MAY 2018

Policy Notes and Reports 22

Western Balkans EU Accession: Is the 2025 Target Date Realistic?

Richard Grieveson, Julia Grübler and Mario Holzner

The Vienna Institute for International Economic Studies
Wiener Institut für Internationale Wirtschaftsvergleiche

Western Balkans EU Accession: Is the 2025 Target Date Realistic?

RICHARD GRIEVESON
JULIA GRÜBLER
MARIO HOLZNER

Richard Grieveson and Julia Grübler are Research Economists at the Vienna Institute for International Economic Studies (wiiw). Mario Holzner is Deputy Director at wiiw.

The authors would like to thank Robert Stehrer, wiiw Scientific Director, and Vladimir Gligorov, wiiw Senior Research Associate, for valuable comments and ideas.

Abstract

The European Commission has set a target date of 2025 for Western Balkan EU accession, while also outlining a broader new strategy which includes Brussels taking a more active role in solving political disputes in the region, and upgrading infrastructure as part of the Berlin Process. We welcome these moves: economic underdevelopment in the region is closely tied to political fractures. Aside from resolving political conflicts, improved governance in the region will also be necessary. In terms of meeting economic accession criteria, the region faces a host of challenges, but we believe that a focus on upgrading infrastructure and developing a much bigger and more competitive industrial base should be the priorities. While the economic influence of third parties in the region is not as significant as often portrayed, this is not guaranteed to last, particularly in the case of China, which is set to increase its economic presence in the Western Balkans in the coming years. Even if the region takes a great leap forward towards the EU, there are other barriers in the way which could also hold back accession. Nevertheless, while the 2025 target represents a highly ambitious best-case scenario, it could serve as a powerful incentive for countries in the region to speed up their reform agendas. We do not completely rule out at least Montenegro and Serbia joining the bloc by 2025 or shortly thereafter.

Keywords: integration, governance, economic growth, competitiveness, industrialisation, infrastructure, economic policy, Western Balkans, EU

JEL classification: E60, F15, F21, F43, H54, O11, O14, O18, O20, O24

CONTENTS

TABLES AND FIGURES

Western Balkans EU accession: Is the 2025 target date realistic?

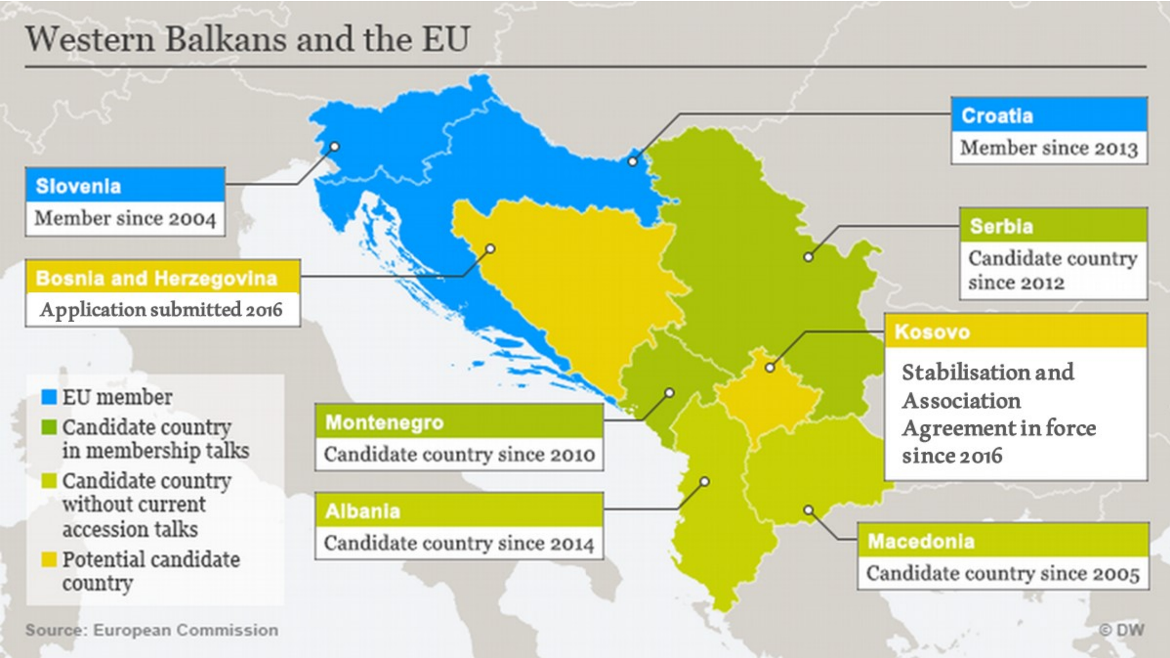
The target is highly ambitious, but at least for Serbia and Montenegro, not completely unrealistic. Solving political disputes within the region, and upgrading infrastructure, governance and the industrial base, should be the priorities.

