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CHAPTER II

SERBIAN AGRIBUSINESS ON THE ROAD MAP TO THE EU ACCESSION

SASA DRAGIN

*Ministry of Agriculture, Forestry and Water Management
of the Republic of Serbia*

MIRJANA MILOSEVIC

*Ministry of Agriculture, Forestry and Water Management
of the Republic of Serbia*

MILAN STEGIC

*Ministry of Agriculture, Forestry and Water Management
of the Republic of Serbia*

MILOŠ MILOVANOVIC

*Ministry of Agriculture, Forestry and Water Management
of the Republic of Serbia*

IVANA IVKOV

*Ministry of Agriculture, Forestry and Water Management
of the Republic of Serbia*

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CHAPTER II

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Sasa Dragin, Mirjana Milosevic, Milan Stegic,

Miloš Milovanovic, Ivana Ivkov

*Ministry of Agriculture, Forestry and Water Management
of the Republic of Serbia*

1. Introduction

The area of agricultural production is in many ways an important area of the Serbian economy. Agriculture greatly contributes to the overall values of society, much more than it is the case in many other countries. In addition, it employs, directly and indirectly, a large part of the total population of the country. It directly provides livelihood to all persons engaged in agricultural activities (17.2% of the working population cited Agriculture as the main source of income¹). Indirectly, it provides income for persons employed in production and transport processes that do not take place exclusively in the field of agriculture but have the purpose of its support (production of fertilizers, agricultural machinery, equipment for packaging and transport of agricultural products ... and together with the primary agricultural production make one third of the workforce of the country). Agriculture has also become the activator of economic growth in rural areas of the country and the balance of regional disparities (almost a half of the country's population lives in rural area).

However, agriculture brings with itself certain political, social and economic responsibilities. These responsibilities exist in every country, regardless of the importance that agriculture has in the national economies of these countries. These responsibilities lead to difficult decisions that are often not guided solely by economic interests and which may even contribute to conflicts on the worldwide agro-economic scene.

In countries like ours and in most countries in transition, the responsibility is huge. Agriculture in these countries, as a rule, employs a large part of the total population, plays a significant part in the total foreign trade of the country and makes a great part of the total value created in the society. There is no doubt that in such circumstances the responsibility of those leading this sector has a worrisome dimension. Since the agriculture in these countries is, for the second time in the history of mankind, a driving force of development of the whole economy, decisions made in relation to this sector of the economy have far-reaching implications for the entire economy of these countries.

If we add to it the role imposed on agriculture in the early years of transition - an absorber of surplus employees in non-agricultural industries undergoing privatization and restructuring- then the situation becomes even more dramatic. In this situation, the agriculture (and those who head it) have a formidable task to perform. They are expected to reconcile, on the one hand, the vast and sometimes unrealistic expectations of the public who see agriculture as the future of society, provider not only for the country but also for the neighboring countries, and on the other hand, the realistic achievements that agricultures of transition countries have (due to many years of international isolation, low levels of investment, outdated techniques of production, processing and marketing of agricultural and food products, underdeveloped markets ...).

Since the Republic of Serbia clearly expressed its desire to become a member of the World Trade Organization, and later the European Union, its economy, and thus its agriculture as an extremely important part, will be limited by the influence of several factors. Both these multilateral systems regulate, in different ways, relationships among all involved in the process of production, processing and marketing of agricultural products and foodstuff, regardless of whether they are producers, processors, transport or, the most numerous ones- the consumers.

¹ 2002 Census

Agricultural policy as a state instrument for stimulating the development of this sector remains limited on two sides. On the one hand, there are the specific rules provided for the financing of agricultural production within the WTO / EU, and on the other hand, there are the limited state funds intended for placement in this sector of the economy. Placed between a hammer and an anvil, so to say (restrictions regarding the application of specific measures and insufficient funds for settling the total accumulated needs of agriculture) the state is trying to find the optimum. It is trying, using all means available (which are far from the necessary ones), to assist the transition of this sector to a successful, modern and market-oriented part of the economy in ways that do not flout the rules of financing and trade in agricultural products.

