

Supporting lagging regions by delivering on economic potential and equality of opportunity in Serbia

Executive Summary:

Lagging regions in Serbia face a number of constraints to raising their level of growth and to translating economic growth into improved welfare. Notably, these include: difficulties in attracting and maintaining the young population; promoting entrepreneurialism and competitive local enterprises; delivering quality public services and enhancing livability of local environments. However, regions that are centrally located and/or have agglomeration potential have significant opportunities to develop their local economies. Moreover, all lagging regions have the potential to contribute to the national economy regardless of location and potential through raising the endowments of their inhabitants and increasing connective infrastructure.

As a companion piece to the Western Balkans and Croatia Urbanization and Territorial Review (World Bank, 2019) using up-to-date national data, the main added value of this technical note is to present a spatial lens for Serbia on how to analyze the challenges and potentials of lagging regions and develop suitable solutions to address and nurture those. The results from the analysis are specific to the region but some general insights may inform other lagging regions in Serbia.

This note begins with a broad assessment of lagging regions in Serbia, identifying those that are significantly trailing behind in terms of income per capita ('low income') and those that, while not poor, are stagnant and diverging from the national average ('low growth' lagging regions). The note describes characteristics of lagging regions in terms of poverty levels, human capital outcomes, delivery of social services as well as institutional capacity. It also showcases a spatially informed policy framework, guided by "3Cs" (Concentrate, Connect, Capacitate) that can be applied to address lagging regions challenges.

The arguments on lagging regions are illustrated by focusing on the case study of Central Banat (Srednjobanatski), including an emphasis on the city of Zrenjanin, as a case example of a 'low growth' lagging region in Serbia, as well as the district of Raska as an example of a peripherally located, low income lagging region. The analysis draws on and hopes to complement regional and local strategies of the districts and local self-governments.

For the case of Central Banat, through contextualizing the 3Cs formula, three policy priorities could be identified, namely 1) concentrate and coordinate investments through cooperation among regional and local institutions; 2) connect ideas, people and businesses through connective infrastructure and knowledge networks and 3) capacitate dynamism of the local economy through increased livability of a "magnet" city with enhanced service delivery. Raska has some more limited potential given its peripheral location, but investments in livability of the cities, sectors with comparative advantage as well supporting effective circular labor migration of young people could yield substantial local economic benefits.

The note is by no means meant to be complete given data constraints, but mainly to be used as an internal discussion document to raise the importance of addressing the challenges of lagging regions in a different manner than policy as usual, while continuing to emphasize national policies to raise endowments (social protection schemes, education policies, health programs etc.). Future research could take a more in depth look at the specific role that secondary/middle cities can play in lagging regions and how to further local capabilities in spite of limited agglomeration potentials.

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This case study was prepared by Thomas Farole and Solene Dengler as a companion to the Western Balkans and Croatia Urbanization and Territorial Review¹ (World Bank, 2019), which assesses the territorial dimensions of recent development in the Western Balkans and Croatia and outlines policy responses to support faster, more inclusive, and sustainable growth across the region. The note addresses lagging regions in Serbia, with a focus on the districts Raska and Central Banat, as respectively case examples of a peripherally located, low income lagging region and a relatively centrally-located, 'high-potential' but currently low growth lagging region. The authors wish to thank counterparts from the Ministry of Construction, Transport and Infrastructure, World Bank colleagues as well as local consultants Jelena Tanasijevic and Dragisa Mijacic for their valuable contributions to this note.

Key figures and statistics in this note:

- **Serbia has currently larger welfare disparities than in economic output.** The coefficient of variation between regions of income or consumption was on average 20% in recent years - higher than on average for OECD countries (16%) and for countries in Europe and Central Asia (Bussolo, Davalos, Peragine, & Sundaram, 2018), while regional inequality measured by the coefficient of variation of GVA per capita at NUTS3 level was 0.33 in 2018, which was slightly below the average for recent EU Accession countries (0.35) and slightly above the average for the EU15 (0.29).
- **We identify thirteen “low income” lagging regions in Serbia out of total 25.** Nine of these regions are growing more rapidly than the national average and so are converging; but 4 of the lagging regions (Zaječar, Pomoravlje, Jablaniča and West Bačka) are not only among the poorest regions in Serbia but have been diverging further in recent years². Another two regions – Šumadija and Central Banat, are not among the poor regions but have been diverging in recent years and so are categorized as “low growth” lagging regions.
- **Spatial policies in Serbia will become ever more essential to help dampen or prevent negative impacts on growth and shared prosperity.** In 1997, Bulgaria had similar levels of disparities between the capital region and others than today in Serbia (coefficient of variation of GVA per capita of 2.15 and 2.23 respectively) and had even lower levels of disparity between the capital region versus the poorest regions (3 and 3.34 respectively).
- **The shares of households at risk of poverty is up to ten times higher in municipalities of low income lagging regions** compared to municipalities in leading regions (World Bank, 2019).
- **In lagging regions, secondary cities have insufficient population to play a role as a driver of growth via agglomerations effects.** The population of secondary cities in lagging regions has also been declining from 2011 to 2018.
- **Labor market outcomes broadly align with income levels.** Employment rates were 4 percentage points higher in leading than in low income, diverging, regions (47% compared to 43% in 2017).
- **Access to water supply and sewerage systems in Serbia is clearly linked to municipalities' household income levels** (World Bank, 2019) and is also a general issue, as only around 20% of the Serbian population has access to safely managed sanitation services (World Bank, 2020).

¹ Most recent data has been used for some graphs and statistics, results are varying from the WBCUTR from 2019 (classification of regions, graphs) but main messages remain the same.

² This is diverging from the WBCUTR (World Bank, 2019) given updated data used but without major implications on overall messages.

COVID19 insights:

While this technical note is not aiming to analyze in detail the implications on lagging regions of COVID19 situation given lack of timely information and data, a few important pieces of information can be noted (as of 12th June 2020) that are likely to impact some conclusions from the analysis and the capacity of national and local governments to further local economic development. In fact, according to an OECD report from June 2020 (OECD, 2020), optimistic growth predictions for Serbia, low levels of unemployment as well as low debt levels are likely to be overturned by the crisis situation. Given major implications in domestic markets and growth fundamentals of the national economy, the World Bank estimates as a downside scenario a -5.3% drop in GDP in Serbia in 2020 (compared to a pre-COVID estimation of +3.9% and a baseline scenario of -2.5% that assumes a fast slowdown of the outbreak, containment measures being lifted end of June and a gradual recovery beginning from second half of 2020) (World Bank, 2020). Vulnerable workers and SMEs, particularly those dependent on external trade, as well as FDI flows are likely to be disproportionately affected in lagging regions and will require continued and targeted interventions for economic recovery. Moreover, many local development strategies had emphasized tourism and leisure events as potentials for growth, and therefore innovative solutions will have to be found to diversify from these sectors or respond to changing demands. Some opportunities could be furthered in this regard such as online retail, which has increased by 80% since the beginning of the year and may perhaps become an established trend. Most LSGs in Serbia during the crisis stopped all public procurement and the budget revenue will be decreased, since the biggest share of local revenue are property taxes and employment taxes. This may affect the ability for capital investments that are needed particularly in lagging regions to raise endowments and enhance livability and health of local populations. A further challenge faced in this regard was the sudden return from the diaspora during the crisis that overwhelmed the capacity of utilities. It will remain to be seen whether utilities will adapt their strategies long term or whether they expect a “return to normal”.

1. Addressing lagging regions to enhance prosperity in Serbia

Serbia needs to address its spatial inequalities to maximize the country’s potential. The shares of households at risk of poverty (living on less than 60% of the national median income) is up to ten times higher in municipalities of low income lagging regions compared to municipalities in leading regions (World Bank, 2019). This is all the more concerning combined with a recent relatively poor performance of leading regions, labor mobility barriers, high outmigration, population decline and lack of maximization of existing potential of some regions and especially middle cities in the country.

While raising the competitiveness of leading city-regions will contribute to economic growth, addressing the challenges of regions left behind in Serbia will be critical for shared prosperity and sustainable growth. Moreover, factors such as EU accession and rapidly changing technology is likely to deepen regional disparities in the coming years, with associated risks to political and social cohesion.

Using a spatial lens enables to i) identify differential challenges preventing local economic development, ii) analyze the untapped potential of regions/cities and iii) support the understanding of dynamics within regions between municipalities and between lagging and leading regions. This approach complements national level policies to reduce poverty as well as traditional approaches to drive prosperity focusing on capital cities / main agglomerations and can therefore contribute to develop more effective national, regional and local policies.

1.1. Lagging regions in Serbia: spatial dynamics, poverty and economic potential

While Serbia must accelerate overall economic growth, particularly through raising the competitiveness of leading city-regions, addressing the challenges of regions that are being left behind will be critical for shared prosperity and sustainable growth. This will require targeted development strategies that maximize the potential of regions by building on and strengthening endowments, while ensuring that individuals, no matter where they live, have access to quality public services and mobility to take advantage of opportunities that become available to them – in their region or elsewhere in the country.

1.1.1. Welfare vs. output disparities in Serbia

Economic activity is never evenly distributed. While disparities in economic output have been large across countries in the past, national incomes have been converging over the last 20–30 years (Lakner & Milanovic, 2013). Within many countries, however, there has been increasing concentration in output and wealth in core metropolitan regions, while rural and peripheral regions increasingly lag. Such patterns are evident around the world, and Serbia is no exception.

Regional disparities in economic output are not necessarily a problem and, in fact, is associated with faster overall growth in many countries. However, large disparities in GDP per capita across regions not only raises concerns about equity but can act as a hindrance to overall national growth and can result in lagging regions getting locked into long-term ‘low growth’ paths.

Serbia has currently larger welfare disparities than in economic output. The coefficient of variation between regions³ of income or consumption was on average 20 percent in recent years - higher than on average for OECD countries (16 percent) and for countries in Europe and Central Asia (Bussolo, Davalos, Peragine, & Sundaram, 2018). Average per capita household income also varies widely, from 544,555 Serbian dinars (RSD) in Novi Beograd to RSD 156,060 in Tutin municipality (WBCUTR 2019). Regional inequality measured by the coefficient of variation of GDP⁴ per capita at NUTS3 level, on the other hand, was 0.33 in 2018, which was slightly below the average for recent EU Accession countries (0.35) and slightly above the average for the EU15 (0.29) (Figure 1). Moreover, regional inequality as measured by GVA declined somewhat between 2013 and 2018⁵.

The relatively low disparity in economic output may be explained by an underperformance of leading regions. This may be explained among others by a relatively poor performance of leading areas, spatial differences in the redistribution of economic gains, low population numbers in lagging areas “inflating” GDP per capita figures and by relatively ineffective internal labor mobility. Indeed, economic activity remains quite concentrated (Mijačić & Paunović, 2011; Živanović & Gatarić, 2017; Joksimović & Golić, 2017). 39 percent of national GDP is generated in Belgrade, and most active enterprises are concentrated

³ “Regions” is used in this document both for actual statistical regions in Serbia (equivalent to NUTS 2) and for districts (equivalent to NUTS 3). The data for GDP is for regions in Serbia, the rest of the data used throughout the document is generally for districts or municipalities. For the analysis of responsibilities, the focus is generally laid on districts and municipalities and occasionally on regions. Figures in PPS are used when comparing Serbia internationally whereas national currency (RSD) is used for within-country comparisons.

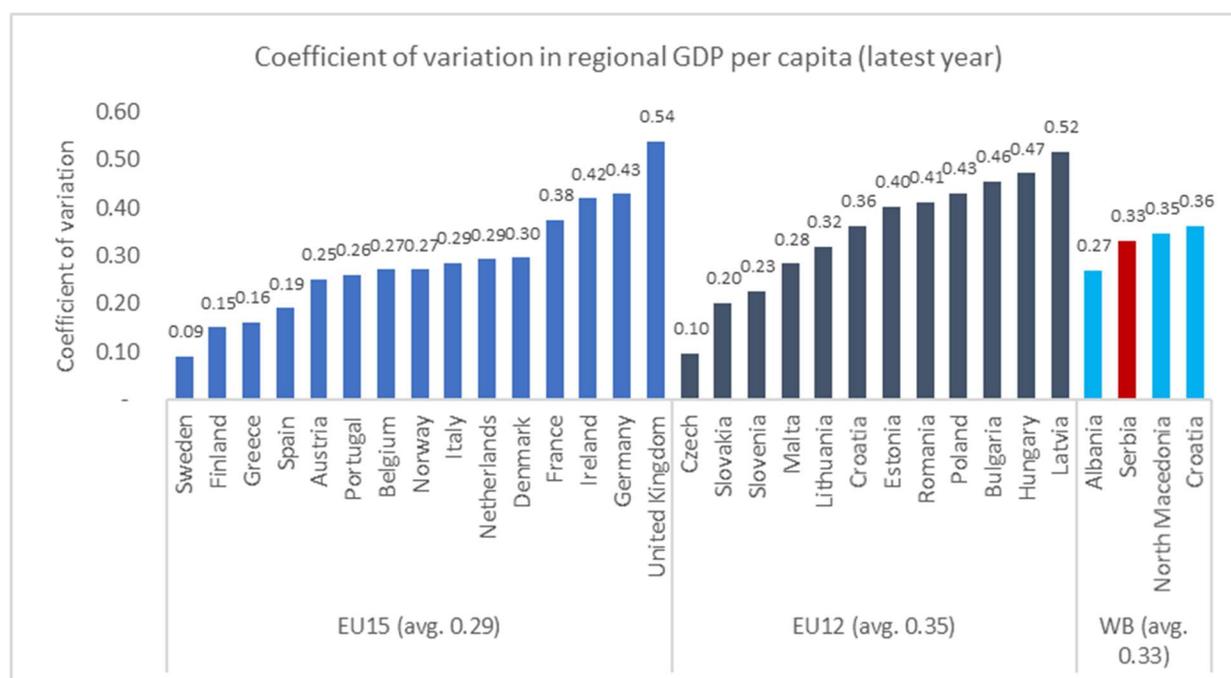
⁴ GDP data in Serbia is only available for regions, therefore for NUTS3 level (district) analysis GVA is used for Serbia and GDP for other countries.

⁵ Data was updated since the WBCUTR from 2019 but results are similar.

there, while 80 percent of assets, revenues, income and employment are concentrated in around 23 towns and municipalities (Jakopin, 2014; World Bank, 2019).

In the near future, regional disparities may increase. Factors such as EU accession, demographic decline, and rapidly changing technology is likely to substantially deepen regional disparities (including in economic output) in the coming years, as observed in recent EU accession countries such as Poland, Hungary or Croatia (Figure 2). In 2014⁶, the disparity measured in terms of GVA per capita between the capital region versus the national average, secondary regions or the poorest region was much lower in Serbia than for example in Bulgaria. In 1997, Bulgaria had similar levels of disparities between the capital region and others than today in Serbia and had even lower levels of disparity between the capital region versus the poorest regions. This could indicate that spatial policies in Serbia will become ever more essential to help dampen or prevent negative impacts on growth and shared prosperity.

Figure 1: Regional inequality in Serbia is lower than regional comparators and much lower than in many recent EU accession countries



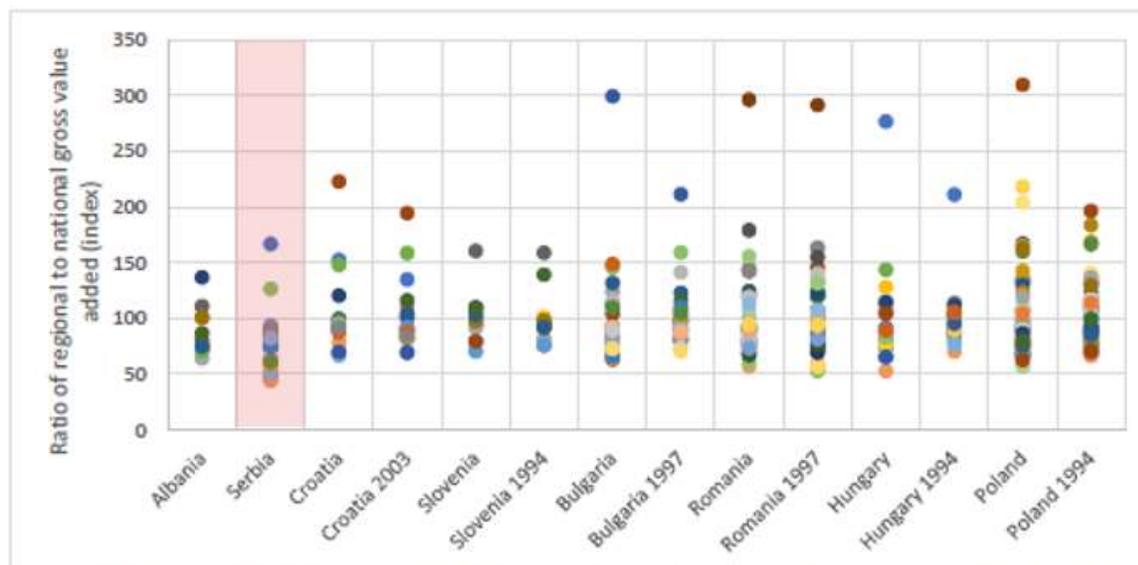
Source: Data from Cambridge Econometrics European Regional Database and national statistics for the Western Balkans and Croatia, latest year available; Note: Regions are at the Eurostat Nomenclature of Territorial Units for Statistics level 3 (NUTS3) regional classification, the most detailed level.

Table 2: Serbia's disparities between the capital and other regions compared to Bulgaria

Comparative measures of GVA per capita	Serbia 2014	Bulgaria 2014	Bulgaria 1997
Capital region vs. average	1.67	2.99	2.11
Capital region vs. second region	1.32	2.01	1.33
Capital region vs. average of other regions	2.23	3.22	2.15
Capital region vs. poorest region	3.34	4.75	3.00

⁶ 2014 was used for comparability purposes across all countries as in figure 2.

Figure 3: Serbia may experience increase in regional disparities as EU comparators (2014 unless otherwise indicated for comparability purposes)



Source: Data from Cambridge Econometrics European Regional Database and national statistics for the Western Balkans and Croatia.

Note: Regions are at the Eurostat Nomenclature of Territorial Units for Statistics level 3 (NUTS 3) regional classification, the most detailed level.