I. INTRODUCTION: A NEW APPROACH FROM THE COMMISSION

The EU-Western Balkans summit will take place on May 17th in Sofia. According to statements from the EU ahead of the meeting, it will focus on three things:

- Reaffirming the EU's commitment towards its Western Balkans partners and reiterate the region's belonging to the European family.
- Strengthen links between the EU and the Western Balkans in infrastructure, digital and human connectivity.
- Working more closely together to tackle common challenges, such as security, migration, geopolitical developments and good neighbourly relations.

Figure 1 / Status quo: 15 years after the Thessaloniki promise



Note: As of December 2017 – Serbia: 12 chapters out of 35 opened, of which 2 preliminarily closed, Montenegro: 30 chapters opened, of which 3 preliminarily closed.

15 years after the Thessaloniki promise, most countries in the region are still stuck in the waiting room. Croatia joined in 2013. Otherwise Macedonia has been a candidate since 2005 (but held back by a name dispute with Greece), Montenegro since 2010, Serbia since 2012 and Albania since 2014. Bosnia submitted an application to join in 2016, and Kosovo's Stabilisation and Association Agreement (SAA) with the EU came into force in the same year. Membership talks have started for Serbia and Montenegro, and the European Commission recommended recently that talks should also start with Albania and Macedonia.

A new approach from the EU

In 2014, European Commission President Jean-Claude Juncker said that no country would join the EU during the current parliament. However, this was accompanied not long after by a greater attention by some bigger EU member states on the region, emphasised most clearly by the Berlin process. This was followed in 2018 by an ambitious new strategy for the region accounted by the European Commission, which set a target date of accession of 2025 for Serbia and Montenegro[1] (with a note that others could also catch up).

The approach of the European Commission, Germany and France in particular reflect the acknowledgement that a lot is at stake. We see four reasons for the renewed focus on the Western Balkans now:

- First, the 2015 **migration crisis** drew attention to the importance of the Western Balkans for the EU in a security sense. From the perspective of governments in countries like Germany, such an inflow of people in such a short space of time, and the sense the national governments were not in control of their own borders, must not happen again. The migration has risen up the agenda since then in much of Western Europe. In Austria, the far right have ended power, while the hard-right Alternativ für Deutschland is now the biggest opposition party in Germany according to most opinion polls.

- Second, there was a concern that some of the **intra-regional conflicts were heating up**. Recent high profile incidents involving Kosovo and Serbia represent a key example of this. The threat of instability in Bosnia has also risen.

- Third, there are growing concerns—loudly and regularly expressed in the media in Western Europe—about the **growing influence of outside powers in the region**. This has included (but is not limited to) worries about Russia, Turkey and China.

- Fourth, there is a clear feeling in Brussels that ultimately **the Western Balkans belongs in the EU**. Geographically, the region is surrounded by EU member states. This sense of the EU being the Western Balkans' ultimate destination appears to be both stronger and more widespread than in the case of, say, Ukraine. The fact that Albania and Montenegro are NATO members, while not directly connected to EU membership, also matters, in further reinforcing the region's tilt towards euro-Atlantic institutions.