To sum up, as pointed out by **Jelic and Jovanovic (2009)**, the most important thing is that Serbia remains on the road of entry into the European Union. It means that it will be open many programs which will support Serbia in this early stage and, in the accession process.

2. Macro-economic indicators of agriculture in Serbia

Agricultural production in Serbia is far more than an economic sector that provides food security for the citizens of the country and the raw materials for the food industry. The role that agriculture plays for our country surpasses by far the role of agriculture in developed countries. This sector employs a large part of the labor force in Serbia, 44% of the country's population lives in rural areas and find their most basic income in agriculture or in industries closely related to agriculture. Due to years of isolation and reduced efficiency of other sectors of the economy of the country (secondary and especially tertiary sector of the economy) it adds considerably to the total income of the Republic of Serbia. In the years of transition it represents an absorber of surplus labor force from other sectors of the country's economic activities and is the only area of the economy with internationally confirmed success.

Agriculture in Serbia has great economic strength, agriculture is the basis of economics and holder of rural development. However, it takes on a new, multifunctional character, greatly facilitated by the new understanding of the rural in Serbia. The overall development of the rural areas of the country, aided by the strengthening the economic performance of agricultural production and development of the activities more or less related to agriculture (rural tourism, the old crafts, conservation and exploitation of cultural heritage, ...), leads to the transformation of this sector into an attractive environment for living, working and prosperity of all its inhabitants.

The great importance of agriculture is reflected in its share in the gross domestic product (GDP) of the Republic of Serbia, which was 10.62% of total GDP in the year 2009. The agricultural sector achieved positive results in 2009, which mitigated the fall of the overall GDP of Serbia that was the result of the economic crisis (Table 1.).

The performance of the agricultural sector varies from year to year, and the share of agriculture in total GDP is constantly decreasing. During the transition period the share of agriculture in GDP has reduced from 14.30% to 10.62%. Such a tendency has also been observed in other countries in transition.

Table 1. The share of agriculture in GDP of the Republic of Serbia

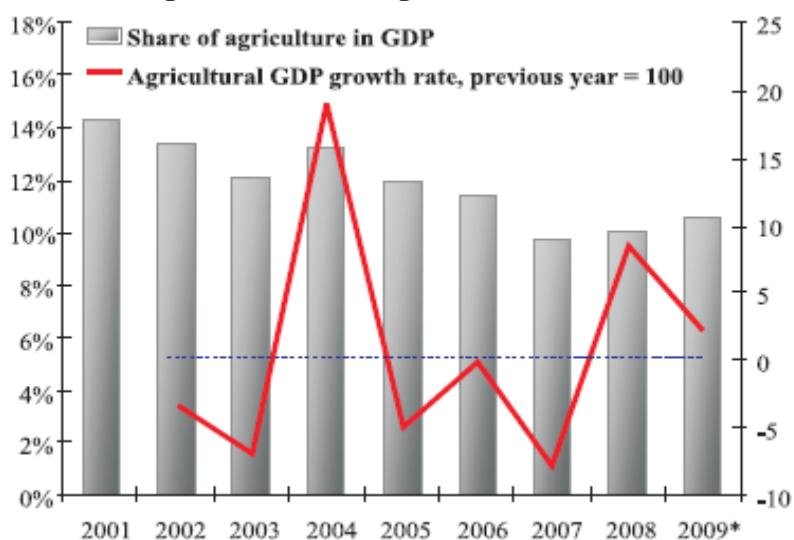
Year	Agriculture, hunting, forestry, fisheries (millions RSD)	Gross domestic product of the Republic of Serbia, at 2002 constant prices (millions RSD)	The share of agriculture in GDP	The rate of growth, the previous year = 100
2001	133.927,3	936.543,7	14,30%	
2002	129.629,5	972.900,7	13,32%	-3,2
2003	120.603,8	996.714,0	12,10%	-7,0
2004	143.545,8	1.079.044,2	13,30%	19,0
2005	136.500,2	1.139.590,6	11,98%	-4,9
2006	136.205,3	1.198.964,9	11,36%	-0,2
2007	125.576,6	1.281.694,8	9,80%	-7,8
2008	136.316,2	1.352.418,0	10,08%	8,6
2009*	139.340,5	1.311.864,8	10,62%	2,2

