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The new era of industrial policy in Eastern Europe: from SDG assessment to policy solutions

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Abstract

Recent years have witnessed an emerging shift towards **more active industrial policy interventions in Eastern Europe**, which suggests a renewed consensus on the importance of industrial development. However, challenges remain in the design and implementation of industrial policies, which often prevent their successful deployment. The latest data on Sustainable Development Goals (SDGs) progress in the region, along with the goals closely related to industry, reveal that **while Eastern Europe is performing above the average in energy access, employment and infrastructure, it also faces a strong deceleration in economic growth, and slow progress in innovation, clean energy and resource efficiency.** Targeted interventions to spur industrial competitiveness and bring the region closer to realizing the SDGs by 2030 are urgently needed. This policy brief presents some areas where modern industrial policies can accelerate SDG progress by leveraging advanced digitalization, clean energy production, foreign direct investment (FDI) attraction and regional integration. Case studies from the region underscore the importance of **collaboration with relevant stakeholders, policy continuity and cross-regional alignment for the successful implementation of industrial policy and sustainable growth.**¹

Key Messages

- 1.** Eastern Europe is ahead of other developing regions in its overall progress towards industry-related SDGs, but still faces significant gaps in critical areas such as clean energy and innovation.
- 2.** Modern industrial policy can help to accelerate progress by leveraging emerging opportunities around green technologies, global value chains (GVC) and regional integration.
- 3.** Cultivating wider societal consensus, strengthening institutional capacity and enhancing collaborative approaches is key to overcoming implementation challenges that have hindered industrial policy success in the past.

How far is Eastern Europe from achieving the industry-related SDGs?

Under SDG 9, industrial development constitutes one of the 17 objectives of the 2030 Agenda for Sustainable Development, and is a prime driver of progress for the achievement of the other objectives.² Given industry's strong linkages and multiplier effects on the rest of the economy, policies that strengthen productive and innovation capabilities in the industrial sector are particularly well-suited to permeate to other SDGs.

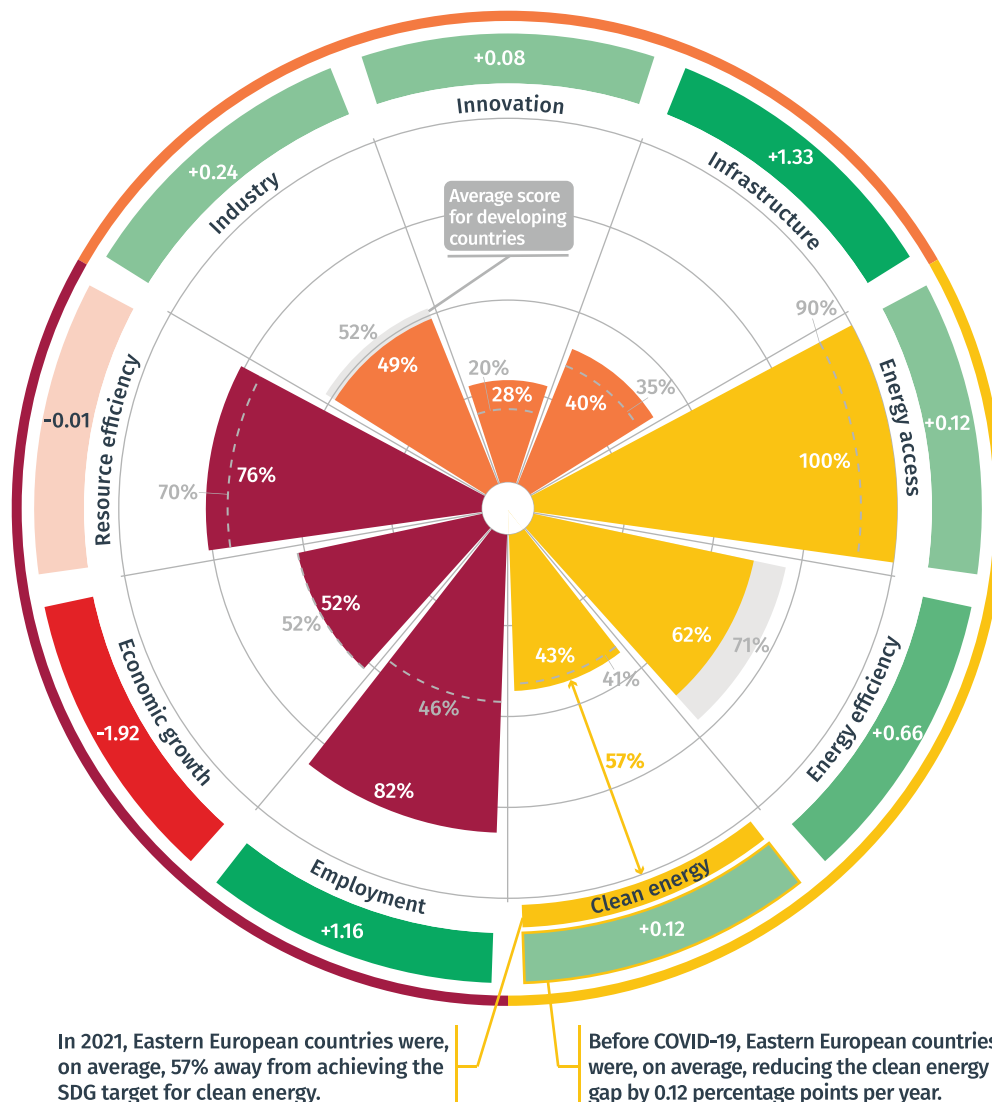
Manufacturing industries drive sustainable development by accelerating growth, fostering innovation, creating jobs, reducing poverty and hunger, creating more equal societies, and fighting climate change. Industry does so through direct and indirect channels. The former contributes to achieving certain goals by providing goods, creating jobs and accelerating technological change and economic growth. The latter takes place primarily through the impact of industry on economic growth and job creation (SDG 8) and the energy transition (SDG 7).