---

1 https://ec.europa.eu/commission/news/strategy-western-balkans-2018-feb-06_en

The new Commission strategy notably puts a much bigger focus on taking a hands-on approach to solving political conflicts in the region. For two decades, the EU strategy for the Western Balkans has been characterised by a focus on economic connectivity as a way of driving political conciliation. In short: countries that trade with each other and that are well connected will not fight each other, and may eventually become friends. In addition, the EU has sought to open its markets to the Western Balkan countries to help develop the external sectors of the region. Western Balkan countries have enjoyed free trade with the EU since 2000. Regional trade integration was cemented by the Central European Free Trade Agreement (CEFTA) in 2007. The new Commission strategy, by contrast, acknowledged that often political tensions are themselves a barrier to greater connectivity and trade between countries.

Figure 2 / Political crisis hotspots in the Western Balkans

Source: BBC.

Figure 3 / EU actively supports reconciliation

Source: European Commission.

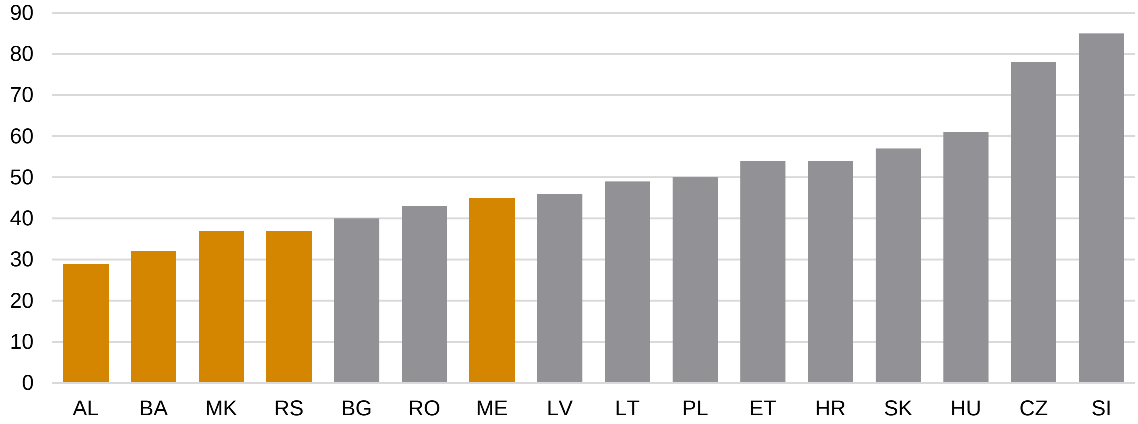
Ambitious targets

The new target for accession is highly ambitious, even for Serbia and Montenegro, and probably deliberately so. However, we do not reject it out of hand. In this paper, we aim to assess how realistic the 2025 target date for accession is, and where the main barriers are to achieving this.

At least for some countries in the region, economic development per se is not a problem for EU accession. Or put another way, the economic problems of the Western Balkans are not necessarily explained by or encapsulated in GDP per capita income levels. Particularly in the cases of Serbia and Montenegro, GDP per capita levels as a share of the EU average are roughly in line of those with Romania and Bulgaria when they joined the EU in 2007 (Figure 4). Even as of 2016, data on wage convergence with Austria in PPP terms showed almost all countries in the region at a higher level than Bulgaria. Montenegro is particularly advanced on this measure.

Figure 4 / Per capita GDP at PPP

EU average = 100. Year of accession, 2016 for Western Balkan countries.



Sources: Eurostat, wiiw.

Economic challenges

However, the economic challenges to accession are clearly significant and numerous. The most recent Commission progress reports, published in April[2], refer to various idiosyncratic obstacles to Western Balkans economies on their road to EU accession. Clearly, the challenges faced by Montenegro (the region's most developed economy) are not the same as those faced by Kosovo (the least developed). However, looking across the reports, there are several common themes. A lack of competitiveness, big external deficits, high public debt, rigid labour markets (according to the Commission linked to high unemployment and large-scale outward migration), weak governance, a large informal economy, and infrastructure deficiencies appear in most if not all country reports.

2 https://ec.europa.eu/neighbourhood-enlargement/countries/package_en

II. FOUR BIG CHALLENGES FOR THE NEXT DECADE

Among these various factors, four things stand out as particularly problematic in our view. Tackling and resolving political conflicts (which act as a barrier to economic development), infrastructure deficiencies, weak governance and the generally small industrial base are particularly pressing issues. This is not the whole story, but solving these four issues would provide help to solve the region's economic problems more generally, and improve its ability to meet the criteria for EU accession.