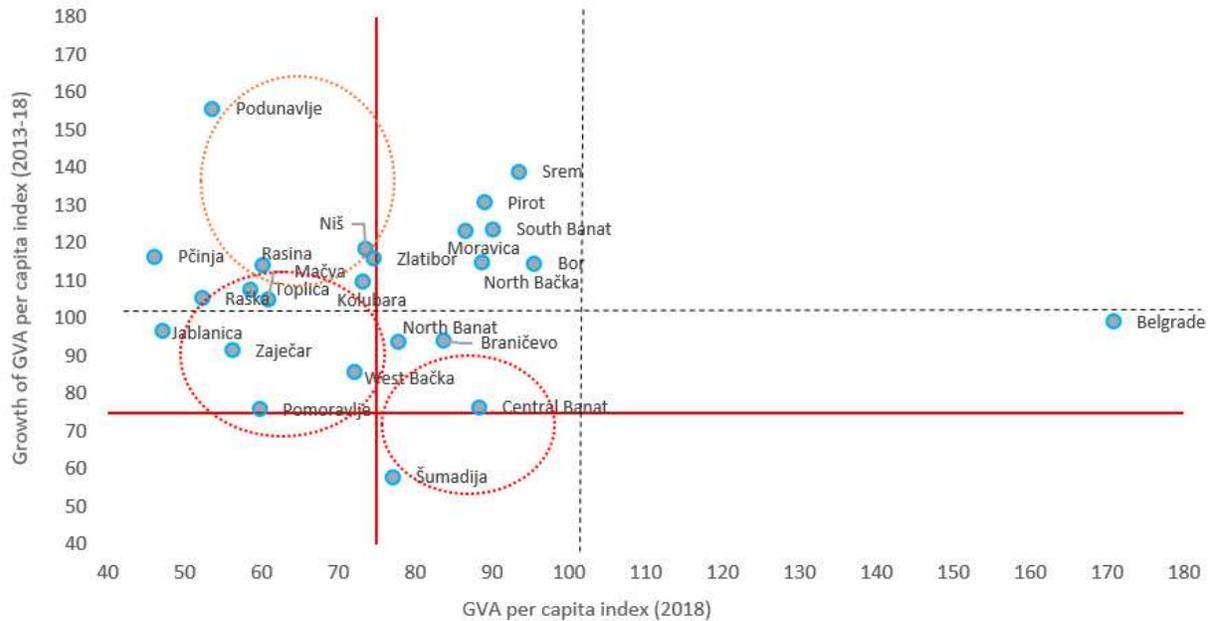
1.1.2. Description of lagging and leading areas in Serbia

Thirteen lagging regions can be identified in Serbia. In line with the approach of the EU cohesion policy's "Lagging Regions Initiative", we identify leading and lagging regions according to criteria of both income level and growth, so that we identify two types of lagging regions – those that are "low income", or poor, and those that are "low growth", which are not necessarily poor but are increasingly diverging⁷. Using these definitions, we identify thirteen (13) "low income" lagging regions in Serbia out of total 25 (Figure 3). Nine (9) of these regions are growing more rapidly than the national average and so are converging; but 4 of the lagging regions (Zaječar, Pomoravlje, Jablaniča and West Bačka) are not only among the poorest regions in Serbia but have been diverging further in recent years⁸. Another two regions – Šumadija and Central Banat, are not among the poor regions but have been diverging in recent years and so are categorized as "low growth" lagging regions. See Annex 3 for a full listing of regional categorizations.

⁷ In the European Union, low income lagging regions are defined as NUTS 2 regions with GDP per capita below 50 percent of the EU average; low growth regions are those with GDP per capita below 90 percent of the EU average that have failed to converge toward the EU average over the past decade. For the analysis in the Western Balkans and Croatia, we adjust this to define low income regions as those with incomes below 75 percent of the Western Balkans and Croatia average and low growth regions as those with below-average incomes that are growing at below 75 percent of the Western Balkan and Croatia average. The analysis in this section is based on national comparison based on income levels or 2015 GVA per capita in euros at purchasing power standard and growth measured as the change in gross value added per capita in constant terms using national currencies over 2010–15, which is a relatively short period. The analysis uses the regions defined in the Eurostat Nomenclature of Territorial Units for Statistics level 3 (NUTS 3) regional classification.

⁸ This is diverging slightly from the WBCUTR (World Bank, 2019) given updated data used but without major implications on overall messages. Only West Bačka, Zlatibor and Kolubara are now lagging instead of leading regions; Sumadija became a low growth instead of a leading region; while North Banat, Bor and Braniceva have upgraded from low growth to leading regions.

Figure 3: Mapping leading and lagging regions in Serbia by growth and income level (2013-18)

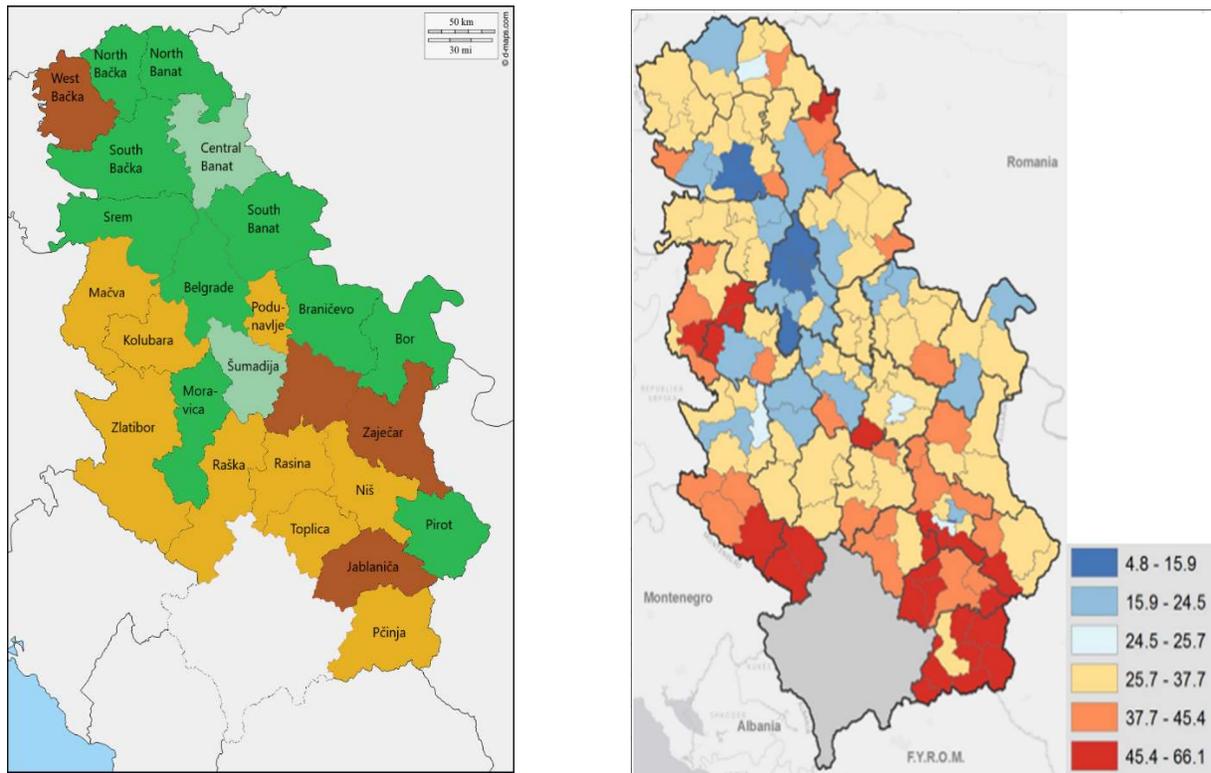


Source: Based on data from Statistical Office of the Republic of Serbia

Note: Axes cross at regional averages

“Low income” regions tend to be clustered, while “low growth” regions have a more varied geographical distribution. In Serbia, “low income” regions tend to be clustered geographically and are often rural and peripherally located, although there exist lagging regions located adjacent the leading metropolitan regions (Figure 4). Many are located around interior borders. “Low growth” regions, by contrast have a more varied geographical distribution. Lagging regions overall include a mix of those regions that are undergoing structural transition (typically formerly leading industrial areas that have suffered from deindustrialization) and entrenched poor regions that have long lagged the national economy and increasingly face challenges of demographic decline. Poverty rates are higher in rural areas and in South Serbia but with also pockets of poverty in the North-East and West, as well as adjacent to Belgrade in Podunavlje.

Figure 4: Comparing leading-lagging regional categorization (left, 2018, NUTS3 regional level) with poverty levels (right, 2012, municipality level)



Sources: 1) Own calculations, P3C (Statistical Office) Serbia; 2) Dávalos, María; Thomo, Ledia. "Portraits of poverty and inequality in Serbia". 2016, Washington, D.C.: World Bank (The maps were rescaled to fit the page and thus do not reflect the true size and geographic layout of countries)

Note (left map): dark green= leading regions; light green= 'low growth' lagging regions; light brown= 'low income', converging lagging regions; dark brown = 'low income', diverging lagging regions.

1.1.3. Growth dynamism and agglomeration in Serbia

Serbia's main urban areas overall lack the dynamism needed to enable faster economic growth through agglomeration effects and catch up with comparators including from the European Union (WBCTUR, 2019). As Serbia's urbanization rate has stalled at around 55% (much lower than comparators in ECA around 70%¹), which implies that the easy growth dividends from urbanization are likely over, the country would have to rely on leveraging the potential of agglomeration economies in existing cities and towns.

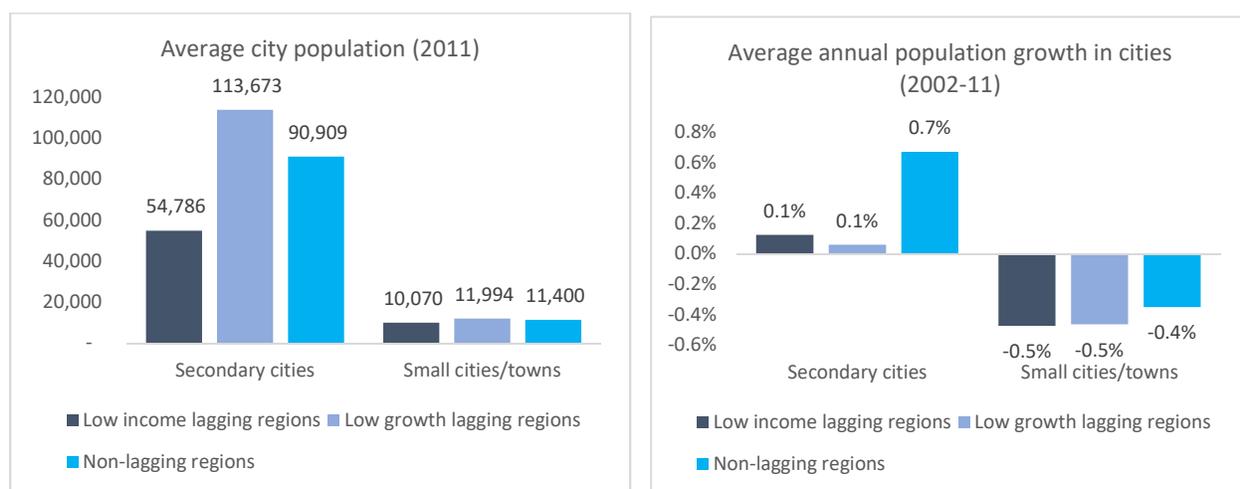
Enhancing dynamism would require focus on increasing the attractiveness of cities and reducing costs of congestion in larger growing cities.⁹ Belgrade has been underperforming compared to secondary cities

⁹ While cities generate agglomeration economies due to the close proximity of firms and workers that results in better matching, learning and sharing (Duranton and Puga, 2004), they also generate negative externalities in the form of congestion costs that directly impact the cost of living and doing business in cities (Duranton, 2010). These costs have several components ranging from poorly defined property rights, provision of public goods like roads and transport and sewerage to the quality of air, public spaces like parks and level of traffic and crime in cities. As cities grow larger, these congestion costs also increase. Capitalizing on agglomeration thus entails ensuring urbanization is managed well and congestion costs are minimized. (content from WBCTUR 2019)

or other capitals in the region (World Bank, 2019). Serbia's three largest cities (Belgrade, Novi Sad, and Nis) have a total population of about 2.3 million; and Belgrade alone accounts for 40% of GDP and 35% of jobs. However, Belgrade has grown slower than the rest of the country, particularly relative to secondary cities. Its growth has also been less dynamic than in comparator metropolitan areas with similar demographic trends such as Bucharest or Sofia.

In lagging regions, secondary cities¹⁰ have insufficient population to play a role as a driver of growth via agglomerations effects. Looking back at census data from 2011 (WBCUTR 2019), there was a clear difference between the size of secondary cities¹¹ in lagging regions versus those in non-lagging regions, while no significant size difference could be found for smaller cities/towns. A slightly higher average size can be found for low growth regions but as there are only two low growth regions, this may not be considered representative. Moreover, secondary cities in lagging regions seemed not to be magnets for population contrary to non-lagging regions. This may highlight that secondary cities were not developing sufficiently to play a role as a driver of growth in the lagging regions. Finally, we can notice, perhaps not surprisingly, the demographic decline story is worst in the currently assessed lagging regions, knowing that 72% of cities in Serbia are declining in population (WBUCTR 2019). The story and trends are similar when looking at more recent but projected population data (until 2018), except that population has been declining in lagging regions in the period 2011-2018.

Figure 5: Average city population and growth for secondary cities by regional categories (2002-2011)



Source: National Statistical office data (population projections, latest census data; new census planned in 2021); city categories used for the Cities in ECA report 2017 (Restrepo Cadavid, Cineas, Quintero, & Zhukova, 2017).

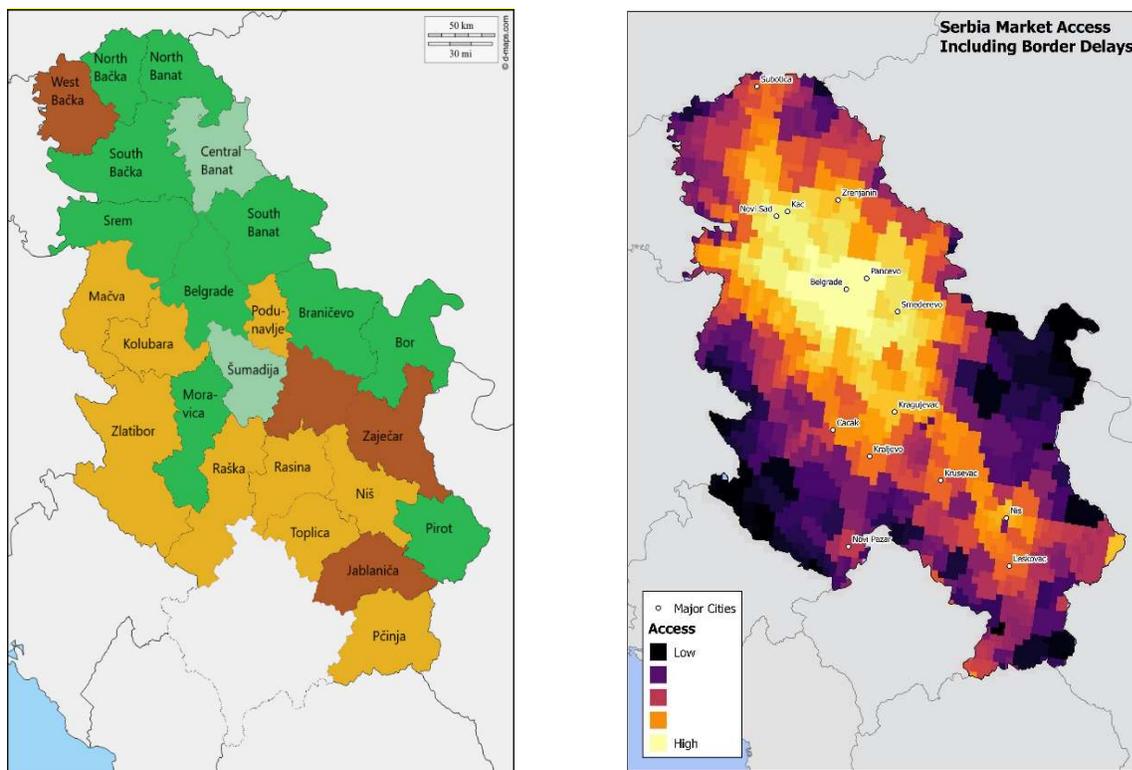
This lack of agglomeration potential is compounded with location challenges and low market access. Reducing market access barriers is an essential part of addressing lagging regions, as these tend to be clustered across borders and tend to specialize in sectors (agriculture, tourism, services) which are most often traded regionally. Most lagging regions face large gaps in market

¹⁰ Cities in the top quintile of the urban population distribution in each country minus the capital city. Cities are categorized as capital (Belgrade), secondary, or other. 'Secondary' goes down to ~ 35,000 population and covers 33 cities; 'other' goes to < 1,000 population and covers 121 cities/towns. Data goes through 2018 for population (estimates) and 2012 for economic output. Economic output is based on nightlights data; because of the data available for this, it is necessary to create 'agglomerations' which go slightly beyond the administrative boundaries of the cities.

¹¹ Secondary cities are defined here according to population criteria, which may differ from official definitions (see Annex 5).

access (Figure 6), intraregional connectivity, with secondary road networks being underdeveloped and limited resources to maintain them.

Figure 6: Comparing leading-lagging regional categorization (2018) with market access (2018)



Sources: 1) Own calculations, P3C (Statistical Office) Serbia; NUTS3 regional level 2) World Bank Geospatial Operations and Support Team; : Market access measured as GDP-weighted travel time to all European markets

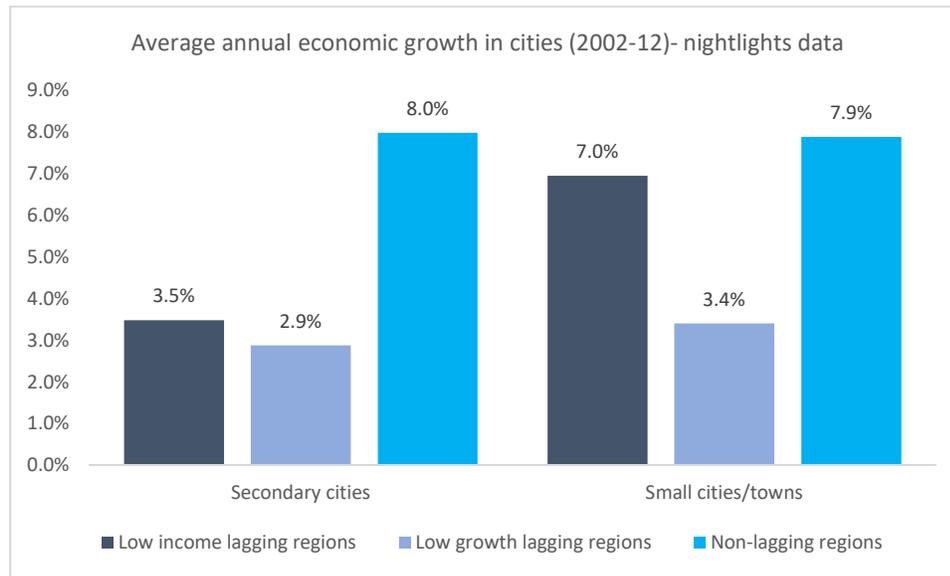
Note (left map): dark green= leading regions; light green= 'low growth' lagging regions; light brown= 'low income', converging lagging regions; dark brown = 'low income', diverging lagging regions.

Note (right map): black = low market access; yellow = high market access

Overall, secondary cities were broadly not driving the growth compared to smaller cities but there seemed to be some untapped potential. In a previous analysis¹² (World Bank, 2019), secondary and small cities in Serbia have been found to perform better than comparators globally and in Europe and Central Asia. Having a closer look nationally, we can see that secondary cities in lagging regions were underperforming from 2002 to 2011 compared to small cities. This could be explained by the power of cities being more limited in low income, generally rural peripheral, regions but could also point to missed opportunities for secondary cities in lagging regions. In low growth regions, it would seem that both secondary cities and smaller cities / towns were underperforming compared to their potential. However, more recent data would have to be collected to verify whether this would be applicable after 2012.

¹² The approach and dataset follow Restrepo et al. (2017), which in the absence of robust economic indicators for cities of all sizes uses the intensity of nighttime lights emitted by cities as a proxy for economic activity. Long-term economic growth, proxied by growth in nighttime light intensity, was analyzed to assess the contribution of city size and of the capital and secondary cities in the Western Balkans and Croatia and in ECA as a whole. The compound annual growth rate of nighttime light intensity was estimated for three periods (1996–2000, 2000–05, and 2005–10) and then regressed on the log of city population, using fixed effects by country to account for national differences in growth rates.

Figure 7: Average annual economic growth in secondary cities by regional categories (2002-2012)



Source: Nightlights data and city categories used for the Cities in ECA report 2017 (Restrepo Cadavid, Cineas, Quintero, & Zhukova, 2017).

1.1.4. Poverty and social cohesion: a spatial lens

Low-income lagging regions are broadly those with highest levels of poverty, despite pockets of poverty around major agglomerations. As shown above, low-income lagging regions are those with high levels of poverty¹³, poor human development outcomes, and high gaps in terms of infrastructure service delivery and quality of municipal services provided (particularly water and wastewater treatment). Poor labor market and human capital outcomes can be linked to issues in service delivery, a major impediment for these regions to develop their potential and for people to raise their endowments and participate in economic activity.

