



SERBIA AS THE STRONGEST LINK?

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Global Value Chains (GVCs)

For small economies linking up with GVCs that account for nearly 80 percent of global trade could be greatly beneficial for promoting exports and integrating into global trade without having to build expertise in all aspects of production of a good.

In the long-run, participation in GVCs has a positive impact on income per capita, investment and productivity.

However, the gains are not equally distributed (as upper-middle and high-income countries benefit much more) and may be one-off and countries do not always achieve more dynamic industrial development in the long term

COVID-19 pandemic revealed profound weaknesses of GVCs

- The COVID-19 pandemic exposed the fragility of a model distinguished by high fragmentation and interdependences between MNCs and suppliers located across several continents.
- Current pandemics affects production and transportation costs, make it difficult to resume sustainable business on a global scale (e.g. South Asia – North Europe freight rates are 560% higher compared to October 2020).
- Trade is likely to fall more steeply in sectors characterized by complex value-chain linkages (e.g. electronics and automotive products)
- The effect is widespread as at least 2/3 of the companies report supply chain disruptions or delays in receiving goods leading many firms to downsize production capacities or shut down their production activities.
- Lawmakers, regulators and corporate stakeholders are demanding increased corporate responsibility across supply chains (German, US

Supply disruption and Demand Voilatility

Fluctuations and price increases

Delays in shipments, moving cargo, loading, unloading

Reduction in production capacity

Difficulties in obtaining information (lack of transparency)

Determinants of GVC linkages

Gravity factors

agglomeration and dispersion forces predominantly determine the distribution of economic activity (GVC links)

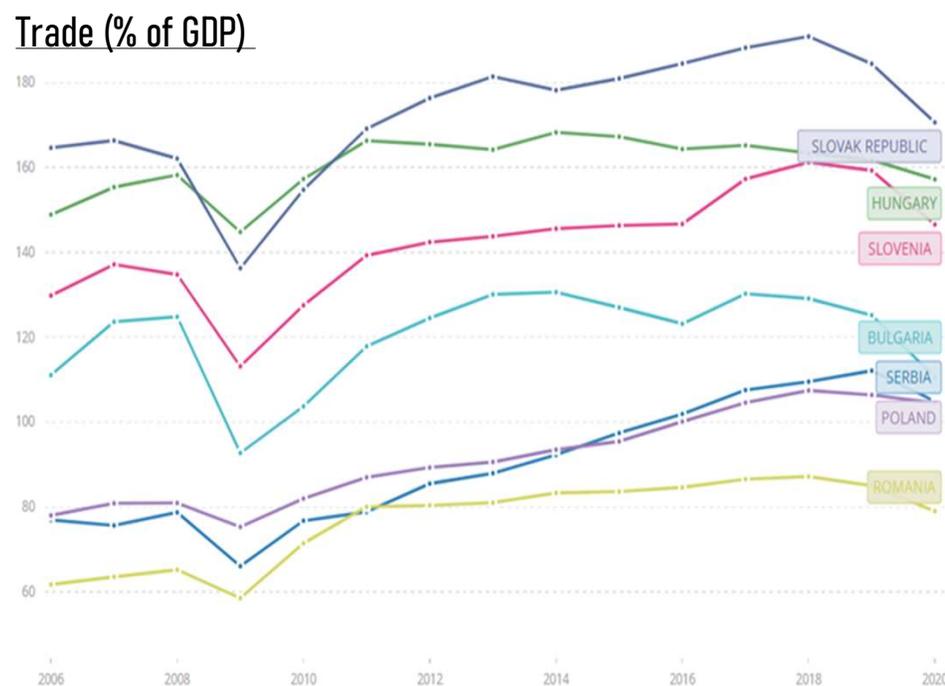
Policies

improving absorption capacity (dealing with skills shortage, low institutional quality, logistic issues)

