SUBSIDIES AND STRUCTURAL TRANSFORMATION IN SERBIA: IS A PARADIGM SHIFT IN INDUSTRIAL POLICY WARRANTED?

Marija Marčetić, Bojan Kocić, Jovana Anđelković

Toplica Academy of Applied studies, Ćirila i Metodija 1, 18 400 Prokuplje, Serbia, neimar.marija@gmail.com, bojan.kocic@yahoo.com, jovana.andjelkovic@vpskp.edu.rs

PRELIMINARY REPORT/SHORT COMMUNICATION

Received: 23 July 2026.
Accepted: 26 October 2026.
Published: 15 November 2026.
DOI: https://doi.org/10.63395/STEDConf15022026156M177

Corresponding Author: Jovana Anđelković, Toplica Academy of Applied studies, Ćirila i Metodija 1, 18 400 Prokuplje, Serbia, jovana.andjelkovic@vpskp.edu.rs

Copyright © 2026 Jovana Anđelković et al., published by UNIVERSITY PIM. This work licensed under the Creative Commons Attribution-NonCommercial-NoDerivs 4.

Citation: Anđelković, J. et al., (2026). Subsidies and Structural Transformation in Serbia: Is a Paradigm Shift in Industrial Policy Warranted? In Kojić, D. & Sredić. D. (eds.) *Conference proceedings, International Conference on Social and Technological Development: STED 2026* (pp. 177-183). Trebinje, B&H: University PIM.

ABSTRACT

This paper analyzes the impact of Serbia's subsidization policy during 2015–2025 on the structural transformation of the economy. Subsidies in Serbia have been widely used as tools of industrial and fiscal policy aimed at increasing employment, attracting foreign direct investment and supporting domestic sectors. Integrating industrial policy theory, political economy and structural transformation frameworks, the study evaluates whether the current subsidization model has led to a shift toward high-productivity, technologically advanced sectors, or merely sustained a low-cost, investment-dependent growth pattern. The analysis indicates that subsidies have produced short-term gains in employment and investment but have not significantly enhanced long-term productivity or structural change. Additionally, the fiscal burden of subsidies remains considerable, and institutional mechanisms lack transparency and systematic impact evaluation. The paper concludes that reform of the subsidization model is warranted — toward productivity-linked, innovation-oriented support that fosters domestic value chains. Policy recommendations include shifting from employment-based subsidies to productivity-conditioned instruments, instituting rigorous ex-post evaluations, and strengthening domestic supplier networks.

Keywords: subsidies, industrial policy, structural transformation, fiscal policy, FDI, development strategy

INTRODUCTION

Subsidies are among the most important—and most controversial—instruments of economic policy in contemporary states, particularly in transition economies such as Serbia. Between 2015 and 2025, Serbia intensified support for economic activity through direct financial incentives, tax relief and measures designed to attract foreign direct investment (FDI). The central issue is

whether this policy facilitated a transition towards high-productivity and technologically advanced activities or merely sustained a growth model based on low labour costs and externally financed investment.

The arrangement agreed with the International Monetary Fund (IMF) in 2024 placed particular emphasis on macroeconomic stability, fiscal discipline and reforms supportive of sustainable growth. Under the subsequent Policy Coordination Instrument, Serbia committed to keeping the fiscal deficit at no more than 3 per cent of GDP during 2025–2027, while preserving priority expenditure, including public investment [1]. Although the arrangement does not call for the abolition of subsidies, it strengthens the case for assessing whether individual measures generate sufficient economic and social returns. Expenditure that does not improve productivity must be weighed against investment in infrastructure, education and innovation.

Available evidence also requires careful interpretation. State aid includes not only direct subsidies but also tax incentives and other support measures. Lutovac Đaković and Anić report that state aid in Serbia was generally higher relative to GDP than in the European Union during the period preceding the pandemic and increased sharply in 2020. By comparison, state aid in the EU rose from 0.92 per cent of GDP in 2019 to 2.36 per cent in 2020 and subsequently declined to approximately 1.1 per cent in 2023 [2]. These figures demonstrate both the exceptional effect of crisis support and the need to distinguish total state aid from direct budget subsidies.