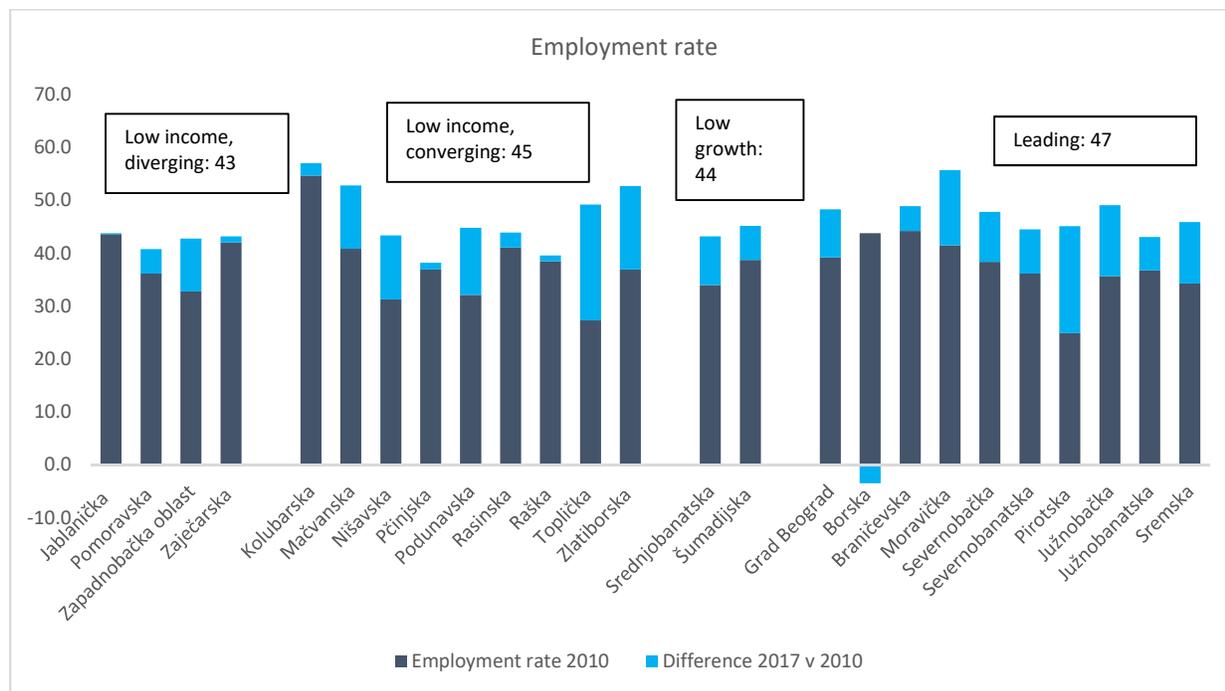
Labor market outcomes broadly align with income levels (see Table 2). In fact, employment rates were 4 percentage points higher in leading than in low income, diverging, regions (47% compared to 43% in 2017). Among the lagging regions, low income converging regions seemed to have the highest employment rates and also growth in employment (9 percentage points increase 2010-2017, equivalent to leading regions). These insights are confirmed when looking at labor force participation rates, where rates are even higher on average in low income converging regions rather than in leading regions (55% vs. 53% in 2017).

There appears to be some untapped potential in terms of capturing entrepreneurial activity for economic transformation. The self-employed average shares were highest in low income and in particular in converging regions, indicating a possible issue of self-employment not being able to contribute to higher value-added and rising incomes. In the cases where labor outcomes are poorly aligned with income levels, this could be due to higher levels of agricultural employment, lower levels of private sector wages

¹³ Latest available data disaggregated at the level of municipalities on poverty from National Statistical Office is 2013 so that there may be a divergence between poorest in terms of poverty levels (2013) and current GVA data (2018).

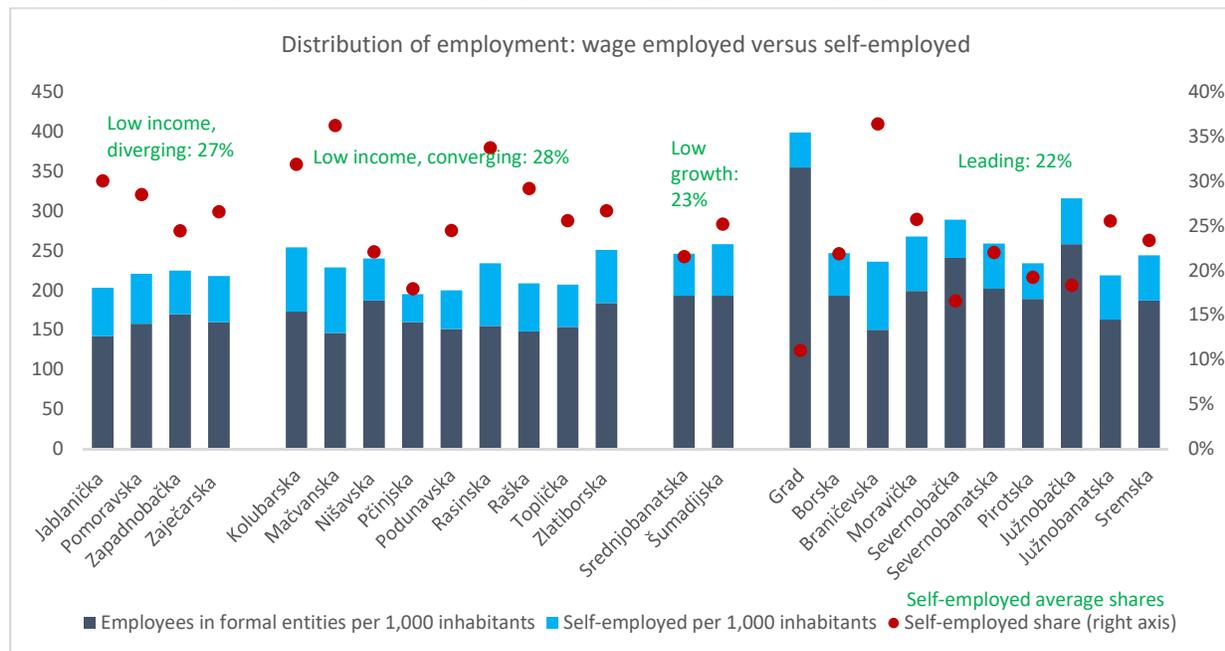
employment and higher levels of labor mobility (rural-urban migration) that reduce the working-age population.

Figure 8: Employment rates in lagging vs. leading regions (2010-2017)



Source: National Statistical office

Figure 9: Wage employment vs. self-employment in lagging vs. leading regions (2017)



Source: National Statistical office

In addition to having high outward migration, internal migration has been relatively lower in Serbia than in other transition economies. According to the LITS survey in 2016, the share of people who have ever moved from one part of a country to another is below 30 percent (EBRD, 2016a), compared to 71% in Estonia, 54% in Slovenia or 48% in Bulgaria (World Bank, 2019). While international migration, particularly to the EU, is appealing, internal labor migration can be an important force for raising incomes and for people to maximize their potential. Several studies have confirmed the need for Serbia to enhance its internal mobility strategies and policies (IOM, 2010) as the combination with the slow pace of productivity growth limits the potential for robust increase in labor earnings (World Bank, 2020). As Serbia works in the coming years to enhance the competitiveness of their cities and boost productivity, wage differentials between urban and rural areas are expected to rise and may make internal labor migration more attractive. In general, this is indicating a potential for facilitating within-country mobility to move to jobs (World Bank, 2020).

Differences in individual endowments were found to be an important driver of differences in living standards between regions. For example, education and household characteristics generally accounted for more than half of income or consumption disparities between urban and rural areas and between the capital city and the rest of the country in Serbia (World Bank, 2019). In lagging regions, the share of population receiving social assistance can be up to six times higher than the national average. These lacking endowments could explain why the participation in economic activity has been relatively low.

High human capital gaps in lagging regions are likely to greatly reduce the country's ability to shift to a more knowledge-intensive economy. In fact, educational attainment is strongly and positively correlated with the municipality's average income or consumption. This may be amplified by spatial sorting as the most skilled workers migrate from lagging to leading regions. There are also differences in educational quality (learning outcomes¹⁴), although performance is in line with regional averages from Europe and Central Asia.

There is a correlation of certain health outcomes and poverty rates for municipalities. The correlation is less clear with economic outcomes (GVA) at district level, which could for example be due to high investments in health and social infrastructure in Serbia in lagging regions through national or donor funds or also pockets of poverty in the districts as well as other factors playing a role (for example potential linkages between poor urban wastewater systems and life expectancy in low growth regions). It would also appear that there is no substantial correlation but high gaps in lagging regions for infrastructure service delivery and quality of municipal services provided (particularly water and wastewater treatment).

Relatively low sanitation and waste management, particularly in poorer municipalities, presents an environmental and health risk. Access to water supply and sewerage systems in Serbia is clearly linked to municipalities' household income levels (World Bank, 2019). Only less than 25 percent of Serbia's population has this access, the second lowest rate among the Danube riparian countries. The urban-rural disparity in terms of access to improved sanitation is also prevalent. More than 80 percent of Serbia's urban population has sewer connection compared to 20 percent of the rural population. Only 12 percent of the population is connected to urban wastewater systems, and this collected urban wastewater is not adequately treated. Moreover, only around 20% of the Serbian population has access to safely managed sanitation services (World Bank, 2020). This is an impediment to the development of human capabilities and endowments, the attraction of business and the development of productive local economies.

¹⁴ Harmonized learning outcomes, which draw from standardized testing scores, particularly from Programme for International Student Assessment (PISA).

Table 2: Comparing economic and social outcomes across Serbian regions (regional rankings)

Information on districts			GVA and poverty		Labor market outcomes				Social outcomes and service delivery			
District name	Economic status	Density/location	GVA per capita	Poverty rate	Labor force participation	Employment rate	Average earnings	Net migration	Life expectancy	Infant mortality	Water supply (HHs connected)	Urban wastewater (HHs connected)
Jablanička	Low income, diverging	sparse peripheral	24	25	17	16	25	20	14	7	19	17
Zaječarska	Low income, diverging	sparse peripheral	21	14	20	19	18	14	17	2	10	11
Pomoravska	Low income, diverging	sparse central	19	16	18	22	22	9	9	14	23	8
Zapadnobačka	Low income, diverging	sparse peripheral	16	15	23	21	16	18	20	15	5	25
Pčinjska	Low income, converging	sparse peripheral	25	24	25	25	23	22	15	3	12	12
Raška	Low income, converging	sparse peripheral	23	22	16	24	24	8	10	10	13	5
Podunavska	Low income, converging	dense central	22	10	13	13	6	21	22	4	17	7
Toplička	Low income, converging	sparse peripheral	20	23	5	5	21	23	16	8	24	13
Rasinska	Low income, converging	sparse central	18	19	15	15	20	19	3	11	15	14
Mačvanska	Low income, converging	sparse central	17	21	3	3	19	17	18	9	22	21
Kolubarska	Low income, converging	sparse central	15	17	1	1	11	12	6	16	14	15
Nišavska	Low income, converging	dense central	14	13	9	17	13	3	5	20	25	24
Zlatiborska	Low income, converging	sparse peripheral	13	18	4	4	17	24	4	21	20	6
Šumadijska	Low growth	dense central	12	6	14	11	9	5	7	13	8	2
Srednjobanatska	Low growth	sparse central	8	12	19	18	7	15	23	23	7	16
Severnobačanska	Leading	sparse central	11	11	21	14	12	10	25	6	2	18
Braničevska	Leading	sparse central	10	4	8	7	5	13	11	17	21	23
Moravička	Leading	sparse peripheral	9	7	2	2	15	11	2	25	11	3
Severnobačka	Leading	sparse central	7	3	11	9	10	4	21	24	6	19
Pirotska	Leading	sparse central	6	20	10	12	8	16	19	1	16	10
Južnobačanska	Leading	sparse central	5	9	22	20	4	7	13	12	9	22
Sremska	Leading	sparse central	4	8	12	10	14	6	12	19	3	20
Borska	Leading	sparse peripheral	3	5	24	23	3	25	24	5	18	9
Južnobačka	Leading	dense central	2	2	7	6	2	2	8	22	1	4
Beogradska	Leading	dense central	1	1	6	8	1	1	1	18	4	1

Data source: National statistics office, Social outcomes were sourced from Devinfo data; latest available data

Red to green scale: rankings from worst to best performance (among regions within countries)

1.2. Potential national approaches to address lagging regions in Serbia

Strategies to address the challenges of lagging regions need to be determined based on structural characteristics of the regions to avoid one-size-fits-all approaches, although as a complement to general national poverty reduction and sectoral strategies. There is therefore a role to play to address lagging regions for the national, regional and local level and ideally these policies would be coordinated for maximized development outcomes. A combination between top-down and bottom-up strategies, projects and ideas can ensure that general spatial national factors can be considered and specific potentials of regions can be furthered.

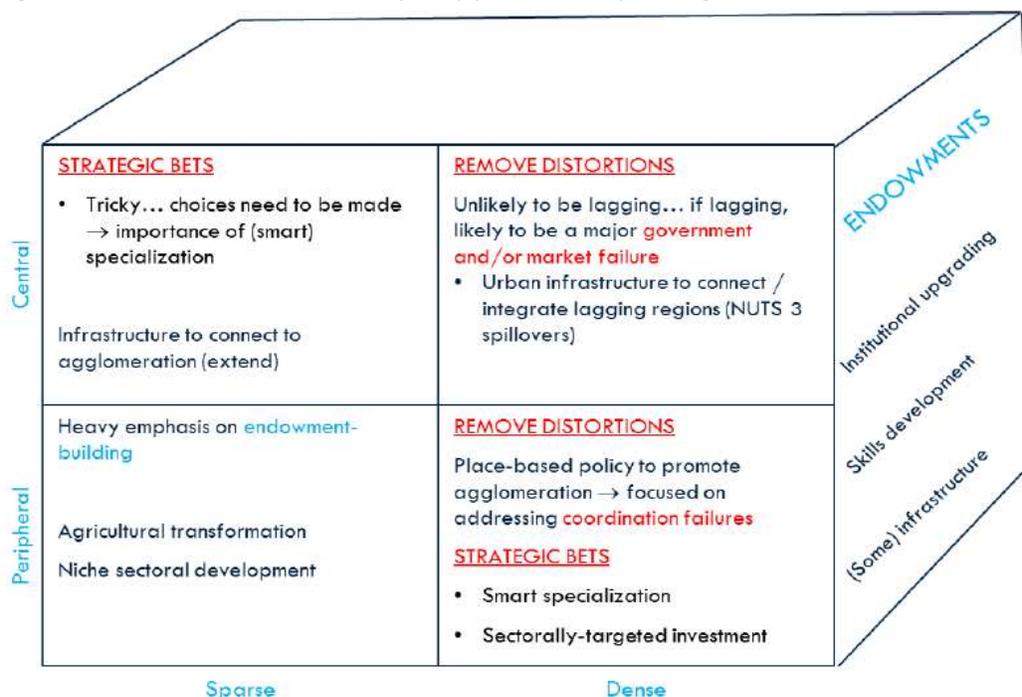
1.2.1. Policy approaches to address lagging regions – some general principles

Strategies to address the challenges of lagging regions around the world have often assumed (if implicitly) that all regions might follow similar development paths and reach similar income levels. This approach may result in limited development resources being spread evenly across locations, and in one-size-fits-all programs. A more effective approach recognizes that not all regions have the same development prospects and starts with the explicit objective of maximizing the *potential* of each region based on its unique capabilities (Barca, 2009; Farole, Goga, & Ionescu-Heroiu, 2018). This approach is complementary to national policies around poverty reduction or social protection systems.

Structural factors play a significant role in shaping regional potential. *World Development Report 2009: Reshaping Economic Geography* (World Bank, 2009) reflects this clearly with its focus on density (and the formation of urban agglomerations that drive productivity growth), distance (and access to market opportunities), and division (whether policy or other barriers undermine prospects for forming and connecting to agglomerations).

The focus on structural characteristics – in particular *density* and *distance* – can support the development of nationally informed and specific strategies. In Figure 10: 10, we set out a basic framework for approaching lagging regions. Density is related to the potential for urban agglomerations, distance to market opportunities and division to policy barriers that limit the prospect for forming/connecting agglomerations. The framework emphasizes building *regional endowments* (both territorial and individual endowments) through policies that are broadly universal, even if designed and delivered for specific location contexts. These are supported by *distortion-removing* policies – targeting government, market, and coordination failures in lagging regions with the highest potential – to maximize the effectiveness of place-based sectoral interventions (*strategic bets*).

Figure 10: General framework for policy priorities depending on structural characteristics of regions



Source: Farole, Goga, and Heroiu (2018)

1.2.2. The 3 Cs and diversified challenges and approaches

Policy makers can follow the basic principles of 3C (Concentrate, Connect, Capacitate). This will help to ensure inclusive growth across the portfolio of leading and lagging regions, tailored to the needs of individual regions. The challenges faced by the leaders (capital city regions, some secondary cities) and the laggards (sparse and peripheral or stagnating areas) require different policy responses for achieving inclusive growth. Lagging subnational regions should not be expected to be growth leaders and should first be empowered and well-resourced to provide services to the population. But even peripheral areas often have assets with a certain economic potential that are underused due to various constraints related to governance, market, or coordination failures.

Concentrate One of the main challenges for lagging regions in Serbia will be how to attract and retain the young workforce (high potential regions) and/or how to deal with population decline effectively (low potential regions). Rapid demographic decline intensifies the challenge of balancing service delivery with the high costs of provision in remote areas and there is a need to develop tailored “smart decline” strategies. Regional and national policies on lagging regions are particularly important to further functional linkages, bundle resources efficiently for investments across administrative boundaries and ensure the coordination of sectoral and place-based approaches.

Connect Connective infrastructure to cities nearby (through addressing the large gaps in intraregional connectivity, including the maintenance of secondary road networks) is also central to increasing returns in lagging regions and promoting economic inclusion. For more peripheral regions, the economic rationale for developing secondary road networks may be less persuasive, although there may be an equity argument for investing in rural roads to enable service delivery. Given the scale of outmigration in many

lagging regions, a priority for regional development strategies is to find innovative ways to ensure connectivity and service delivery to rural areas and consider opportunities to expand the railway network, which has proven successful in other EU countries or even surrounding municipalities that are close to international railway connections.

Capacitate Ensuring equitable access to high-quality public services is the most important priority for equipping individuals with key human capital and connecting them to opportunities, regardless of where they are born. Good governance at the local and regional level can play an important role in increasing local development and can be supported by a clearer definition of roles, functions and resources for sub-national governments (Kmezic and Dulic, 2018). Developing competitive, tradable sectors in lagging regions, may involve both facilitating foreign direct investment (FDI) and strengthening the local enterprise base. Ideally, these are complementary, with FDI bringing supply chain opportunities and new technologies that can help upgrade enterprises. Linkages to the agribusiness sector in surrounding municipalities and large companies need to be furthered for long-term development as well as an identification of competitive sectors with upcoming EU accession.

