



## Free trade zones in Serbia – current situation overview

*Free trade zones in Serbia have had a very important impact on economic growth and transformation. The most important areas in which free trade zones have influenced the Serbian economy are acquisition of foreign direct investment (FDIs) and putting trade deficit under control. In 2016 there were 14 free trade zones across the country, covering more than 2200 ha, with 265 companies that employed in total more than 25 000 people and generated 16.5% of total Serbian exports. Current data show that 10% increase in production within free zones in Serbia would increase Serbia's GDP for 0.7%. Although position of companies operating in free zones is somewhat improved, they are still burdened with the bulk of regulatory and tax burden, as are other companies in Serbia.*

Although free trade zones are an old instrument for FDI acquisition and involvement in international trade, their development in Serbia took off only in recent years. There are 14 free zones in Serbia, employing 25 000 people and producing.

Trade Zone	Area	No of companies	No of employees
Pirot	122 ha	102	6 016
Zrenjanin	98,1 ha	8	3 263
Subotica	84,1 ha	32	4 298
Novi Sad	89,3 ha	66	1 880
Kragujevac	176,5 ha	11	3 405
Šabac	292,4 ha	8	450
Užice	55,4 ha	10	1 959
Kruševac	64,9 ha	7	1 100
Smederevo	540,1 ha	9	2 205
Svilajnac	40,2 ha	3	370
Apatin	415,2 ha	2	86
Priboj	26,1 ha	5	16
Beograd	98,3 ha	2	127
Vranje	123,4 ha	-	-
<b>Total</b>	<b>2 226 ha</b>	<b>265</b>	<b>25 175</b>

Free trade zones in Serbia in 2016.

The national Bureau for free zones was established in 2008, with the aim of supervision of their conduct and development, and the National Strategy for free zones 2011-2016 was adopted in 2011. After these measures, free zones vigorously continued to develop. Employment in free zones grew approximately 4,5 times since 2008, and investments grew more than 6 times. Even better numbers are attested for turnover, exports, and production, which: 7.4, 8.8 and 9.4 times higher than their initial values in 2008.



Had the production in Serbia followed the pattern provided by free zones, Serbian GDP in 2016 would have been 316 billion euros or 44 500 euros per capita, which would make Serbia one of the wealthiest countries on the Old Continent, between Sweden and Denmark.

	Investments	No of employees	Exports	Production	Total turnover
2008	37.5	5 515	243.6	260.0	651.7
2009	19.0	4 960	227.6	251.9	559.1
2010	71.2	7 886	295.3	431.3	991.5
2011	387.3	7 929	497.5	647.9	1 280.3
2012	755.6	14 579	819.1	899.3	2 499.6
2013	197.9	18 313	2 088.4	2 430.1	4 935.1
2014	208.7	19 255	2 030.5	2 348.8	4 794.9
2015	155.8	22 242	2 051.0	2 313.9	4 625.2
2016	236.4	25 175	2 151.7	2 444.3	4 822.1
Index 2008=100	630	456	883	940	740

Free trade zones development in Serbia 2008-2016; all numbers in million euros except the number of employees and index.

Free zones have become very important segment of the Serbian industry, since almost one fifth of all industrial output is produced in free zones (2.44 billion euros out of 14.26 billion, or 17%). The available data a clear dual pattern of the Serbian industry: those operating within and out of free zones. Although the data are scarce (with time series gathered only for 2008-2016) the overall industry in Serbia had much smaller output growth than the industrial enterprises located in free zones, which is mostly attributed to high investment inflows and establishment of new enterprises. Free zones have, therefore, become an important instrument for attracting FDIs in the country, although free zone location and benefits were just one of the measures used, usually accompanied by subsidies, tax waivers and other benefits. The most important new FDI ventures that opened their facilities in Serbia, such as FIAT automobile factory in Kragujevac and other automobile components producers, located their production in free trade zones.

	FDIs	FDIs in % of GDP	Free zone investments	In % of FDIs
2008	2 500	7.4%	37.5	0.0%
2009	2 100	6.7%	19.0	0.0%
2010	1 100	3.8%	71.2	0.1%
2011	3 300	9.9%	387.3	11.7%
2012	800	2.4%	755.6	94.5%
2013	1 300	3.8%	197.9	15.2%
2014	1.200	3.7%	208.7	17.4%
2015	1 800	5.4%	155.8	8.7%
2016	1 900	5.5%	236.4	12.4%

In million euros, unless indicated otherwise.



Investment in free zones have mostly gone to manufacturing and production of tradable goods. This is also important due to macroeconomic instabilities due to current account deficit that Serbia experiences, and due to the fact that most FDIs in Serbia were allocated to nontradable goods, such as construction, telecommunications, retail trade and financial services.