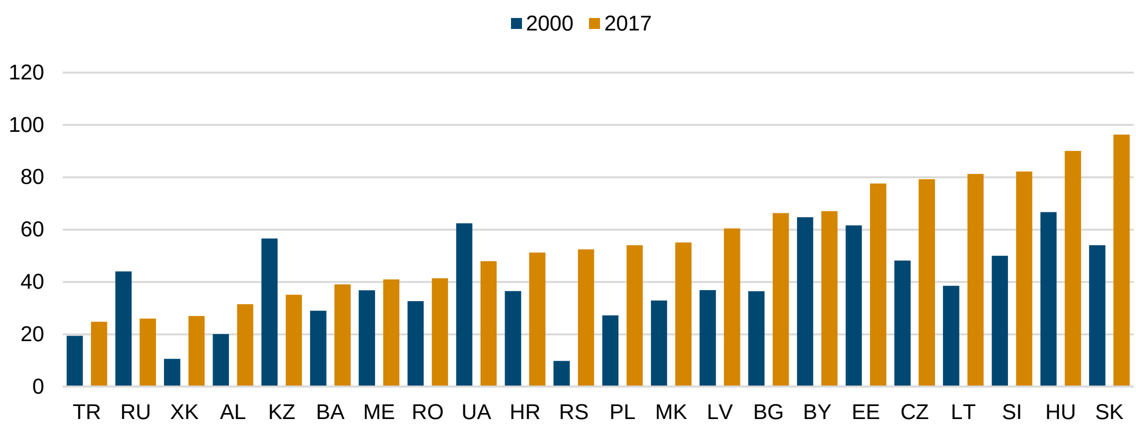
1. Solving political conflicts as a first step for economic development

We welcome the greater focus on solving political conflicts, given that these are often a barrier to economic connectivity and development in the region. By taking a more active stance in the region, including via the "Brussels process", the Commission could drive political reconciliation that delivers important economic benefits as well.

Admittedly, the Commission approach of the past two decades has produced positive results from an economic perspective. Since the EU opened its markets to the region in 2000, the overall shares of exports in GDP in the Western Balkans have doubled. Macedonia and Serbia in particular have achieved relatively high levels even compared with many EU member states (Figure 5).

Figure 5 / Exports of goods and services

% of GDP



Sources: wiiw, national statistics offices. Note: BiH and Kosovo data for 2005 and 2017.

However, efforts to stimulate intra-regional trade have been much less successful. With the exception of Montenegro and Kosovo (which both anyway have very low merchandise trade/GDP ratios), the shares of merchandise exports to partners within the region have generally fallen over the past decade. While total exports have grown strongly over the past ten years, trade within the region has largely been flat over the period, and in almost all cases accounts for a fairly low share of the total.

An important reason for subdued regional trade, especially compared with exports outside the region over the past decade, is a shortage of demand. While Western Balkan exports to the EU are effectively supply-constrained (the region can sell as much as it can produce), those within the region are demand constrained. Even by European standards, most of the Western Balkans has had a tough post-crisis period. In Serbia, comfortably the region's biggest economy and therefore most important potential source of regional demand, real final consumption expenditure in 2016 (last year for which full comparable regional data are available) was still below 2008-09 levels. Montenegro and Bosnia also recorded among the weakest performances in CESEE over this period.

However, a lack of demand is clearly not the only issue. Domestic demand in Albania and especially Kosovo have risen quite strongly since 2008, without any discernible impact on regional trade patterns. It is clear that political factors, and specifically multiple instances of bad bilateral relations between countries in the region (combined with related connectivity deficits), have held back intra-regional trade growth. In this sense, while we welcome attempts to further facilitate trade via, for example, a regional common market[3] (as floated by Johannes Hahn, the European Commissioner for European Neighbourhood Policy and Enlargement Negotiations), we believe breaking the political barriers to higher trade is a greater priority.