Table 3: The 3Cs policy formula for Serbia – a menu of spatially informed policy options

Note: Highlighted in green are functional linkages / investments across administrative boundaries

Examples of policy guidance for typologies of cities/regions	Capital cities and secondary city-regions	Small / declining regions	Low income sparse and peripheral regions	Low growth regions with agglomeration potential
Examples of municipalities / cities within these typologies of regions	Belgrade, South Bačka (Novi Sad), Niš	Zaječar	Raška, Jablanica, Pčinja, Topliča	Central Banat
CONCENTRATE	Invest in urban amenities to reduce congestion costs; improve land administration and management of assets	Prioritize smart decline strategies to avoid “overinvesting” (for example densification strategies)	Emphasize efficient investment in infrastructure and encourage spatially coordinated investments	Invest in urban infrastructure particularly in middle/secondary areas to maintain population and leverage regional endowments
CONNECT	Connect secondary cities with agglomerations and improve	Ensure a basic level of infrastructure and urban services	Close gaps in access to basic services; enhance connective	Connect cities with large agglomerations; promote local supply linkages with FDI in

	business environments and trade / value chain linkages		infrastructure with high expected returns; promote niche sectors with comparative advantage and reduce border frictions	value chains and promote entrepreneurs with linkages to knowledge networks
CAPACITATE	Address skill gaps and enhance entrepreneurial skills; enhance the dialogue between public and private sector; utilize local planning instruments and enhance own-source revenues or leverage private sector financing	Ensure quality foundational education and health; enhance the capacity of local governments to develop and implement smart decline strategies	Elevate human capital and endowments and encourage labor mobility; strengthen the capacity of local governments for financial management; ensure coordination of sectoral interventions and enhance capacity in selected niche sectors	Strengthen capacity for sector-specific skills and leverage regional universities; build local government for financial management and raising own-source revenues; increase regional coordination and encourage economic diversification

The table below compares two case studies that are analyzed in more detail in this note, illustrating the examples above of “low income, sparse, peripheral regions” and “low growth regions with agglomeration potential”. Central Banat case is described in more detail in section 2 on Boosting local growth, whereas more details on Raska can be found in the annex.

Table 4: Comparing a low income and low growth lagging region - Raska vs. Central Banat

	Raska	Central Banat
Location and main factors	Situated in South-west part of Serbia Population: 309.258 City of Kraljevo - administrative center City of Novi Pazar Municipality of Raska Municipality of Tutin Municipality of Vrnjačka Banja	Situated in North-east part of Serbia Population: 187.667 City of Zrenjanin - administrative center Municipality of Novi Bečej Municipality of Nova Crnja Municipality of Sečanj Municipality of Žitište
Main challenges faced for development	Major local financial constraints to support investment needs Inadequate investments in regional/local basic infrastructure – especially roads, water supply, waste management, for touristic areas Poor business environment with mismatch between workforce and needs of the labor market	Depopulation of region and brain drain Lack of coordinated strategies for regional economic linkages Inadequate investments into local infrastructure (city) supporting services and amenities that could attract a dynamic and qualified labor force Insufficient promotion of local businesses
Potential identified	Natural resources: ore and mineral deposits, forest potential; water, agricultural land Tourism potential with cultural and historical monuments, mountains etc. Metal industry (Kraljevo), wood processing and textile industry (Novi Pazar) SME development and connection with Faculty for mechanical engineering in Kraljevo and creation supply chain for FDI investments Housing programs in Raska municipality for young	Traditionally industrial region Agro-processing industry Tourism development potential (spa and rural tourism) Link better SMEs with large businesses (FDI) to further effective value chain development Investment in connective infrastructure and knowledge networks Human capital with young ICT entrepreneurs
Policy priority 1: Concentrate	Concentrate and coordinate investments in regional basic infrastructure such as roads, water supply, wastewater and waste management systems and enhance city livability.	Invest in the city infrastructure to attract human potential and leverage surrounding endowments
Policy priority 2: Connect	Connect people and businesses, promote sectors with comparative advantage such as metal and wood processing industry and promote effective labor migration	Connect ideas, people and businesses through linkages to agglomerations and knowledge networks
Policy priority 3: Capacitate	Capacitate the local economy through strengthening financial management of local governments, ensuring coordination of sectoral interventions and furthering skills development linked to job opportunities	Capacitate dynamism of the local economy through increased livability of a “magnet” city with enhanced service delivery and encouraged diversification

1.2.3. Building local and regional capacity for growth

The literature on regional and local economic development increasingly emphasizes the importance of local institutional capabilities and local coalitions for growth. General capabilities of multiple actor, including to build and sustain coalitions to articulate and deliver on growth strategies are crucial for effective long-term development (Crescenzi, 2005; Ramirez de la Cruz, 2009; Farole, Rodríguez-Pose, & Storper, Cohesion Policy in the European Union: Growth, Geography, Institutions, 2011). Developing competitive, tradable sectors in lagging regions, may involve both facilitating foreign direct investment (FDI) and strengthening the local enterprise base. Ideally, these are complementary, with FDI bringing supply chain opportunities and new technologies that can help upgrade enterprises. Cooperation at the regional level within Serbia and between municipalities is essential particularly to enhance sectoral and value chain linkages and ensuring that the incentives for FDI at the local level are not creating an unequal playing field for SMEs.

In lagging regions, coalitions for growth tend to be weak and unrepresentative. The Vojvodina region, for example, has been successful in creating ICT clusters and industrial zones and attracting FDI and in some cases the linkages with entrepreneurs could be furthered, such as in the city of Novi Sad, but further progress is needed to create linked production and services hubs such as in recent EU accession countries (Poland, Romania...). Although there are business networks cooperating with the local administration in Serbia, the inclusion of SMEs, universities and civil society in the development of strategies is low. Moreover, regional institutions are underdeveloped, are not aligned with political and administrative structures and do not operate within a clear national legal and institutional framework. This prevents the effective promotion of coordinated national sectoral investments at the regional/district level, inter-municipal cooperation as well as the promotion of cross-border programs in certain regions.

Enhanced spatial planning can support the development of productive linkages. As structural factors play a significant role in shaping regional potential, regional spatial planning can support sectoral coordination and enhanced connectivity for people and goods between lagging regions, agglomerations and external markets (World Bank, 2019). Spatial and urban planning requires improvement across all levels of Government - the national level, city level and at the municipal level, as well as improved coordination mechanisms amongst them (World Bank, 2020). Better aligning the spatial planning of different levels of government and different sectoral plans within cities would help ensure better, more efficient and accountable municipal management. Following the adoption of the Law on National Planning, bylaws have been prepared for the implementation on long-term and mid-term regional and local development plans.

Weak local and regional government capacity as well as financial constraints are preventing effective local investment to enhance livability and competitiveness in Serbia. Evidence from the World Bank's World Governance Indicators suggests that Serbia has substantial institutional weaknesses in both government effectiveness and transparency (World Bank, 2019). Capacity, particularly in management and financing, is low at the local level in most lagging regions (Milutinovic & Jolovic., 2010) as well as access to resources. This is an issue given the high reliance of the institutional structure on the capacity of local economic development offices in municipalities. This is also affecting the capacity for integrated urban planning and development (World Bank, 2020). While the government is tackling these issues and adopted a Sustainable and Integrated Urban Development Strategy in June 2019, greater progress is still needed.

The lack of resources at the local level is preventing an effective realization of their responsibilities.

Capacity, particularly in management and financing, is low at the local level in most lagging regions (Milutinovic & Jolovic., 2010) as well as access to finance (World Bank, 2019). This is a particularly pressing issue given local government responsibilities for infrastructure investments and attracting FDI in a limited capacity context. While local governments can generate their own revenue streams, low-growth lagging regions are at a disadvantage as they have a limited local tax base, which is why they tend to rely mostly on national government transfers. City governments however appear to have a weak financing base to be able to undertake large infrastructure projects and expand public services. Most of the discretionary revenues are used toward operational costs, subsidies and on servicing debt rather than on large capital investments on public infrastructure. There is a need for increasing own-source and discretionary finance, providing larger cities and urban centers with more authority to increase revenues, and access other forms of finance (PPS, capital markets) to increase investment in urban infrastructure.

Regional institutions can support the development of successful regional investments. The use of regional development institutions is common in the European Union, which allocates substantial resources along regional lines. Regional institutions can improve the identification of development needs and the coordination of service delivery and can support local government by coordinating across multiple local authorities. They also allow for investment in specific technical capacities that may be unavailable in local authorities. The most successful regional investments across countries in the EU have been in countries that have started building effective regional institutions before EU accession to be able to invest effectively and then scale up investments with cohesion funds. This has enabled to further economic linkages within and across regions within countries, such as for Poland.

While some regional capacities have been developed in Serbia, the approach to regional development remains centralized and top-down. Serbia has developed useful institutional capacity to support the regional development agenda, but important shortcomings in the approach to regional development may limit effectiveness (Manić, Popović, & Molnar, 2012).

First, regional development institutions do not always align with political and administrative structures and regional development authorities are formed by local stakeholders. While in theory these may be much better aligned with administrative structures (many are closely linked to city administrations), in practice most of the 16 accredited regional development authorities operate at the NUTS 3 level, for which there are no equivalent administrative structures¹⁵.

Second, regional development institutions do not operate within a clearly established national legal and institutional framework, with a clear national strategy for regional development. A Strategy for Regional Development for 2007–12 established the basis for Serbia’s regional program, but a new strategy was never adopted once it expired and plans to change the law never materialized. The regional strategy of Vojvodina expired around 2013 and there is only an Action Plan, with a strategy still to be drafted and approved by the provincial government. Most sectoral strategies included in the Strategies for Sustainable Development 2014-2020 of municipalities focus mostly on tourism development, while the potential in the region seems quite limited and where coordination would be most essential.

Institutional changes diluted the focus on regional development. The Development Agency of Serbia has been more focused on investment promotion than on regional development, yet they are still in charge of accreditation of RDAs and monitoring of their work. On the other hand, the Ministry without Portfolio

¹⁵ Regional development authorities (RDAs) cover one, two, or in a few cases three NUTS 3 regions. A few cover functional spaces across NUTS 3 regions, such as the Sandzak Economic Development Agency, which works from Novi Pazar; RDA Panonreg, from Subotica; and RDA for Podrinje, Podgorina and Rađevina, from Loznica.

in charge of regional development primarily focuses on support to agricultural cooperatives and support to the villages and small communities, while this lack of integrated sectoral strategies is at the core of lagging performance both at the city and district levels, as for example in Central Banat.

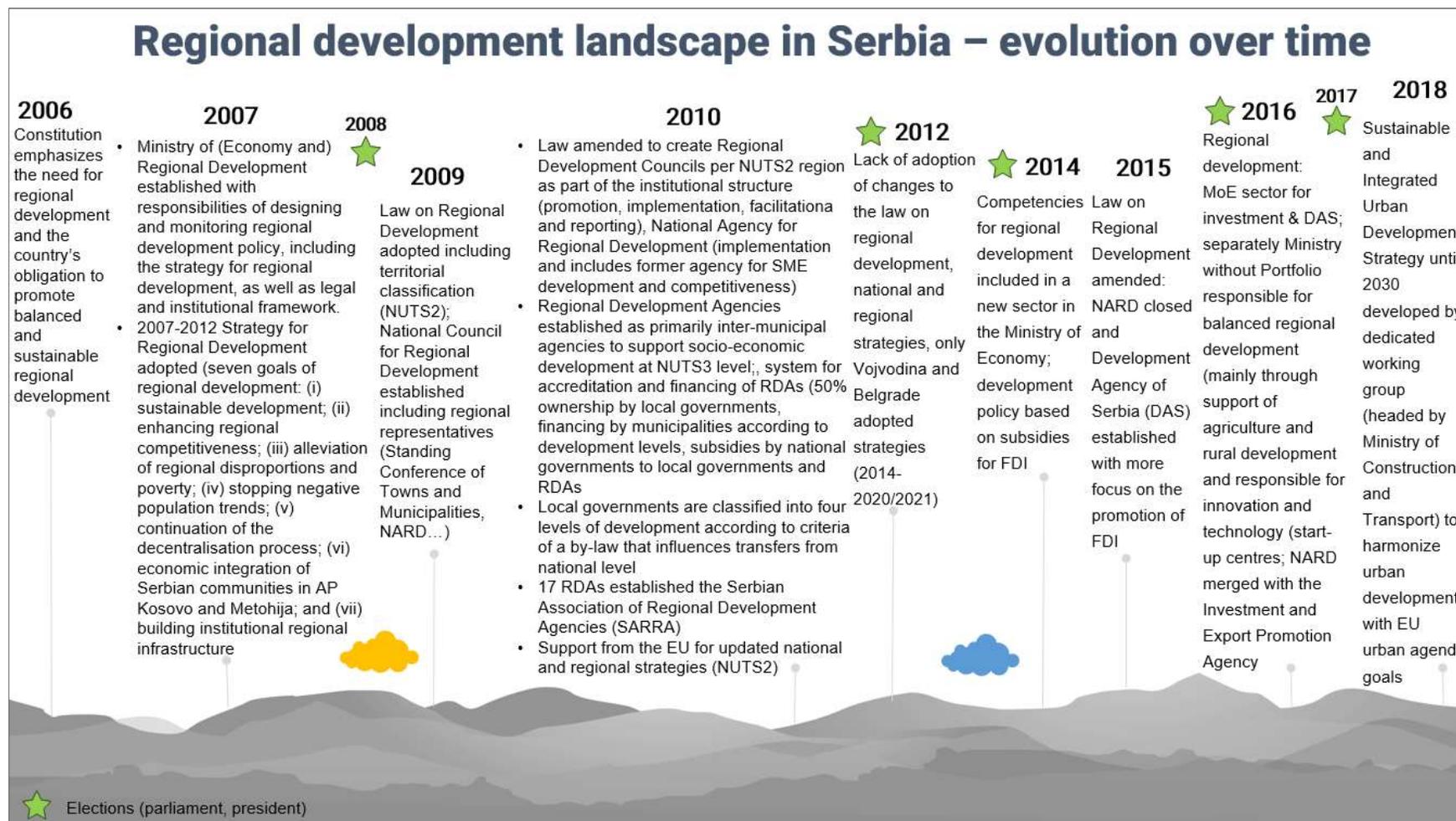
Regional funding and support schemes are misaligned with differentiated needs of lagging regions.

According to the law on budget 2015-2019, the total budget allocated for regional development across ministries was 5,23 billion RSD for 2019 (around 50 million USD), which represents around 0.4 percent of the new approved total planned expenditures for Serbia in 2019 (1269 billion RSD, around 12 billion USD). The budget allocated to the Ministry without Portfolio in 2019 is 13 percent of the budget of the Ministry of Economy for regional development. For the Ministry of Economy, the budget allocated for general economic and commercial affairs (including local and regional infrastructure, business zones, enabling business) was planned to decrease from 2015 to 2019 (1,98 billion to 1.74 billion RSD) and budget allocated to balanced regional development also since 2016. Incentives for regional development were in 2013 mostly to encourage employment (29 percent), encourage agriculture (52 percent) and traffic infrastructure (12 percent), with less support for communal infrastructure or for education, science and culture except in 2012. Incentives were mostly non-refundable subsidies and for agricultural holdings (number and amount) as well as large companies (amount). This emphasis of funds would clearly be an impediment for the economic transformation of Central Banat and in general low-growth lagging regions, which are in dire need of investment into higher value-added activities and particularly R&D.

Third, regional development agencies have recently been integrated into organizations with a wider remit, an organizational change that brings both opportunities and risks. In Serbia, as of 2016, the National Authority for Regional Development was merged with the Serbia Investment and Export Promotion Agency to establish the new Development Agency of Serbia. The effect has been to further decentralize the activities of regional development authorities, but at the cost of a loss of influence given the generally stronger role of local governments in Serbia. Moreover, the reorganization has pushed the orientation of regional development toward a narrow focus on attracting investment.

The result is that regional development authorities play a limited, largely technical role in regional development. They help local authorities prepare projects (including project proposals for cross-border programs) and contribute local knowledge about access to financing. In Serbia, evidence suggests that, at least in some regions, regional development authorities have also helped local authorities prepare development plans. However, they tend to lack the authority (and the resources) to deliver comprehensive regional development plans and funding to support implementation is limited.

Figure 11: A chronology of the regional development landscape in Serbia (2006-2018)



2. Boosting local growth: the example of Central Banat district

2.1. A region lacking capabilities and dynamism

Central Banat district has experienced lower growth rates within a generally dynamic region (Vojvodine). Possible reasons for this underperformance will be outlined in the next sections as well as possible avenues for strategies and policies to maximize the potential of the district, its main city Zrenjanin as well as surrounding municipalities. This section will show that the main potential for Central Banat lies in i) raising the livability of its main city, focusing resources on the development of emerging innovative and dynamic sectors, ii) increase physical and digital connectivity with major agglomerations to ensure productive knowledge and trade linkages within the country and cross-border and iii) enhance inter-municipal cooperation and sectoral coordination to ensure effective, targeted and financially viable investments in infrastructure.

2.1.1. Overview

Central Banat district is situated in the north-eastern part of Serbia or eastern part of the autonomous province (region) of Vojvodina. Vojvodine represents 27 percent of the Serbian population and that includes the second-largest city in Serbia, Novi Sad (270,000 people). Central Banat covers the territory of the city of Zrenjanin (seat of the administrative district) and the municipalities of Sečanj, Žitište, Novi Becej and Nova Crnja. Its population was around 176,000 people in 2018. The region abounds in watercourses with water management significance (the rivers Begej, Stari Begej, Begejski kanal, Tisa, Tamiš and Kanal DTD). More details on municipalities of Central Banat can be found in Annex 1.

The qualitative insights below are mostly based on results from a field study undertaken during a World Bank mission in December 2018. During the mission, the team met with representatives from ministries, local governments (municipalities of Zrenjanin, Nova Cnja, Žitište, Sečanj and Novi Becej), business associations, regional chamber of commerce, regional development agencies, start-up incubators and civil society to understand challenges and potential in the case study district of Central Banat (Srednjobanatski), Vojvodine region.

2.1.2. Economic context and general challenges to develop a dynamic Central Banat

Central Banat is part of a region, the autonomous province of Vojvodine, that has been performing above the national Serbian average in terms of GDP per capita compound annual growth rate during the past ten years . Vojvodine has historically been a leading region within Yugoslavia (Milanovic, 1987) and also during the high growth period for Serbia 2000-2008. The region is also known for being the major attractor of foreign investment in Serbia apart from Belgrade.

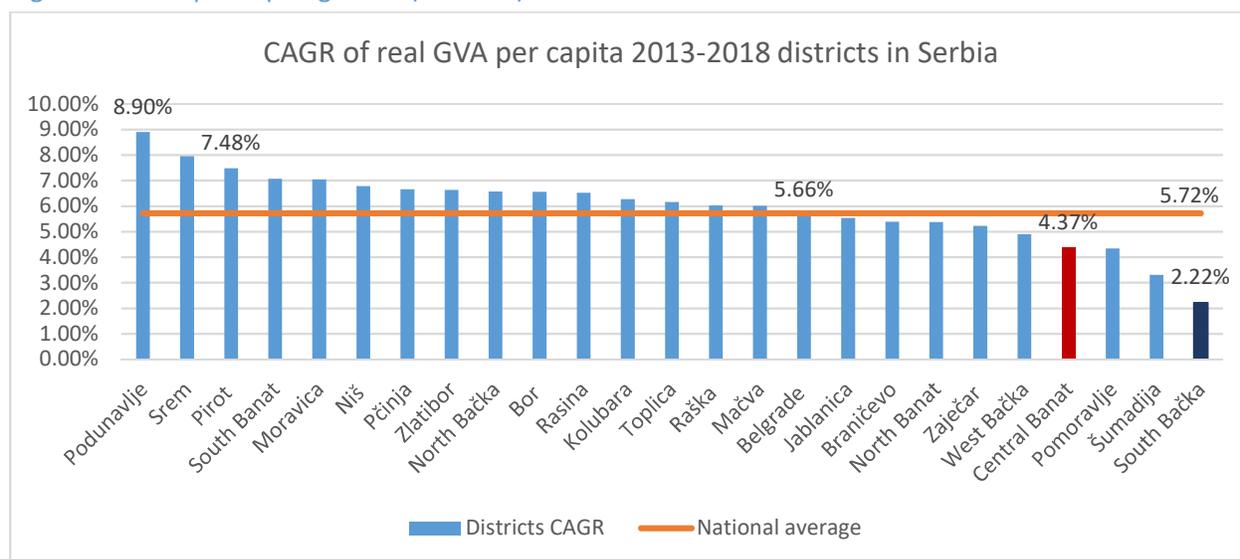
Central Banat is a relatively high-income region in Serbia based on Gross Value Added¹⁶ compared to other districts. With a GVA per capita in RSD in 2018 at 530,927, Central Banat is around 88 percent of the national average and ranks 9th among 25 districts. Central Banat has historically been successful economically. It was the third largest industrial center in Yugoslavia and is still one of the largest agro-

¹⁶ Statistics for GDP are only available by regions 2010-2018. GVA data is available by districts 2013-2018.

industrial centers in Serbia.