Where does Eastern Europe³ stand in achieving these crucial SDGs? Recent research conducted

by UNIDO reveals that while progress towards achieving SDGs 7, 8, and 9 in Eastern Europe is above the average compared to other developing regions, some challenges lie ahead⁴ (see Figure 1).

The SDG assessment highlights a region with universal energy access and above-average energy efficiency scores, a solid foundation in infrastructure development and positive progress in quality job creation. However, important gaps still remain in three critical areas: economic growth, clean energy and innovation. According to these estimates, if the pre-COVID-19 trend continues, Eastern Europe will not reach its clean energy targets by 2030, highlighting the need for accelerated efforts in this sector. The sharp deceleration of economic growth observed before the pandemic underscores the urgency of economic revitalization strategies to sustain inclusive development. In parallel, despite outperforming other developing countries in innovation, the region's average score is still 70 per cent below the corresponding SDG target.⁵ Well-crafted industrial policies can harness Eastern European countries' strengths to accelerate progress in these three critical areas.

Figure 1. Distance to SDG targets: Eastern Europe in 2021



Note: The values represent the average level of SDG target achievement for each dimension in 2021, aggregated at the regional level using population weights. The grey areas represent the performance of all developing countries. The shaded rectangles on the outer side of the figure reflect the average annual convergence speed towards the target in the decade before the COVID-19 pandemic. This is calculated by subtracting the index values in 2019 from those in 2009, and then dividing the result by ten years.

Source: UNIDO Industrial Development Report 2024, Figure 7.1, page 138.

Industrial policy landscape

During the post-socialist transition period, Eastern European countries — particularly across Central Eastern Europe and parts of South-eastern Europe — followed a **market-driven industrialization strategy**, using FDI attraction instruments as the main policy tool. Market forces took the lead in determining which sectors and activities were

dominant in the regional economies, resulting in a specialization of assemblers in the manufacturing value chains. While this model catalysed the region's integration into GVCs, **it fell short in promoting clean energy use, sustained economic growth and innovation.**

Since the early 2000s, the region has gradually shifted from market-driven industrialization to one supported by industrial policy. Currently, the two areas of green and digital transformations, commonly referred to as “the twin transition,” feature heavily on Eastern European countries’ agendas. However, having strongly relied on market-driven industrialization, the successful formulation and deployment of industrial policies continue to be challenging in the region. This is broadly a result of untargeted policies dominating industrial policymaking and institutional shortcomings that pose implementation challenges.