*estimation

Source: Statistical Office of the Republic of Serbia, *Quarterly report-Gross Domestic Product at constant prices 2002*, Notification No. 179

The fluctuation in the growth rate of agriculture in the period between 2001 and 2009 is characterized by extreme variability (Graph 1.). The range between the highest and the lowest growth rate in the mentioned period is about 23%, which indicates the unpredictability of developments in this sector.

In the year 2009, the estimated agricultural rate of growth was 2,2%, which was contributed by the production of corn, wheat, sugar beet and fruit (especially apples and plums). Additionally, as pointed out by **Cokorilo and accomplices (2009)**, the agricultural sector was achieved positive results in 2009 and, the mitigation of falling Gross Domestic Product was significantly influenced by this sector.

Graph 1. The share of agriculture and the growth rate of GDP between 2001 and 2009

Source: Statistical Office of the Republic of Serbia

Comparative analysis of the agricultural sector of Serbia with the results achieved in the agriculture of the European Union and countries in the region shows that the growth rate of this sector does not differ significantly from the neighboring countries (Table 2.).

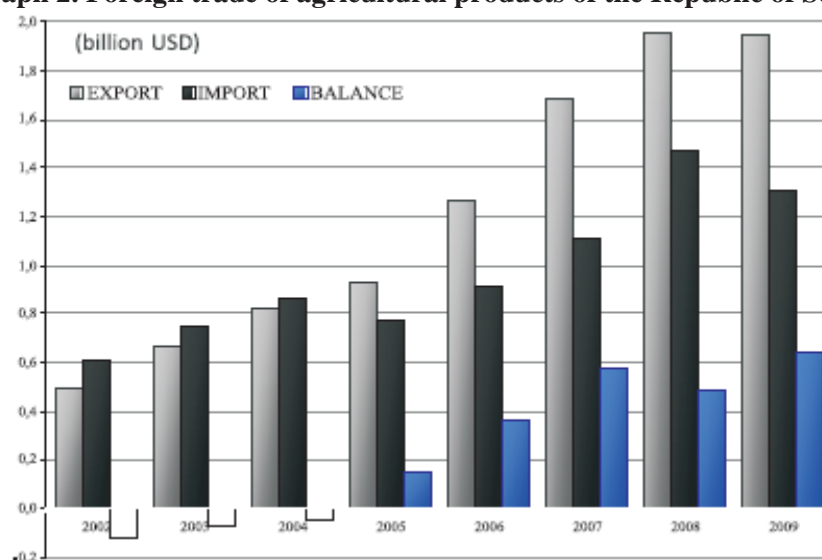
Table 2. The growth rate of the agricultural sector

%	2001	2002	2003	2004	2005	2006	2007	2008
EU 27	-0,5	0,2	-4,6	11,2	-4,9	-0,7	-1,8	3,2
Serbia	/	-3,2	-7,0	19,0	4,9	-0,2	-7,8	8,6
Bulgaria	0,3	4,3	-2,3	2,3	-9,3	-1,0	-29,7	24,6
Croatia	2,2	4,4	-7,4	10,2	-0,4	1,9	1,4	3,2
Hungary	16,2	-9,9	-0,2	54,0	-3,9	-6,5	-21,3	54,3
FYR Macedonia	-0,7	-2,1	4,9	6,4	0,3	4,8	-2,9	/
Romania	28,2	-6,9	5,0	18,6	-17,2	3,4	-15,3	18,8
Slovenia	-0,7	15,1	-19,9	10,9	-0,6	-4,5	2,2	0,2

Source: Eurostat, Statistical Office of the Republic of Serbia

Despite the reduced share of agriculture in the total GDP, which is expected in a transition economy, it will remain an important segment of the economy of Serbia in the future. Agriculture is the sector with a positive foreign trade balance, which is the backbone of the development of the foreign trade of Serbia (Graph 2.).