This paper therefore asks whether Serbia's subsidy system during 2015–2025 produced substantive structural transformation and whether the existing model should be changed. The analysis brings together industrial-policy theory, political-economy arguments, academic studies and selected policy and budget documents. It is primarily qualitative and interpretative; it does not claim to identify the causal effect of subsidies through an original econometric model. The working proposition is that employment- and investment-based incentives can produce short-term gains, but will not generate sustained productivity growth unless they are linked to technological upgrading, knowledge transfer, domestic supplier development and credible performance evaluation.

THEORETICAL FRAMEWORK

Subsidies and Industrial Policy

The literature commonly considers subsidies in two principal ways: as an instrument of industrial policy and as a potential source of market distortion. From the first perspective, selective support may be justified when it helps infant industries overcome coordination failures, acquire capabilities and move towards activities with higher productivity and competitiveness [3]. Modern industrial-policy theory nevertheless treats support as an experimental and disciplined process. Assistance should be conditional on observable performance, limited in duration and withdrawn when beneficiaries fail to meet agreed objectives [4].

The opposing view emphasises government failure. Selective assistance may direct resources away from their most productive use, encourage rent seeking and create a "picking winners" problem because public authorities cannot reliably identify firms that will become competitive [5]. Such risks are particularly pronounced in transition economies with weaker institutions, limited disclosure and insufficient ex-post scrutiny. The relevant policy choice is therefore not simply between intervention and non-intervention, but between poorly governed support and a transparent, conditional system capable of learning from both successful and unsuccessful measures.

The conceptual model used in this paper separates policy inputs, transmission mechanisms and final outcomes. Fiscal subsidies, tax incentives and other forms of state aid can influence FDI and employment directly. Their developmental value, however, depends on intermediate mechanisms - technology transfer, the acquisition of skills and the integration of domestic suppliers. Only when these mechanisms operate can short-term investment contribute to productivity, structural transformation and fiscal sustainability (Figure 1).

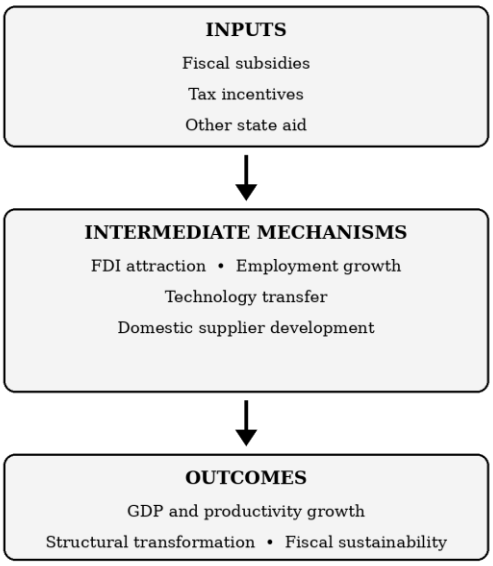


Figure 1. Conceptual framework of the study
Source: Authors' conceptualisation

The model implies an efficiency threshold. Where spillovers, domestic linkages and performance evaluation are absent, subsidies may stimulate investment and employment temporarily without changing the productive structure. In that situation, the fiscal burden can rise while the economy remains dependent on labour-intensive activities. A future quantitative study could test this proposition using sectoral productivity, export sophistication, domestic value added and the participation of Serbian firms in supplier networks.

Structural Transformation

Structural transformation denotes the reallocation of labour and capital from low-productivity activities to sectors with higher productivity and value added. It is a central condition of sustainable long-term growth and generally requires investment in research and development, human capital and technological upgrading. Relevant indicators include the technological composition of exports, domestic value added in production and the depth of local supplier networks.

