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EFFECTS OF THE PROCESS OF DEINDUSTRIALISATION AND THE CONCEPT OF A REINDUSTRIALISATION STRATEGY OF SERBIA

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1. INTRODUCTION

For decades, Serbia like the other ex-planned economies, had been realizing a development strategy based on the process of industrialization. Industry had an important role within the national economy regarding its contribution to GDP formation, its share in total employment and international trade. However, the economic crisis during the 1990s, combined with a neo-liberal concept of development during the transition period since 2000, has resulted in a very low level of development of domestic industry.

In the most advanced Central and Eastern European countries, after the so - called transition drop in the first years of market reforms, industrial production has recovered and doubled during the last two decades. At the same time, industrial production in Serbia is still 40-70% less than at the end of 1980s, when the maximal level was reached; and even some industrial branches have completely collapsed. The trend of deindustrialization is reflected in the reduction of total industrial output, a drop in industrial employment, decrease in export of industrial products with negative impact to the international trade balance, as well as in a drastic decline in the contribution of industry to GDP formation. These negative tendencies were even exacerbated during prolonged global economic crisis.

Reindustrialization can be seen as a vehicle for both: overcoming the current economic crisis and, at the same time, sustainable economic development. Reindustrialization as a process includes two lines of activities: the first one is related to existing companies and their restructuring in order to make them competitive on the global market; and the second one is related to newly- established companies, with the idea of creating new jobs.

The aim of this paper is threefold: firstly, to analyze the process of deindustrialization in Serbia, its causes and consequences in a wider context of deindustrialization in transitory economies; secondly, to examine the existing level of industrial development; and thirdly, to review current development documents, both Serbian and European, in order to find suitable elements for Serbia's potential strategy of reindustrialization.

2. THE PROCESS OF DEINDUSTRIALIZATION

Countries of Eastern and Central Europe, for several decades, had been practicing an industrial-led kind of development strategy. It was part of the socialist experiment, in which the role of the state was very important.

Domestic savings were transferred into investments, mainly into industrial capacities, on the basis of a centralized decision-making process, in which central planning was the key for distribution. Although, as part of former SFRY Serbia was somewhat a different case given the specific mix of market - plan economy, regarding industrialization as a key vehicle for development it was not an exemption. As a result, those countries for several decades had a high rate of GDP growth (Table 1), with a high share of industry in GDP formation and high share of industry in total employment. Those high rates of growth were related to an extensive sort of development, with low productivity of companies, as they were neither efficient nor profit-oriented. In the specific international alliance of socialist countries, COMECON - the Council for Mutual Economic Assistance, there was a kind of specialization between countries and companies, without the intention of being competitive on the global market.

Table 1 Industrial output (increase p.a. - %)

Period	World	Socialist country	Developed country	Low-developed country
1961-1985	5.1	6.9	3.9	4.6
1971-1985	4.2	6.6	2.7	3.1
1981-1985	3.2	5.5	1.8	-0.5

Source: Vukmirica V. 1988 - Capital and Socialism, Belgrade, p.58

During the 1980s, socialist countries were faced with limits of growth (Table 2). The fall of the Berlin wall was, at the same time, the start of market-oriented reforms in these countries. As a widely-accepted proposal for reforms, the so - called Washington consensus (Bukvić, 2011), a mix of privatization, liberalization and stabilization was realized (Williamson, 1990). The important point of this set of measures was their speed, the so - called shock therapy, in order to make reforms irreversible.

Table 2 Industrial Output 1990-2002 average %

Country	%	Country	%
Albania	2.5	FIROM	-2.1
Belorussia	-0.7	Moldova	-9.5
Bulgaria	-3.3	Poland	5.8
Croatia	-1.0	Romania	0.3
Czech	-0.3	Russia	-4.5
Estonia	-0.7	Slovakia	-3.4
Hungary	3.9	Slovenia	4.7
Kazakhstan	-5.4	Ukraine	-7.9
Leetonia	-5.1	Uzbekistan	-2.1
Lithuania	4.2	China	12.6

Source: World bank, World Development Indicator 2004, p.182-184

All former socialist countries were faced with a transitional drop during the first phase of the reform process (Table 2); the industry being particularly hampered (Božić, 2009).