Trade openness

Serbia is a typical small emerging economy that relies on export-led growth

Serbian trade openness has increased substantially over time



Backward and forward linkages

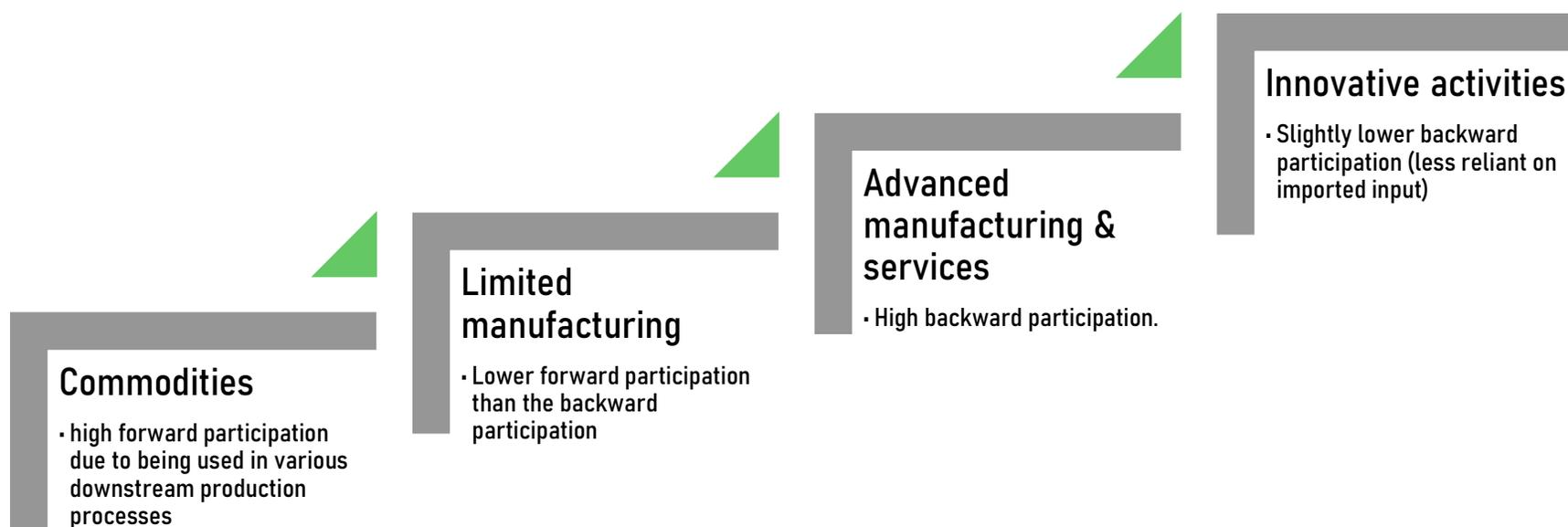
Serbia is currently economy with:

- intensive “backward” linkages (foreign value-added) and
- some “forward linkages” (the domestic value-added is embodied in intermediate exports that are further re-exported to third countries)



Source: WDR (2020)

WDR GVC Ladder



It took almost two decades for Serbia to move from economy mostly in commodities to the one with the limited manufacturing GVCs alongside commodities (WB WDR 2020)

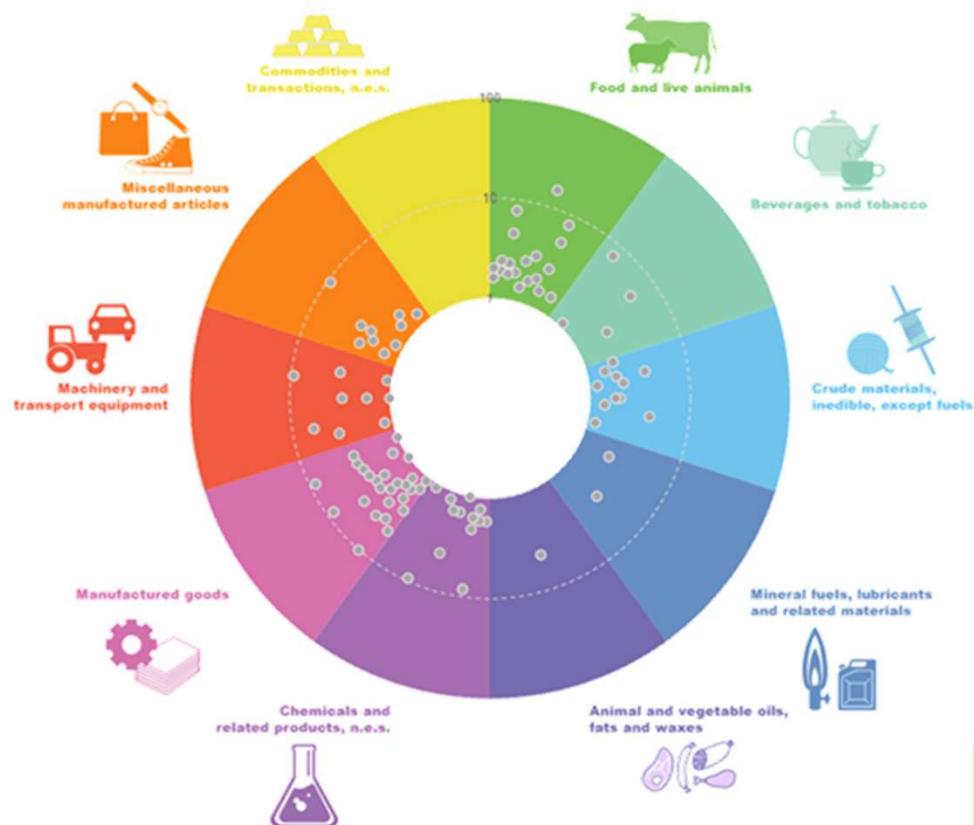
Thanks to FDI, the structure of exports is changing toward medium and high technology