Ćorović, Gligorijević and Manasijević find that Serbia achieved macroeconomic stabilisation and export growth during the first two decades of the twenty-first century, but that structural transformation remained incomplete because of weak productivity, low technological intensity and an insufficiently developed high-value-added sector [6]. Subsidies in transition economies may consequently serve both a stabilising purpose, by preserving employment, and a developmental purpose, by attracting capital. These objectives are not equivalent. Delević's municipal-level analysis shows that FDI incentives increased employment within subsidised firms but did not produce a statistically significant broader effect on local employment [7].

SUBSIDY POLICY IN SERBIA: A RETROSPECTIVE, 2015–2025

Scale and Structure of Subsidies

Serbian subsidies are distributed through several channels, ranging from agricultural payments and support for public enterprises to financial incentives for companies opening production facilities. Although it falls just outside the period examined, the 2026 budget illustrates the continuing scale of this policy: RSD 214.46 billion was planned for subsidies, with almost half allocated to agriculture [8]. The composition of expenditure therefore matters as much as its

aggregate value, because different instruments pursue different social, regional and industrial objectives.

A prominent feature of Serbian investment policy has been the use of substantial incentives to attract foreign investors. This approach can expand production and employment, yet it can also favour large firms and projects based on labour-cost advantages. Medić argues that the interaction of corporate taxation and subsidy policy has contributed to an uneven investment environment in which domestic private investment remains weak relative to FDI [9]. The relevant assessment should therefore consider not merely the number of supported projects and jobs, but their technological content, duration and links with domestic enterprises.

Effects on Economic Structure and Structural Transformation

Employment generated by subsidised FDI is an important benefit, especially in areas with limited job opportunities. However, project-level employment is not synonymous with structural transformation. When supported firms import most inputs, perform mainly assembly operations and create few links with domestic producers, the effect can remain confined to the beneficiary. Development then risks becoming locked into a peripheral structure instead of progressing towards diversified activities with higher value added. Hausmann and Rodrik emphasise that development requires learning about productive capabilities; policy should therefore reward discovery and capability building rather than the indefinite maintenance of existing activities [10].

The Serbian evidence points to limited spillovers. Delević finds a positive effect on employment in subsidised enterprises, but no corresponding increase in wider local employment [7]. This distinction suggests that the effect has been predominantly quantitative—the creation of supported jobs—rather than qualitative, through technology, productivity and supplier development. The policy problem is not that labour-intensive investment has no value, but that assistance based only on job numbers can preserve a low-cost assembly model unless it is accompanied by training, research collaboration, local procurement and measurable technological upgrading.

Fiscal Effects

From a public-finance perspective, subsidies are justified only when their long-term social return exceeds their direct and opportunity costs. If support does not create durable externalities, it becomes a recurring fiscal burden. The relatively high level of state aid identified by Lutovac Đaković and Anić reinforces the need for transparent selection criteria and systematic evaluation [2]. IMF fiscal commitments add a further constraint: within a deficit ceiling, poorly performing subsidies compete directly with public investment and other priority expenditure [1].

The distribution of incentives also affects domestic investment and regional development. Medić finds that subsidy and tax arrangements may disproportionately benefit large and foreign investors while failing to remove key barriers faced by domestic firms [9]. Uvalić and Bartlett likewise document persistent regional disparities in Serbia and stress the limited effectiveness of regional-development policy instruments [11]. Consequently, the fiscal assessment of subsidies should include additionality, cost per sustainable job, productivity effects, domestic procurement and regional spillovers—not merely the announced value of an investment.

Institutional and Political Framework

Institutional quality determines whether selective support corrects market failures or creates new distortions. In Serbia, detailed and comparable ex-post evaluations are not routinely available for every programme or project. This limits the ability of public authorities, researchers and citizens to determine whether promised employment, investment, training and technology-transfer obligations were fulfilled. It also increases the risk of rent seeking described in the government-failure literature [5].