Finally on politics, the Commission believes that intra-regional disputes must be solved before countries join the EU. This is partly informed by past experience, and particularly the Croatia-Slovenia dispute over the sea border in the Gulf of Piran[4], which officials in Brussels are keen to avoid in the future. Most importantly here, the Commission has stated a legally-binding agreement between Kosovo and Serbia must be signed before either joins the EU[5]. This makes sense to us, although it is clear that the challenges are enormous. Among other things, we have noted the legitimacy issues that leaders on both sides, but perhaps especially in Kosovo, will face in pushing through any possible agreement domestically[6]. Here perhaps more than anywhere else under the new strategy, the involvement and role of the Commission, and the EU more generally, will be key.

2. The challenge of bad governance

The quality of governance and institutions matters a lot for growth, including in the CESEE region (Guriev 2017). Moreover, upgrading governance standards to EU levels are a key part of meeting the accession criteria.

We find that the governance deficit in the Western Balkans is big, even compared with the laggards among current EU member states such as Romania and Bulgaria. On average, using the World Bank governance indicators, the six Western Balkans countries stand at around two thirds of the levels of Croatia, Bulgaria and Romania when they joined the EU (Figure 6).

Moreover, we find that based on current trends, meeting the EU accession criteria by 2025 looks very ambitious for even the frontrunners among the Western Balkan countries. Our baseline scenario sees Montenegro reaching the level of governance required to join the EU in around 12 years, while Bosnia will take 23 years (Figure 7). A leap forward in governance standards is certainly not

3 https://wiiw.ac.at/challenges-to-a-customs-union-and-common-market-in-the-western-balkans-n-227.html

4 https://wiiw.ac.at/slovenia-and-croatia-at-sea-n-234.html

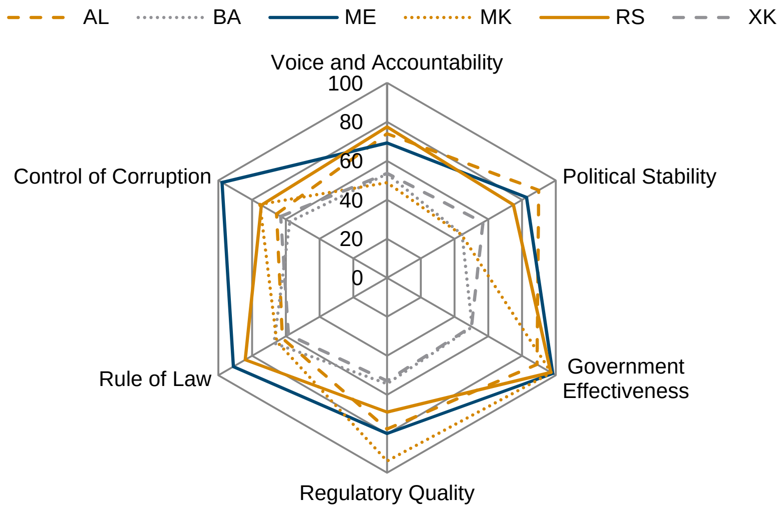
5 https://www.theguardian.com/world/2018/apr/26/now-chance-kosovo-deal-serbian-president-what-cost-aleksandar-vucic

6 https://wiiw.ac.at/serbia-and-kosovo-legitimacy-deficits-are-barrier-to-brussels-agreement-progress-n-296.html

impossible, but will require a more concerted effort at the local level than we currently see. Political fragmentation and instability in some countries will make this even more challenging (and emphasises the importance of a more active role for the EU).

Figure 6 / Large governance deficits – a third of the way still to go

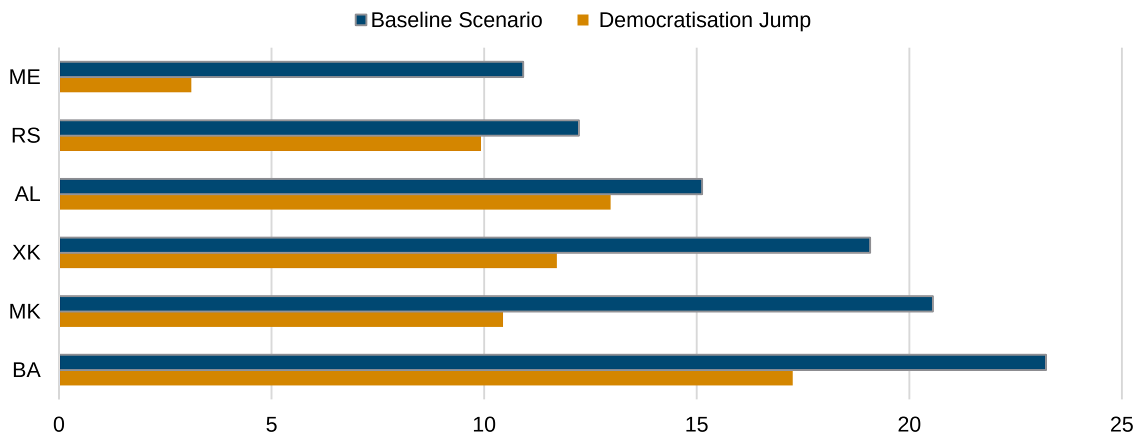
2016 governance indicators in % of average for BG, RO, HR upon EU accession