Central Banat suffered a collapse at the beginning of the new millennium and continues to lag behind in terms of growth compared to other districts. Its real GVA per capita growth was the fourth lowest among all districts 2013-2018, amounting 2.2 percent compared to an average rate of 5.7 percent across Serbia (Figure 12). It has to be noted that the timeframe is short and that most of the faster growing regions have been starting from lower bases. General slowing of national growth and multiple factors may interplay to explain the sluggish growth of the district. But the fact that Central Banat is performing poorly on other development indicators may support the hypothesis that this lagging behind is not only a short-term phenomenon.

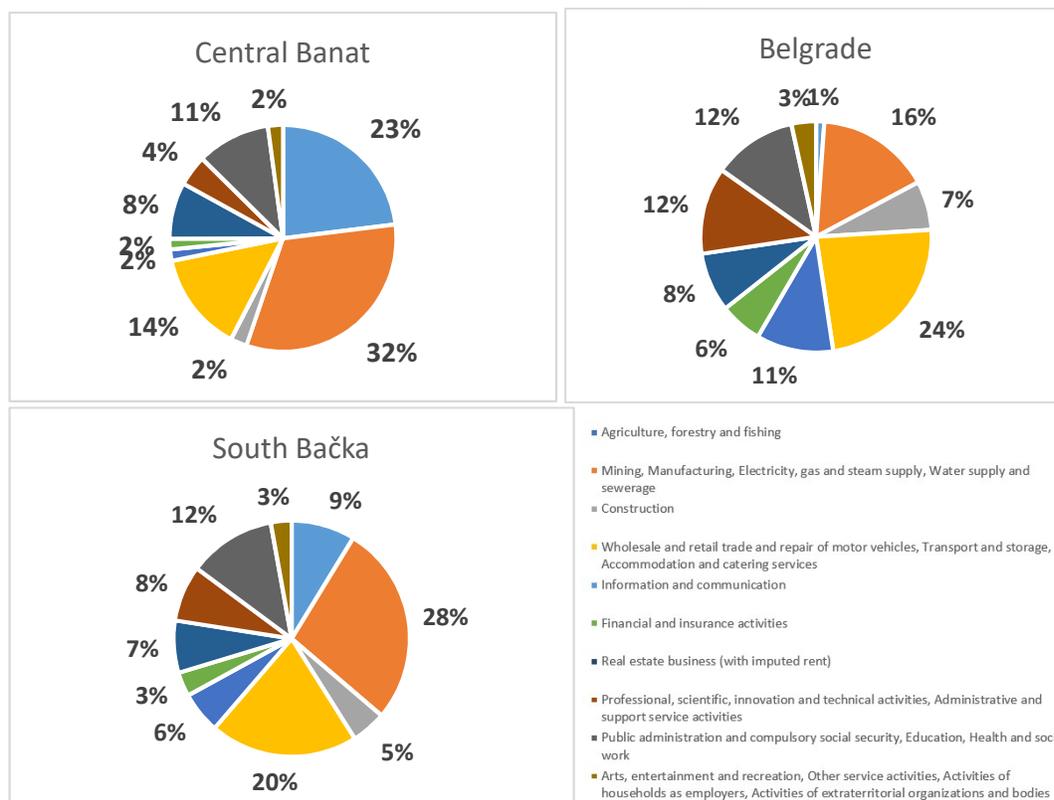
Figure 12: GVA per capita growth (2013-18)



Economic transformation is an essential feature for more advanced local economic development. It can be of particular importance in low-growth areas that need to further the transition from an industrial hub past to a more diversified model. However, foreign directors and local entrepreneurs face in general different challenges for business development. Strategies to attract them may not always be complementary and can sometimes become detrimental to one type of investor.

The situation for lack of economic transformation is somewhat different in low growth than in low income lagging regions, although some of the symptoms are the same. Low growth regions like Central Banat often have an established (and often export-oriented) industrial base that is struggling to maintain competitiveness. Moreover, they tend to have a less diversified economy and less based on higher value-added activities than leading regions.

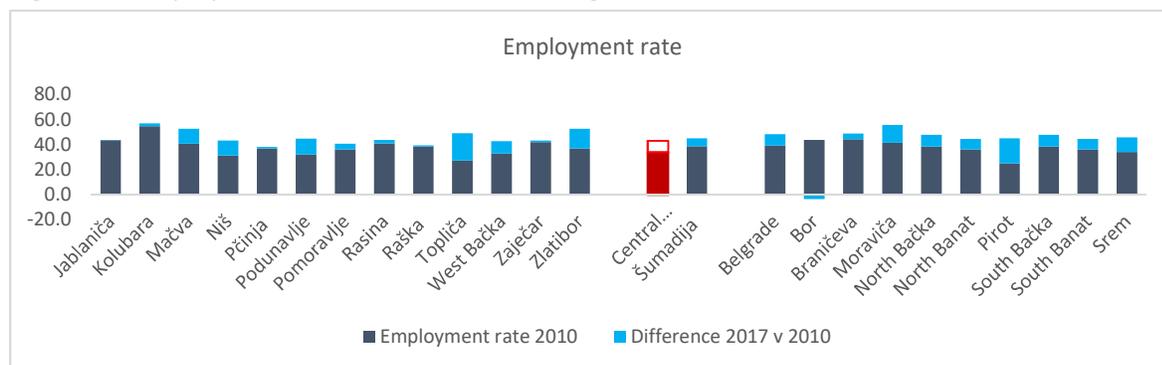
Figure 10: Gross value added by sectors: Central Banat, Belgrade, and South Bačka (2018)



Source: Based on data from national statistics office

Central Banat’s economy is much less diversified than in other dynamic regions. Around 70 percent of Central Banat’s GVA is in agriculture, mining and manufacturing or wholesale and retail while in Belgrade this is at around 40 percent. In Central Banat 16 percent of activities are in IT, finance and insurance, real estate or scientific/technical activities compared to 37 percent for Belgrade and 24 percent in South Bačka district comprising Novi Sad. The district’s employment rate is low (43 percent, ranking 18th among 25 districts), and has increased only slightly between 2010 and 2017 (Figure 14). The poverty rate- at 29 percent - is also still high, ranking 12th among districts.

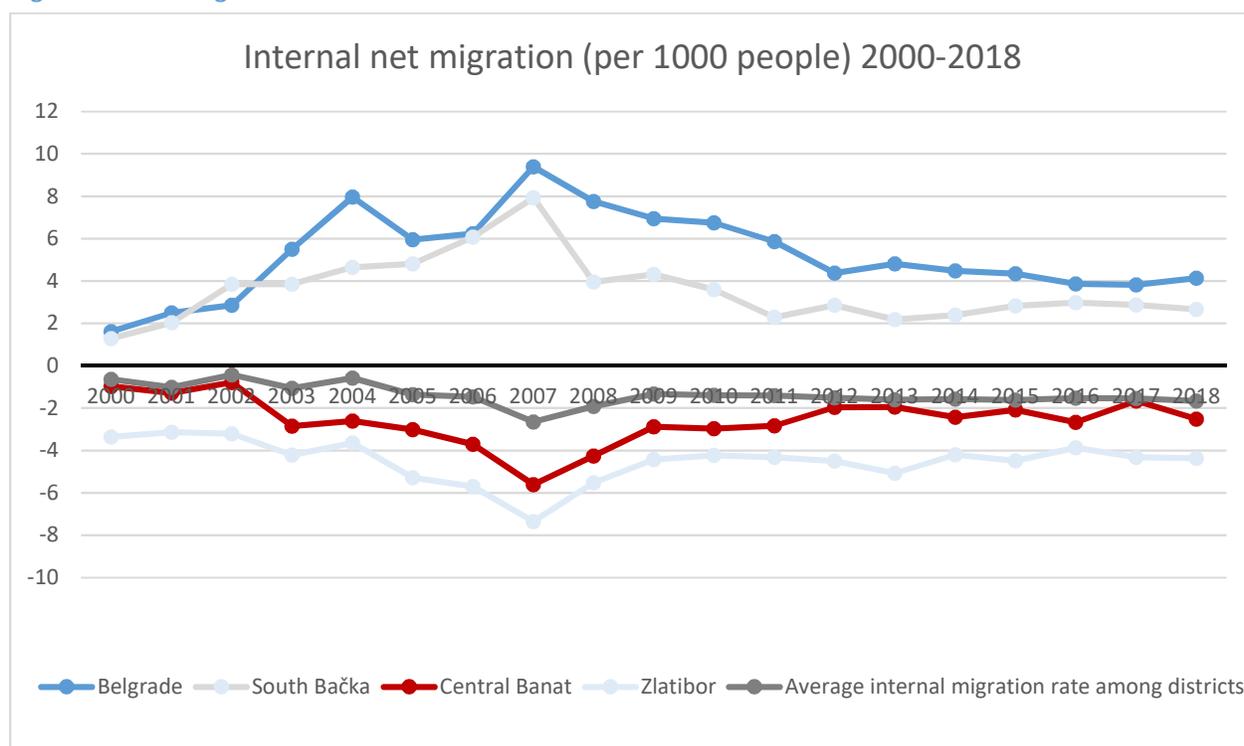
Figure 11: Employment rate and trends across regions (2010-17)



Source: National Statistical Office

Demographics are both a cause and a consequence of Central Banat’s economic challenges over recent decades. The population fell by an average of 8 percent over between 2010 and 2018 (and by 19 percent between 2000-2018). This is broadly in line with trends across Serbia, where population increased only in three districts over the last decade – Raška, Belgrade, and South Bačka. Central Banat has also experienced an overall negative net migration over the past two decades compared to districts like Belgrade or Zlatibor and constantly under the average of all districts (Figure 1215). The negative net migration was mainly driven by rural municipalities, which have experienced a negative net migration of more than 2 per 1000 people compared to 1 for Zrenjanin. Given the high negative net migration of surrounding municipalities and Zrenjanin it has to be asked why the city has not managed to attract people in close proximity and beyond.

Figure 12: Net migration trends



There are structural factors in Central Banat that may explain why the district has been underperforming compared to its potential. Its main city Zrenjanin has not yet managed to transition to a future-oriented knowledge and production center surrounded by municipalities focusing on agro-processing and tourism. These factors will be outlined in more detail in remainder of this section and include: i) missing inter-municipal and coordinated sectoral investments, ii) lack of connective infrastructure and knowledge networks and iii) missing development of local endowments and low livability of urban environments.

The analysis aims to differentiate, wherever possible, between factors preventing the main city Zrenjanin to flourish and those holding the surrounding municipalities behind. The municipalities surrounding Zrenjanin are characterized by a high number of unemployed people (mostly unskilled and with a high representation of minorities), lower average incomes (around 75-85 percent of Zrenjanin average), higher shares of social welfare beneficiaries, poor access to public services (historically bad water quality), a low level of entrepreneurial activity (and mostly connected with low-value added, agriculture-related activities), and high outward migration (mostly to Novi Sad, Zrenjanin and EU countries

especially for minorities who own passports). The population is mostly engaged in agriculture and related activities, small or informal services (for example repair of motor vehicles) as well as in the public sector. Many work in large factories in Zrenjanin and Kikinda.

2.1.3. [Specific challenge 1: Missing inter-municipal and coordinated sectoral investments](#)

As part of a low growth area, municipalities in Central Banat should be coordinating on most efficient investments and bundling resources to reap the limited agglomeration benefits around Zrenjanin. They should also enhance the common usage of natural resources and investments to raise public services such as water quality or public transport for commuting. There are two main factors preventing the coordination of strategies and investments, namely 1) the lack of regional development institutions with a mandate to further integrated investments across administrative boundaries and 2) institutional and financial constraints to fulfill local investment needs.

RDAs support inter-municipal cooperation only in limited ways and particularly in “small and devastated villages” (of which none in Central Banat). Cross-border cooperation is only supported by specific projects (such as a regional center for tourism in Nova Crnja or prevention of floods and environmental protection in Novi Becej) but not in a strategic, coordinated way with an Action Plan. This would seem particularly important given that the municipalities cross to the border in Central Banat are lagging most behind. Moreover, FDI is not the responsibility of RDAs but of the National Development Agency with local governments (local economic development offices), which may have the advantage to further locally relevant projects but bears the risk of non-coordinated investments and a type of competition among local governments that may be harmful in the long term.

Linkages to major agglomerations could be strengthened. In Central Banat, there would be a clear need for coordination in the district between Zrenjanin and surrounding municipalities (public transport for labor force and commuting possibilities, common investment in water infrastructure and access to regional and EU funds etc.) but also establishing stronger connections with Belgrade and Novi Sad. The linkages to Belgrade and Novi Sad could be furthered particularly in the areas of economic specialization, investment into R&D and knowledge networks of universities to further a productive triangle.

The role the RCR Banat can play is limited by its mandate. The Regional Center for Socio-Economic Development - Banat (RCR BANAT) is a regional development institution, accredited in 2011 by the Development Agency of Serbia in accordance with the Law on Regional Development of the Republic of Serbia. It is established as a semi-private company as founders are municipalities from the region (50 percent is public ownership) but funding is 25 percent from membership fees and 75 percent from projects (mainly EU CBC co-funded). The RCR is covering five local administrations including one in North Banat. The main goal of the RDA is to provide standardized services to its members and the SME sector with financial support from the NDA, policy recommendations and action plans as well as technical support to SMEs and local governments (local economic development, social inclusion, tourism...).

Although the RCR Banat has been supporting municipalities effectively, the role played has been insufficient to ensure effective common investments particularly in services or infrastructure that would enhance functional linkages between urban areas and surrounding municipalities. Working on the promotion of the region as well as its development, RCR BANAT, in partnership with founders and all relevant institutions, since its inception (2002) to date, implemented over 100 projects financed from international and domestic sources of financing and attracted more than 20 million euro. Its role is to determine the key priorities of Banat development, to support local self-governments in strategic planning, positioning and improvement of technical and logistic capacities for the realization of local development programs and provision of services, promotion and strengthening of the institutional

framework for the development of MSMEs and entrepreneurs in the region, identification, preparation and implementation of projects that contribute to the development of infrastructure as well as strengthen the business and human base and help the region to become more innovative.

Moreover, while local governments can generate their own revenue streams, low-growth lagging regions are at a disadvantage as they have a limited local tax base (exacerbated by property rights issues limiting its potential), which is why they tend to rely mostly on national government transfers. In Serbia, local functions are largely confined to infrastructure and the largest source of finance is the personal income tax. Issues mentioned above of decreasing disposable incomes, large outmigration, constrains to labor mobility and rising informal sectors could indicate a need to increase the share of other sources of discretionary revenues to ensure the ability to cover infrastructure investment needs alongside social services such as education. This is particularly the case in a place like Central Banat where furthering the emerging entrepreneurial sector would be essential also by reducing the potential heavy tax burdens for freelancers or SMEs.

Gaps in service provision could be due to fewer resources, less efficient spending, and less effective local institutions in some locations. Investments in new capacities only made up 20 percent of total investments in Zrenjanin in 2011 (compared to 60 percent at the republic and provincial levels) and investments per capita reached 40 percent of national average in 2011. Moreover, population density has an impact on the cost of service provision and in Serbia densely populated municipalities have higher levels of income, lower rates of poverty and have slightly higher population growth rates or slower population decline. In Zrenjanin, 41 percent of the population is over 50 years old and 70 percent of the population is of working age so that strategies for managing ageing places would need to be considered (examples of smart responses to city decline can be found in Chapter 1 of the upcoming Western Balkans and Croatia Urbanization and Territorial Review 2019).

The strategy of Zrenjanin describes several factors preventing effective and sufficient investment in infrastructure. This includes a lack of financial resources for reconstruction, insufficient functioning of public enterprises¹⁷ particularly for maintenance and poor technical and technological equipment of public utilities. The issue in Zrenjanin is that infrastructure is generally well-developed but has been built for the highest level of services that is costly and difficult to maintain, so that often replacement is or seems the only option. Poorer localities such as Novi Pazar managed to achieve greater than average outcomes, while some localities that are not as poor have weaker service provision outcomes. This variation suggests that factors other than local income level can strongly influence basic service provision.

Finally, the capacity of local governments and other stakeholders to form cohesive, sustainable coalitions for local economic development varies. In lagging regions, these coalitions tend to be weak and unrepresentative. Although there are business networks cooperating with the local administration in Serbia, the inclusion of SMEs, universities and civil society in the development of strategies is low.

2.1.4. [Specific challenge 2: Lack of connective infrastructure and knowledge networks](#)

For secondary cities with the potential to be regional growth poles, a short-term priority is to ensure adequate infrastructure to support private investment and enable opportunities for commuters. Capital

¹⁷ Zrenjanin has seven public utility companies or enterprises, including the public utility company "Vodovod i kanalizacija" for water and sewerage. Public utilities are managed by local governments and operate solely in their jurisdiction. There is no competition for municipal services with linked low incentives for efficiency.

stock is low and declining in Serbia as across the Western Balkans and Croatia (World Bank, 2017). Combined with land rights issues, which are particularly pronounced in Serbia, lack of infrastructure is a major impediment to private investment.

The impact of improved connectivity depends on mobility capacity and conditions. For sparsely populated central regions like Central Banat, improving connectivity with large agglomerations can open opportunities for product and labor market integration. At present, the region's market access is relatively good, although remains significant scope for improving connectivity. A modelling analysis showed that improvements in roads and reduction of border frictions could have substantial positive impacts on real wages (World Bank, 2019). Adding improvement of amenities, it would seem that there could be a population increase in Central Banat. Moreover, there is a lack of connectivity with other major agglomeration and development of public transport for linkages with surrounding municipalities.

In terms of mobility, in Central Banat, lack of access to good job opportunities already pushes many skilled youth to migrate to Novi Sad or abroad. Despite rising employment opportunities in Zrenjanin, brain drain is increasingly becoming a problem, with a likelihood of being exacerbated with EU accession. The unattractiveness of jobs and low wages (Figure 16) compared to costs of living are some of the factors contributing to it. In fact, young people are said to prefer activities as IT freelancers for foreign companies (no taxes) and managerial rather than manual or vocational jobs (also linked to the historically less well perceived vocational schools). On the other hand, the workforce with lower levels of education that could potentially benefit from work in the industrial sector appears to be less mobile. This is in line with overall observations of low labor mobility in Serbia compared to other transition economies: the share of people who moved internally was below 30 percent in Serbia (EBRD, 2016a), with most migration being rural to urban and urban to urban, most migrants young men and with a high asset index (EBRD, 2016).

Beyond having a population with a good foundational education, a critical element in the competitiveness of regions is the availability of sector-specific skills. Across the Central Banat district and beyond, one of the biggest challenges is seen as the future of available workforce given loss of / ageing population and skills mismatch. Vocational programs and technical schools are often under-resourced and with outdated curricula, which impart skills that are mismatched to labor market needs. The latest World Bank's Skills Measurement Employer Survey suggests that the skill mismatch is still large in Serbia, although low compared to other countries in the region.

