



# Raising Competitiveness Through Industrial Policy

**31 January**

Belgrade

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# Structure of the presentation

1. Global trends in manufacturing
2. Setting the scene
3. Productivity and country competitiveness
4. Internal and external factors of productivity
5. Policy implications for Serbia
6. The downsides of industrial policy
7. Competitiveness and the European integration process
8. How the OECD can support Serbia



# 1. Global trends in manufacturing

Major science and technology driven changes in the production of goods and services are currently unfolding:

- ❖ Raise in productivity, mostly through automation and technology
- ❖ Outsourcing of service activities (e.g. logistics, IT services, etc..)
- ❖ Establishment of Global Value Chains (GVCs), particularly network industries
- ❖ Delocalisation of labour-intensive operations
- ❖ Change in the skill composition
- ❖ ICT, 3D printing, industrial biotechnology, nanotechnology, internet of things and robotisation have the potential to dramatically transform the manufacturing sector over the medium term



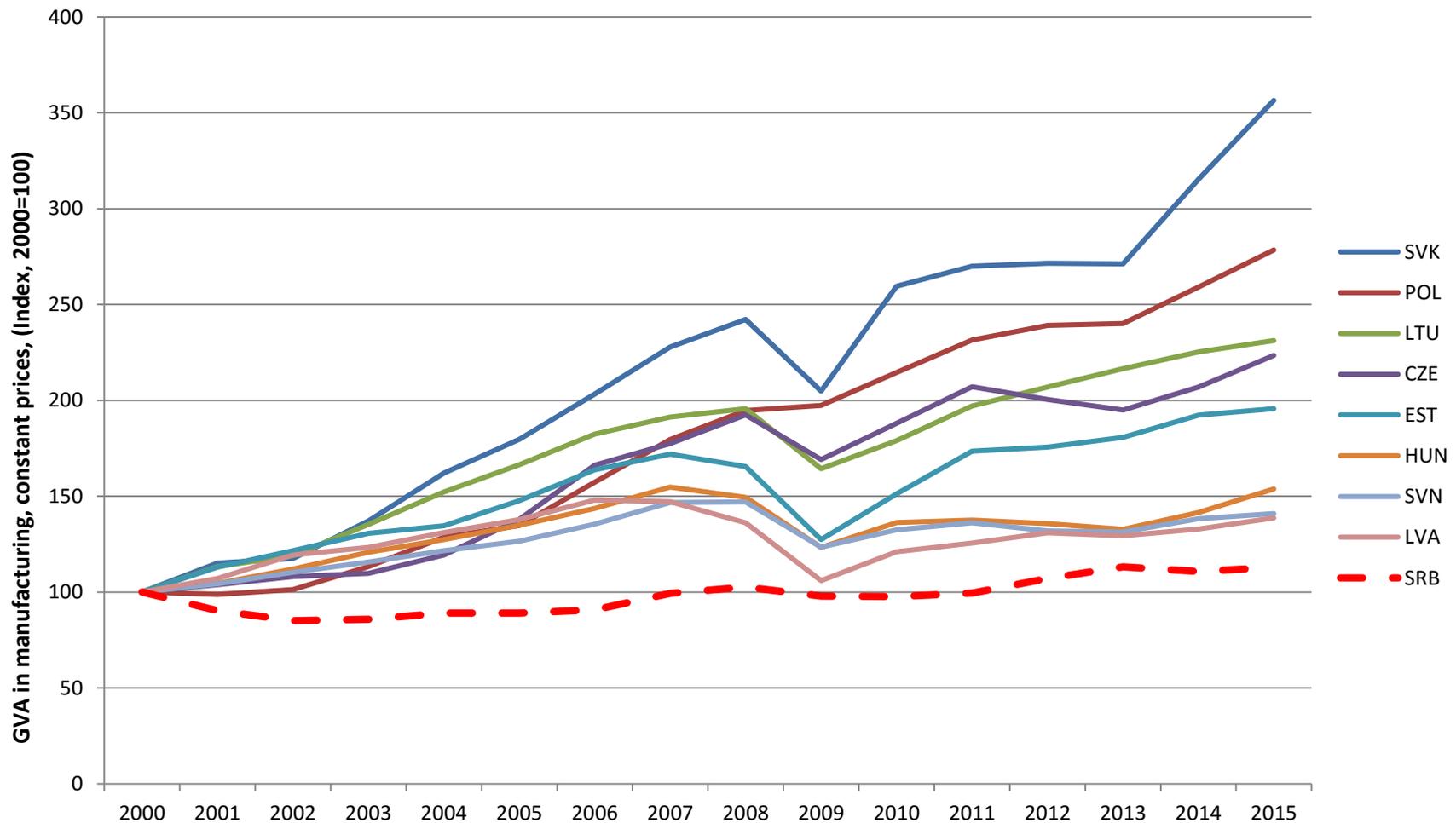
## 2. Setting the scene

- ❖ Although it remains an important component of the Serbian economy, manufacturing has stagnated since the early 2000s
- ❖ The sector suffered from the lack of investment in the '90s, and was able to attract only a fraction of the investment that went into Eastern Europe since the beginning of the 2000s
- ❖ Since 2014, there were signs of revival, mainly driven by FDI
- ❖ The share of value-added manufacturing has been stable around 25%, lower than in successful new member states of the EU
- ❖ **Manufacturing in Serbia has been long characterised by under-investment**
  - In an initial phase, FDI went mostly into non-tradable good sectors and remained subdued compared to other sectors, while domestic investment was also limited
- ❖ **New investment is needed to fill the competitiveness gap**
  - Despite recent improvements, productivity level of Serbian manufacturing is at about 40 percent of that in countries like Hungary, Czech Republic, Poland or Slovakia, though it is comparable to Bulgaria and Romania
  - While salaries in Serbia are lower than in Central Europe, they do not compensate for productivity (World Bank, 2012)



