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ORIGINAL SCIENTIFIC ARTICLE  
DOI: 10.5937/ekonomika2302013M  
Received: February, 16. 2023.  
Accepted: March, 31. 2023.

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## CHANGING TRENDS IN THE PUBLIC SECTOR IN THE REPUBLIC OF SERBIA<sup>4</sup>

### Abstract

*The authors deal with the problems of the public sector, which has a great share in economic growth. The public sector of Serbia is in imbalance and fundamental reforms are necessary. Given the legacy of privatization ‘through connections’, the public sector has also fallen into crisis. The sale of public companies was carried out in a non-transparent manner. Problems in the relationship between the public sector and the private sector confirm the need of restructuring the public sector.*

**Keywords:** public sector, changes, transformation, privatization, infrastructure.

**JEL classification:** E66

## ТРЕНДОВИ ПРОМЕНА ЈАВНОГ СЕКТОРА У СРБИЈИ

### Апстракт

*Аутори се баве проблемима јавног сектора који има велики удео у привредном расту. Јавни сектор државе Србије налази се у дисбалансу и неопходне су темељне реформе. С обзиром на наслеђе “бурazerске” приватизације и јавни сектор је запао у кризу. Продаја јавних предузећа обављена је нетранспарентно. Проблеми на релацији јавни сектор - приватни сектор потврђују потребу о неопходности реструктурирања јавног сектора.*

**Кључне речи:** јавни сектор, промене, трансформација, приватизација, инфраструктура.

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<sup>4</sup> The work is part of the project: Kosovo and Metohija between national identity and European integration (MPNTR – 47023)

## Introduction

The public sector has a large share in the economic growth and development of any national economy. Without the public sector, there would be neither production of goods of national importance and nor the provision of public services. Also, there wouldn't be health and social protection, which would be at the service of citizens as well as human and material resources (local, regional and national). Thanks to them, the state apparatus runs the country, defines policy and resolves current problems, and implements long-term plans. The public sector of the Republic of Serbia is in imbalance and fundamental reforms are necessary in order to establish macroeconomic stability. The public sector is characterized by instability, especially in finance, which is why the question of transformation of the public sector arises. In order to eliminate anomalies in the public sector, it is necessary to analyze it. Without a stable public sector, we cannot count on economic growth and an increase in citizens' standards. The economy of Serbia is still in some kind of transition process, and therefore the public sector is in a gap between the norms and the European regulations that need to be adopted or have already been adopted. Instability is inherent thanks to the bureaucratic apparatus. It is too cumbersome and as such adopts and implements new regulations in an untimely manner. The size of the public sector depends on the state structure. Our state sector is still under the influence of the vestiges of socialism. After the democratic changes, the state organization begins to take on the influence of the liberal concept, which entails the reduction of the public sector and the rationalization of available resources, which is, among other things, one of the conditions for joining the EU. With the new concept came privatization, which did not bring the expected results. Our leading economists are still dealing with the place and role of the public sector in society and its rationalization. The goal of our work is to explain the role and importance of the public sector and the changes taking place within it. Then, to explain in detail the restructuring of the public sector and investments.

The volume, that is, the size of our public sector is not proportional to the realized GDP (gross domestic product). If the public sector is efficient, then there is a positive reflection on the economy which enters the stabilization phase. The public sector of Serbia shows considerable weakness and that is why strong interventions by control authorities are necessary.

## Public sector restructuring and investment

Countries that have completed the reorganization and transformation of the ownership structure face many economic problems. They can be seen through the relationship between the public and private sectors. In our case, the private sector complains about the public sector and demands various corrections from the state. The meeting of the public and real economy in our country is in a chronic gap, and many legal acts and regulations will be needed which will differ from the previous ones in order to eliminate the problems. Privatization itself was announced after the October 5th changes as a saving model for failing state-owned companies (Ote, 2009, p. 19).

Economic institutes are paid with state money or money from the association, and of course, here, optimism pays off when necessary. It is evident that the results are weak

or, if there were any, they are far less than expected. The organizational structure is still in the process of reorganization.

Problems in the relationship between the state sector, the economy and the private sector are still current. The expected positive effects of the reorganization and change of ownership were absent while the anomalies of the system became even more visible. 'The thing that does not respond to what people want - or even what they need, it reacts to money' (Moore, Collins, Rosset, Esparse, 2005, p. 221). Francis Moore gave a very clear definition of what drives the system. According to him, profit, newly created value, are necessary for the results to be seen in action.