This is particularly important as the majority of unemployed people in Central Banat are unskilled (education premium is high) and are of middle age. In Zrenjanin, on the other hand, more than 52 percent of unemployed people are skilled or with higher than secondary education, which shows a mismatch beyond simple level of education. Zrenjanin has two technical faculties with more than 4,000 students (one being from, the University of Novi Sad) and several technical colleges / high schools including for medicine and agriculture, but development is not sufficient to ensure appropriate education for the workforce matching changing needs. In fact, changing skills requirements such as increasing need for social skills or time management require an emphasis on education quality and appropriate curricula beyond technical skills.

Skills mismatch, a lack of suitable employment opportunities to attract qualified young people, and low flexibility of the labor force are some of the factors explaining a low performance on employment¹⁸. While low income regions tend to face structural labor market challenges, including heavy reliance on

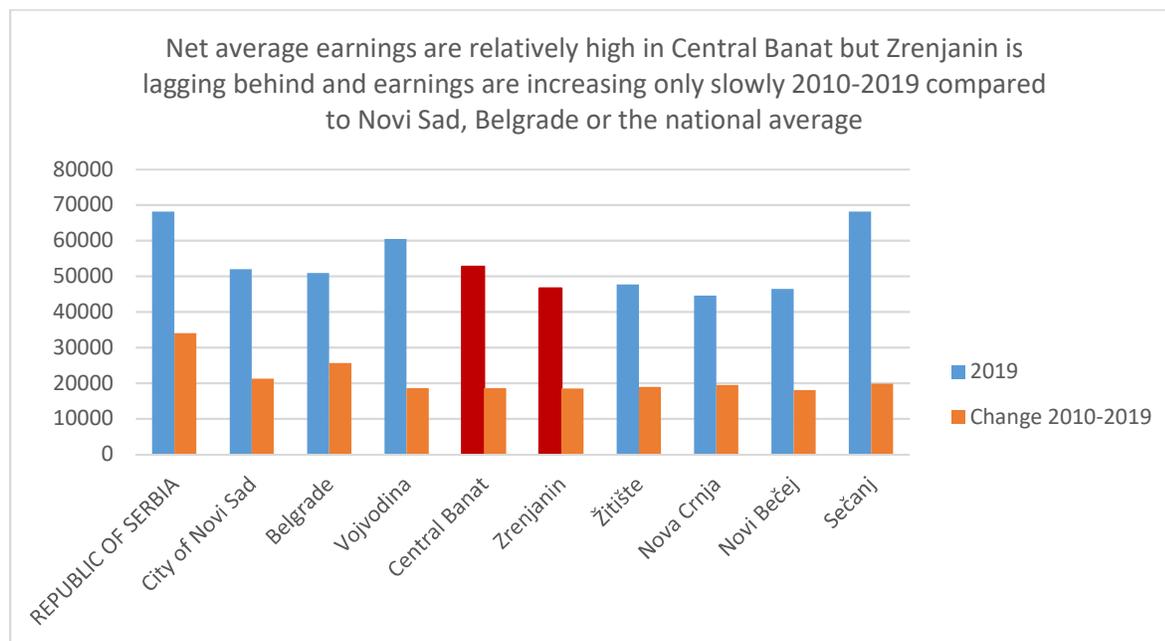
¹⁸ It has to be noted that apparent decreases in unemployment that can be observed in the data in Zrenjanin are mostly due to a change in accounting factors rather than a real decrease.

self-employment, low growth regions like Central Banat face both cyclical and structural challenges, including high levels of youth and long-term unemployment. Employment growth over 2010–17 in low growth regions trailed the rate in low income regions by one-third and that in leading regions by two-thirds.

Furthering only physical infrastructure would be unlikely to address the challenges faced in the district.

Therefore in addition to the question of physical connective infrastructure, there is a need to consider 1) knowledge networks and coordinated educational strategies across administrative boundaries (including cooperation with the private sector for vocational education), 2) digital connectivity and 3) reducing barriers to mobility particularly for the potential industrial workforce. In addition to attracting the workforce from villages surrounding Zrenjanin and enhancing the digital and knowledge networks to enhance the niche specialization for the city in terms of university research, it would therefore be essential to identify the factors that could keep the young workforce in the region or reduce barriers to labor mobility. This will require more research as the current data on internal migration in Serbia yields insufficient details for advanced analysis.

Figure 13: Net average salaries and change in net average salary in Central Banat and select regions / cities (2010-17)



Source: Based on data from national statistics office (DevInfo)

2.1.5. Specific challenge 3: Missing development of local endowments and low livability of urban environments

A recent study confirmed earlier indirect findings that leisure amenities or “beauty” of the city are related to urban development and economic growth (Carlino & Saiz, 2019). An assessment of secondary city performance in Romania shows that the main growth poles outside of the capital city¹⁹, with productivity around double the regional average, function as “magnet cities” (Cristea et al. 2017), attracting migrants from the regional hinterlands, even though it has to be noted that Romania shows a

¹⁹ Braşov, Cluj-Napoca, Constanţa, Craiova, Iaşi, Ploieşti, and Timişoara

clear premium for city size in both productivity growth and potential for generating spillovers to the hinterland.

Zrenjanin and surrounding municipalities have faced numerous challenges in terms of service delivery.

In terms of infrastructure, the most important is the quality of drinking water, maintenance of buildings, local and regional roads but also general waste treatment and other environmental factors that are at risk. Quality provision of services is essential both to raise individual endowments, for health and safety purposes and to attract innovators, highly educated people and young entrepreneurs who may have a broader choice of location for their activities both abroad and within the country. This is in addition to general impediments for entrepreneurial activity faced in the area.

The city of Zrenjanin is the densest river hub in Europe, represents an important ecological corridor and is often called “the city on water”. It has several national parks with high diversity of birds and species (including one on the Ramsar list). Unfortunately, water and wastewater management has been a problem for the past 50 years and numerous analysis have been undertaken to find solutions as well as works undertaken to resolve the issues. The quality of underground water is compromised, costs of exploitation are high (due to network losses, large distances and low reliability of waterwork systems and monitoring) and there are no reservoir spaces or wastewater treatment plants. In Vojvodina, aquifers contain high concentrations of arsenic and a study found in 10 municipalities in Serbia that 63 percent of water samples exceeded Serbian and European standards for arsenic concentration in drinking water, there are large variations in arsenic among supply systems (D. Jovanovic, 2011) and a high presence of methane and other gases in the network, with numerous connected health problems and safety hazards.

Central Banat was ranked in 2017 16th (from 25) with 47 percent of households only connected to the urban wastewater system, although in terms of water supply it was ranked 7th with 86 percent of households connected in 2011. This shows strikingly the issue with quality of water rather than access. In Zrenjanin tap water is still not drinkable - the use of water for drinking and food production has been banned in Zrenjanin and neighbouring settlements since 2004. Moreover, wastewater may cause problems for the prevalent agricultural system, ecosystems but also for health and tourism activities connected to the spas as the aquatic systems are being polluted. Finally, frequent flooding since the 18th century may exacerbate environmental issues in addition to substantial economic costs, which would necessitate adaptation measures: in 2006 floods caused around 43 million USD and Central Banat was one of the most affected areas with 42000 ha under water.

There are a number of other issues affecting livelihoods and business in the district. There is a poor supply of electricity and broadband, which affects industry and services sectors (Zrenjanin had the worst electricity supply in Vojvodina in 2012). The density of the road network in Zrenjanin and Central Banat lags behind the average of the Republic of Serbia (0.28 for both entities compared to 0.51 national average) and the existing road network, particularly linking to other main Serbian and foreign cities needs to be maintained or expanded. There has practically been no investment into the railway infrastructure although the spatial plan foresees the expansion of the railway network. Zrenjanin also faces a number of issues around urban decay, with an abandoned art-nouveau brewery in the heart of the city that closed in 2002 after a privatization deal, an abandoned old nunnery close to the Town Hall or “a bridge over nothing” that was built in the 1960s but lost its river in the 80s due to the construction of an artificial lake. Moreover, Zrenjanin is listed as one of the areas with lowest forestry levels in Europe and increasing industrial activity as well as congestion may cause increased air pollution in the future.

In addition to the low livability of the city to attract people and businesses, there are a number of specific barriers to local business development and economic transformation. The combination of these

factors yields the risk for a continued low-growth path for Central Banat with little dynamism and sustainable growth often provided by local business establishment, particularly when linked to high value-added global value chains (including in the services/IT sector).

While building dynamic small and medium-size enterprises is typically the aim of interventions through enterprise-level programs in lagging regions, gaps in financing, technology, and market connections remain formidable barriers. These obstacles are compounded by a lack of scale and access to skilled labor or resources for R&D and innovation. In the agricultural sector, the fragmentation of holdings, ageing households and low level of processing capacities are some of the barriers to incentivize agriculture. Moreover, the incentives for FDI have created an unequal playing field with SMEs and lack of value chain linkages may have slowed down the development of enterprises (Aničić, Laketa, & Vukotić, 2011). Foreign investors benefit from a number of incentives from local, provincial and national governments such as regulations (taxes, fast licensing etc.), infrastructure (circle road for the city), public service provision and dedicated workforce. By law, local businesses would in theory have the same position as foreign investors but in practice their previous investments are not considered and financial incentives are only available for investments that are higher than 1 million € or tax incentives (return on investment) only for investments higher than €10 million. The impact of these subsidies has not been evaluated so far.

Historically, Zrenjanin has been a city with low levels of entrepreneurship. This is compared to places like Srem, Indjija or Stara Pazova – an industrial center that housed very large companies during the socialist period. Calls for applications from the national development agency and regional agencies for training and support received few application from local SMEs in the past, which may confirm a lack of dynamism in the sector, lack of independence or inadequate offer of support.

Central Banat has had relative success in attracting FDI through targeted efforts to overcome investment constraints. Between 2007 and 2013, there were more than 150 million Euro worth of investments from domestic and foreign companies. However, success in leveraging dynamic gains from FDI through supply chain links and spillovers of knowledge and technology has been elusive for Central Banat. The region risks getting locked into a role as a low-wage, low value-added location, with the risk that footloose investors may shift locations if the availability of cheap labor dries up (whether because of rising wages or, as is already happening, because labor supply limits are reached).

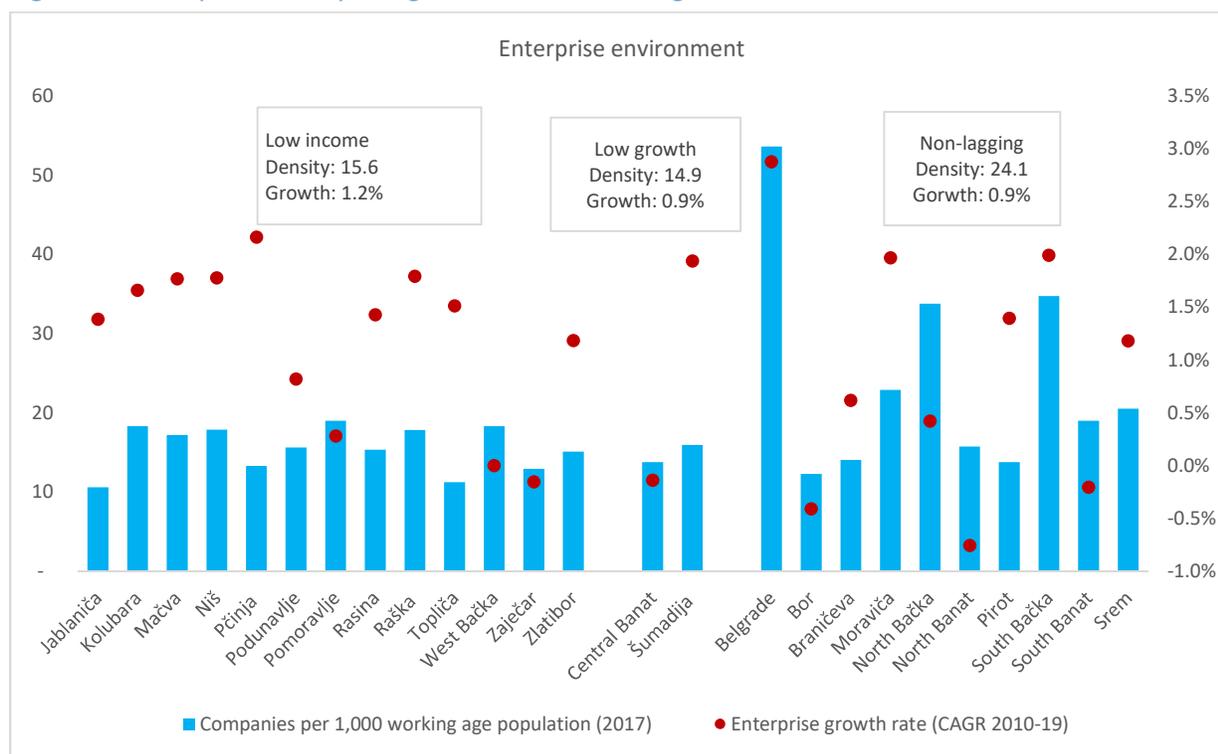
Zrenjanin has attracted manufacturing investment by developing industrial parks (two industrial zones and one free-trade zone on 2000 ha of land) and supportive infrastructure. It started in 2008 as an initiative by the chamber of commerce and the former mayor (now Minister of Economy) and is now a city-owned project. Dräxlmaier first invested in 2007 in the production of wire harnesses for automobiles, then expanded in 2017 with an additional 3000 jobs with now in total 6400 employees in Zrenjanin. Essex Europe, a South Korean copper wires producer, established a plant in 2018 and will employ at the beginning 170 people. Investment of up to €1 billion is anticipated from a Chinese rubber factory with more than 13000 jobs created. This has had a large spillover effect on rural parts of Central Banat—for example, the Dräxlmaier plant (a German wire harness manufacturer for automobiles) outside Zrenjanin is the largest employer for most of the surrounding municipalities. Yet the region struggles to retain skilled youth, whose exodus has contributed to skills gaps and anemic entrepreneurialism.

For regions like Central Banat, reliance on established manufacturing sectors, often with very large enterprises, contributes to constraining the establishment and growth of new firms, so firm density remains low. At the enterprise level, low growth regions have fewer established firms, with a density of 15 compared to 24 for non-lagging and equal enterprise growth rates despite starting from lower bases (0.9 percent) (Figure 17). Central Banat has experienced a relatively low enterprise growth rate in past

years and the number of enterprises per 1000 working age population is still 26 percent of Belgrade’s and 40 percent of South Bačka’s (district of Vojvodina comprising Novi Sad). This may also be due to a high share of informal productive activities: in Zrenjanin, only 11 percent of entrepreneurs submitted reports to the Business Registers Agency in 2012 and the trend has been rising in recent years, which matches observations from stakeholders of rising chosen informal activities beyond agriculture especially for younger people (i.e. freelancing in IT). Moreover, large productivity gaps are barriers to firm competitiveness. Enterprise-level data for Serbia indicate that average labor productivity is more than 10 percent lower in low growth regions than in non-lagging regions. Central Banat’s average firm productivity trails that of Belgrade’s by nearly 40 percent and South Bačka’s by nearly 50 percent.

Overall, to ensure a dynamic development of Central Banat with Zrenjanin at its center, there would need to be much more focus on policies and investments to enhance the livability of the city and enhance business environments linked with regional and national sectoral policies to create a dynamic knowledge and entrepreneurial hub. This would be in addition to national and regional policies to enhance business environments and access to finance particularly for SMEs and start-ups.

Figure 14: Enterprise density and growth rates across regions



Source: Based on data from national statistics office; spatially disaggregated working age population data was only available until 2017

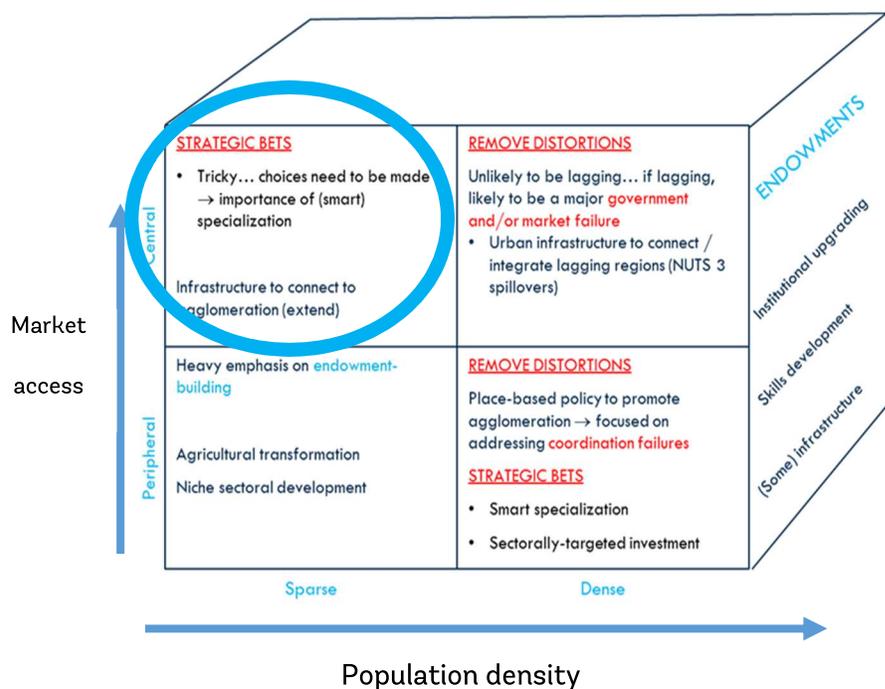
2.2. The 3 Cs policy formula contextualized to Central Banat

Central Banat is categorized as being relatively sparsely populated (although with some agglomeration potential in Zrenjanin) but centrally located. Regions in this category are typically located within proximity of larger agglomerations and therefore the priority is typically to improve connectivity of the

region. Place-based policies may also be relevant in this type of region. The challenge here is that limited agglomeration potential means that specialization is likely to be particularly important, which raises the typical risk of regional industrial policies that aim to ‘pick winners’. Policies that promote density and accessibility must also be accompanied by reforms to strengthen the development of tradable sectors, build endowments through human capital development and capacity of regional institutions. Given the broader scope and relevance of these policies, the coordination between local, regional and national institutions for combined strategies is essential.

The priorities discussed in the remainder of this section for Central Banat and Zrenjanin are broadly in line with strategic priorities at the local level. These priorities are highlighted in bold below, although those presented here are perhaps more ambitious in trying to develop Zrenjanin as a knowledge center. For example, the city of Zrenjanin selected ten priority projects for its strategy 2014-2020:

- **Improvement of the quality of drinking water in the territory of the city of Zrenjanin**
- **Reconstruction of water supply and sewerage network in the territory of the city of Zrenjanin and inhabited places**
- **Construction of a regional landfill with a recycling center in Zrenjanin**
- Improving the quality and capacity of industrial and free zones
- Improvement of agrarian infrastructure and defense system against natural disasters
- **Construction of a wastewater treatment system**
- **Reconstruction, rehabilitation and construction of local roads in Zrenjanin and populated cities**
- Increasing the level of processing (finalization) of agricultural products
- Development of population policy instruments and activities for the protection of families with young children
- **Developing new concepts of education that are in line with local and wider needs**



	Challenges	Policy opportunities
CONCENTRATE	Missing inter-municipal and coordinated sectoral investments	Strengthen regional and local institutions and combined development of strategies to raise the efficiency of investments
CONNECT	Lack of connective infrastructure and knowledge networks	Increase secondary physical connective infrastructure; enhance digital/knowledge hubs; reduce barriers to labor mobility
CAPACITATE	Missing development of local endowments and low livability of urban environments	Enhance the quality of municipal services and the livability of the city to further the role of district agglomeration / "magnet city"

2.2.1. Policy priority 1: CONCENTRATE and coordinate investments through strengthening cooperation among regional and local institutions

From the perspective of supporting lagging regions, institutions must be considered at two levels: i) the national institutional structures to support regional development policymaking and to support delivery; and ii) local government capacity. It is equally important to strengthen the two levels to enable improved inter-municipal cooperation for enhanced common investments and the coordination at regional level of sectoral investments and connectivity strategies requiring larger financial investments.