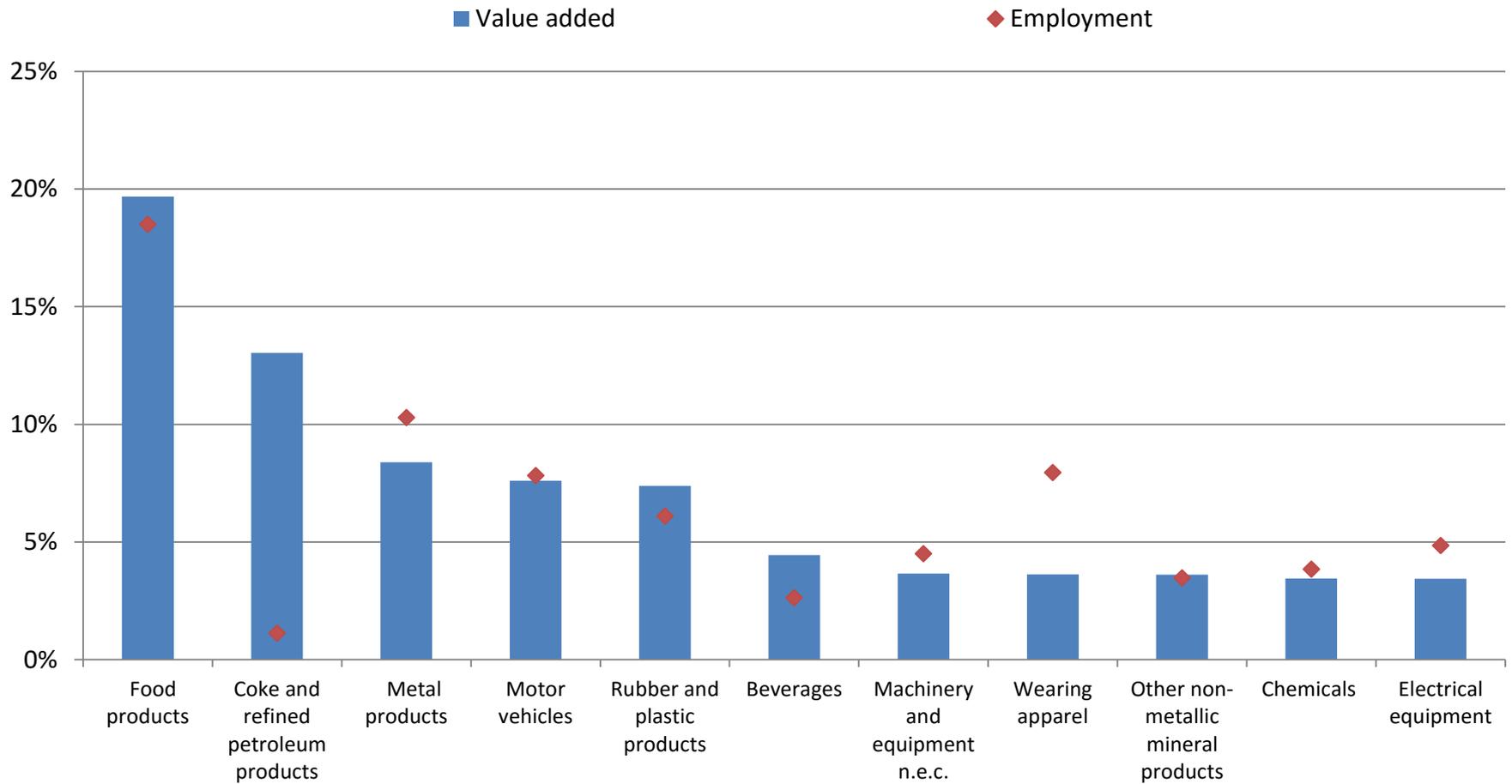
## 2. Setting the scene

Value added growth in the manufacturing sector



