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**SERBIA'S COMPETITIVENESS STRATEGY UNDER
MACRO-ECONOMIC REFORMS AND PRIVATISATION**

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Introduction

In the global and integrated world economy, competitiveness is a preoccupation of all countries, including the developed, developing as well as those in transition. To understand competitiveness means to understand the sources of prosperity. High income, strong national currency, and high return on investment result in a high standard of living.

In the industrial economy the cost level determines the competitive position and factor revenues and, through them, income per capita. A conventional view of the sources of competitiveness focuses on external factors of production such as natural resources, labour, and financial capital. This leads to cost leadership and subsequently to “comparative advantage”. In the information economy, the focus on competition is moved from external factors to internal factors such as knowledge and information. Globalisation and hyper-competition relativise the importance of the external sources of comparative advantage , creating conditions for rapid and sustainable productivity growth by using the internal sources of “competitive advantage”.

In order to capitalize knowledge and information, it is necessary to have a strategy. Strategy is a set of complex interactions between a company and its environment. Company strategy is based on distinctive (or core) competence. The major internal factors of distinctive competence are intangibles (non-material assets). The major external factors are the national strategy of competitiveness and the quality of business environment. Regardless of the focus, the recognisable results of the national strategy of competitiveness are regulations and institutions at the macro level and the industry clusters (7, p.19) and the value networks (5, p.3). at the mezzo level.

The main objective of this paper is to point out the necessity of Serbia’s competitiveness strategy formulation and implementation. In order to meet this objective, the analysis starts by measuring competitiveness by using various indexes. This is followed by an analysis of the factors affecting the competitiveness of Serbia as well as its position vis-a-vis other economies. The elaboration is followed by explanation of the methodology of formulation and implementation of the strategy of competitiveness. The paper ends with a brief conclusion relevant to strategy makers.

The Competitiveness Indexes

For over a quarter of a century, the World Economic Forum has been measuring global competitiveness. The 2004-2005 report (8) covers 104 countries representing over 97% of the world output. The World Economic Forum measures competitiveness by means of the Growth Competitiveness Index, Business Competitiveness Index, and Global Competitiveness Index.

The Growth Competitiveness Index consists of three pillars: (1) the quality of macro-economic environment, (2) the state of the country’s public institutions, and (3) the country’s technological readiness. Consequently, the Growth Competitiveness Index can be decomposed into three indexes: macro-economic environment index, public institution index, and technology index.

The Business Competitiveness Index concept is complementary to the Growth Competitiveness Index. This concept encompasses micro-economic fundamentals of prosperity. There is no doubt that macro-economic, political, legal and social conditions affect the economy's performance. It is well known that adequate monetary and fiscal policies and an efficient legal system and regulatory bodies significantly contribute to the soundness of the economy. The Business Competitiveness Index pays particular attention to corporate strategy and quality of business environment.

The inadequate level of entrepreneurial capacity is of particular importance to developing countries and countries in transition, since it leads to an negation of various positive stabilisation and/or monitoring programmes subordinated by international financial institutions. Privatisation and financial markets development, that enables access to the global capital market, leads to certain capital inflow, and creates an illusion of progress (short-term growth without long-term development).

The progress at the micro-economic level requires a specific business environment. According to M. Porter (9, p. 22), the business environment consists of four related factors: (1) specialised factors of production like human capital, infrastructure (physical, administrative, informative and scientific), and natural resources, (2) competitive context (intellectual property rights, open and vigorous competition and meritocratic incentive systems across institutions), (3) demand conditions (demanding local customers, evolution in the customers' behaviour, specialized market niches), and (4) related industries/supporting industries (local suppliers, industry clusters and similar). These constitute the well-known "Porter's diamond" factors of business environment.

Competitiveness depends on the level of economic development. Porter (9, pp. 33-34) classifies countries into three groups according to the economic development level by using GDP adjusted by PPP p.c.: (1) low-income countries, (2) medium-income countries, and (3) high-income countries. Low-income countries base their competitiveness on the abundance of natural resources and cheap labor. The low competitiveness level measured by the business competitiveness index is a result of inadequate infrastructure, access to capital, educational system, industry clusters as well as an extremely low innovation potential. Medium-income countries also rely on low costs, but these are a consequence of investments in the improvement of the existing technology. In addition to the improvement of the existing technology, these countries use brand development strategies, thus penetrating a larger number of stages in the value chain and development of own sales channels. These countries are also characterised by the efforts towards eliminating various social deviations (corruption, for example). High-income countries concentrate their efforts on technological innovations.