The transitional gap was widely explained by international financial institutions and other advocates as a consequence of the mistakes in the macroeconomic policies introduced; unreadiness for market reforms; the lack of some necessary reforming steps; limits of political system, etc. However, especially on the basis of bad reforming results in Russia, during the second half of the 1990s, the shock therapy was abandoned in favor of the so - called gradualist approach. This new model argued in favor of gradual reforms, the importance of institutional and legal frameworks and minimal social costs of reforms (Stiglitz, 1999, Nellis, 1999, Fisher and Sahay, 2000).

The transitional gap was inevitable and understandable. During the first transitional phase, domestic industry was suffering because of the lack of domestic demand for its products resulting from a decreasing standard of living, problems of other industries and demand of imported products available at the time. Domestic industry was not subsidized any more, especially its export. Industrial companies were also subjects of complex restructuring, including privatization, layoffs of surplus labor. As a result, the importance of industry was declining within national economies; its share in GDP formation and in total employment was decreasing. In newer, more difficult circumstances for international trade weak industrial companies could not compete with the more efficient ones from developed countries, and consequently export was decreasing with inevitable balance of payments problems.

During the second transitional phase, recovery started (Table 3) after a decade of transition. However, one can see that among transitory countries there are differences- between those advanced transitory economies, which have succeeded in transforming their economies to more efficient and even competitive ones on the global market, and the rest of the ex – socialist countries, which were not so successful in market reforms and restructuring.

Table 3 GDP increase p.a. (%)

	1990 -2000	01	02	03	04	05	06	07	08	09	10	11	2012
World	2.3	1.4	1.7	2.6	3.8	4.5	5.2	5.4	2.8	-0.6	5.3	3.9	3.5
Developed c.	2.4	1.0	1.2	2.0	3.2	2.6	3.0	2.8	0	-3.6	3.2	1.6	1.4
- EU	2.1	1.7	1.0	0.7	2.0	2.2	3.6	3.4	0.5	-4.2	2.0	1.6	0
Transition c.	-2.5	4.5	3.9	5.9	5.9	5.9	6.4	5.4	3.2	-3.6	4.5	5.3	1.9
LDC	4.9	2.4	3.5	4.5	5.8	7.3	8.2	8.7	6.0	2.8	7.5	6.2	5.7

Source: UNCTAD, Trade and Development Report 2004, p.4, World Bank, Data basis

3. DEINDUSTRIALIZATION IN SERBIA

Serbia, as part of the former SFRY, introduced a specific mix of market – plan in the post-war era, but was similar to other socialist countries in regard to industrialization as a vehicle for fast development. The difference was the fact that in SFRY (Serbia) industrialization was not always in favor of producing means of production, machinery and other means for production (heavy industry). This was the case until 1957, but after that industrialization was in favor of products for consumption (light industry).

As the result of the process of intensive industrialization in Serbia, the share of industry in GDP formation was more than 40% from early 1960s and stayed very high for more than three decades (Republic Statistical office). The share of industrial employment in total employment was also very high. Regarding international trade, former SFRY was specific among socialist countries, as its export and import volume was oriented similarly to both developed countries and Eastern European socialist countries.

During the 1990s, Serbia was faced with a deep economic crisis and its GDP dropped more than 50% due to: 1) the break-up of the single market of former SFRY, 2) the sanctions introduced by the International Community, including international trade and 3) direct damages during the bombing campaign in 1999. During this period, the main exporting companies were hampered, such as the traditional exporters: furniture, textile, leather and footwear manufacturers; while food industry and energy sector suffered minimally. The drop in GDP and industrial output during the 1990s (or their very low starting points) are the reasons why after the beginning of market reform in the late 2000 Serbia was not faced with the so - called transitional gap. On the contrary, due to low level of GDP (GDP p.c. was 1,100 USD prior to the reforms) during transition period until the world economic crisis (2001-08) the Serbian average rate of GDP growth was 5.4% (Graph 1). However, one has to see that GDP is still bellow maximal level, reached at the end of the 1980s (75% of its maximal level, while FYROM is on 100%, Montenegro 90%, Croatia 110% and Slovenia 156%).

One has to be aware that this growth was unequal for different sectors: while services had more than average rate of growth, industrial growth was below average (2% on average in the period 2001-08). In GDP formation industrial contribution is now 1/5, agriculture 1/10; while services have more than 50%. More importantly, industrial share in GDP decreased during the transition period (Table 4, 5) (Stevanović et al, 2008, Mičić & Zeremski, 2011). To conclude, Serbia is facing the process of deindustrialization during transition.