*Laissez-faire*, the free market and its invisible hand have become a fetish that resolves all problems. However, in reality, it turned out that this is not exactly the case. All former socialist countries started the transition process in an economic system that was not adapted to the market conditions of the economy (Milošević Šnjegota, Tomaš Miskin & Kalabić, 2017, p. 422). Big giants were sold at an extremely low price, and their stable business was either never established or it was reduced to the bare survival of former state-owned companies within the economy. In the case of privatized and restructured companies, many business improvement strategies are limited due to problems related to individual owners, control of companies by external investors, and all due to the still weak state system (Duvnjak and Stanišić, 2011, p. 289). Good examples such as the Smederevo ironworks and the mining and smelting basin Bor, which were taken over by the Chinese and are now operating successfully, are rare.

Economic publications often talk about the importance of monitoring and evaluating performance, regardless of whether it is a company or the entire country. Results are expected from politicians, managers, workers, companies... It has become common to say that it is important to monitor and evaluate performance because the public sector and the economy are oriented towards the same. Thus, there should be a matrix according to which incentives will be given to the successful, that is, depending on the performance. Measurements are also an indispensable factor - what we measure affects what we do as we collectively or individually target what we measure. The relationship between actions of implementing measures and goals is complicated; Stiglitz, Sen, Fitoussi, (2009, p. 8) express their position on the importance of comprehensive monitoring of success and rewards for achieved results. A big problem in Serbian public enterprises is certain limits. 'There are few restrictions that constrain and hinder the economy of Serbia as much as it is the case with the public enterprises. That broad economic segment, which in large part represents the ungrateful heritage of the socialist order, has spread in many directions like an insurmountable malignant tissue that deeply embeds itself in all pores not only the economy, but society as a whole.' (Majar, 2015, p. 9). Many resources available to state-owned companies remain unused. The general apathy that prevails among employees leads to an inevitable decline in activity. The newly created value is therefore smaller, so the state budget as well remains deprived of amounts that are not small. 'The logic of the functioning and organization of the public sector in the Republic of Serbia has not changed significantly over time, even though the society has gone through major changes. The logical question is, why didn't this happen?' (Veselinović, 2014, p. 3). Veselinović makes it clear to us where most of the problems come from. That's why the question arises, why don't we finally start with a comprehensive, thorough restructuring of the public sector? After the political

changes in 2000, major reforms of the economic system began, which aimed to create an open economy (Kastratović, 2016, p. 82). In May 2001, Serbia adopted a low level of privatization with all its weaknesses, which was the reason why its persistent application could not a priori provide good results by increasing the competitiveness of the Serbian economy. (Kovačević, 2010, p. 46) Privatization 'through connections' reigned in our region. The controls were too weak. State-owned firms were sold lightly with little or no concern for the social aspect. Tens of thousands of workers were dismissed with low severance pay or without any compensation.

In those years, we saw unpleasant scenes in the media that shook the entire public opinion, but the state institutions remained silent. The transition should have been accompanied by a package of social measures; however, this was not the case in Serbia. It is a well-known fact that in our country the transition was delayed, especially with the achieved level of development of the transition in other former socialist countries (Đorđević, Veselinović, 2010, p. 1).

The total inflow of funds from the sale of public companies was around two billion euros. The largest inflow of capital came from foreign investors. 4,338 out of a total of 4,600 state-owned enterprises were in the process of privatization as of August 1, 2006. At the auction sale, 2480 were found, and 1640 were sold, shares of 682 companies were sold, and at the tender, 66 companies were sold out of 100 companies. (Đuričin, 2006) In the last 12 years, the inflow of foreign capital has increased significantly, partly through the purchase and restructuring of failing state-owned firms and partly through the opening of new firms. 'Thanks to the demanding economic reforms it carried out in the previous period, Serbia has positioned itself as one of the most important investment destinations in Central and Eastern Europe. The list of companies operating successfully on the Serbian market is led by Bosch, Michelin, Siemens, ZF, Panasonic, NCR, Microsoft, Gorenje, Brose, Continental, Magna, Cooper Tires, Johnson Controls, Johnson Electric, Leoni, Fiat, Chrysler Automobiles, Yazaki, Eaton, Stada, Swarovski, Aunde, Calzedonia, Mei Ta, Schneider Electric, Geox, Tarkett, Ling Long, Adient, Minth, Toyo Tires, MTU, Barry Callebaut, as well as many others' (Development Agency of Serbia, 2022).