	Manufacturing	Trade	Finances	Real estate	Other
<b>2005-2008</b>	17%	11%	35%	17%	21%
<b>2009-2012</b>	26%	21%	23%	6%	24%
<b>2013-2015</b>	37%	14%	19%	10%	19%
<b>2016</b>	34%	9%	20%	19%	18%

Macroeconomic imbalances within the Serbian economy were stemming out from high "twin deficits": budget deficits and current account deficits. The fiscal consolidation implemented in since 2015 with cutting retirement benefits and wages eliminated further deterioration of the fiscal position, putting the high public debt on a downward spiral and budget deficits under control (with the fiscal deficit envisaged to only 0.5% of GDP). Current account deficit, on the other hand, was largely curtailed by the rise in exports, that was mostly due to new investments. Free trade zones have largely contributed to the significant alleviation of the current account deficit.

	Imports	Exports	Deficit	In % of GDP
<b>2010</b>	12,385	7,364	5,019	16.9%
<b>2011</b>	14,289	8,474	5,815	17.4%
<b>2012</b>	14,783	8,770	6,013	19.0%
<b>2013</b>	15,451	10,984	4,466	13.0%
<b>2014</b>	15,489	10,891	4,328	13.0%
<b>2015</b>	16,405	12,052	4,353	13.0%
<b>2016</b>	17,026	13,408	3,618	10.4%

In billion euros, unless otherwise indicated.

	Total export	Free zone export	In % of the total export
<b>2010</b>	7,364	295.3	4.0%
<b>2011</b>	8,474	497.5	5.9%
<b>2012</b>	8,770	819.1	9.3%
<b>2013</b>	10,984	2 088.4	19.0%
<b>2014</b>	10,891	2 030.5	18.6%
<b>2015</b>	12,052	2 051.0	17.0%
<b>2016</b>	13,408	2 151.7	16.0%

In billion euros, unless otherwise indicated.

Furthermore, the production conducted by free trade zone has been in recent years stable at 7% of GDP, which is significant for the whole of the economy. However, it shows how much more economic potential remains unused in Serbia.



	2012	2013	2014	2015	2016
Production in free zones as % of GDP	2.8%	7.1%	7.0%	6.9%	7.1%

Free trade zones are very important for the Serbian economy, having attracted a significant portion of FDIs allocated to tradable goods production; which was a strong boost to the significant reduction in the current account deficit reduction that took place since 2012. Without free trade zones, macroeconomic imbalances in Serbia would still be high, with the current account deficit at a much higher level, or its reduction would have been done through significant negative shocks to the overall economy. The level of employment that free trade zones provide are small compared to the overall economy, but their importance cannot be overlooked in smaller municipalities where they are located, or the economic transformation they provided for whole communities, such as in the case of the city of Kragujevac and companies working in the free zone in that city. Free trade zones cannot be overlooked even when production is taken into account: current data show that a 10% increase in production in free zones would increase Serbian GDP for 0.7%. This is important for future policies in this area: the data show how important free zones are for the economy of Serbia, as well as the fact that there still are almost endless opportunities for their development, since their number and scope is limited.

## Current free zones legal framework in Serbia

Free zones in Serbia were legally established in 1996, with new regulations adopted in 2005 and 2006 (Law on free economic zones, Official Gazette 62/2006), which is still in power. This law creates an environment for opening and managing of free zones in the country. Free zones can be open with a written agreement of the Government of Serbia, following a formal request by a company that has registered for free zone management with the authorities, as well as a written benefit analysis drafted by the Ministry of finance on potential expected benefits of the zone (according to criteria set by the Directive on criteria for estimation of economic conditions for establishment of free zones). The zone is managed by the company, which can be in private ownership, which have to draft annual report to the Bureau for free zones within the Ministry of finance. The company can charge fees and other charges for its services, from which it can derive profits.

Directive on criteria for estimation of economic conditions for establishment of free zones stipulates that a new free zone is economically sound if the proposed are has an international river or airport or connected to international road network (highways E) via regional roads. Other conditions are:

1. planned investment (in infrastructure and buildings) is at least 3 million euros, of which 1 million is invested in the first year since the zone becomes operational
2. foreign investment should be at least 50% of the total investments



3. the magnitude of production and its turnover is going to be positive for Serbia's current account (total value of exports will be higher than the total value of imports)
4. employment plans of the zone and companies operating in it considers employing at least 100 people in the first two years of the zone's operation
5. it includes purchase of new technical equipment that lead to technology transfer
6. area of the zone is within scope of underdeveloped areas of the country
7. operation of the companies within the zone would have a beneficial impact on companies outside of the zone

There is also a list of preferential industries for setting new zone, which include:

- manufacturing of textiles and clothes
- processing rawhide and of base metals
- manufacturing of metal products and metal equipment
- production of electrical appliances and office machinery
- production of radio, tv and communication equipment
- production of medical, precision, and optical appliances
- production of vehicles and trailer, and other transport equipment.