Industrial policies found in the region are multifaceted, reflecting a notable diversity in natural resources, productive factors and institutional capabilities. However, countries also share common characteristics that define policymaking in Eastern Europe. Firstly, given the geographical specificities of the region, the European Union (EU) plays a major role in setting the tone of industrial policy, especially for the EU member states and potential candidate countries. As a result, industrial policies in the region often entail the translation of EU industrial policies into domestic contexts.

Opportunities and actions

There are ample opportunities for tapping into the region’s potential through innovative industrial policy. Climate change and the energy transition, advancement in digital technologies, the reconfiguration of global value chains, and regional integration are global phenomena that call for new forms of industrial policy to turn these challenges into development opportunities.



Energy transition

Eastern Europe possesses suitable preconditions for producing renewable energy from wind and solar, which are largely untapped resources

Another defining feature in policymaking are the Smart Specialization Strategies (S3), which are increasingly adopted across the region to identify a country’s research, innovation and entrepreneurial potential for building a comparative advantage. The experiences with the S3 in different parts of Eastern Europe reveal that implementation can be challenging due to the absence of private sector actors when formulating these strategies, and a lack of technical capabilities in local institutions to take a leading role in implementing the S3 process.

Finally, FDI attraction initiatives remain central to industrial development strategies across the region. However, these initiatives generally fail to integrate and promote local upgrading and innovation in the wider industrial strategy. Recently, there are increasing efforts to focus on key sectors, such as information and communication service centres, which have received preferential FDI treatment with mixed outcomes in countries like Czechia, Slovakia, Poland, Bulgaria, the Republic of Moldova, Belarus and Georgia.

across the region. Enhancing renewable energy production would allow the region to position itself as a primary driver of Europe’s transition towards a greener and more sustainable energy landscape.

At present, there are significant differences in the progress towards SDG 7 (affordable and clean energy) across the region. While some countries are hesitant towards the green transition and continue to support and subsidize fossil fuels, others have taken a clear stand by prioritizing renewable energy production.

Montenegro, for example, is becoming a regional renewable energy hub by focusing on clean energy as a key priority sector and strategic goal for the country. Over the last decade, Montenegro has increased its renewable energy capacity. Today, approximately 79 per cent of the country's total electricity generation capacity is derived from renewable sources, ranking the country second in Eastern Europe, and substantially exceeding the European average of 54 per cent. This expansion of renewable energy resulted from active government support. Key policy instruments included the harmonization of the national energy market to align with EU standards; feed-in-tariffs incentivizing renewable energy projects by guaranteeing fixed, preferential prices for renewable energy producers; streamlining the permit process for running renewable energy projects; and the provision of substantial tax incentives to promote renewable energy sources.

To expand access to clean energy, the region could benefit from adopting a “mission-oriented” approach⁶ to industrial strategy. Under this setting, the SDGs would act as the foundational principle, with concrete and measurable targets formulated in the industrial policies. Given the potential social fallout feared in the heavily fossil fuel-reliant parts of the region, embedding other SDGs (such as SDG 8 – economic growth and job creation) in industrial policymaking can guide the provision of social safety nets, for impacted individuals to ensure that no one is left behind.

Digitalization



The digital transition presents a promising avenue for advancing regional industrial development by driving job creation (SDG 8) and industrial upgrading (SDG 9). Advanced digital production technologies play a major role in enhancing the productivity of manufacturing firms and driving industrial competitiveness.⁷ Strengthening industrial innovation ecosystems can also help to create jobs by absorbing the highly skilled labour force to develop export-oriented, knowledge-intensive business services tied to advanced manufacturing models.

Some parts of the region, such as North Eastern European countries, have implemented policies to develop a competitive digital economy. Policy actions include using public procurement to support the information technology sector, establishing a legislative environment conducive to new firm creation, and promoting digital skills through education. While significant progress has been made in many Eastern European countries concerning digitalization, limitations still exist in strengthening industrial innovation ecosystems.