Graph 2. Foreign trade of agricultural products of the Republic of Serbia



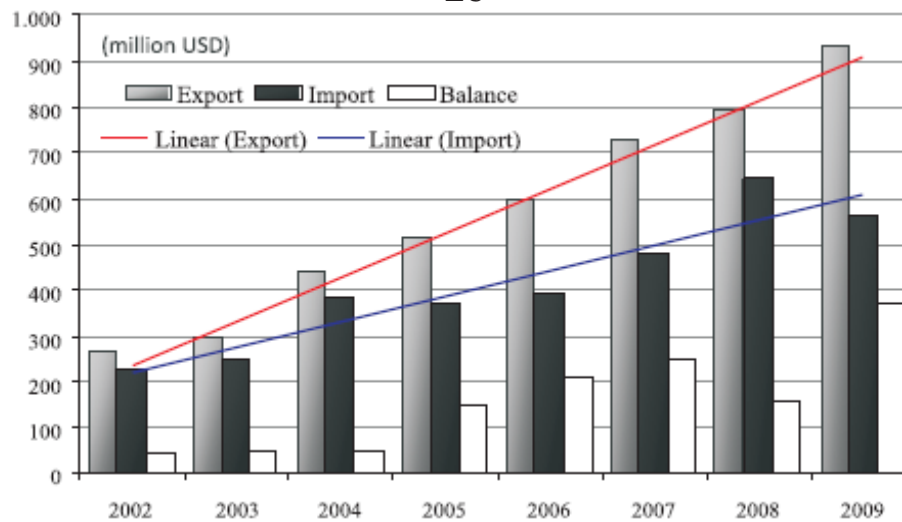
Source: Customs Administration

Since 2001, when the exchange recorded a deficit of USD 136.4 million, for the first time a surplus of about USD 150 million was recorded in the year 2005. With the growing trend, there was a surplus of about USD 638 million in 2009. The main destinations for export are the markets of the EU countries (for which we have preferential access), as well as the markets of the CEFTA region (with a high degree of trade liberalization).

In the last five years, the agriculture of Serbia has recorded a gradual growth in foreign trade and positive balances due to the expansion of markets (Graph 3.).

If one looks at the foreign trade with the EU in the last 8 years, the average growth rate of the exports to the EU is 19.6%, and that of the imports from the EU is 14%.

Graph 3. Foreign exchange in the field of agriculture between the Republic of Serbia and the EU



Source: Customs Administration

It is expected that, with the integration of Serbia into the EU, the growth of imports will be faster than the growth of exports. This is probably the biggest fear related to the EU accession that is imposed on agricultural producers. This fear is quite well justified, because the production in which Serbia is uncompetitive, and with easier access to our market, there will be an increase in imports of these products. However, at the same time, the access to cheaper and better quality raw materials provides an opportunity for development of many new production complexes, because agricultural production is in a highly related and dependent market chain, in which one production is an input to another.

It is expected that at the beginning of joining of the Republic of Serbia to the European Union there will be an increase in foreign trade of agricultural and food products. Based on the results achieved in the past ten years, there is an obvious positive trend of exchange in favor of the Serbian side. However, with the full integration into the single market of the EU, with the complete elimination of tariff protection and with elimination of non-tariff barriers to trade, it is realistic to expect a better use of opportunities by the Serbian exporters, but also an easy access to the Serbian market for EU importers. Adjustment of agriculture in Serbia to new conditions of the global paradigm will lead to better allocation and thus, to resources, from less to more productive users, to higher employment, traffic growth and a better selection of goods.