Serbia's Competitive Rating

Serbia is a part of the union state named Serbia and Montenegro. From both an external as well as internal perspective, it is a fragile state. According to international statistics, Serbia has three primary problems: (1) a trade deficit, (2) a relatively small privatised sector, and (3) a high level of indebtedness.

Trade deficit evolution in Serbia and Montenegro for the last four years provides a rough insight into competitiveness (see Figure 1). The trade deficit is growing year after year. At the end of 2004, it was about \$7 billion US dollars. An economy whose imports are valued as more than double its exports cannot be competitive.

Figure 1: Serbia and Montenegro balance of payments in billion US dollar

Description	2001	2002	2003	2004*
Current Transactions				
Goods exports	2.003	2.412	2.477	3.239
Service exports	0.740	0.809	0.100	0.129
Goods and service exports	2.743	3.221	3.484	4.531
Goods imports	4.837	6.320	7.324	9.418
Service imports	0.323	0.537	0.718	0.963
Goods and service imports	5.160	6.857	8.042	10.381
Goods balance	(2.834)	(3.908)	(7.077)	(6.179)
Service balance	0.417	0.272	0.289	0.329
Goods and service balance	(2.417)	(3.636)	(6.788)	(5.850)
Interests paid	0.740	0.158	0.219	0.248
Interests collected	0.480	0.620	0.690	0.600
Interest balance	(0.260)	(0.960)	(0.150)	(0.188)
Net transactions with households	1.204	1.505	2.304	2.890
Current account balance (without grants)	(1.239)	(2.227)	(4.634)	(3.148)
Official transfers (grants)	0.591	0.496	0.476	0.433
Current Account Balance	(0.648)	(1.731)	(4.158)	(2.715)