The share of industrial employment is similar (1/5) in total employment, with the same declining tendency (Table 6). During the 1990s, labor surpluses within industrial companies increased due to governmental social policies, which abandoned layoffs, except when they were really necessary. So in the restructuring process, more people lost their

job, while the development of private small and medium companies¹ was not fast enough to absorb increasing unemployment.

Graph 1 Serbia – BDP and Industrial output increase p.a. (%)

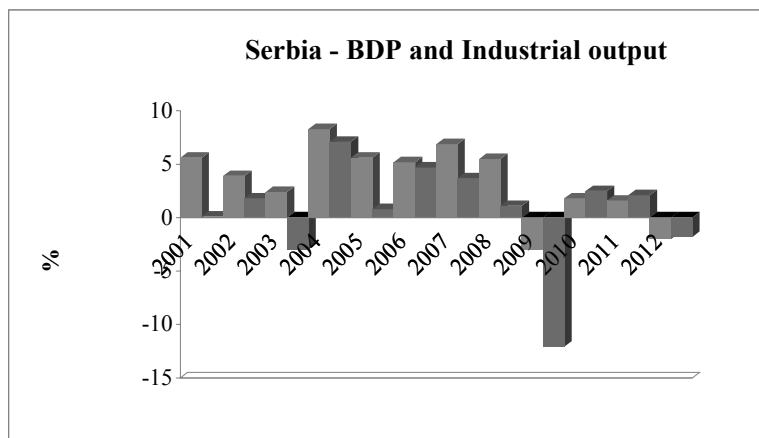


Table 4 Industrial output increase p.a. (%)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
EU-27	0,1	-0,5	0,4	2,4	1,3	4,2	3,6	-1,8	-13,8	6,8	3,2
Slovenia	3,6	2,2	1,0	3,7	4,6	6,3	7,4	1,6	-17,6	6,0	2,8
Slovakia	3,6	7,4	15,3	3,6	1,0	15,7	16,9	3,1	-13,7	18,3	7,2
Poland	1,4	1,5	8,6	11,8	4,4	12,2	9,5	2,0	-3,6	10,8	7,2
Hungary	4,0	3,2	6,6	6,9	7,3	10,6	8,0	-1,0	-17,4	10,3	5,5
Czech	7,6	4,0	1,6	9,7	4,3	8,7	10,6	-2,4	-13,1	9,8	6,4
Romania	3,8	-0,4	-0,7	1,9	-2,7	9,8	10,1	2,6	-5,9	5,5	6,0
Bulgaria	2,0	4,9	12,9	12,6	7,2	6,2	9,5	0,4	-18,2	2,0	5,8
Croatia	6,4	4,9	3,3	2,5	5,0	4,3	5,0	0,7	-8,9	-1,5	-1,2
Serbia	0,1	1,7	-3,0	7,1	0,8	4,7	3,7	1,1	-12,1	2,1	-3,4

Source: EUROSTAT, Republican Statistical Office RS

Table 5 Industrial share in GDP (%)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Slovenia	30,1	29,6	25,3	24,7	24,0	23,8	23,4	22,8	23,1	24,6
Slovakia	25,2	23,5	25,9	27,1	26,4	28,2	27,9	27,0	25,8	25,9
Poland	27,0	26,5	29,2	30,8	30,7	31,3	26,3	25,4	24,3	24,5
Hungary	26,9	26,2	25,6	25,8	25,9	26,0	25,5	25,1	25,5	27,2
Czech	37,5	27,5	38,2	40,2	40,4	36,2	28,7	38,7	29,2	29,3
Romania	28,2	28,4	25,0	24,7	24,6	24,3	24,4	22,9	27	29
Bulgaria	25,2	25,6	20,6	26,0	26,1	24,1	24,1	-	22,1	23,1
Croatia	20,4	19,4	18,0	18,2	17,9	17,7	17,6	17,5	18,4	19
Serbia	21,6	21,2	19,9	19,6	18,7	18,7	17,2	17,3	19,6	21,4

Source: EUROSTAT, Republican Statistical Office RS

¹ Unemployment started decreasing again from 2006 (Statistical office of RS).