3. The process of accession of Serbia to the European Union

The EU policy is not a static system but it represents living matter that has evolved greatly to the present form from its initial, original idea. The dynamics of its expansion can be seen in picture number 1. The Republic of Serbia is well on the way to become a part of an innovative and dynamic system and on that way it also accepts the obligations arising from the membership / accession.

Picture 1. The EU enlargement in stages



Source: European Commission, Brussels

It is certain that this road will be neither easy nor quick. It is necessary to undertake a number of activities that require the involvement of not only state authorities but also national (and international) scientific and professional public as well as all those competent to help Serbia to become a member of that system. On this road, agriculture (and not only agriculture but also industries dependent on it) may expect big changes the cause of which is approaching the EU.

The reason is simple. In order for a country to be able to function as a member of such a complex system consisting of 27 countries so far, it has to be able to implement all that is required for agriculture, and industry in general, of other member countries.

In other words, it means the following. If we wish to sell our products to the EU citizens, then those products must be of at least the same quality, health safety and hygiene, as the products produced by the farmers of the EU. In fact, our products must be of higher quality than those produced in the EU, *otherwise, why would anyone prefer our products to those they have used so far, and which have satisfied their needs?* This again means that our products must be manufactured in accordance with the procedures of production, which are mandatory for producers in the EU. *Otherwise, why would their manufacturers have to comply with certain standards and ours would not?* Is it not easier for the European Union to import food from us and avoid the standards, rules, regulations and other requirements in production? *Maybe it is easier, but what will their farmers do then?* What will the food processor companies and processors of other agricultural products do?

Before explaining the causes and the process of creation of this policy, and defining the term agricultural policy, it is necessary to answer the following question, *What is the Common Agricultural Policy of the EU?*

Agricultural policy can be defined as a set of different measures which are used to regulate relations between the participants in the process of producing and processing agricultural products. Thus, agricultural policy incorporates measures of land policy, the policy of financing agriculture, pricing policy of agricultural products, foreign trade policies in agriculture, fiscal policy, agriculture investment policy and so on. All these policies together make the agricultural policy.

It is important to highlight that agricultural policy cannot be a policy for itself but is a part of an overall economic policy that a certain country follows. This means that agricultural policy cannot be significantly different from the economic policy of the country- it must serve the purpose of achieving the goal of the overall economic policy. If the country decides that its best interest is to become competitive in the world market and that it is in its interest to join some international organization (for example, the European Union or the World Trade Organization), then all its policies must lead to this goal. Foreign policy must seek to fulfill its objectives, as well as the policy of defense, economic policy has an objective to facilitate the development of competitiveness, the fiscal policy to stimulate entrepreneurship and, of course, agricultural policy to enable the improvement of agriculture and food industry.

After defining agricultural policy, there is another question that arises: *What is The Common Agricultural Policy and why does the European Union have a common agricultural policy? Why does every country not follow its own national agricultural policy and what is the purpose of such a large and demanding common agricultural policy?*

The EU currently has 27 member countries which is more than 4 times the initial number of countries that were the bearers of this mechanism. These countries are mutually very different. The diversity is reflected in the conditions for agricultural production, for example the potentials of agriculture in Greece or Portugal are totally different from those in Finland or Denmark. The representation of certain types of agricultural production is different as well (what most grown in Italy are fruit and vegetables and in Lithuania cereals). Also, the number of people directly or indirectly engaged in agriculture is very different. Finally, and perhaps most importantly, the significance of agriculture itself to their economy is completely different.

