

After the recent visit of President Vučić to the People's Republic of China, the signing of a free trade agreement with this country was announced. Free trade is a good thing for all participants in the exchange because it improves specialization in production and productivity. This makes us all richer. The domestic media pay great attention to this agreement, interpreting it in very contradictory ways, but when you actually scratch under its surface, it can be seen that this is much more political marketing before the elections than a significant economic step forward.

What are the key reasons behind signing this agreement? Do they have justifications for the euphoria due to the announcement of great progress in the domestic economy, as well as the fear that we will stifle the domestic economy with Chinese goods? Whose side is this agreement more inclined to?

Trade is good for everyone

On a personal level, we all know that trade is good for us - instead of raising chickens, wheat, cows and pigs ourselves, to make a ham sandwich, we buy it all in the store and pay with the money we earn from our profession. Would anyone be a good lawyer, programmer, or tailor if they devoted more than half of their work time each day to other jobs, instead of paying other people for them, from making drills to making pizza dough?

However, this logic, which we all adhere to in our personal lives and which we do not think about much in our daily activities, stops where the boundaries begin. Suddenly, for most people, this becomes counterintuitive, because they view international trade as a war, where if one side wins, the other must lose, instead of both winning. That is why free trade does not have many proponents in politics, although it is quite different among economists. "We should not import what we can do ourselves; we need to protect domestic producers from competition from abroad" - these are just some of the excuses against free trade that can be found among a large number of people, but which is also worrying among the media and even some prominent economists.

Current trade with China - it is important to observe the overall trade results

Trade between Serbia and China is quite strained on the Chinese side - Serbian exports to that country are significantly lower than imports from it: 377 million USD compared to 3.29 billion USD. This fact does not mean much, because we need to look at the overall trade results, not just individual countries. It is completely natural that there is an economic deficit or surplus with individual economies, depending on their structure, but only the final result is important.

It is true that exports from Serbia to China have increased significantly over the past few years, from just over six million USD in 2012 to the current 377 million USD. But this is not the whole story: the largest part of this growth is the export of only one Chinese company to its home country, and that is Zidjin in Bor. Exports of copper and related metals (such as silver, platinum or gold) account for \$ 238 million, or nearly two-thirds of exports.

On the other hand, imports are primarily electrical machinery, telecommunications equipment, industrial machinery, textiles and clothing.

Serbia and China are both countries with high tariffs, although China became a member of the World Trade Organization in 2001. The average MFN (Most Favored Nation) tariff on industrial products in our country is 6.3% and in China it is very similar to 6.5%. As Serbia is still not a member of the WTO, both countries apply customs rates that can be significantly higher than these. If Serbia cared about free trade, it should have become a member of the WTO by now, so that would only reduce customs duties between China and Serbia enough that a special trade agreement would probably not be needed.

Expected effects - the reality is that the economic impact will not be too significant

Many fear that the free trade agreement would destroy the few industries that have survived in Serbia, while the government and the media that support it say that the Serbian economy will now prosper, because the openness of the world's largest market will bring new, large foreign investments. But the reality is very far from both of these attitudes. First, China has been a world workshop for a couple of decades, since its opening to the world. Therefore, it is understandable that it has a trade surplus with the largest number of countries with which it trades at all - it is the same with the EU and the USA, as it is with Serbia. But we have already had experience with the great opening of trade, first during the liberalization process after October 5, and then after the Stabilization and Association Agreement (SAA) with the EU, due to which we have practically no customs duties on imports of industrial products from Europe.

The closure of a large number of factories after 2000 will be the result of decades of economic destruction due to wars, sanctions and bombings in the 1990s, when our industry spent a decade declining and a significant part of it lost the technological race with foreign competition.

After the full implementation of the SAA from 2014, we do not see a decrease, but on the contrary a significant increase in industrial production in Serbia. It will be similar in the case of signing a trade agreement with China - the economic impact will not be too significant, Serbia will not just be flooded overnight with cheaper Chinese products that will destroy Serbian industry.

One of the arguments that say that customs protection is a rather bad thing for the protection of domestic industry is that in small and poor markets, such as Serbia, it is almost impossible to establish economically rational production that includes economies of scale of any more demanding product. is a production intended exclusively for domestic consumers. That is why we do not have "Made in Blace" smartphones, because the production for the market of seven million people, not very rich people in Europe, does not pay off too much: phones will be very expensive, so few people will buy them.

If we look at the sector from which we mostly import products from China (electrical

appliances and machines), large producers of these products operating in Serbia predominantly produce for export, not for sale on the domestic market. It is similar even with the textile and clothing industry.

But this does not mean that certain sectors may not be affected by competition from China, which has so far been artificially kept away from high tariffs. In order for these companies to survive, they simply have to offer their consumers better and cheaper products. And that is all good for us who buy products like this: consumers do not exist just to keep unproductive factories through our pockets.

The emergence of cheaper import solutions also means an increase in the living standards of broad sections of the population, especially the poorest. The opening of Chinese stores in Serbia probably had a greater impact on raising living standards in the country than all foreign direct investment combined.

Economic, foreign or domestic policy - it is better to open a factory in China than in Serbia

What is visible from the statements of President Vučić is the further focus on FDI as an instrument of economic development. It is stated that foreigners will now invest in Serbia if this agreement is signed. The domestic industry is still the last political hole. This is, of course, just pre-election political marketing.

If you want to export something to China from the domain of industry, it is much easier for you to open a factory in China itself than in Serbia. China is far away, transport costs have increased significantly, there is already a serious industrial base there, and when you look at exports from the EU to China, for example, these are technologically demanding products that are not produced in our country. Which means that there is still no production and organizational knowledge here to easily transfer these technological processes, as in the case of an industry that already exists and has a tradition and trained workers (for example, metal, textile or automotive industry).

China already has free trade agreements with countries such as Georgia, Australia, Chile, Costa Rica, South Korea, Mauritius, New Zealand, Singapore, Iceland, Pakistan, Peru and Switzerland, not to mention Hong Kong and Macao, which are part of China, but they have their own special trade policy. And negotiations are coming to an end with Norway and Moldova, and among the regional agreements there are agreements with ASEAN (Singapore, Malaysia, Indonesia, Thailand, Vietnam, Laos, Cambodia, Brunei, Philippines and Myanmar) and APTA (Bangladesh, India, Sri Lanka)). Therefore, Serbia will not be a big exception at the global level that such an agreement with China has a significant impact on the attractiveness of Serbia, as an investment destination.

Therefore, the reasons for the free trade agreement with China can be found in the domain of political and diplomatic, rather than purely economic. And even here, we cannot estimate the impact of the possible lobbying of Zidjin, a Chinese state-owned company, on Chinese

officials in order to facilitate their export of copper back to their home country. As an economic partner of China, Serbia is so small, both on the side of exports and imports, that it is hard to believe that such announcements would have come about without some lubrication and pushing from this side.

But domestic policy is not only present in China. With the upcoming elections in April, the current regime in Serbia is trying to repeat the great economic promises of a better life. In this domain, China is already playing a notable propaganda role, sometimes even with very grotesque scenes that seem to have been directed by David Lynch - from President Vučić's announcement that the Chinese will open a flying car factory in Serbia to Dragan Marković Palma waving chicken legs behind the podium promising their large exports to China.

So, although signing a free trade agreement with China would be a good thing for Serbia - because consumers would have more money to spend on other things and because it would facilitate the export of our companies to the market there, the scope of this move should not be euphorically overestimated, Talas writes.