According to the IBM Institute for Business Value: 'Global Location Trends 2020' report, the Republic of Serbia is the world leader for the fourth year in a row in terms of the number of jobs created through foreign direct investment projects in 2019, and all according to the population.

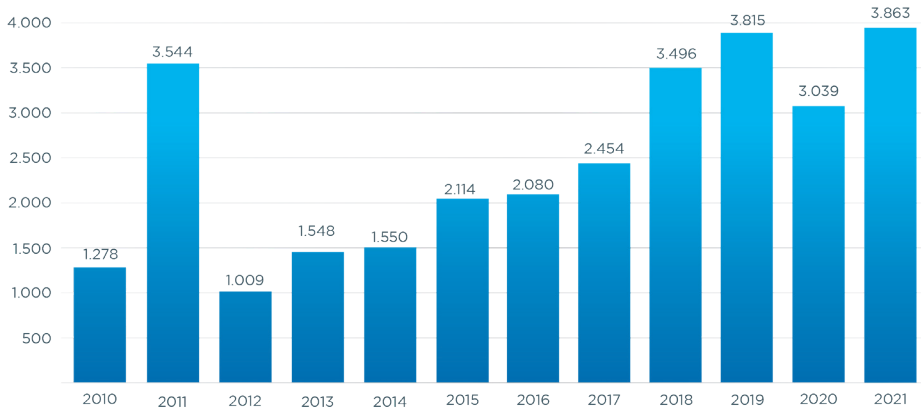
According to the criterion of the number of new jobs created (regardless of the population size) through FDI, the implementation of which began in 2019, Serbia took a high 5th place among European countries (Development Agency of Serbia, 2022).

In 2019, Serbia ranked first in the world in terms of the number of direct foreign investments. International capital flows associated with investments in companies in which a foreign investor takes a controlling stake are called direct investments (Alfaro & Chauvin, 2017, p. 5) According to the annual report published by FGI intelligence part of the British newspaper 'Financial Times'. 107 greenfield projects enabled Serbia to attract 12 times more foreign direct investment than it could be expected from its economy. (Development Agency of Serbia, 2022). We can see the improvement when there are investments in existing and new companies. One of the examples is 'Tigar Tyres' company in Pirot, who, from a failed giant with dirty technologies and weak payment power has now become a serious business entity under Michelin. 'Tigar Tyres'

in Pirot is an example of a healthy business and a company where capable workers can achieve a high personal income for our conditions.

It is obvious that investments, if they are the result of quality investment programs, bring good effects. However, there are other examples.

*Inflow of foreign direct investments:*



*Source: National Bank of Serbia according to the Development Agency of Serbia, available at <https://ras.gov.rs/rs/podrska-investitorima/zasto-srbija/uspesne-price>*

State-owned companies that successfully operate after a change of ownership are rare. Here, we specifically mean companies that were established by foreign direct investors. Their operations proved to be efficient and there was no need to reorganize the company, but the companies started working immediately. On the other hand, many problems were encountered in companies bought by foreigners. Regulations are out of date, not to mention the quality standards, technology, a workforce that was insufficiently qualified and unprepared for changes. Investors met with companies that were still operating as if they were in the era of socialism. ‘In the previous period, Serbia achieved a certain technological development primarily through the application of foreign technologies, less by developing and applying its own technologies.’ (Mitrović, 2009, p.89) ‘The key motives of foreign investments are production aimed at securing resources, securing markets, increased efficiency and acquiring strategic advantages’ (Cvetanović, Despotović, & Milanović, 2018, p. 22). We are a country rich in resources; foreign investors are satisfied with our strategic position, with the cost of labor and the developed road infrastructure as well as with the subsidies that the state provides for foreign investors.

Although we entered the process of restructuring public companies, the entire public sector, and the process of implementing new technologies took place relatively slowly. For the majority of our employees in public companies, the introduction of new programs like SAP (System Analysis Program) was perceived as difficult, and implemented inefficiently. It can be concluded from all this that where we as a country did certain things on our own, it went very badly and that without the complete takeover of our companies by foreign companies, the implementation of new ideas and knowledge takes place with a lot of difficulties.