Note: The Worldwide Governance Indicators (WGI) combine the views of a large number of enterprise, citizen and expert survey respondents. Percentages were calculated after adding a standard deviation of 1 to the original values.
Source: WGI, wiiw calculations.

Figure 7 / Bridging the governance gap within 8 years is unrealistic

Years necessary to reach the governance level of BG, RO, HR upon EU accession



Note: The average governance reform speed of Bulgaria, Romania and Croatia in the 8 years prior to their accession was assumed. In case the countries experienced a faster speed between 2010 and 2016 (last data point) their own speed was applied to the difference of the 2016 level and the average level of the benchmark countries upon their accession. One year was subtracted in order to make it comparable with the announced 2018-2025 target accession period of eight years. The 'Democratisation Jump' excludes the sub-indicators:
Voice and Accountability as well as Political Stability.
Source: WGI, wiiw calculations.

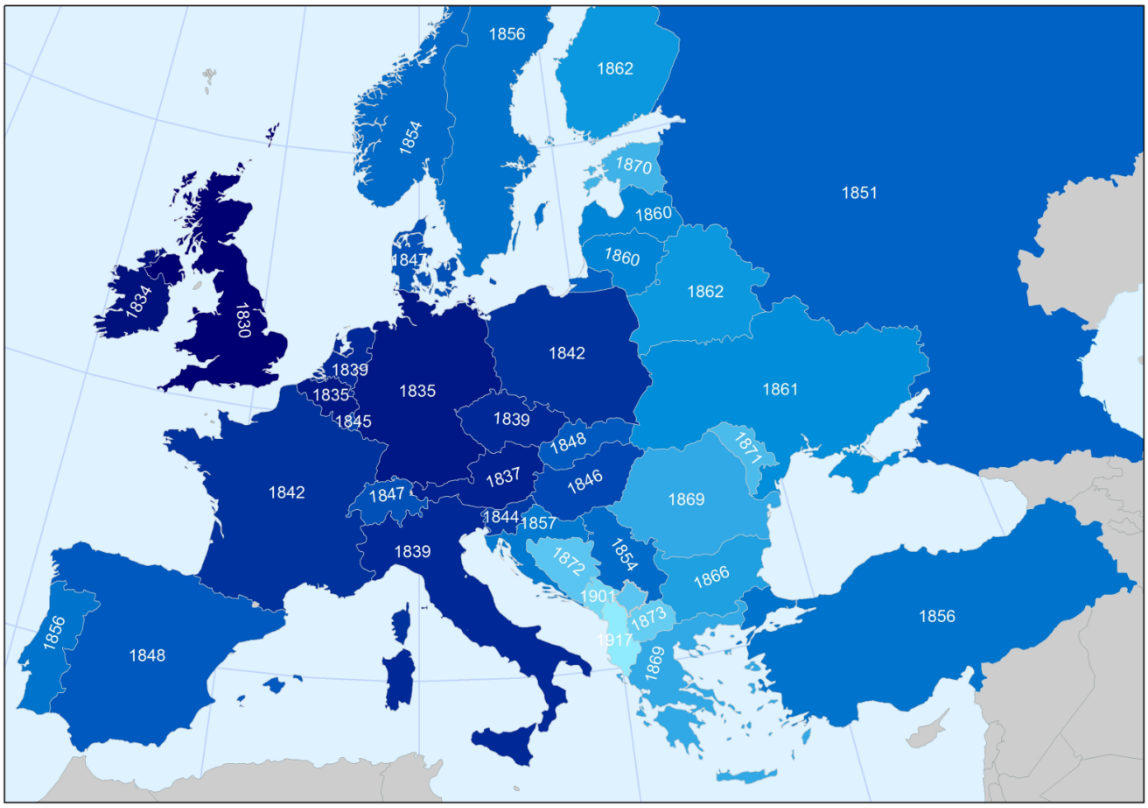
A strong improvement in democratic standards—as partly seen more recently for example in Macedonia—could reduce the time needed for reform. In a second 'democratisation jump' scenario Montenegro could reach the respective governance levels of Bulgaria, Romania and Croatia upon their accession in just three years. The others would still need around 10-13 years, Bosnia even 17.

