

From the Editor



Observed in a broader context, from 2001—when Serbia's economic transition effectively began—until 2025, Serbia achieved an average GDP growth rate of 3.2%, which is approximately equal to the average recorded by the other four Western Balkan countries, and only slightly above the average of the Central and Eastern European (CEE) countries that in the meantime became EU members (3%), which were already more developed than Serbia at the beginning of this period. At the same time, Serbia's economic growth during this period was significantly above the EU-27 average (2.3%), which can be explained, among other things, by differences in the initial level of development. These results indicate that over the past quarter of a century Serbia has achieved a certain degree of convergence in terms of economic development relative to the EU average, i.e. relative to developed European countries, but not relative to comparable CEE countries.

According to the speed of economic growth, the past three decades can be divided into three sub-periods: (i) 2001–2007, a period of rapid growth, with an average annual GDP growth rate of 6% (at the level of average growth in CEE countries and above the Western Balkan average of 4.7%); (ii) 2008–2017, a period of slow growth, with an average annual GDP growth rate of only 0.9%, due to global factors (the global financial crisis and the Eurozone crisis) and internal factors (fiscal consolidation, floods, and an inadequate business environment). In this period, Serbia's economic growth was below the CEE-EU average of 1.6% and the Western Balkan average of 2.3%; and (iii) 2018–2024, a period of faster growth, averaging 3.6% per year (above the CEE-EU average of 2.3% and the Western Balkan average of 2.9%).

Economic growth depends on three groups of factors—human capital, physical capital, and technical progress. The solid growth dynamics recorded by Serbia over the past seven years are primarily the result of a strong increase in labour force activation and investment in physical capital. In the period from the end of 2017 to the end of 2025, the number of formally employed persons increased by 316 thousand, while the unemployment rate declined from around 14% to 8.2%, approaching the CEE-EU average of about 5%. At the same time, the activity rate increased from 52.9% to 55.9%, also approaching the average of comparable CEE countries of around 58%. Employment growth in this period was largely driven by the employment of low- and medium-skilled workers in technologically less advanced sectors, such as traditional manufacturing, construction, and traditional services. Labour shortages in certain segments lead to an increasing need for the import of labour, which, together with the mentioned indicators, indicates that in the coming period it is possible to expect only a modest additional contribution of the growth in the use of physical capital to overall economic growth, given that the labour force pool has already been largely utilised and that demographic and migration trends are unfavourable.

Another important generator of Serbia's economic growth over the past seven years relates to a strong increase in investment in physical capital, from around 16–17% of GDP annually to 23–24% of GDP. This increase is the result of a strong rise in public investment (by around 4 pp of GDP), investment by foreign companies operating in Serbia (by around 2 pp of GDP), as well

as household investment (by 1% of GDP), while investment by domestic companies in this period even slightly declined (by 0.5 pp of GDP) – accounting for only slightly more than one fifth of total investment.¹ Although the increase in investment in the previous period is unequivocally positive, several important facts can also be observed that limit the positive effects on Serbia's economic growth. The increase in public investment, after several years of remaining at a low level, is economically justified and as such can stimulate future growth both on the demand side (during the implementation of infrastructure projects) and on the supply side (through the creation of conditions for the growth of private investment). For this effect to materialise, it is necessary that these investments be directed toward projects for which it has been methodologically established that they are socially profitable, and that their contracting and implementation be carried out in a competitive and efficient manner, which did not represent the dominant practice in the previous period. With regard to the investments of foreign companies, it is observed that they were largely directed toward technologically less advanced branches of traditional sectors of the economy, such as the production of automotive parts, rubber, oil processing, mining, the food industry, etc. The investments of these companies were mostly financed through foreign direct investment, which in previous years was high in gross terms, but whose net amount (when payments made by foreign companies on the basis of returns on capital are deducted) has been declining – for example, in 2024 net FDI amounted to only €275 million, although in gross terms it reached €4.6 billion. In the coming period, a decline in both gross and net amounts can be expected, as indicated by data for 2025, which is the result of both global challenges and internal factors of the Serbian economy – such as strong wage growth and rising unit labour costs, as well as domestic risks and increasing uncertainty in relations with European Union countries, from which a large share of investment originated. Therefore, in the coming period it is not possible to count on a more significant additional impulse of foreign investment to total investment and economic growth, and it is even possible that this contribution will be reduced.

The level of investment achieved in Serbia during the 2020s is close to, or even slightly higher than, the average of CEE countries (where investment amounted to around 23% of GDP), but for convergence in capital capacity it will be necessary for investment in Serbia to remain relatively high, i.e. higher compared with other CEE countries, over a longer period of time. These data at the same time indicate that the scope for a more significant increase in economic growth through a stronger increase in investment in Serbia is limited, given that investment is already relatively high compared with other CEE countries, and that there is also a risk of a reduced contribution of foreign investment to this factor. In this regard, some scope for improving the contribution of investment to economic growth exists primarily in the segment of improving the efficiency and effectiveness of public investment and creating the preconditions for an increase in investment by

¹ Petrović, P., Brčerević, D., and S. Minić (2025). *Economic Development of Serbia: Between Institution Building and the Middle-Income Trap*. ResearchGate. Available at the following [link](#).

domestic companies. For this to occur, it is necessary to resolve key problems related to the quality of the business environment (the rule of law, administrative efficiency, suppression of corruption, etc.) and to achieve stronger integration of Serbia into European and global financial and economic flows.