The industrial share in international trade is very low, as there are a few tradable products for export. Prior to the 1990s, industrial production in Serbia had a high share of energy, food and raw materials in total production, and obviously was not competitive abroad. During the 1990s, this industrial structure deteriorated even further, as food and energy production had minimal decrease in comparison to other. In the period of transition, a lot of companies that had been traditional exporters were closed. Serbia, during the last decade, had exported fewer products, with low technological level and high contribution of human labor. Serbian trade deficit increased and reached maximal level of 8 billion USD in 2008.

Table 6 Serbia - Employment Structure %

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Agriculture	19,6	20,9	20,6	23,9	23,2	20,4	20,7	25,0	23,9	22,2	21,2
Industry	33,5	31,4	29,6	27,4	25,9	24,4	23,0	22,0	25,2	26,0	26,9
Services	46,9	47,7	49,8	48,7	50,8	55,2	56,3	53,0	50,9	51,8	51,9

Source: Republican Statistical Office RS

If we analyze the causes of the deindustrialization process, we can see that they are: the break-up of the single market of former SFRY; privatization process with restructuring of companies, which includes inevitable layoffs of labor surpluses; liberalization of internal market and international trade; low level of FDI (foreign direct investments), mainly brownfield investments through privatization of companies and banks; low level of domestic savings, and the lack of industrial policy.

The consequences of deindustrialization can be summarized as follows: non-sustainable development process, high level of unemployment, high international trade deficit and balance of payments problems (Adžić, 2010). Those problems after the beginning of the global economic crisis have only further exacerbated. Industrial companies, being less flexible than those in the service sector, were hampered even more during the crisis and could not easily adjust to the difficult circumstances on the global market and weaker foreign demand. So, the decline in industrial production was deeper than in the other sectors (Table 6).

4. EUROPEAN REINDUSTRIALIZATION STRATEGY

Institutional arrangements, such as economic restructuring, have contributed to global deindustrialization. The impacts of the global crisis in Europe are reflected in the further deindustrialization - 3 million industrial jobs have been lost since 2008; industrial production is 10% lower than prior to the crisis; decline in manufacturing and competitiveness, etc. (EC, 2012).

The European Commission launched a new strategy to reindustrialize Europe, with an aim of creating new jobs. Reindustrialization of Europe is based on the “green way” and

challenges of climate change. The European Commissioner for Industry and Entrepreneurship (Antonio Tajani) urges that “Europe must reindustrialize for the 21st Century” because a “strong industrial base is vital to a prosperous and economically successful Europe. The plan includes “pillars” in order to “restore the attractiveness of Europe as a production location”, which are: 1) Increased investments in factories and research and development, 2) expansion of the internal market and “the opening of international markets”, 3) “open access to international markets” for companies, especially SMEs, through new trading arrangements, 4) education and training, and better matching of supply and demand for labor. In a new European industrial strategy, published in October 2012, the EC proposed an increase of the manufacturing sector of up to 20% of GDP, a return of factories to Europe, with arguments for reversing the trend of off-shoring. Europe should ride the new industrial revolution by heavily investing in innovative, clean sectors. According to a strategy on industrial policy of EU- European Commission has re-discovered industry as a source of wealth creation (“back to the roots”) and, in the same time, has given unconditional priority to the EU’s climate targets. The share of industry in the EU’s GDP should increase to 20% by 2020 (in 2012 15.6%). The strategic goal of European green economy is to link energy policy with climate policy and industrial policy. This implies high costs for companies as a result of climate policies, carbon regulation and rising energy prices. Consequently, business representatives in EU pointed out that it is a signal of small revolution, because the reindustrialization of Europe and reduction of greenhouse gases, the share of renewable energy, are contradictory (*Die Welt*, 2012). In accordance with the *Lisbon calls for EU reindustrialization*, 2012, reindustrialization was proposed to the EU Competitiveness Council, especially because of corporate relocation and loss of EU jobs.

According to the document *Mission Growth: Europe at the Lead of the New Industrial Revolution*, 2012, Europe’s economy cannot survive in a sustainable way without a strong and profoundly reshaped industrial base. In accordance with the opinion of the European Commission, the key pillars of the reinforced industrial policy of EU are: 1) Investments in innovation; 2) Better market conditions; 3) Access to finance and capitals and 4) Human capital and skills.