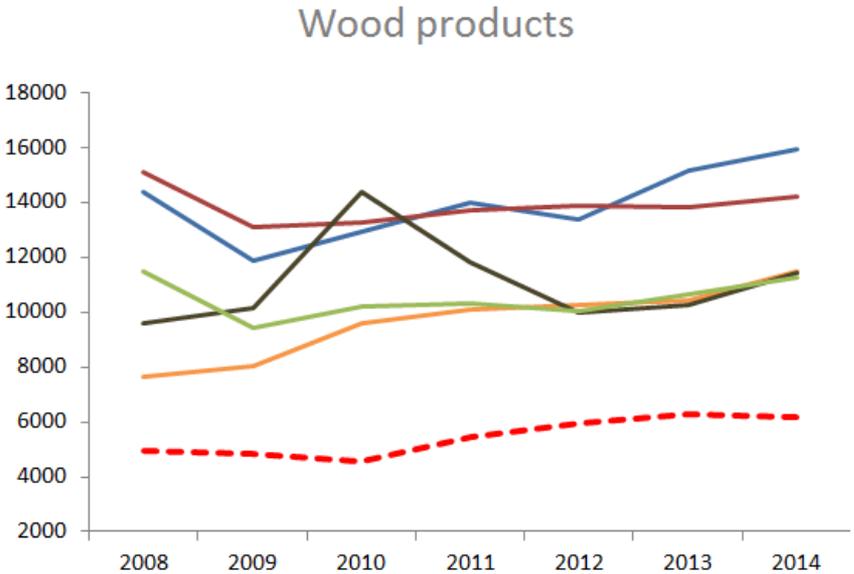
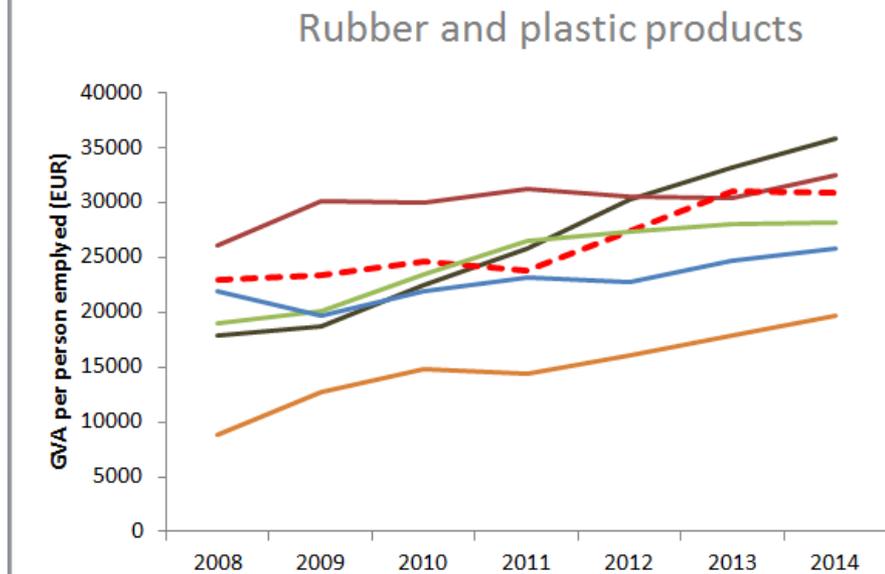