As pointed out by **Bozic, Muncan and Miljkovic (2009)**, the Common Agricultural Policy-CAP is a complex policy for management in agriculture and rural development. It represents a first and rare policy of the EU, which provides the highest level of integration and serves the Member States to transfer their sovereignty to the common organs.

The Common Agricultural Policy is a complex system of principles, rules and instruments aimed at achieving specific goals. The common policy of all member countries is used to regulate the process of primary production and processing of agricultural and foodstuff in all the countries of the EU.

Since the EU is a single legal entity as viewed from the standpoint of the world trade, then as such it must have a single tariff protection. The Common Agricultural Policy has the task of shaping the foreign policy for the EU market as a whole (it determines the cost of customs duties for import of products to the EU market).

In addition to these objectives, the CAP is an attempt of improving, which is upgrading the living conditions of people living in rural areas, accelerating agricultural productivity growth, stabilizing the market of agricultural products and the impact on prices of agricultural products and foodstuff which skyrocket in those years.

What is more, the CAP intended to achieve its goals through providing sufficient quantities of food at any time, at stable prices, which would also ensure a decent and regular income for farmers as well as compensation for their honest and hard work.

The CAP, being an agricultural but also a social policy, is an attempt of reconciliation between the opposing interests of farmers and non-agricultural population of the EU, that is those it was created for, on the one hand, and explicit demands of the World Trade Organization, led by the countries with comparative advantages in agricultural production, on the other hand.

The Common Agricultural Policy is the most expensive policy from the standpoint of the central budget of the European Union. For many years, its share in the total, central budget was more than a half of the total available funds. This fact which puts agriculture at the top of the list of the European priorities is often wrongly interpreted in the local public.

The demands for increasing the budget issue intended for the agriculture of Serbia have been heard many times so far. This increase is often based on emulating the European Union and there is an inevitable remark that the EU allocates a half of its budget to agriculture whereas the Republic of Serbia allocates much less, of course, in relative terms. By comparison, the agricultural budget of the Republic of Serbia in 2010 makes about 3% of the national budget. We are ignoring the fact that these two figures cannot be compared.

The reason is as follows. Those who continually cite this fact as obvious evidence of inadequacy of domestic agricultural policy do not know that education and health care, as two largest items of almost every national budget in the world, in the European Union are not funded from the central budget where

from the Common Agricultural Policy is financed. Education and health care are funded from the national budgets of member countries. If the education and health care (along with the military) are included in the overall expenditures of the EU, the situation becomes drastically different. Thus the share of agriculture in the total budget accounts for less than 2% of total expenditure of the EU member states (European Commission, October 2004) which places agriculture, in relative terms, and after taking into account this fact, at the bottom of priorities for funding.

4. Serbian Agribusiness and the Stabilization and Association Agreement with the EU

Serbia initialed the Stabilization and Association Agreement with the European Union and its member countries on 7th November 2007 and signed it on 29th April 2008. As pointed out by Todorovic, **Davidovic and Sretic (2008)**, this Agreement represents a qualitatively new level of relations between Serbia and the European Union, since Serbia and the EU for the first time entered the phase in which their relations are regulated by a comprehensive agreement. This Agreement regulates almost all aspects of mutual relations between the EU and Serbia, and above all their mutual economic relations.

So far, relations between Serbia and the EU have been based on unilateral declarations of will between the two sides. The purpose of this Agreement is to guarantee the prospect of membership in the European Union to the country that signed it, that is, Serbia, which is the main difference between the association agreements and all other agreements that the EU concludes with third countries.

This Agreement makes Serbia a country with a clear perspective of membership in the EU.

Leaving aside the political element of the Stabilization and Association Agreement, the essential element of this Agreement is the creation of a free trade zone between the European Union and Serbia. This zone will be created in the interim period of six years from the date of bringing the Agreement into force.

This agreement provides free access of the goods originating from Serbia to the EU market. This will inevitably lead to changes in the way business is conducted and in the position of domestic firms in the EU market. The Agreement is supposed to provide the elimination of tariff protection for the import of goods from the EU for a large number of commodities, which would change the current market situation in Serbia.