Source: The National Bank of Serbia

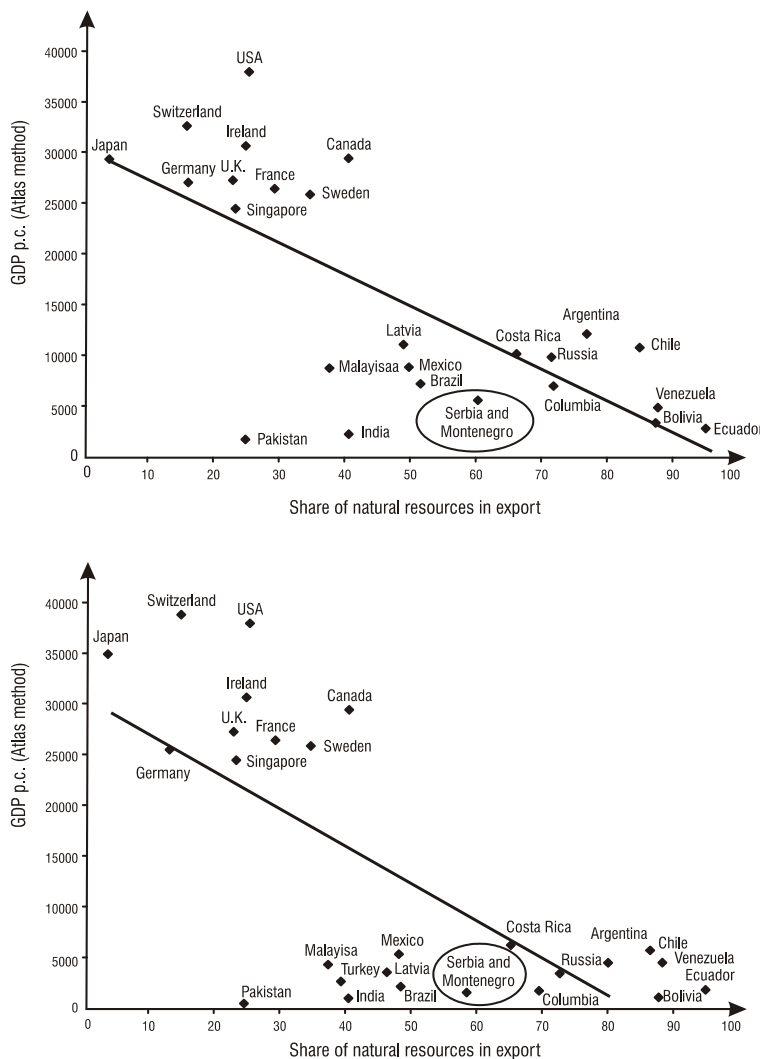
Note: * As at November 1, 2004

A more precise insight into the Serbia and Montenegro competitiveness level can be obtained by establishing a relationship between income and natural resources's share of total exports. Income is measured by the PPP p.c. and the GDP p.c. Figure 2 shows that natural resources constitute almost 60% of Serbia and Montenegro's exports. This is the main reason why the standard of living of the population is so low. The absence of a competitiveness position can be best explained by comparing it to other economies in transition. Namely, in economies in transition, natural resources's share of exports varies between 37-48%, by the income level which varies in the range of \$8-15 thousand US dollars (measured by the PPP p.c).

One of the most significant opportunities for an increase of competitiveness is privatisation. In the case of Serbia, distinctions should be made between companies privatised according to the insiders privatisation models (the privatisation laws adopted before 2001) and the companies privatised according to the sale models (the laws adopted after 2001). It can be concluded that, of 2,000 companies privatised through the insiders privatisation models, about 1,500 companies operate profitably. Apart from this group of companies, there is also a group of about 2,600

companies which should be privatised according to the 2001 Law on Privatisation based on the sale option. The sale is performed by applying several models which represent various privatisation tracks. The Agency for Privatisation has estimated that, of this number, about 2,000 companies will be privatised according to the accelerated auction sale method, about 480 of them according to the auction sale method, about 100 of them by tender sale and about 20 of them according to the initial public offering method. In addition to the initiated privatisation, the new law also regulates the privatisation termination process in the companies which initiated privatisation according to the insiders privatisation model, i.e. through the sale of minority stakes (of the Share Fund and individual owners).

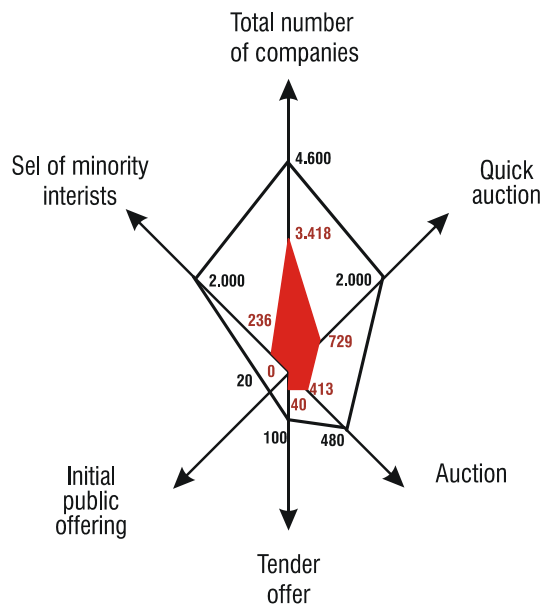
Figure 2: The relation between the income and the share of natural resources in export



The rhythm of creating the preconditions for the transformation of an inefficient sector into an efficient one (privatised companies) can be seen in Figure 3. The figure shows the scheduled privatisation objectives and realisation by privatisation tracks. Specifically, as of December 31, 2004 from 4,500 companies the sale of minority stakes was characteristic for 236 companies, the

accelerated auction for 729 companies, auction for 413 companies, tender sale for 40 companies, while the initial public offering had not yet started. The shaded part of the radar diagram in the previous figure is an approximation of the efficient sector, while the non-shaded part represents the total real sector.

Figure 3: The privatisation level in the real sector



Two criteria can be used for the estimation of a country's indebtedness level. First, the ratio between the current debt value and GDP. The marginal value of this criterion should not exceed 0.8. Second, the ratio between the debt value and the annual goods and service exports. The marginal value of this criterion should not exceed 2.2. Exceeding one of the marginal values mentioned is a sufficient reason to be classified as a "highly indebted" country. The amount of Serbia's external debt as of Jun 1, 2005 was about \$13.7 billion USD, which classifies Serbia as a highly indebted country. Specifically, Serbia is slightly below the marginal value of the first criterion ($0.68=13.7/22.1$) but significantly above the marginal value of the second criterion ($3.7=13.7/3.7$). The absolute level of debt is not excessively high. However, the economy's inability to service that debt is a cause for concern.