Alignment of administrative structures, democratic and political authority such as in Poland and other EU countries as well as building coalitions for territorial development and growth strategies among the different levels of government is important to further local economic development. Policy reforms should focus on clearly and transparently defining the role of regional development institutions within a national legal and institutional framework with a clear national strategy for regional development.

Comprehensive regional development plans and investments with vertical and horizontal institutional cooperation have proven very fruitful in successful transitions of EU member states and could support the effectiveness of existing programs. The NDA and RDA structures/departments should be strengthened to collect and compile national, regional and local strategies to enhance interlinkages and cohesive strategies. The autonomy of drafting strategies should be left to local authorities with the support of regional agencies and donors in a coordinated way to ensure local relevance and independence.

Box 1: Lessons from the European Union on organizing regional development: The examples of Greece and Poland

Cohesion policy programs vary considerably across the European Union. In Greece, for the 20 years over 1993–2010, regional programs reflected the priorities of the central government, with no strong regional institutions and procedures for local participation in decision making. In 2010, Greece introduced elected local authorities and decentralized EU funds. However, a strong administrative disconnect remained between management of the EU funds at the regional level and the existing structure of government, resulting in parallel systems (the same thing happened in Romania). The regional funds are managed through a parallel Special Management Authority (SMA), chaired by the elected president of the regional government. The relationship between the regional government and the SMA has meant that the regions have been able to use the SMA in their regional planning strategy and in prioritizing their programs in line with the regional operational program (ROP) at the national level. In contrast, the municipalities, which have a nonhierarchical relationship to the region, are unable to capitalize on SMA resources in the same way and therefore enter into the discussions on the ROP at a disadvantage. Furthermore, because of the nonhierarchical relationship between local and regional entities in Greece, priorities may not be aligned, as local governments tend to follow the priorities of their thematic parent ministry rather than those of the region.

Poland has a more hierarchical system with greater administrative alignment, with the regional level of government (*województwa*) corresponding to NUTS 2 regions. Below this is the county or district level, and below that are the towns and rural communes. Each level is governed by an elected council (self-government). There is an overlap between the central administration and the elected councils in that the provincial governor is nominated by the president. This appears to enable a more coordinated approach to regional development, while also providing a clear channel for prioritization and program development to emerge from the local level. Most notably, in contrast to Greece and Romania, which have a single national ROP, Poland has 16 autonomous ROPs, reflecting strategies designed by/for individual regions.

In terms of local institutions, recommendations have called for improvements in local capacity (Farvacque-Vitkovic & Kopanyi, 2014; World Bank, 2020); less fragmentation, particularly in the use of structural funds (Lupu & Asandului, 2015); and concentration of investments, as in Poland (Tridico, 2007; Churski, 2014). Other recommended models for upgrading the capacity for financing and data collection at the local level, which are being developed in Serbia partly, are Galicia's intermunicipal investments (Hulbert, 2012) and Abruzzo's performance-based transfers (d'Agostino & Scarlato, 2015). Policies should focus on improving local government capacity, better exploiting sources of local revenue (e.g. in regions with significant natural capital) and increasing the participation of local governments in decisions over strategic local investment. This can also include support for strengthening coalitions for local development (dynamic business networks and civil society) and enhancing municipal service delivery.

Local governments in Central Banat have generally expressed satisfaction with being able to drive local investments and have highlighted effective cooperation with national and regional level in terms of FDI attraction. They have highlighted the benefits of cooperation with regional and national level (for example cooperation agreements China-Serbia) and stated that generally political support was necessary for any strategy of local development. They were generally rather satisfied with the cooperation with the RDAs and financing from province (development fund) and capital investment. They saw a need to improve the cooperation with the Chamber of commerce that mainly focuses on Zrenjanin and the cooperation is mainly restricted to capacity building activities.

Zrenjanin gives evidence of strong cooperation between various actors particularly on FDI attraction.

This relates to urban development, promotion of skills, and support for socially disadvantaged groups among the chamber of commerce, the local government, foreign investors, StartIT Center, and the association of large businesses (Zrepok, whose members represent 25 percent of GDP in Central Banat). However, development strategies are lacking to support SMEs and start-ups, with only one document having been adopted at the assembly of Vojvodina in 2002 and a line in regional budgets for incubators (covering power, infrastructure, rent etc.). There would be a need for an enhanced inclusion of civil society and expanded business networks (including SMEs and start-ups) in the drafting and implementation of local development strategies.

Reaching out to the university and dynamic start-up associations to target young entrepreneurs could strengthen the ability of these coalitions to attract young people to Zrenjanin and enable sustainable economic development. In similar contexts, such as Abruzzo (Italy), Dolnoslaskie (Poland), and Galicia (Spain), efforts to further academic tourism, invest in research and development on employment, strengthen trade unions, bridge social capital, and establish links with other growth poles have supported development. Zrenjanin is also already supporting surrounding municipalities by employing the workforce and regional projects (for example waste treatment) and municipalities are recently working more closely together, which should be supported particularly for municipal service, transport and the employment sectors. This cooperation could be promoted further in cooperation with the regional development agencies.

2.2.2. Policy priority 2: CONNECT ideas, people and businesses through connective infrastructure and knowledge networks

Along with the structural factors (density and distance), human capital is by far the most important factor affecting the development potential of lagging regions (World Bank, 2018). For centrally located regions such as Central Banat, development of secondary road networks can be an effective investment to integrate the regional economy. Enhancing public transport for commuting to the main agglomeration can also be an effective way to utilize most effectively limited human resources in regions with currently declining population.

Considering digital connectivity and knowledge network development can support the integration into global services and technology value chains linked to R&D and specialization in the university faculties and technical schools located in Zrenjanin. It is also central to support labor mobility, and thus help people in lagging regions move to take advantage of opportunities elsewhere. Thus, ensuring the equal quality of education, both foundational knowledge and technical skills, across all regions of a country is vital. However, it is important to link this skill development to short and long term economic opportunities, particularly those attractive to young people to create a knowledge-based region around an attractive university city.

The completed construction of a highway from Zrenjanin to Belgrade in the next three years (reducing travel time from 1.5 hours to 30 minutes) and a speedway from Novi Sad to Belgrade could yield promising benefits. It would bring Zrenjanin and its surrounding municipalities within commuting distance of Belgrade and could enhance linkages to the pan-European Corridor X. This could be transformative if the development of multimodal transport infrastructure creates an economic corridor linking Zrenjanin to Belgrade. In Romania, a comprehensive long-term strategy that includes investment in roads along with commuter rail, logistics infrastructure, and business parks, has contributed to successful corridor development between Timisoara and Arad, strengthening the competitiveness of

cities in both nodes. Similar strategies were pursued in Dolnoslaskie, which has become a major transport hub in Poland (OECD, 2008).

Zrenjanin could also play more of a role of an agglomeration surrounded by municipalities. In fact, a Chinese company explicitly asked for workers from areas surrounding Zrenjanin as a condition for the establishment of larger rubber factories that would require a larger workforce. Finally, overcoming border frictions could be transformative. For example, the municipalities in Central Banat (Serbia) that are located along the Romanian border have already benefited from cross-border investments, and further development of cross-border tourism offers promise. Here, while borders remain a barrier, delays are minimal. Further EU funding could be beneficial particularly given increasing trade linkages and potential linkages between universities.

Moreover, reducing barriers to internal labor mobility identified such as affordable housing, access to information on jobs, costs of moving, access to pre-school education, livability and attractiveness of cities has been identified as essential (WBCUTR 2019, (IOM, 2016)). This can lessen labor market frictions and help people and especially young people to benefit more from concentrated economic activity in urban areas and other regions with high economic potential. Labor mobility also facilitates more efficient factor allocation in the economy, thus increasing productivity generally.

Evidence from dynamic lagging regions in recent EU accession countries points to the importance of good quality universities, particularly those with strong faculties in technology, as key to the dynamism of secondary cities (Box 1). This marks a clear gap in Zrenjanin, whose faculty (linked to the university of Novi Sad) has a traditional engineering focus and that is mainly known for its good high schools in technical subjects and applied sciences. Emphasizing the use of ICT in schools from a young age and enhancing tech-related studies could contribute substantially to the competitiveness of the city district and region, help attract more IT companies and also fulfil changing requirements of foreign investors that will shift production to lower-wage regions.

In Zrenjanin, local and regional institutions are working with the Serbian Ministry of Education and the private sector to develop suitable dual education (automotive, cooking oil, IT, etc.) and general education upgrades to become a university center. Moreover, as the technical faculty in Zrenjanin “Mihaljo Pupin” is linked to the university of Novi Sad, this creates interesting knowledge linkages between the municipalities. Finally, several donor programs have supported the high technical school of vocational studies and the Center for Research and Transfer of Technologies was recently established. However, limitations of FDI (short term orientation based on low wages) needs to be considered so that in addition to offering short-term training for employment in large companies (rubber, wiring, welding, mechatronics, textile specialization for example), the focus should be on developing innovation capacity, especially in more broadly defined technology areas that allow productivity to rise without being locked into narrowly defined sectors and firms. Young people could also be supported through programs, stipends, campus accommodation or credits as well as a supporting educational, urban and cultural infrastructure.

For low growth urban regions like Zrenjanin, a priority is to establish strong education support systems that involve higher education institutions, the private and public sectors, and civil society (Materu, 2007; Caniels & Bosch, 2011). Such cooperation can improve the relevance and quality of tertiary and vocational education, while the creation of entrepreneurial universities, research and development labs, and technology transfer centers can strengthen regional innovation systems (Etzkowitz & Klofsten, 2005; Puukka & Marmolejo, 2008). Private sector involvement in managing institutions and designing curricula have been a major success factor in Brazil’s National Service for Rural Apprenticeship (SENAR), a pioneer

in vocational education and training in rural areas, and Namibia’s network of Community Skills Development Centers (COSDECs), which provide competency based skills training to communities across the country (World Bank, 2007). Cooperation with large companies to provide training could reduce costs for the municipality that could then focus on the improvement of general and IT education.

Romania managed to strengthen the development prospects of secondary cities as “magnet cities” (Cristea, et al., 2017) **through an emphasis on knowledge networks.** The country enhanced the entrepreneurial environment and the role of universities (attracting young people) while furthering competitive sectors linked to EU value chains (promoting opportunities), although a clear premium to city size has to be considered in terms of transferability of experiences. North Macedonia is also seen as a rather positive example in the region in terms of the development of the business environment. In similar contexts, such as Abruzzo (Italy), Dolnoslaskie (Poland), and Galicia (Spain), efforts to further academic tourism, invest in research and development on employment, strengthen trade unions, bridge social capital, and establish links with other growth poles have supported development.

Box 2: Dynamic universities can advance the development of a lagging region: Iasi, Romania

The Northeast Region of Romania managed an effective transition, while being the poorest region in the country (at the NUTS 2 level), and one of the poorest in Europe, with a peripheral location, low urbanization, and heavy dominance of small-scale agriculture. The region has a bright spot, though, in the city of Iași, which is the third largest university center in Romania, with a student population of around 55,000 (15 percent of the population of Iasi across its four main universities. This brings to the city a constant flow of young and well-educated people, which is critically important in an environment of overall demographic decline.

While Iași is only 12th in the country in economic output, it is 4th in the number of migrants it has attracted. Its universities draw students not only from nearby cities (Bacău, Piatra Neamț, and Suceava), but also from other large university towns (Brașov, Bucharest, Cluj-Napoca, and Timisoara) and from neighboring countries (notably, Bulgaria, Hungary, Moldova, Serbia, and Ukraine). As a consequence, Iasi has developed a large and diverse pool of human capital, which has supported the growth and transformation of the local economy. With more than 1,000 information and communication graduates each year, the city has shifted from a reliance on manufacturing to develop a strong information technology sector. Iasi is now the third largest information technology outsourcing location in the country and hosts large international firms including Continental, Oracle, Pentalog, and Xerox.

2.2.3. Policy priority 3: CAPACITATE dynamism of the local economy through increased livability of a “magnet” city with enhanced service delivery

The opportunity for lagging regions to leverage middle or secondary cities varies considerably. Many lagging regions do not have a secondary/middle city with high potential as an engine of regional growth but secondary cities may use these approaches in their transformation. In Serbia, the Nis region has high agglomeration potential (through the city of Nis), while the cities of Zrenjanin (in the low growth Central Banat region) and Novi Pazar (in low income Raska) may have the scale to support agglomeration.

For low growth regions, which tend to have established agglomerations, it is equally important to strengthen the city’s dynamism to retain the skilled youth population. Establishing an urban environment that is attractive to younger, skilled workers requires making available good quality, affordable housing and services and investing in cultural infrastructure. This is an essential factor to

support an emerging entrepreneurial ecosystem.

An analysis in Central Banat of the local and regional constraints for (young) entrepreneurs through a survey would help to defined targeted strategies to resolve complex issues such as rising informality of freelancers. This should be connected to the different support mechanisms for entrepreneurs (start-up hubs, dedicated coaching facility at the university etc.) and generally making the city attractive through a “positive competition” with Novi Sad as outlined in the next section. Given ageing population and the high share of unemployed with secondary education, retraining and support of entrepreneurship for adults should be promoted. Moreover, there should be an integrated sectoral approach linking the sectors of agriculture, industry and tourism with efforts to reduce potential negative externalities (i.e. industrial sector vs. agro-ecological and health tourism).

Generally in Zrenjanin, an integrated urban approach should be pursued, with a clear priority to ensure quality provision of municipal services such as wastewater and waste treatment but also to improve the economic and social environment. A company recently acquired land in Zrenjanin’s industrial zone to expand a medical waste treatment facility recently for healthcare institutions from Serbia, although it faced some opposition from surrounding municipalities, which shows some potential for private sector cooperation. Moreover, it is essential to improve the urban environment through urban regeneration projects, connectivity (already started with the ring road, the pedestrian zone and the highway connecting the city to Belgrade) as well as improving the residential area (including measures for affordable housing). The spatial plan in Serbia envisages the reconstruction of the water supply network and the expansion of the sewerage network is in progress. Zrenjanin has a great potential as a cultural center, start-up hub and is seen by some young people as a potential new “hipster paradise”. However, strategies should also be pursued for reducing the potential negative impact on poorer populations and risks of minority displacements (Carlino & Saiz 2019) such as affordable housing opportunities.

There have also been some limited successes in improving infrastructure in rural areas surrounding Zrenjanin. Nova Crnja has improved LED public lighting and local roads through PPPs and is currently repairing schools. They have a dedicated public utility company but efforts to improve water and sewage systems have failed. Novi Becej, on the other hand, has an own system water supply and have separate water communities, which has enabled 94 percent of households to be connected (compared to an average 74 percent among all Serbian districts), although there is little information on quality. The municipality is also investing in infrastructure for families, children and young people as well as investing in Industrial Zones, in the hope that it will attract inhabitants. Coordinated municipal investments should be promoted to enhance synergies.

The improvement of the business environment such as proper definition of property rights, adequate tax rates and incentives for formalization needs to be continued. The recent amendments to the national tax legislation may yield promising results particularly for the SME sector that has been disadvantaged.

In addition to agricultural value chains, higher value-added sectors should be nurtured. Measures to support agricultural companies include commercial loans, legalization of titles, incentives and restructuring packages for enterprises. There are some great opportunities in Zrenjanin and surroundings for the development for example of fish breeding and fishing as well as some potential for tourism (including wellness, cultural and musical, sports, ecological excursions) with linked employment. Given however the structure of wages, employment and education levels, the bulk of entrepreneurship should be promoted in higher added value sectors, particularly IT linked to industrial sectors, to ensure that working age population can be attracted and to promote a brain “circulation” or “gain” rather than “drain”. Moreover, environmental protection needs to be ensured to enable these sectors.

Box 3: Vision into the Future 2025: Central Banat has succeeded to become a start-up hub

In Serbia, Zrenjanin has managed to build strong coalitions for local economic development. The “I love Zrenjanin” platform, a marketing website for the city initiated by a young entrepreneur, was the first of many platforms targeting young, skilled workers. The city administration in Zrenjanin started with a local economic development office (that had the task to create a favourable business environment with local action plans for employment and development 2018-2020), a business council and a Business Registers Agency. There is now a strong cooperation on urban development, promotion of skills, and support for socially disadvantaged groups among the chamber of commerce, the local government, foreign investors, StartIT Center, the association of large businesses (Zrepok, whose members represent 25 percent of GDP in Central Banat), university and dynamic start-up associations. Targeting young entrepreneurs and coordinating with surrounding municipalities and cross-border regions has strengthened the ability of these coalitions to attract young people to Zrenjanin, in addition to efforts to increase livability, affordability and business environments but also enable families to live outside the city and commute easily to work. A strong adult education offer and retraining has also enabled particularly artisans to become modern entrepreneurs.

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Annex 1: Overview of municipalities and their characteristics in Central Banat

Municipality	Characteristics and living standards	Land and population	Employment	Economy
Zrenjanin	Political, economic, cultural and sports center of Central Banat	Population of 117,735 (~2/3 rd of regional population) One of the largest cities in Vojvodina and the largest city in the Serbian part of Central Banat 86 percent agricultural land (76 percent of which is utilized)	15 percent unemployment rate; more than 1/3 of the working age population work in agro-processing; employees mostly in sectors of manufacturing (26 percent), self-employed (15 percent), health and social work (11 percent) and education (9 percent) Average net income: 45,093 RSD in 2017	Historically the third largest industrial center in Yugoslavia but suffered a collapse at the beginning of the new millennium with a more recent renewal One of the largest agro-industrial centers in Serbia: agriculture and food processing represents most of the local economy (oilseeds, dairy products, meat industry, sugar, grains, fodder production etc.) companies in the fields of oil and gas production, chemical industry, metals, oil and sand, water products, textiles, production of medicines, construction (building materials), transport and other activities 1236 active companies were registered and 3387 entrepreneurs in 2018, with a small but accelerated increase since 2014 Two industrial zones and one free trade zone

Municipality	Characteristics and living standards	Land and population	Employment	Economy
Nova Crnja	Relatively underdeveloped rural region; 100 percent of inhabitants had access to drinking water but close to none to a sewage system	Population of 9,400 Small municipality along the border with Romania; 91 percent of the territory is agricultural land	~50 percent unemployment ²⁰	Hosts the most famous cooking oil factory in the region “Banat”, one of the largest employers and has three working zones There is no formally established office for local economic development but most potential is seen in tourism and agriculture, particularly in fruit production with connected biogas waste plants. EU accession is expected to bring further benefits given good existing cross-border connections
Žitište	Encompasses some of the most under-developed units of local self-governments	Population of 16,800	Low employment levels; high levels of outmigration	GDP is 60 percent below national average Focusing on developing agribusiness opportunities
Secanj	On the border with Romania Environment is rich in minerals, agricultural land, water resources and natural environments for recreational, fishing and tourism activities.	Population of 12,000	It has around 20 agricultural unions, but most agricultural companies have been privatized with declining numbers of employees	GDP is around 60-80 percent of the national average Industrialization began in the late ‘70s and it hosts large companies in the car industry, sock production, the production of fodder and oil production (greenfield investment) Big industries with large numbers of employees discontinued their activities; high levels of youth outmigration Within the industrial zones of 30 ha, 17 ha are rented to companies.

²⁰ The statistics are contested as farmers are said to register for unemployment given co-ownership of land with the household/family and related income sharing and graduate students register to ensure health insurance coverage and to be registered for job opportunities for example offered by foreign investors.

Municipality	Characteristics and living standards	Land and population	Employment	Economy
Novi Becej	The railway that connects Belgrade to Timisoara passes through all settlements in the municipality	Population of 22,000	Despite employment opportunities outward migration is high; programs for prequalification are low quality; problems to find replacements particularly in public administration.	GDP is more than 80 percent of the national average Despite substantial unused potential and a specialization in roof tiles production with the technology leader company (but also metal, ceramics, food and textile for example) the economy faces a slow transition process, decline in business activity, insufficient investment and outflow of workers. It has three working zones.