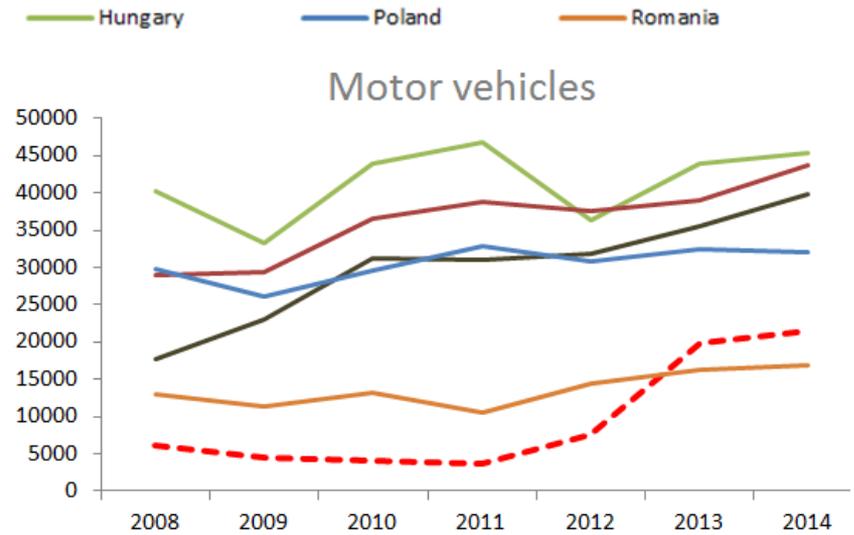
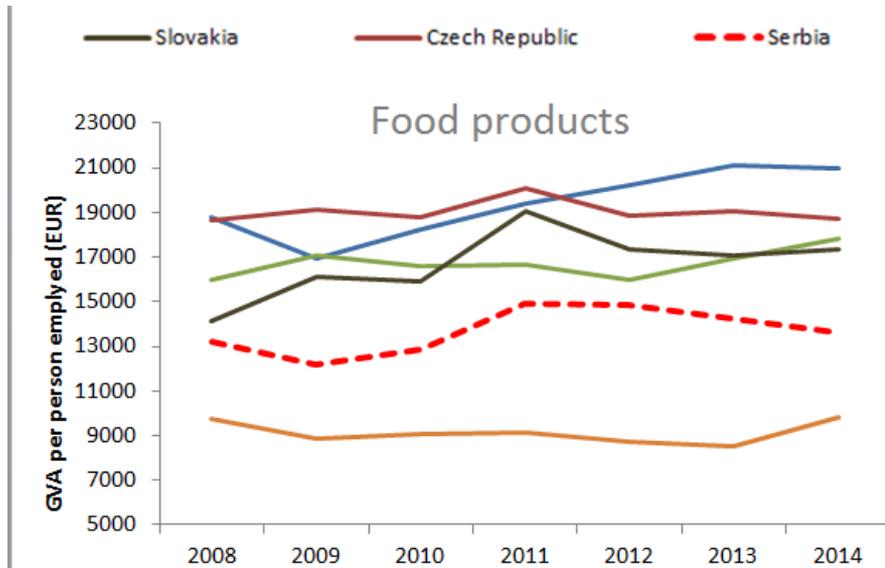
## 2. Setting the scene