A regional study by Petreski et al. identifies weaknesses in the transparency, targeting and monitoring of state aid across the Western Balkans [12]. For Serbia, reform should therefore

establish a public register with comparable project data, predefined performance indicators, counterfactual impact evaluation and recovery clauses where commitments are not met. Independent ex-post assessment should be incorporated into the policy cycle, and future assistance should reflect verified results rather than the continuation of established programmes by default.

Directions for Reform

The first direction of reform is to replace predominantly input-based conditions with outcome-based criteria. The amount of capital invested and the number of jobs announced are easy to observe, but they reveal little about the quality and durability of the supported activity. Eligibility and payment schedules should also reflect productivity growth, the share of skilled employment, certified training, research and development expenditure, export sophistication and the proportion of inputs purchased from competitive domestic suppliers. Indicators must be tailored to the sector, defined before support is granted and verified over a period extending beyond the minimum contractual term.

Second, the additionality of public support should be demonstrated. A subsidy creates value only if it induces investment, employment or technological upgrading that would not otherwise have occurred. This requires a documented assessment before approval and a credible counterfactual evaluation afterwards. Similar supported and unsupported firms, regions or projects can be compared where data permit. Results should be reported as ranges and accompanied by methodological limitations, since a simple comparison of outcomes before and after a grant may mistakenly attribute wider economic trends to the subsidy itself.

Third, policy should strengthen connections between foreign investors and the domestic economy without imposing inefficient local-content requirements. Supplier-development programmes can help Serbian small and medium-sized enterprises meet quality, certification, delivery and digitalisation standards demanded by multinational companies. Incentives may reward verified supplier mentoring, joint training, research partnerships and domestic procurement achieved through open and competitive processes. Such measures would convert the presence of foreign firms into an opportunity for capability formation instead of treating the initial investment as the final policy outcome.

Finally, governance safeguards should apply throughout the life cycle of support. Decisions should disclose the legal basis, selection criteria, expected benefits and maximum fiscal exposure, while protecting legitimately confidential commercial information. Contracts should contain proportionate clawback clauses, and evaluations should be published in a standard format that permits comparison across programmes and years. Periodic spending reviews can then redirect resources from measures with weak additionality towards innovation, skills, infrastructure and other public goods that benefit a wider group of firms.

Evaluation Framework and Limitations

A practical evaluation framework should distinguish relevance, efficiency, effectiveness, impact and sustainability, consistently with the established OECD/DAC evaluation criteria [13]. Relevance concerns whether an intervention addresses a demonstrated market or coordination failure. Efficiency compares verified results with the full fiscal cost, including tax expenditure and administrative costs. Effectiveness measures compliance with contractual objectives, while impact asks whether observed changes were caused by support rather than by macroeconomic conditions or firm characteristics. Sustainability examines whether employment, productivity and supplier relationships continue after the assistance expires. Treating these dimensions separately would prevent the number of announced jobs from becoming a substitute for a comprehensive assessment.

Data architecture is equally important. A unique project identifier should link the decision granting aid, the contract, budget execution, tax expenditure, employment records and subsequent monitoring. Aggregate reporting alone cannot reveal concentration among beneficiaries, repeated support, regional distribution or the difference between authorised and actually paid aid.

Publication in a reusable format would enable independent analysis while anonymisation and clearly defined exceptions could protect personal data and legitimate business secrets. Consistent time series would also permit comparison between instruments and reduce the risk that programme redesign obscures poor historical performance.

The sequencing of reform should reflect administrative capacity. Serbia could first standardise contracts, indicators and reporting across existing programmes; it could then pilot counterfactual evaluation in sectors with sufficient firm-level data; and finally integrate evaluation results into future budget decisions. Immediate termination of all incentives would create uncertainty and could weaken legitimate development projects. A gradual transition, announced in advance, would instead allow investors and domestic firms to adapt to stronger productivity, training and supplier-development requirements.

The conclusions of this paper are subject to limitations. State aid, direct subsidies, tax relief and investment incentives are related but not identical categories, and published sources do not always apply them consistently. The available studies also differ in period, unit of analysis and outcome variable, which restricts direct comparison. The paper therefore identifies patterns and institutional implications rather than estimating a single net effect for the entire subsidy system. Further research should combine beneficiary-level fiscal data with employment, productivity, trade and ownership records and should assess heterogeneous effects by sector, firm size, region and type of support.