Due to the nature of this Agreement and its main consequences, that is, creating a free trade zone, it is necessary for Serbia's economy to be aware of the rights and obligations arising from it. Only then can the economy of Serbia prepare itself most efficiently for economic changes that will inevitably happen in the years to come.

The agriculture of Serbia has already found the right way towards the EU market. Almost a half of total export is directed to the EU market (the average for the period between 2002 and 2009 is 48%), and it produced an average annual surplus of more than USD 159 million (for the period between 2002 and 2009).

How will SAA affect the relations of trade in agricultural products of Serbia with the agricultural products of the European Union and should there be any fear of "free trade"? Under what conditions will the trade in agricultural products of Serbia with the agricultural products of the European Union be carried out after the entry into force of the trade part of SAA? What are the changes made by signing SAA in this sector of economy? Is Serbian agriculture ready for Europe?

In order to answer these questions, we are going to start from the already existing conditions of foreign trade of agriculture in Serbia.

What had the dominant influence on the increase of the volume of export of agriculture is the foreign policy of the Republic of Serbia, whose implementation began after the changes in the year 2000 and with the integration of the Serbian economy in international trade based on market principles.

The foreign trade system was liberalized; the quantitative restrictions on import and export, export quotas, licenses and the like were all lifted.

However, despite the reform of the customs system and the significant lowering of duty rates, a relatively high import protection of agriculture was provided - at a level of about 21% in average, including all three forms of import protection (tariffs, seasonal import duties and surtax). On the other hand, access to foreign markets has been made considerably easier. The access to the regional market has been made easier particularly through bilateral free trade agreements and the access to the European market through ATM (Autonomous Trade Measures) approved by the EU to the Western Balkans countries at the end of November 2000.

Thanks to this asymmetric mode (ATM), the European Union managed to allocate a part of its profit to the agriculture of the Republic of Serbia, for the purpose of economic recovery of its future partner and a member. As a result, the Serbian agriculture has been recording a positive foreign trade balance in trade with the EU for years now. These measures have provided preferential export to our agriculture, which implies duty-free imports from Serbia for all the products and in unlimited quantities, except for fish, young beef, sugar and wine, for which preferential quotas have been established. The quotas for wine and fish were the same for all the countries of the Western Balkans. The necessary condition for export to the EU market is the quality and health safety of the products in accordance with the EU standards. The same standards are applied to producers in the EU, as well as to products imported from any other market including the market of the Republic of Serbia and are fully transparent and non-discriminatory.

Serbia has a preferential status in export, in accordance with the ATM, and a full import tariff protection, as follows:

- ad valorem duty, which is calculated as a percentage of the base; the base for calculating is the import value of goods increased by a certain share of VAT,
- seasonal duties (which is 20% and is applied only to certain varieties of fruit and vegetables in a particular period of the year), and
- special taxes (or surtax) that is charged in the absolute amount per unit of imports and are a kind of protection of domestic production from price fluctuations on the world (European) market as it is charged in the absolute amount per unit.

The status in trade with the European Union that is listed above and which has been applied, implemented or preferred for seven years, provided enough time for:

- the recovery of Serbian agriculture from the years of unfavorable economic conditions during the economic blockade in the nineties,
- the recovery of the agricultural production factors,
- the reorganization and restructuring of production,
- the implementation of the privatization process,
- the registration of farms, that is establishing direct communication between agricultural producers/farmers and their responsible ministry
- establishing market economy, enhancing productivity in production and increasing competitiveness in exports, and finally,
- adopting the required standards of quality and health safety of their products, and so on.

By concluding and implementing the SAA and establishing a free trade zone with the European Union, Serbian agriculture gets the chance to check to which extent it managed to take the advantage of the opportunities and preferential terms that it has been receiving for the past seven years from the strong economic integration. It should be stressed that the EU has not dictated their preferential terms by eliminating the export incentives that Serbia provides by annual regulations for the export of certain agricultural products and foodstuff.