According to the World Economic Forum 2004-2005 Report (8, pp. 6-74), the characteristic indicators for Serbia and Montenegro are as follows. According to the Growth Competitiveness Index, among 104 countries ranked, Serbia and Montenegro holds the 88th position. At the same time, its rank is worse than in 2003 when Serbia and Montenegro was ranked 77th. The Growth Competitiveness Index components point to the reasons for low competitiveness. Namely, the technology index puts Serbia and Montenegro in the 77th position, the public institutions index puts it in the 85th position, while the macro-economic environment index puts it in 102nd place.

According to the Business Competitiveness Index, Serbia and Montenegro ranks 85th among 103 countries ranked, which is a symbolic improvement over 2003 when Serbia and Montenegro

ranked 87th. The Business Competitiveness Index components are such that the company strategy index ranked Serbia and Montenegro 87, while the business environment quality index ranked 81st.

The Global Competitiveness Index values classify Serbia and Montenegro in the group of countries that are in Development Stage 1 (income is below \$2,000 US dollar p.c. and the share of primary products in exports is over 70%). Among 41 countries in this group, Serbia and Montenegro ranks 33rd. Namely, only Sri Lanka, Tanzania, Uganda, Ukraine, Venezuela, Vietnam, Zambia and Zimbabwe are behind. The overall ranking of Serbia and Montenegro is 96th among 104 countries.

In this stage of development the government role is important and it stretches from geopolitical repositioning, new regulation, and practicing convenient macro-economic policies. Government policies should relax the country risk, improve the business climate, and increase the level of economic freedom.

A Look Ahead

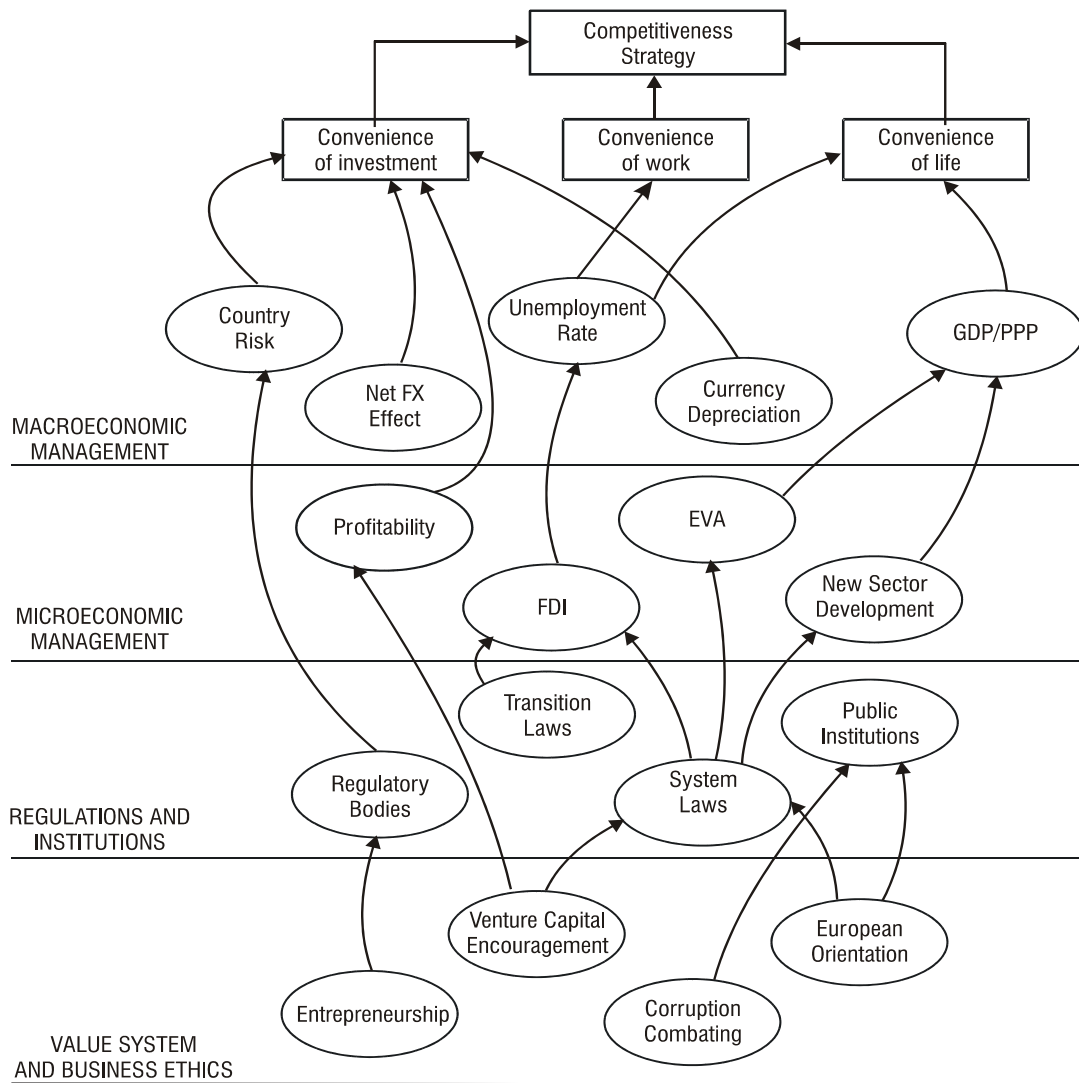
The new competitiveness strategy for Serbia should rest on four pillars. The first is macro-economic management. Macro-economic management includes maintaining price and currency stability as well as fiscal discipline (on both a macro and micro level). The second is micro-economic management. This comprises business strategy, corporate governance, business process optimisation, manager education and training, etc. This pillar refers to both greenfield and existing companies. The third comprises legislations and regulatory bodies and its primary objective is to act as a mechanism for companies control. The choice is to be made between the bank-centered system and the market for corporate control. For stated-owned network technologies the choice is to be made between various levels of liberalisation. The fourth refers to the soft elements of business environment like value systems, corporate culture, business ethics, and venture capital encouragement. The main ingredients in these pillar are European orientation and anticorruption strategy.