Economic growth, in addition to an increase in the quantity of human and physical capital, can also be achieved through an increase in output using the same quantity of labour and capital, owing to better technology, knowledge, organisation and efficiency, which represents technical progress, i.e. total factor productivity. According to empirical research, the potential growth rate of Serbia's economy over the past seven years amounted to around 3.9%, of which the contribution of total factor productivity accounts for only slightly more than one fifth (around 22%), while in CEE countries that contribution is close to 50%.² Serbia's lag in terms of the contribution of technical progress to economic growth is the result of lower capital and technological endowment, limitations with respect to the level and quality of the education of the labour force, the institutional framework for the development and diffusion of innovations and new technologies, and an unfavourable economic structure dominated by traditional sectors (agriculture, classical manufacturing industry – food, textile, etc.), as well as traditional services (transport, tourism, trade), while the share of advanced sectors (ICT, scientific and innovative activities and advanced branches of manufacturing – such as the production of pharmaceutical products, electronic equipment, automobiles, etc.) is modest.

According to the World Bank classification, countries are divided, based on the level of gross national income (GNI), into low-, middle- and high-income countries. With GNI per capita of USD 11,700 in 2024, Serbia belongs to the group of upper-middle-income countries, and in order to move into the group of high-income countries it is necessary for GNI to increase by a further one fifth (to close to USD 14,000 in 2024 terms). Given that all CEE countries that in the meantime became EU members managed to position themselves in the group of developed countries, which so far has not been the case for any of the Western Balkan countries, this objective can be considered attainable, subject to the fulfilment of appropriate preconditions. However, empirical data show that two thirds of middle-income countries fail to cross the upper threshold of that zone, which is a phenomenon known as the "middle-income trap". In order for Serbia to avoid the middle-income trap and maintain a solid dynamic of economic growth in the medium and long run, it is not possible for future growth to be largely based on increased utilisation of labour and investment in physical capital, although some scope in this segment also exists – through improvements in the educational structure and quality of the labour force, improvements in the quality, i.e. effectiveness, of public investment, and the creation of conditions for an increase in domestic private investment. In line with the above, future economic growth in Serbia, in order to be dynamic and sustainable, needs to be oriented toward strengthening the contribution of technical progress, through increasing capacity and incentives for the development and diffusion of innovations, the application of new technologies, and the development of technologically advanced branches of the economy.

According to numerous econometric studies, more efficient and more inclusive institutions have an unequivocally positive effect on all three levers of economic growth – on human capital through encouraging immigration, on physical capital – through encouraging investment, and on technical progress – through encouraging entrepreneurship, investment in innovation and the search for returns based on competitiveness, rather than through rent-seeking. On the basis of the results of numerous studies, it is estimated that improving the results Serbia achieves with regard

to the quality of institutions according to relevant international indicators, i.e. reaching the average of CEE countries in this domain, could on average increase the rate of economic growth by up to one percentage point per year. This means that through such a leap, the income of future generations would on average be higher by around 35% compared with the income level that would be achieved in the absence of such an institutional development leap.

In addition to improving the quality of institutions, the dynamics of future economic growth can be significantly influenced by the quality of public policies. Empirical research shows that differences in the quality of public policies and institutions explain more than half of the variation in the speed of economic growth of post-socialist economies, while the other half can be attributed to the characteristics of these countries and global economic developments.³ In the case of Serbia, in order to achieve dynamic and sustainable economic growth in the medium term with the aim of avoiding the middle-income trap, it is necessary to implement public policies that would further utilise the potential of the first two growth factors (physical and human capital) and lead to a significant leap in terms of technical progress. Given the complexity and multidimensional nature of these issues, this would imply the implementation of synchronised and well-coordinated policies across different segments. The basic precondition for this is the conduct of economic policy in a manner that ensures macroeconomic stability (a low fiscal deficit and public debt, low inflation), alongside improvements in the structural characteristics of fiscal policy (a moderate reduction of public expenditure and the tax burden, tax system reform that would contribute to improving the international competitiveness of the economy and the green transition, improving the efficiency of public expenditure policy – particularly public investment, and improving the efficiency of the operation of public enterprises). The achievement of this result could also be supported by the implementation of well-targeted industrial policy programmes (toward technologically advanced branches, i.e. toward an environmentally and economically sustainable energy transition, etc.). In addition, it is necessary for public policies to ensure improved conditions for the development of domestic entrepreneurship and the development and diffusion of innovations and new technologies, through investment in education and research and development – through public universities and institutes and through encouraging private sector investment in research and development – as well as the development of technology transfer programmes – linking scientific institutions with the economy in order to accelerate the commercialisation of innovations – and through stable programmes of support for innovation and start-ups and strong protection of intellectual property. Furthermore, the focus of public policies should be on the development of human capital through investment in education, training and retraining programmes for workers in rapidly changing industries, attracting talent from the diaspora, stronger inclusion of the real sector of the economy into global value chains, and the integration of Serbia's economic, legal and institutional system into European institutional frameworks, with the aim of removing barriers to trade, capital flows, and the transfer of knowledge and technology.

Belgrade, December 2025. Prof. Saša Randelović, PhD
Executive Editor, Quarterly Monitor



² Petrović et al. *Ibid*

³ Arsić, M., Randelović, S. i A. Nojković (2025). *Government policies and economic growth: Evidence from emerging economies in Europe and Central Asia*. Working Paper.