Revealed Comparative Advantage

The revealed comparative advantage of Serbian exported products are indicated in the plot for all product groups which have an RCA greater than 1

>1 the share exports in a Serbia's total exports relative to the share of such exports in total world exports

Serbia, has also RCA in services (IT sector, business services)



Source: UNCTAD (2019)
Products plotted are SITC revision 3 product groups at the 3-digit level

GVC Integration Options

Countries can join GVCs either by

- facilitating domestic firms' entry through local suppliers' integration or
- attracting foreign investors either via greenfield or brownfield FDI.

So far Serbia mostly focused on the second option via subsidies

Some evidence of spillover effects

Serbia's absorptive capacity to play a role in affecting the extent of spillovers.

Spillovers and absorptive Capacity

Upstream and downstream effects (Brussevich & Tan,2018)

- Positive - Serbian suppliers or firms are located in the same industry as FDI firms, enjoy higher productivity stemming from technology transfer, higher quality standards, or higher competition.
- Negative - Productivity of domestic firms sourcing from industries with a large share of FDI firms find their productivity reduced, presumably due to mark-ups

Numerous anecdotal evidence

FDI subsidy policy

Four criteria – jobs, investment, sector and regional development

Maintenance condition

Time to rethink how to enhance absorptive capacity and GVC linkages

Criteria	Sector	Municipality development level			
		I	II	III	IV
Minimum jobs created	Primary	25	25	25	25
	Manufacturing	50	40	30	20
	Services	15	15	15	15
Minimum investment	Primary	€ 200,000	€ 200,000	€ 200,000	€ 200,000
	Manufacturing	€ 500,000	€ 400,000	€ 300,000	€ 200,000
	Services	€ 150,000	€ 150,000	€ 150,000	€ 150,000
Maximum subsidy for investments (in tangible or intangible assets or for gross wage expenses after full employment for the investment project has been achieved)		10%	15%	20%	25%
Maximum subsidy for investments over €50 million		– Maximum 25% for an amount over €50 million – Maximum 17% for an amount over €100 million			
Maximum subsidy for gross wage expenses* *maximum per job created		20% €3,000	25% €4,000	30% €5,000	35% €6,000
Additional per-job subsidy for labour-intensive manufacturing on gross two-year wage expenses		– Over 200 jobs created , extra 10% – Over 500 jobs created , extra 15% – Over 1,000 jobs created, extra 20%			

Source: Delevic (2019) based on RS MoE data

Local suppliers' integration

Several successful programs – e.g. subsidizing the introduction and certification of food safety and quality systems, organic products and products with a geographical indication

