

Serbia is a country with a favourable geographic and strategic position, a historical gateway between East and West, located on two important Pan European corridors linking Western European countries with the Middle East. Belgrade, the capital city with a population of 1.6 inhabitants, is the regional leader and ex Yugoslavian political, economic, educational and cultural centre. Flights from most major European cities to Belgrade take no more than three hours. Serbia has the same time zone as most of continental Europe (GMT+1).

Serbia is an investor friendly country, offering generous incentives – financial, tax and other. Foreign investors are financially supported for new created jobs.

The workforce in Serbia is highly competitive and cost efficient. The country offers a well-educated, multilingual, hard working, diligent and loyal labour pool.

In March 2012, the country was granted an EU candidate status, as an award for its ten year long efforts in implementing political, economic and legal reforms.

From a real estate perspective, Belgrade's office market is tenant favourable and the current supply is able to meet the highest office requirements.

## Information on content providers

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**Serbia Investment and Export Promotion Agency (SIEPA)** is a government organization dedicated to effectively helping foreign investors and buyers, while raising Serbia's profile in the minds of international business decision-makers. Created in 2001 by the Government of the Republic of Serbia, its mission is to support foreign companies seeking to set up or expand in Serbia and Serbian companies when doing business worldwide.

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October 2012

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