Data source: National statistical office, Business registers agency

Annex 2: Categorization of leading and lagging regions in Serbia

Low income, diverging (4)	
Zaječar	sparse peripheral
Pomoravlje	sparse central
Jablaniča	sparse peripheral
West Bačka	sparse peripheral
Low income, converging (9)	
Raška	sparse peripheral
Mačva	sparse central
Niš	dense central
Pčinja	sparse peripheral
Podunavlje	dense central
Topliča	sparse peripheral
Rasina	sparse central
Zlatibor	sparse peripheral
Kolubara	sparse central
Low growth (2)	
Šumadija	dense central

Central Banat	sparse central
Leading (10)	
Belgrade	dense central
South Bačka	dense central
South Banat	sparse central
Moraviča	sparse peripheral
Pirot	sparse central
North Bačka	sparse central
Srem	sparse central
North Banat	sparse central
Bor	sparse peripheral
Braničeva	sparse central

Annex 3: Cities, municipalities and towns in Serbia

The official definition of cities and municipalities is given in The Law on the Territorial Organization of the Republic of Serbia ("Official Gazette of RS", no. 129 of 29 December 2007, 18 of 1 March 2016, 47 of 20 June 2018, 9 of 4 February 2020 - other law) It is describe in the law that territorial organization of Republic of Serbia consist of municipality, cities and the City of Belgrade as capital, and of autonomous provinces (Article 2). By the Law municipalities according to the article 11 is basic territory unit of local self-government, winch has at least 10.000 inhabitants. Also it is stressed that municipalities established before adoption of this Law may have less than 10.000 inhabitants. Also, when there are special economic, geographical or historical reasons, a new municipality with less than 10,000 inhabitants may be established. According to the Article 17, cities are territorial units which represents the economic, administrative, geographical and cultural center of the wider area and has more than 100,000 inhabitants. Exceptionally, when there are special economic, geographical or historical reasons, it can be determined that the city is a territorial unit with less than 100,000 inhabitants, if it meets all other criteria provided by law. City of Belgrade as Capital is established by the Law on Capital City. ("Official Gazette of RS", no. 129 of 29 December 2007, 83 of 5 August 2014 - dr. Law, 101 of 16 December 2016 - dr. law, 37 of May 29, 2019). The competencies between cities and municipalities are different in the way that cities can establish communal police.

Without exceptions, the categories of local self-governments are therefore as follows:

- municipality 10.000-100.000
- cites 100.000 and beyond
- capital

Annex 4: Boosting development in a poor peripheral area: the case of Raska

Background

Raska district (upravni okrug) is one of 25 administrative districts in Serbia. The district is located in the southwestern part of the Republic of Serbia, surrounded by Zlatibor, Moravički, Šumadijski, Pomoravski and Rasinski district, and in the South it borders with Montenegro. It covers 5 local self-governments:

- City of Kraljevo - The seat of the Raska district
- City of Novi Pazar
- Municipality of Vrnjačka Banja
- Municipality of Tutin
- Municipality of Raška

Raska region covers a land of 3.923 square kilometres and according to the census (2011) has 309.258 inhabitants, estimation for 2018 (source National statistical office) is 305.147 inhabitants.

Territory	Area km ²	Number of settlements	Inhabitants	Population density, number of inhabitants on km ²
Republika Srbija	88.499	6.158	7.020.858	-
Region Šumadije i Zapadne Srbije NUTS 2	26.493	2.112	1.941.130	73
Raska Region	3.923	359	305.954	78
Kraljevo	1.530	92	119.585	78
<i>Vrnjačka Banja</i>	239	14	26.322	110
<i>Novi Pazar</i>	742	99	105.490	142
<i>Raška</i>	670	61	22.981	34
<i>Tutin</i>	742	93	31.576	43

Source Business Register Agency

According to the national act on level of development²¹ of LSGs in Serbia (*Uredba o utvrđivanju jedinstvene liste razvijenosti regiona i jedinica lokalne samouprava*), the most developed LSG in Raska region is Vrnjačka Banja in the 2nd group (80-100% national average), then Kraljevo and Novi Pazar in the 3rd group (60-

²¹ The bylaw on development establishes a list of development of regions, which are according to the level of development classified in developed and underdeveloped regions, and local self-governments, which are classified into the first, second, third and fourth groups and devastated areas based on data from the body responsible for statistics and finance. The classification of the region is based on the value of gross domestic product per capita in the region in relation to the national average, for the reference period. According to the level of development local self-governments are classified into 1) First group consists of 20 local self-government units whose level of development is above the national average, 2) Second group consists of 34 local self-government units whose level of development ranges from 80% to 100% of the national average, 3) Third group consists of 47 underdeveloped local self-government units whose level of development ranges from 60% to 80% of the national average, 4) Fourth group consists of 44 extremely underdeveloped local self-government units whose level of development is below 60% of the national average, 5) Devastated areas consist of 19 local self-government units from the fourth group whose level of development is below 50% of the national average.

80%) and Raška and Tutin in 4th group. Tutin municipality is in the group of devastated LSGs according to the same government act.

Level of development of LSGs in Raska district according to the national act

I Group >100	II Group 80% - 100%	III Group 60% - 80%	IV Group < 60%
	Vrnjačka Banja	Kraljevo	Raška
		Novi Pazar	Tutin

Resources, climate and infrastructure

Due to its geographical location, the roads leading to the valleys of Raska and Ibar provide cultural, trade and other connection with the Danube, Pannonia and Central Europe at north, and with the Vardar valley and the Aegean region in the south. The region has **natural resources that represent potential for development**. It is a mountainous region rich in thermo-mineral springs and mineral resources, rivers - the largest are: West Morava, Ibar, Raska, Studenica, Josanica. Many rivers flowing through the Region of Šumadija and Western Serbia represent a significant hydro-energy potential. **Vrnjacka Banja is the most visited spa in Serbia**, followed by Mataruška, Bogutovacka, Josanicka, Rajcinovic and Novopazarska spa, but numerous thermo-mineral springs in the region have not yet been fully explored and utilized. In Raska, Kopaonik is the most visited **ski resort** in Serbia.

Moreover, the moderate continental climate and lowland areas create favourable conditions for **agricultural production**. Almost half of the land of the district is agricultural which is very diverse: arable land, gardens, pastures, meadows, orchards. Due to the hilly terrain, the area is over 40% covered with forests, so the district also has significant **forestry and timber production potential**. The region is **rich in mineral resources** such as coal, lignite, lead and zinc, marble, gravel, sand, limestone, etc. The relief of the Raska District is mainly of the mountain- type, where the Pester Plateau, Kotlenik Mountains in the north, Goč in the east, Kopaonik (the highest mountain of this area, 2017m), Rogozna and Hum in the south and Velika Ninaja, Golija, Čemerno stand out and Jelica in the west. The rivers and streams whose valleys stretch between these mountains belong to the West Morava, Ibar and Lima basins. At the highest altitudes in the municipality of Tutin the climate is mountainous, while in the lower regions, above all river valleys, the climate is continental.

Infrastructure

The District of Raska has a very accessible traffic position due to the road and rail roads that cross its territory - the **Ibar highway**, which runs from Belgrade via Preljina and Kraljevo to Raska and Novi Pazar, to the Montenegrin coast, and the second branch via Kosovska Mitrovica to Skopje and Greece, and the **West Moravian highway** linking Western Serbia via Kraljevo to the Corridor 10, **but road infrastructure in the territory of this district is not at satisfactory level**.

In August 2019, the "**Miloš Veliki**" highway was opened, the section of Corridor 11 from Obrenovac to Preljina in the total length of 103 kilometers, which significantly improved the connection between

Western Serbia and Belgrade. Also, at the end of 2019, the construction of the **highway Pojate-Preljina**, Moravian corridor in the length of 112.3 kilometres, began. The works should be completed in four years, and this road will connect all major cities in central Serbia where more than half a million people live - Cacak, Kraljevo, Vrnjacka Banja, Trstenik, Krusevac, Stalac and Cicevac, as well as Corridor 10 and the highway "Milos Great "(Corridor 11). The network of state roads of the first order is characterized by high traffic load, passing through populated areas and the absence of bypasses, a large number of access roads and connections, high safety risks, traffic of a large number of pedestrians, cyclists and agricultural machines and landslides. The network of state roads of the second order is also characterized by average conditions.

There are **two airports** in the territory of the district: the Morava airport in Ladjevci, in commercial use since 2019, converted from military to civilian airport, and airport of the Magnohrom industry, registered as sports and recreational airport. The importance of recently opened airport Morava is in the economic development of the city and the region.

The characteristics of railway traffic in the territory of the Raska District are extremely modest and below European standards. The quality of the railway infrastructure is at a low level and is characterized by old railways, low speed and poor condition of railway facilities. Reconstruction of the railway network is a precondition for greater utilization of the railway infrastructure for the needs of the development of the local economy.

Regarding water supply, focused primarily on the use of the Ibar and Raska River springs, the **water supply system is characterized by high losses and insufficient pressure.** Most of the rural population uses its own wells for water supply, which are not monitored and controlled. **Wastewater treatment is a major environmental hazard.** Only 16% of the total wastewater is treated, and the only wastewater treatment plant located in the territory of the City of Kraljevo, Also, the sewage infrastructure is insufficient. In the field of energy, different types of energy are represented: wood, coal, oil, petroleum products, electricity, and natural gas. **Renewables are not used to produce energy**, for now only Kraljevo and Vrnjacka Banja are connected to the gas system.

Population and human capital

Within Raska district, most of the population has secondary education. The educational infrastructure and available capacities in the last 15 years were enhanced. The number of primary and secondary schools remained at approximately the same level, the number of pre-school institutions doubled, which is expected given the natural increase in the municipalities of Novi Pazar and Tutin. **Two Universities in Novi Pazar were established** during this period, which led to increase of the number of students enrolled, while the number of graduates of the Raska District increased.

The structure of the working age population indicates that the largest share of population is with secondary education (46.7%), followed by primary education (26.8%), while **population with higher education** has only 4.5 % (college) and 7.5% (university) respectively.

There is a high share of dependent population in the Raska area. Also, the structure of the inactive population shows that the share of the elderly in the category of dependent population is large, and this cannot be considered desirable from the aspect of the smooth functioning of the pension system. The **problem of brain drain** from the region to Belgrade and other part of Europe leads to workforce disbalance and lack of qualified workforce.

Economy

The structure of the **local economy is dominated by micro and small enterprises.** Small and medium-sized enterprises in this area do not have sufficient strength and competitiveness in the market. The profitability of the SME sector of the Raska District sector has been extremely low compared to the more developed regions in the country.

According to statistical data, **Raska district has 2% participation in gross added value of RS.** The District of Raska has an extremely **low share in total investments** of the Republic of Serbia, and except Raška municipality it is low below average in Serbia. One of the big problems that companies and entrepreneurs in Raska region face is **illiquidity.**

The largest number of companies operate in the sectors of trade and processing industry. The economy of the region is diversified, with a tradition in metal industry, food processing and furniture industry in Kraljevo, tourism in Vrnjacka Banja, textile industry, trade and handicraft, footwear industry, construction, cattle breeding and livestock in Novi Pazar and, furniture industry in Tutin and tourism development in Raška. Gross added value figures for 2017 show that 26% of GVA is in services, 21% in construction industry, and 19% in industrial sector.

Institutions

Within Raska administrative district, there are **two regional agencies** that are established, namely the Regional Agency for Spatial and Economic Development of Raska and Moravica Districts²² and the Sandzak Economic Development Agency- SEDA²³. The first regional agency has an office in Kraljevo covering LSGs Kraljevo, Vrnjačka Banja, Raška (from Raska district), Ivanjica, Gornji Milanovac and Čačak. The second agency has an office in Novi Pazar, covering LSGs Novi Pazar, Tutin (from Raska district) and Sjenica .

The Regional Chamber of Commerce²⁴ operated across several municipalities. Within the territory covered by the SEDA, **seven economic clusters** have been established in textile, shoe production, healthy food, tourism, agriculture, construction and furniture.

All LSGs in Raška districts organised offices for local economic development, as there is no strategic document covering all districts and as in line with new Law on system in Serbia, all LSGs need to develop new strategic documents Plans of development until 2021.

²² <https://www.kv-rda.org/>

²³ <http://seda.org.rs/>

²⁴ <https://kraljevo.pks.rs/>

Identification of challenges and potentials

Two interviews were undertaken with Heads of LED units in Kraljevo and Novi Pazar, the two largest municipalities with more than 100000 inhabitants in the district.

Kraljevo

Main challenges in economic development are and will be in the near future the **lack of qualified workforce and creation of supply chains as well as connection of SMEs with new investors**. The new companies (Turkish company "Taypa2" and German company "Leoni") in Kraljevo will employ approximately 7.500 new workers. Generally, the problems are **poor communal infrastructure and lack of adequately educated workforce, given lack of investments**.

The municipality faces a real problem of **brain drain**, particularly of **young people**, and see that improvement of **conditions for employment and quality of life** is the best strategy to retain migrants. When asked, young people often say that they need better jobs, especially for the highly educated, and a better standard of living with enhanced social and cultural life for young people.

The biggest potential of Kraljevo and region are to **enhance the added value of economic sectors within the processing industry**, where there is a long tradition, knowledge, resources and infrastructure such as metal, wood and electrical industry, as well as processing of agricultural products due to favourable natural conditions and fertile land. There is also a potential in **tourism** potential in two complex spas, Maturuska and Bogutovacka banja.

One of the strengths of the municipality are its industrial zones. On the territory of Kraljevo, there are two infrastructurally equipped industrial zones, six commercial and trade zones and two work zones. The municipality also sees a large potential for the **Faculty of mechanic and construction**.

The City of Kraljevo provide **support to domestic and foreign investors** by searching for the best **location for investment** and, in cooperation with the National Employment Service, conducting additional **trainings for the workforce**. The City of Kraljevo cooperates with the local business community with the aim to identify problems that the local government can solve. Through **local employment plans**, Kraljevo **supports start-ups and local business** for employment of new workers. Currently Kraljevo is in the process of developing a **new program** to support the SME sector in line with state aid in the **metal industry**.

Main **problems that the business community often stress are needed improvements of infrastructure, inadequate regulations at the national level and a lack of adequate workforce**. A business community opinion survey in the metal sector in Kraljevo, implemented during 2019 confirmed this, as main problems mentioned were: deficit of skilled labour; poor infrastructural equipment (poor access roads to some large business entities, sewerage networks, public lighting); insufficient information of business representatives on funding opportunities; and insufficient cooperation of the representatives of the city administration of the city of Kraljevo with the existing business community.

In terms of basic service delivery and livability, Kraljevo is performing rather poorly. First, the municipality has a **poor communal infrastructure in waste** management system. There is no sanitary landfill in Karaljevo, and there is a lack of equipment in the local utility company. Rural areas are also not

included in the system of waste collection. Second, there is an evident **lack of conditions for safe water supply** to rural parts of the city (rural systems have no management and quality control) and the municipality has no **wastewater treatment system**. Some villages do not have sewerage network and in most cases the wastewater is drained directly into the environment. The municipality expects support from EU IPA 2017 fund to address this. Third, considering environmental issues, Kraljevo lately had a **big problem in air pollution** and they developed a short term plan for protection. In terms of heating systems, the main problems are lack of constructed heat water systems and a large number of public buildings using their own heating on oil or solid fuel (coal), thereby polluting the air.

In terms of connective infrastructure, a **new highway** is being built close to Kraljevo and a **civil airport** recently opened in Morava. But **local uncategorized roads are in bad shape**, with lack of traffic signalisation and often not wide enough, with a lack of infrastructure for draining. The connections could be improved by the construction of the Morava corridor, a national project that started in 2020. A major priority in terms of infrastructure upgrading would be the construction and development of the **local road network**, especially in rural parts.

Considering cooperation with neighbouring cities and municipalities, the City of Kraljevo has a very **good cooperation in planning and realisation of joint projects**, particularly with the municipalities Vrnjacka Banja, Raska and city of Cacak. The **cooperation with the National Development Agency is effective**, with two investments being more recently implemented thanks to this cooperation. There is an effective communication with the Ministry of Economy, which funded equipment in certain locations for the investments.

The city of Kraljevo was one of the founders of the **Regional development agency RRA**. The RRA conducts programs to support local businesses, with funding from the Ministry of Economy and the National fund for development and supports LSGs in enhancing their capacity for LED. Despite Kraljevo not being located close to the border, there is some on-going **cooperation with LSGs from the northern part of Montenegro**, especially in tourism development projects and improvement of local development.

Novi Pazar

The municipality faces major challenges with **high unemployment (50%), poor infrastructure and a lack of measures and instruments to support the local economy**. Opportunities to support local SMEs are seen as very limited, except for those funded by the national level.

The main potential of the city is seen as its young people and Novi Pazar has traditionally been well-known for its “entrepreneurial spirit”. There are two Universities and several private schools.

The city faces major issues in terms of the **poor quality of administrative and communal services**. A **main problem in infrastructure is waste management**, as the landfill is far from the city and costs of waste disposal are high. Electricity supply is low, given that needs would be 220kw and only 110kw are produced.

Connective infrastructure with other LSGs in region is lacking, as there are no roads between Tutin and Sjenica, Sjenica and Prijepolje, Tutin Rozaje, Novi Pazar Mitrovica. **Connections between these LSGs in Serbia and Montenegro are seen to have the potential to create better conditions for leaving and working in the region**. Road and communal infrastructure is poor, and there is a lack of quality equipment.

Cooperation and communication with the business community is perceived as being excellent, but the implementation of requests is poor, as **main challenges mentioned by the business community (improvements of business climate)** are seen by the municipality as **fiscal** in nature and therefore **not under their mandates**.

Cooperation with regional institutions are efficient, but **cooperation with other cities and municipalities are not sufficient** and cooperation with cross border municipalities is weak and not used enough. **Cooperation with RRA is mainly for education** and improvements for new investments.

Conclusions and recommendations

Main challenges faced for development:

- Depopulation of region and brain drain
- Lack of coordinated strategies for regional economic development
- Local financial limits to support investment needs
- Inadequate investments in regional/local infrastructure – especially roads, water supply, waste management, for touristic areas
- Mismatch between the workforce and labor market needs
- Lack of promotion and cooperation between SMEs
- Insufficient intermunicipal cooperation and regional infrastructure projects

Potentials identified:

- Natural resources: ore and mineral deposits, forest potential; water, agricultural land; cultural and historical monuments.
- Tourism potentials in mountain and snow tourism, spa tourism and rural tourism
- Agriculture potentials (agro-processing)
- Metal industry, wood processing and textile industry
- SME development and connection with faculty for mechanical engineering in Kraljevo and creation of supply chain for FDI investments
- Human capital and skills development for niche sectors, i.e. Kraljevo as an industrial center for the metal industry and Novi Pazar for textile and entrepreneurial activity / innovation
- Housing programs in Raska municipality for young people
- Enhancing quality of life in the cities to attract and retain particularly young, dynamic people
- Cooperation with other municipalities (including cross-border) to enhance linkages, connectivity and effective labor migration.

	Raska
Policy priority 1: Concentrate	<ul style="list-style-type: none">• Concentrate and coordinate investments in regional basic infrastructure such as roads, water supply, wastewater and waste management system and enhance city livability.
Policy priority 2: Connect	<ul style="list-style-type: none">• Connect people and businesses, promote sectors with comparative advantage such as metal and wood processing industry and promote effective labor migration
Policy priority 3: Capacitate	<ul style="list-style-type: none">• Capacitate the local economy through strengthening financial management of local governments, ensuring coordination of sectoral interventions and furthering skills development linked to job opportunities.