The South Moravian region in Czechia provides a good example of fostering local industrial innovation ecosystems (see Figure 2). The region's progress reveals that creating a supportive policy environment around relatively isolated success stories of competitive digital enterprises can lead to wider socioeconomic wins.



Figure 2. Czechia: Fostering an effective subnational innovation system

SUCCESS FACTORS	Long-term commitment of regional and municipal policymakers to instill structural change with the engagement of local experts	Adaptation of policy objectives and instruments to suit different stages of sectoral development	Formulation of specific strategic goals and establishment of a policy evaluation process	Collaborative partnership and co-financing of projects between a broad range of relevant local actors
POLICY ACTIONS	Creation of the South Moravian Innovation Center (JIC) with the aim of supporting entrepreneurship, the commercial use of research and development (R&D) activities, and co-ordinating the implementation of the region's Smart Specialization (S3) agenda	While the first two S3 strategies focused on motivating the emergence of start-ups, subsequent strategies focused on areas such as upgrading of R&D infrastructure, augmenting the international competitiveness of public research institutions, attracting FDI, developing nontechnical competencies of firms, and supporting selected domains of specialization around Industry 4.0 technologies	The most recent S3 strategy (2021-2027) sets the upgrading of activities of MNEs as one of its core targets and maps a number of proposed activities and associated performance metrics for this purpose. The policy evaluation process in turn considers the fulfilment of the strategic goals themselves, as well as the outputs of individual activities related to the overarching target	JIC provides "innovation vouchers", which award SMEs with credit to finance the purchase of services from research institutions. Considering that most businesses applying for the vouchers had no prior experience with academia, the policy tool created a bridge between local entrepreneurs and researchers and motivated continued collaboration
OUTCOMES	<ol style="list-style-type: none"> 1. Diversification of the economic base to encompass emerging innovative and competitive domestic firms. 2. Notable increase in the share of employed persons in high-tech sectors, reaching levels comparable to highly developed regions 3. Stronger local innovation system and a more knowledge-intensive economy 			

Source: Authors elaboration based on Matulova et al. (2015) and JIC (2021).



GVC reconfiguration

In the context of global reshoring trends, where companies are increasingly looking to bring production and services closer to their primary markets or home countries, Eastern Europe is in a good position to capitalize on nearshoring trends. A recent study found that the Western Balkan economies are experiencing increased nearshoring, as

multinational companies are shortening supply chains in response to the pandemic and geopolitical disruptions.⁸ Many of these investments are from Asia, as Asian firms are positioning themselves closer to the EU market they serve. Nearshoring in these countries appears to align with the global trend towards decarbonisation, as foreign companies cited the reduction of CO2 emissions as one of the main motivations for investing in the region.

While Eastern Europe holds notable potential to be on the receiving end of changing FDI patterns, FDI policies in the region tend to act in isolation from industrial policies, each with its mandate and agenda, leading to passive membership in GVCs. Integrating FDI promotion objectives into a wider industrial strategy would allow the region to attract specific types of investment in priority sectors and activities, while boosting a country's domestic capabilities and stimulating SDG 9. Technoparks can achieve this objective by offering a supportive environment for innovation and development. They appeal to technologically advanced companies for which the value of a supportive network and a dynamic ecosystem often outweighs the importance of lower production costs.

The case of Serbia offers an interesting example of how a country successfully attracted innovative, high-tech, high-skill foreign investment while also trying to stimulate domestic innovation and investment. Technoparks have played a notable role in Serbia's industrial policy strategy as a key industrial infrastructure facility to upgrade production processes and foster innovation. The parks target only high-tech companies and provide tailored benefits, advanced machinery and facilities, opportunities for research collaboration, networking resources, and other perks. Most companies hosted in the technoparks are domestic, but foreign companies locate their R&D centres in the park while keeping their production facilities nearby.



Regional integration

Economic growth presents a major challenge for the region, with a projected gap of 48 per cent to achieving the SDG 8 target by 2030. Policy actions focusing on revitalizing key industries, enhancing productivity, and fostering market diversification are instrumental in closing this gap. Leveraging cross-country industrial policy partnerships can enable knowledge transfer, technology diffusion,

access to larger markets, and propel industrial growth and competitiveness among less developed members.