Manufacturing sectors by value added and employment, 2014



# 2. Setting the scene

## Value added per person employed



# 3. Productivity and country competitiveness

- ❖ The concept of competitiveness lacks a universally-accepted definition
- ❖ However, there is broad consensus on its **relation to productivity and the maximisation of value added**
- ❖ **Productivity** relates to how firms combine productive factors and apply technological progress to maximise value added production
- ❖ **Country competitiveness**: differences in productivity levels and trends relative to countries with similar productive composition and operating in the same markets, including the domestic one



# 4. Internal and external factors of productivity

- ❖ There are two levels of productivity
  - ❖ Firm/Factory level
  - ❖ External factors of competitiveness
- ❖ Governments have strong influence on the external factors (e.g. business environment, taxation, competition policies, etc.), while more limited influence on the internal factors
- ❖ **Governments can design framework policies allowing productive firms to thrive:**
  - ❖ Anti-competitive product market regulations
  - ❖ Mechanisms to insure workers against labour market risks
  - ❖ Bankruptcy legislation and judicial efficiency
  - ❖ Risk capital markets
- ❖ **At the firm level, governments can develop proactive policies**, targeted at the segment of companies which are capable of doing so, to reach economies of scope and scale to compete internally and externally



# 4. Internal and external factors of productivity

- ❖ **Large MNEs** dispose of managerial capacities, access to factors of production, capital and more effective organisational systems, maximising internal production systems and benefitting from economies of scope and scale
  - ❖ Government has a role to provide good framework conditions
  - ❖ Limited scope for direct government intervention
- ❖ **SMEs** do not dispose of managerial capacities and access to factors of production
  - ❖ The provision of good framework conditions is fundamental, but not sufficient
  - ❖ Government can help enterprises with growth potential to reach economies of scale and scope



# 5. Policy implications for Serbia

- ❖ Serbia would need to continue to strengthen framework conditions, as well as support SMEs, especially in some sectors, to diversify the economy and create the basis for endogenous growth
  - ❖ **Proactive FDI policy**, including investment promotion and improving the framework conditions,
  - ❖ **Proactive SME policy** with industrial policy element targeted to support SMEs with potential
    - ❖ Relevant SME policies have been adopted by Serbia, but not without issues (e.g. institutional instability and insufficient resources), making targeted SME policies even more necessary



# 6. The downsides of industrial policy

- ❖ Governments often **lack the information and capability** to design effective industrial policies, inviting rent-seeking behaviour from economic agents.
- ❖ Successful implementation of industrial policy will depend on the **nature of the political system and institutions** in the country concerned
- ❖ **Governments could tend to support industries in decline** with the objective to safeguard employment or on the grounds that other governments support the same industries

As a consequence:

- ❖ Governments are not easily able to pick winners but are better placed to act as **facilitators** to enable closer co-ordination between individual economic agents and to allow for experimentation in the economy



# 7. Competitiveness and the European integration process

- ❖ Closely connected to EU market, but not IN, and suffering from competition with countries such as Bulgaria and Romania
  - ❖ Higher transaction costs
  - ❖ Penalisation from potential uncertainties
- ❖ The best way to mitigate these issues is for Serbia to **approximate to EU policies in an irreversible way**
  - ❖ Competition policy
  - ❖ Access to production factors
  - ❖ Legal framework law enforcement and efficiency of the judiciary system
  - ❖ Regulatory policy



# 8. How the OECD can support Serbia

- ❖ Competitiveness in South East Europe: A Policy Outlook
- ❖ SME Policy Index: Western Balkans and Turkey 2016
- ❖ Beyond Industrial Policy: Emerging Issues and New Trends
- ❖ Evaluation of Industrial Policy: Methodological Issues and Policy Lessons
- ❖ Enabling the Next Production Revolution: the Future of Manufacturing and Services



**Thank you for your attention!**

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