Potential interventions

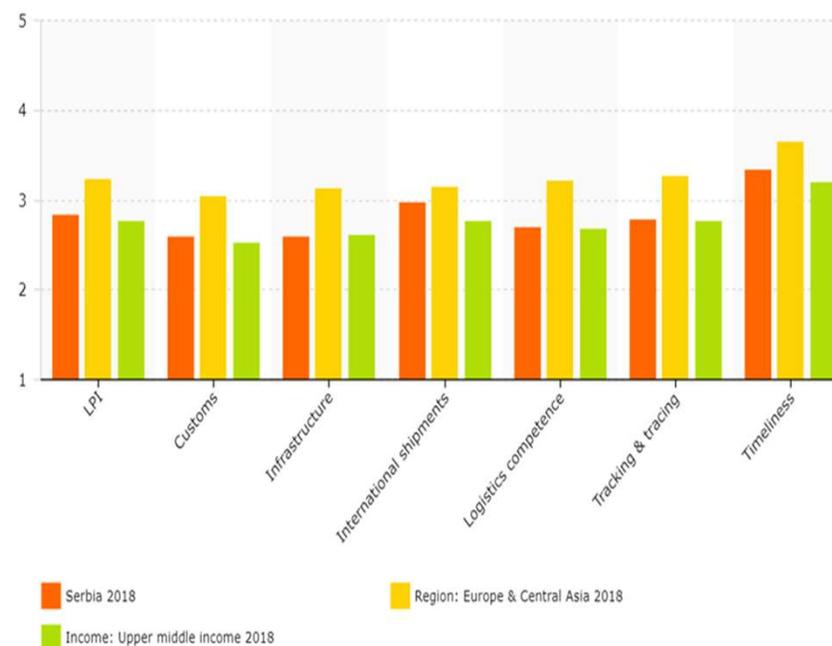
- Export readiness and coaching programs;
- Supply-side capacity building (certification, standardisation)
- Matching demand and mapping supply
- Networking

Serbia's infrastructure and logistic performance

Serbia ranked 65th based on WB LPI score

Serbia is substantially improving quality of trade and transport related infrastructure (railroads, roads, airports information technology);

However, **efficiency of the clearance process** (i.e., speed, simplicity and predictability of formalities) by border control agencies, including customs and competence and **quality of logistics services** (e.g., transport operators, customs brokers) could be improved.



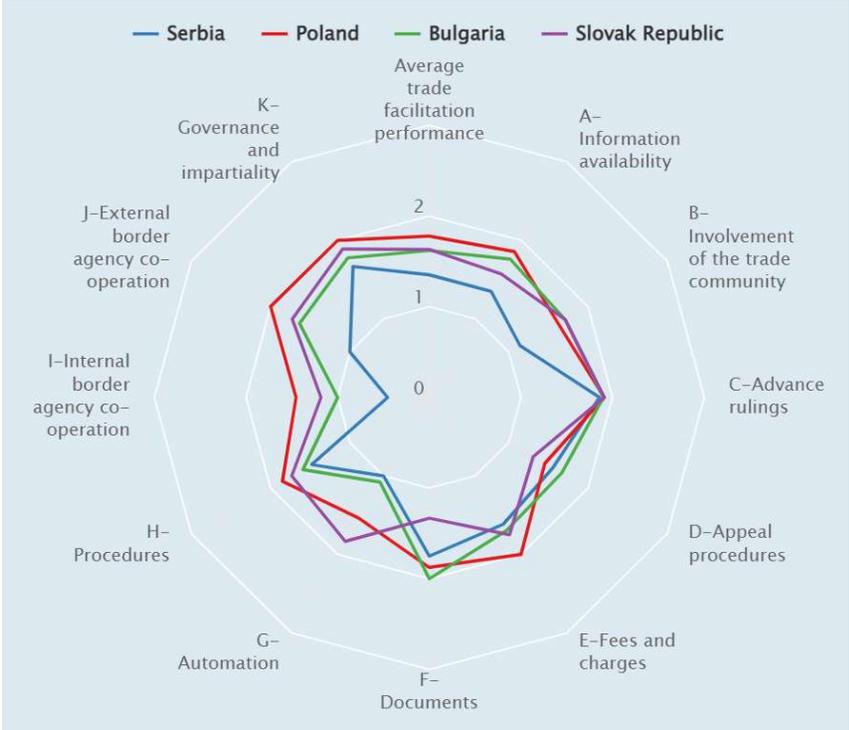
Trade facilitation

Further improvements of automation and reduction of formalities

Trade agreements

WTO Membership

Serbia as a hub for regional value chains



New environment

Calls for “sovereign” or “national” supply chains and re-thinking of domestic companies’ approaches to international outsourcing of production are becoming louder

German Supply Chain Due Diligence Act (+3.000 employees)

- protect human rights
- ensure sustainable production

Focus on

Promotion of standards and certification procedures

Review of transport, logistics and customs clearance regulations

Reassure provision of key inputs (electricity, gas, ...)

Well run communities that invest in crisis prevention and response and that pursue evidence-based public policy will be better able to weather crises and mitigate negative economic impacts.



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