In the new competitiveness strategy, the focus must be shifted from the restructuring of the existing companies to the creation of new ones. Without the value system change, monopolistic behaviour and state paternalism will remain active. It is also necessary to replace defeatism in the non-entrepreneurial culture with the acknowledgement that growth potential is limitless as it is based on knowledge rather than on limited physical resources. Should the formerly stated prerequisites be fulfilled, the following could be expected: proactive management and permanent investment in networking (knowledge and communication).

When formulating and executing the strategy, it is necessary to replace a hierarchial approach with a holistic one, i.e. an approach of unique diversity. The holistic method of formulation and execution is enabled by R. Kaplan and D. Norton's (3), (4) and (5). methodology of a Balanced scorecard/Strategy map.

The main goals of a new strategy of competitiveness should enable Serbia to become a pleasant place to invest in, a pleasant place to work in, and a pleasant place to live in. A feasible competitiveness strategy map with mentioned goals is shown in Figure 4.

Figure 4: The Serbia competitiveness strategy map



Concluding Remarks

The prosperity of economy essentially depends on the competitiveness defined as the level of efficiency in the use of human, financial and natural resources as well as the level of added value perceived by consumers. Both internal stability (political, institutional, and macro-economic) as well as external compatibility with developed economies are a necessary but not sufficient condition for competitiveness improvement in Serbia. The competitiveness roots are in the

micro-economic foundations of the system. The competitiveness improvement in Serbia as a developing country with slow transition based on the correct macro-economic reforms, trade liberalisation and privatisation is neither a sufficient nor permanent source of competitiveness unless it is followed by an increase in the entrepreneurial capacity. More than 80% of variations in income growth can be explained by micro-economic fundamentals. Micro-economic reforms leading to an increase in productivity are the only ways to meet the budget requirements and service debt obligations. In addition, micro-economic reforms reduce interest group pressure on governments, weakening their influence by maintaining macro-economic stability and liberalisation.

These micro-economic fundamentals of competitiveness have tremendous potential. Concerning the use of competitiveness potentials, research has shown that Serbia is in balance with its possibilities. Unfortunately, these possibilities are extremely low.

The positive effects of entrepreneurship, investments and employment are considerably reduced if redistribution mentality and interventionism dominate in the economy. Under such conditions reformers reform only themselves, the citizens are hostages to monopolies, while brokerage activities dominate industrial ones. If brokers of others' values still remain to be the main architects of the transition in Serbia, this could turn the transition from a shortcut on the road from socialism to capitalism into a roundabout way from socialism to socialism. This time, perhaps, with an unfeasible space for redistribution and intervention.

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