5. NEW EUROPEAN INDUSTRIAL POLICY

Those who advocate planning and modern industrial policy emphasize that the main reason for industrial policy definition and implementation is frequent and severe malfunctioning of the market mechanisms (Vujošević, M. at all. 2012). Rapid weakening of EU’s competition abilities forced the EU leaders to perform a deep analysis of the causes and then to propose lines of necessary changes. The analyses have pointed out that the EU have made a crucial mistake “...when its goal was not to preserve strong industry (manufacturing), but to base its economy on the services, which was the widely accepted (liberal) approach”. Faced with stronger US and Chinese competitiveness, the EU

concluded that new solutions have to be found for preserving industry and industrial policy on EU level, which resulted in the *Lisbon strategy 2000*, with several revisions including an updated version, the so-called *The Europe 2020*.

Global evolution of competition in the future (from low-cost competition toward innovation-based competition) is very important for the approach in creating the reindustrialization policy (see Table 7).

Table 7 Global evolution of competition

Low-cost competition	Innovation-based competition
Gains advantage from low cost of resources and labour	Gains advantage from creating a unique market position
Focus on greater volumes and low prices	Focus on new products and processes
Imports and copies technology	Develops world-class technology
Follow trends	Sets trends

Source: Twigge-Molecey C., 2012

In the Strategy “*Europe 2020*” a process of implementing reforms through knowledge and innovation-led growth is seen as crucial in the attempt to overcome the current economic crisis and to make European economies competitive on the global market. Reforms would be implemented in the aim to increase quality in the education process, and enable easy access to results of research and development (R&D) and transfer of R&D to all interested parties. The original plan was to transform Europe into a „knowledge-based economy”. Supporters of reindustrialization argue that manufacturing is the key for creating jobs. The aim of the reforms is also to achieve sustainable development, which includes the establishment and development of a resources efficient, self - sustained and competitive economy. In order to do so, national economies ought to improve their business climate; stimulate the creation of the so - called green businesses and modernize their industrial basis. These reforms mean at the same time an inclusive growth, which means the development of a coherent society in which people are encouraged to predict and manage changes.

EU legal environment and development policies are structured in a way to secure a long-term policy goal – development of low carbon dioxide, green and resources efficient EU. The *EU Climate and Energy Package* (EC, 2009), similar to the *EU Efficiency Action Plan* (EC, 2011), quantified this specific target to achieve the share of 20% of new and renewable sources in total energy production until 2020. Low carbon dioxide economy promotion and process of decarbonisation of economic activities is closely related to the question of climate change and neutralization of the negative influences of human activities.

In accordance with the *Council recommendation of EC on broad guidelines for the economic policies of the EU of The Europe 2020* (Guidelines 6), which are related to improvement in business and consumer climate and industrial basis modernization, there

are recommendations for EU members to support modern, diversified, competitive, resources and energy efficient industrial (manufacturing) basis, especially easy restructuring completely in line with EU competitive rules.

In the reindustrialization of Europe, the next Kondratiev wave is going to be hi-tech and low carbon. Europe has a strong interest to minimize the competitive threat of China's green industrial policy. This means embracing green growth, reinvesting and reindustrializing towards a low carbon future.

If one wanted to summarize the targets of EU industrial policy, then they are as follows: Firstly, to establish predictable legal environment for efficient industrial functioning; Secondly, to secure necessary conditions for industrial development, taking into account that industry is the crucial activity for improving competitive potentials, like technology access, managerial skills, educated human sources, entrepreneurship and financial sources; Thirdly, to establish a framework, institutions and instruments, necessary for business environment, which are efficient and capable to react in due time in line with the defined policy goal.

The Lisbon Revised report (2004, 2010) recommended actions in two areas to set Europe on a path towards greater and more sustainable growth: 1) injecting new impetus into the stalled Lisbon process and 2) broadening the Lisbon agenda to new challenges.

The European capacity for knowledge-based growth, already an important element of the Lisbon agenda, should be vastly expanded by accelerating the development of information technologies across the EU and their application within the workplace.

According to the EC, 2003, general principles of industrial policy are competitiveness, long-term sustainable growth, non-discrimination, subsidiarity, transparency and facilitating cross-border allocation of regional cooperation, the unique rules of regulation, complementarity, cooperation and networking, the principle of competitive procurement, the principles of state aid, prohibitions, control, and consumer protection.