## Management of public enterprises

In Serbia, half of the employees work in state institutions such as the judiciary, police, education, healthcare, while the other half of the employees in the country is consisted of the workforce from the production sector. In most transition economies, the role of institutions and enterprises has changed over the past thirty years. 'It is known that the transition has a destructive effect on the economic structure in the short term and it is being implemented because of the long-term effects. The negative consequences of the transition in the short term are: inflation, slowing down of economic growth, decline in production (overall and especially industrial), increase in unemployment and social insecurity.' (Mitrović, 2010, p. 610) Mitrović shows us the gravity of the situation and the negative effects that follow the transition. Public enterprises preserve social peace and without their existence, no matter how inefficient the business is, the situation in countries like ours would be even more difficult. 'There is a close connection between reforms and economic success. In numerous literatures in this field, it is stated that other factors are also important: initial conditions (initial economic situation) and economic wealth, the institutional condition at the beginning of the transition as well as the political system. These factors had a direct and strong impact on the achieved gross domestic product and had a decisive influence on the selection of reforms and the extent to which countries in transition implemented them.' (Veselinović, 2020, p. 26). That is why the role of state-owned companies is of a great importance because low incomes are characteristic of countries in transition. Although there have been changes and the public sector has been changing in a transitional environment for thirty years now, the very core of the economies of these countries is made up of state-owned enterprises. In order to have a healthy economy, entrepreneurs should have a far greater participation in the creation of the new value. However, the private initiative is hampered by complicated legal procedures, i.e., there was an absence of the 'rule of law'. Positions on the market were taken by foreign companies instead of domestic entrepreneurs. It must be reluctantly admitted that the import lobby and the foreign factor are too strong for small businessmen to resist. Until the emergence of covid in Serbia, economic growth had strong dynamics. However, the inability to perform part of the activity left consequences. Foreign direct investments regulated the negative effects of the external imbalance as much as it was possible. However, it was necessary to take measures to reduce the budget deficit. One of the ways is through proper management of the fiscal policy. The process of public sector restructuring is generally accompanied by fluctuations. Fluctuations can be controlled only by proper management of an efficient economic policy; in our case, it is possible by conducting an expansive fiscal and monetary policy. In crisis periods, increasing infrastructure spending in the short term can boost economic activity in crisis periods. So far, it has been shown many times that the construction industry is able to be the engine of the economy and the driver of other economic branches and thus help to eliminate the negative effects of the crisis caused by rigid changes within the public sector.

When the government of a country that is undergoing restructuring leads an economic policy with visible effects, then companies adapt more quickly to the positive effects of the reforms. However, if the reforms did not have positive effects, the adjustment would be slower. (Adjémian, Cahn & Maggiar, 2008, p. 228)

On the other hand, although the state is working to improve the economic situation, there is a problem of labor migration abroad. Foreign investors are forced to look for workers in the countries around us. Here is the most important part of the problem. Unemployment is decreasing, but the main reason for its decrease is migration. On the other hand, non-productivity, the low level of profits created by public companies occur due to state interventionism and non-financial company goals. The government and local self-governments are often forced to allocate fresh liquidity from the budget and 'pump' money into state-owned companies that do not function well enough in the market economy. The provision of subsidies is particularly emphasized in regions where the economic environment is unfavorable and there is general depreciation. Many things can be learned from the EU. Its prominent members can be a benchmark for leading state-owned companies on the right path. The Republic of Serbia, as a country that aspires to join the European Union, should improve its indicators and continue with harmonization of standards with the EU because this is the only way to effectively complete the process of transition, which it entered late. (Veselinović, 2019, p. 76)

## Conclusion

In this research, the authors deal with the public sector in the Republic of Serbia and the changes that have been going on for a long time. They point to the need for fundamental reform in order to establish macroeconomic stability. They propose the rationalization of available human resources. They explained in detail the consequences of privatization that did not bring the expected results. Aware that there is no economic growth without a stable public sector, they raise the issue of public sector transformation. The public sector in the Republic of Serbia is low-productive and inefficient, set up irrationally. This research paper analyzes the situation in the public sector with an emphasis on the creation of real reasons for its foundation. Creating a favorable environment for successful economic development is not possible without rationalization, significant reorganization and restructuring of public enterprises. However, countries that completed the organizational transformation of their organizational structure a long time ago still face economic problems. In our case, it is the private sector that complains about the work of the public sector. The meeting of the public and real economy in our country is in a chronic gap. However, even though the society was going through great changes, the question arises, why not finally start with a comprehensive, thorough restructuring of the public sector? We have listed the total inflow of funds from the sale of public companies as well as the number of sold companies in the process of privatization. The rule of law is a necessity without which it is not possible to solve the problem of the public sector. Fluctuations can be controlled only by proper management of efficient fiscal and monetary policy. The government and local self-governments are often forced to allocate money from the budget for better liquidity, which is not easy to deal with.



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