Much of Eastern Europe is tightly integrated with the EU (through EU membership, candidate status, or free trade agreements), offering the region ample economic opportunities. Additionally, the EU has expanded the financial and policy space to include industrial policy, which has opened up doors for Eastern Europe to link up to regional industrial policy initiatives. This could bring countries in the region closer to entering regional supply chains and enhancing technology transfer. To do so successfully, Eastern Europe will need to harmonize and align national strategies and efforts to EU-wide priorities, promote greater representation in joint research networks, and strive for the more effective use of EU funds to finance SDG acceleration.

Slovakia's engagement with the EU's Important Projects of Common European Interest (IPCEI) initiative is a good example of successfully linking regional industrial policy initiatives to value chain upgrading. Through the IPCEI, EU member states can support projects that have the potential to contribute to the region's industrial competitiveness but would otherwise be underfunded. Under the initiative, eligible research, innovation and infrastructure projects in targeted sectors (e.g., hydrogen technologies, batteries and microelectronics) are entitled to direct subsidies from member states without being limited by the EU's competition policy. These projects are grouped into value chains to connect companies so they can exchange experiences and collaborate. Yet, industrial policy frameworks such as the IPCEI are rarely picked up by the less economically advanced parts of the EU, reflecting the differing capabilities of individual member states.

To overcome this gap, Slovakia's Recovery and Resilience Plan explicitly sets out the promotion of international cooperation and involvement in

EU-funded initiatives as one of the country's main investment priorities. The Slovak government has adopted several policy actions to increase the access of institutions to cutting-edge projects in the EU. These include the establishment of an innovation agency (VAIA), financial and technical assistance to top-up research financing, and

assistance in the application process and matching of grants. In the case of IPCEI, promising cases are emerging, as ten firms originating from Slovakia have successfully joined the research consortia focused on state-of-the-art value chain development.

Lessons learned

The experiences across Eastern Europe present common challenges to overcome and demonstrate how industrial policy can be put to work for the achievement of the SDGs. Three important takeaways are:

- 1. Success needs policy continuity.** Industrial policy outcomes take many years to materialize. Therefore, cultivating broader societal consensus in Eastern Europe regarding the usefulness and need for industrial policy represents a foundation for success in modern economies.
- 2. Governments need to work with stakeholders.** Collaboration with relevant stakeholders is vital for a successful industrial policy

set-up. As demonstrated in the case of Serbia's technoparks or the South Moravian innovation landscape, good practices emerge when academia, private and public sectors come together to pursue shared objectives.

- 3. International collaboration and regional coordination are crucial.** Given Eastern Europe's tight embeddedness (through EU membership, candidate status, trade or investment) with other economically advanced European countries, participation in cross-regional industrial policy initiatives with countries of different development levels can stimulate learning, domestic capabilities, and drive innovation.

Endnotes

1. This brief summarizes the main findings and messages of UNIDO (2024) "[Industrial Development Report 2024. Turning Challenges into Sustainable Solutions: The New Era of Industrial Policy](#)", Chapter 7. It is important to note that this brief focuses on long-term developments and perspectives in the region and does not consider the impact of recent geopolitical conflicts such as the war in Ukraine.
2. See [UNIDO \(2024\)](#), Chapter 2.
3. The analysis of this brief focuses on all Eastern European States listed in the corresponding [United Nations regional group of the General Assembly](#).
4. It is important to note that there are subregional differences in the SDG indicators presented in this policy brief. To explore the sub-regional data on SDG progress for Eastern Europe, see Figure 7.2. page 139 of [UNIDO \(2024\)](#).
5. The target for innovation is given by the best performer country in the corresponding SDG indicators during the period of analysis. See [UNIDO \(2024\)](#), Annex A for the details.
6. See Mazzucato, M. and R. Kattel (2023) "[Mission-oriented industrial strategy](#)". UNIDO IID Policy brief series, No. 2.
7. See UNIDO (2019) "[Industrial Development Report 2020. Industrializing in the Digital Age](#)". Vienna: UNIDO.
8. See Jovanović, B., et. al. (2024). [Transforming the Western Balkans through near-shoring and decarbonisation](#). Western Balkans 6 Chamber Investment Forum.



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