6. ELEMENTS OF A POSSIBLE REINDUSTRIALIZATION STRATEGY

In the cycle of industrial policies, it can be assumed that after a phase of regression and disintegration, we can expect the progressive stages of reintegration and recovery. There is obvious danger of further hesitation or delay in implementation of new industrial policy solutions (lat. *periculum in mora*). On the basis of the proposed EU policy of reindustrialization one can define the targets in the process of adjustment and harmonization of Serbian industrial policy. It is important to bear in mind that we are facing complex problems today, like EU policy makers, and at the same time, long - term accumulated problems of the non - efficient Serbian industrial policy. One of the key

issues is the adoption and harmonization of Serbia's new industrial policy with the EU industrial policy (Lisbon revisited, 2004, 2010, Savić and Zeković, 2004) based on the principles of competitiveness and sustainability.

Strategy and Policy of Industrial Development of Serbia in the period 2011-2020, 2011, is the first document which defines development priorities. It is also harmonized with EU industrial policy and the *Strategy EU 2020*. The industrial policy is oriented toward export competitiveness of industrial products and emphasizes the importance of structural reforms. According to the document, the restructuring process will be realized through phases such as: 1) revitalization and recovery, 2) restructuring and reengineering and 3) development and competitiveness. Industrial development should be based on investments into new technology, innovations and human capital. Industrial policy should be proactive, oriented toward export competitiveness of industrial products and services with high value added, based on knowledge, innovations and R&D.

Opting for reindustrialization in Serbia has its foundations in the fact that the industry is an activity that can ensure the achievement of key development aims – growth of employment, growth of competitiveness, export, attracting new investments, applying technical progress, the creation of new SMEs. To summarize long - term priorities of industrial policy the following are important: implementation of reindustrialization strategy; harmonization with EU industrial policy; refocusing national industrial priorities, and shortening technological cycles and supporting different sectors on the global market. At the same time, short - term priorities are: growth of industrial competition; establishment of “the role of game” in competition; establishment of proper conditions for new companies and improvement of existing ones; speeding up restructuring and privatization of public companies; restructuring in steel industry, non - ferrous manufacturing and processing industry, and efficient environmental policies.

Industrial policy goals would be achievable and in line with the overall socio – economic development: 1) Strengthening competition, productivity and export growth, 2) Industrial restructuring on the basis of implementation of knowledge-based economy and sustainable development, 3) Improvement of institutional and legal framework and business climate, 4) Employment growth, 5) Harmonized territorial development, 6) Low carbon dioxide activities (in line with climate change requirements), 7) Development of business, innovation and industrial infrastructure (industrial zones, industrial parks, clusters, etc.).

From the territorial point of view industrial policy should be in line with two types of territorial development: 1) Concept of competitive territorial distribution and 2) Concept of cohesive territorial distribution, in accordance with a new regional policy of industrial innovations (Zeković, 2010).

7. CONCLUSION

Countries in transition during the first phase of market reforms faced decline in industrial production and GDP. Serbia avoided this decline, but similarly to the other countries of CE Europe suffered because of the process of deindustrialization, which resulted in high unemployment and balance of payments problems. All those problems became severe during a prolonged global economic crisis. In order to overcome the current crisis, Serbia would use reindustrialization as a vehicle. EU formulated the *Strategy EU 2020*, which recovered reindustrialization as a key to exiting the crisis and improving its global competitiveness. The Serbia's solution has to be similar. It is important to note that reindustrialization is an urgent matter, as Serbia's development problems are very complex, as well as its limitations, including low level of knowledge and practice of strategic planning, management, implementation, evaluation and monitoring.

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SUMMARY

Countries of Eastern and Central Europe have introduced market reform on the basis of the so - called shock therapy, with inevitable transitory drop in GDP, standard of living and industrial production. Those most advanced economies, after more than a decade of restructuring process, have succeeded in becoming competitive on the global market. Serbia was also facing problems with deindustrialization when it started late with market reforms, although the drop was not so deep because the previous economic crisis during the 1990s had already hampered the national economy. Deindustrialization caused problems such as increasing unemployment, balance of payment deficit and finally non-sustainable development, which became more serious during the global crisis. The collapse of industrial development is the "Achilles heel" of the Serbian economy. So, reindustrialization is seen as a vehicle for overcoming the crisis and, at the same time, for creating sustainable development. It is also the key to the recovery of the national economy, to improving its competitiveness and creating dynamic, sustainable and inclusive economic growth, together with increasing employment and standard of living.