However, since the growth of free zones in recent years has been substantial, there are informal information that opening new free zones is not looked upon favorably within the current administration. Since not all free zone work with full capacities (including the zone in Apatin), it would be easier to advocate (if necessary) broadening the geographical scope of the existing zone than setting up a completely new one, and their informal confirmation that this proposal would meet better understanding among the officials.

Companies operating in the free zones are exempted from paying custom tariffs and other import duties, and other consumption taxes, such as the VAT on goods that is exported i.e. is not put on sale in the territory of Serbia. These taxes, however, are paid for the goods sold in Serbia. Transport service for good to and from free zones, and between them themselves; fuels and electricity consumption within the zones and construction material are also VAT exempted. However, all other Serbian laws and regulation are fully implemented in free zones.

The most important laws concerning the operation of free zones are: the Law on custom tariffs (Official gazette 62/2005, 61/2007, 5/2009); the Law on customs (Official gazette 18/2010, 111/2012, 29/2015, 108/2016); the Law on VAT (Official gazette 84/2004, 86/2004, 61/2005, 61/2007, 93/2012, 108/2013, 68/2014, 142/2014, 83/2015, 108/2016); the Law on foreign trade operations (Official gazette 36/2009, 88/2011, 89/2015); the Law on foreign currency operations (Official gazette 62/2006, 31/2011, 119/2012, 139/2014). There are also hundreds of thousands of pages of other sources of regulations in Serbia, as in other European countries.



The strong point in managing free zones in Serbia is that they are not managed by state administration, but by companies. In some cases, owners of these managing companies are local municipalities, but it can be also private entities, as in the case of the Pirot free zone, or the stakes can be divided between them (a minority private or minority municipality ownership). This provides incentives for

As it can be seen from the above, free zones in Serbia provide relatively weak regulatory and tax incentives. The main advantages can be found within the less stringent rules covering trade transaction with foreign entities (more expedient and efficient custom offices) and some tax relief (no custom tariffs, and VAT on energy and construction material used within the zone itself). The VAT exemption is not something special, since VAT taxation in Europe follows the rule of destination: VAT is therefore paid in the country of destination not of origin, so all goods produced in Serbia (both within and outside of free zones) are not taxed with VAT. However, in practice, as in other countries, the VAT is calculated and paid on the whole turnover on a monthly basis for large taxpayers, and the VAT exemption is afterwards calculated and paid back to the company. It is true that some of the companies located in free zones have extremely favorable conditions (such as elimination of corporate tax for 10 years after the first year in which profits were disclosed; tax rebate on income tax and social security contributions that the employer pays from the gross wages; exemption from smaller local taxes and surcharges; high subsidies for opening job placements), but these conditions do not stem from their position within the free zones, but from high level agreements with the national government which were made prior to their investments. Since in some cases (such as in Kragujevac and Smederevo) the free zones were even tailor-made and created just for the convenience of these large investment companies, it would be closed to truth to say that majority of these special treatment came before their inclusion in free zones.

However, the majority of the regulatory and tax burden for companies operating in free zones in Serbia remains. Their position definitely is better than the one of companies operating outside of the zones, but, unfortunately, it would be a far-fetched conclusion that their position is significantly better.

## **The Apatin free zone**

The Apatin free trade zone is located in the municipality of Apatin, situated on the bank of the river Danube in the Western Bačka district. The municipality is well connected with its surroundings via the international river and a decent regional motorway that connects it to the international highway corridor to Belgrade or Budapest. The surroundings provide a pool of workforce due to its high unemployment level, although the wages are a bit higher than the average in the country.



	Municipality of Apatin	District of Western Bačka
Number of inhabitants	29 000	188 000
Number of working age people (15-65)	20 000	129 000
People employed	8 160	53 166
People unemployed	3 597	19 704
Unemployment rate	30.6%	27.0%
Average monthly gross wage	650 euros	520 euros

The free zone is divided in three geographically distinct areas. The main part is 77 ha on the river itself and accommodates bigger enterprises, while the Block 61 of 6 ha accommodates smaller enterprises. Both venues have unused parcels for new investors. There is also a bit allotment of land of 280 ha in Odžaci. However, informal information suggest that this part of the free zone will be dissolved since it has not attracted a critical number of interested parties for investing in it and setting up an operational facility. There is also some informal information regarding opening up a new free trade zone in the city of Sombor, the center of the Western Bačka district. The company that manages the free zone Apatin has mixed but predominantly municipality ownership: 70% the municipality of Apatin, 25% by the municipality of Odžaci and 5% by the company Standardgas Lmt from Novi Sad.