CONCLUSION

The analysis indicates that Serbia's subsidy policy during 2015–2025 generated short-term benefits in employment and investment, but did not provide convincing evidence of a broad transition towards technologically intensive, high-productivity activities. The principal weakness is not the existence of subsidies as such, but a model that places substantial weight on investment and job counts while giving insufficient attention to productivity, technological spillovers, domestic value added and long-term fiscal returns.

A paradigm shift is therefore warranted. Support should be time-limited, transparent and conditional on measurable productivity gains, worker training, technology transfer and domestic supplier participation. Mandatory ex-post evaluation, publication of project-level outcomes and credible recovery mechanisms would improve accountability. These reforms would enable Serbia to retain useful investment incentives while redirecting public resources towards a more innovative, domestically integrated and fiscally sustainable development model.

DECLARATIONS OF INTEREST STATEMENT

The authors affirm that there are no conflicts of interest to declare in relation to the research presented in this paper.

LITERATURE

1. International Monetary Fund, Republic of Serbia: Fourth Review Under the Stand-By Arrangement, Cancellation of the Stand-By Arrangement, and Request for a 36-Month Policy Coordination Instrument, IMF Country Report No. 24/337, Washington, DC, 2024. doi: 10.5089/9798400295416.002.
2. Đaković, M. L., & Anić, A. (2025). Efficiency of State Incentives in Serbia's Industry: Impact on Investment and Employment. *Management: Journal of Sustainable Business and Management Solutions in Emerging Economies*, *30*(2), 27-34.
3. Chang, H. J. (2011, May). Industrial policy: Can we go beyond an unproductive confrontation. In *Annual World Bank conference on development economics* (pp. 83-109). Washington, DC: World Bank Group.
4. Rodrik, D. (2004). Industrial policy for the twenty-first century. Cambridge, MA: John F. Kennedy School of Government, Harvard University.

5. Krueger, A. O. (1990). Government failures in development. *Journal of Economic perspectives*, *4*(3), 9-23.
6. Ćorović, E., Gligorijević, Ž., & Manasijević, A. (2021). Structural changes and economic growth of the Republic of Serbia: The effects of applied structural adjustment models. *Ekonomika*, *67*(1), 1–16. doi: 10.5937/ekonomika2101001C.
7. Delevic, U. (2020). Employment and state incentives in transition economies: are subsidies for FDI ineffective? The case of Serbia. *Transnational Corporations*, *27*(2), 31–63. doi: 10.18356/a6f64950-en.
8. Republic of Serbia. (2025). Law on the Budget of the Republic of Serbia for 2026, Official Gazette of the Republic of Serbia, no. 108/2025.
9. Medić, P. (2025). Corporate Taxation and Subsidy Distortions as Barriers to Private Domestic Investment in Serbia. *Economic Analysis*, *58*(1), 152-172. doi: 10.28934/ea.1964.
10. Hausmann, R., & Rodrik, D. (2003). Economic development as self-discovery. *Journal of development Economics*, *72*(2), 603-633. doi: 10.1016/S0304-3878(03)00124-X.
11. Uvalić, M., & Bartlett, W. (2021*). Regional disparities and regional development policies in Serbia*. Belgrade: Friedrich-Ebert-Stiftung.
12. Petreski, M., Tumanoska, D., Kurta, A., OruÄ, N., KaluÄ‘eroviÄ, J., VukÄ eviÄ, I., ... & Elezi, G. (2024). *Empowering Western Balkans Economies: State Aid Incentives and Transparency in the Region* (No. 2024-12/54). Finance Think-Economic Research and Policy Institute.
13. OECD. (2021). *Applying Evaluation Criteria Thoughtfully*. Paris: OECD Publishing. doi: 10.1787/543e84ed-en.