4.1. And how do we establish a free trade zone for agricultural products?

A free trade zone for agricultural products is established gradually during the transitional period of six years. It is an additional period of adaptation of agriculture to new conditions of market exchange with the market of the European Union, the period during which Serbian farmers should become much more productive and better, that is, more competitive to those of the EU, and they must have adequate support from the agricultural policy of the national economy. The economic effects of establishing a free trade zone with the EU which the SAA brings to Serbian agriculture, among others, will be manifested as:

- cut in input costs, i.e., reducing of the prices of raw materials and intermediate goods that are imported for agricultural purposes from the European Union
- safe and long-term amounts for preferential marketing of products that are regulated by quotas, because with the SAA, the quotas become contractually binding on both sides and cannot be reduced by the unilateral action of the European Commission. The preferential

export quotas that have been used so far for wine, sugar and young beef were the result of one-sided, annual decisions of the EU. Also, the introduction of quotas that have been assigned solely to Serbia, not the region, gives a clear perspective of the marketing of goods to the EU market, which enables planning of long-term market investments that have so far bypassed certain sectors of our agriculture.

5. Conclusion

Indicators of agricultural production suggest that the global economic crisis, which deeply influenced the macroeconomic situation in Serbia, has a limited impact on this sector of economy. It should be said that the incentives undertaken by the government have also affected positive developments in agricultural production. For many years on the world economic scene, the EU has been a source of constant controversy. The EU policy has not nearly finished the period of its development which means that, undoubtedly, big steps are yet to be made...

The CAP today, having been reformed after the explicit requests of numerous directly affected parties, is still a successful policy. Success is not measured only by tons of exported products, nor by the yields and the standard of the rural population, but by the fact that this has been achieved with considerable concern for the food safety, environment protection and for development of rural area, pointed out by **Trbovic and Crnobrnja (2009)**. Highlighting the importance of the development of rural areas and environmental protection represent a new understanding of agriculture, which is no longer a mere source of food and raw materials for industry, but living from nature and in harmony with nature.

As pointed out by **Sevarlic, Tomic and Bugarin (2008)**, agricultural and rural policy should be adopted to CAP, but gradually and in accordance with our national interest and with level of competitiveness of our producers.

The best answer to the question of how the implementation of the SAA will affect Serbian agriculture, considering all the current problems of this sector, is to be given in the years of full implementation of this Agreement.

In addition to a clear political message, and in addition to our country's irreversible road towards the EU, the SAA has a great economic importance for the local agriculture. Probably the two most obvious benefits are the pre-accession funds for the development of the rural economy of Serbia and free, tax-free flow of goods.

Food is cheaper in many parts of the world than in Serbia: while the European countries with much higher living standard import foodstuff of best quality (for which they established high standards), the Republic of Serbia makes the imported food even more expensive by adding high tariffs and protects domestic producers and traders from competition and allows them to remain unproductive and raise their prices according to their own abilities. To sum up: In the years to come food in Serbia will become cheaper and cheaper for consumers, and the selection will be wider.

The SAA brings the need for the Serbian agriculture to prepare seriously for the entrance into Europe. The period of six years is not a long period at all, and from the model of liberalization of the import protection of Serbia to the EU market, we see that for some branches of production it will be significantly shorter. During this time, Serbian farmers will have to become commodity producers. A lot of them have already become ones, but their task will be to be even more efficient, to provide better quality and to become more competitive.

The SAA will accelerate the necessary processes in agriculture, increase the volume of profits in agriculture and improve living conditions in rural areas. The strong potential of Serbian agriculture is a great challenge as well.

However, with joint and systematic work with a predictable, stable and consistent policy, we can respond to all the new challenges that we face on our way of joining the EU.

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