3. Connectivity and infrastructure development

The third major challenge we see is that the Western Balkans suffers from a major infrastructure deficit, which hampers economic development. This is hardly a new issue, and can be traced back at least 200 years. The historical division of the region between empires contributed to this. The region has long suffered from a lack of connectivity and poor infrastructure (Figures 8 and 9), in terms both of links within and outside of the region. Railways, for example, both arrived much later in the Western Balkans than in the rest of Europe, and once they did spread much more slowly (Holzner et al 2015). This played an important role in holding back the economic development of the Western Balkans and its lack of convergence with Western Europe income levels, a challenge that the region is yet to overcome (Figure 10).

Figure 8 / Late introduction of railway time in the Western Balkans

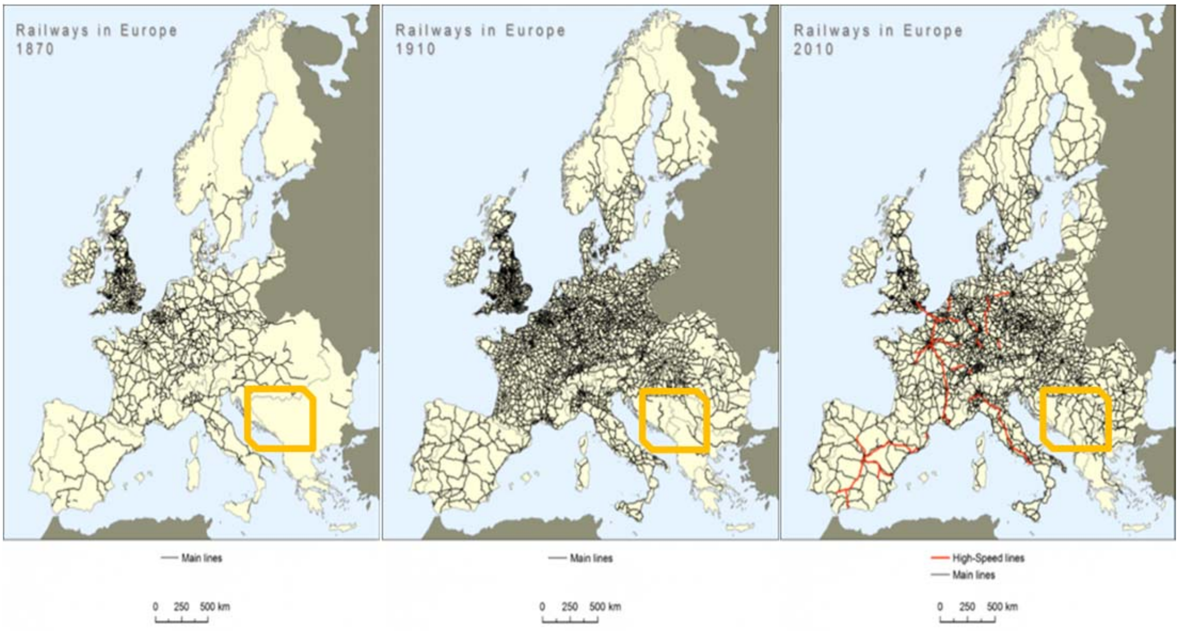
Year of construction of first railway line



Note: Kosovo 1874.
Source: Wikipedia, Wikimedia, FDV.

Figure 9 / Low density of railway network in the Western Balkans

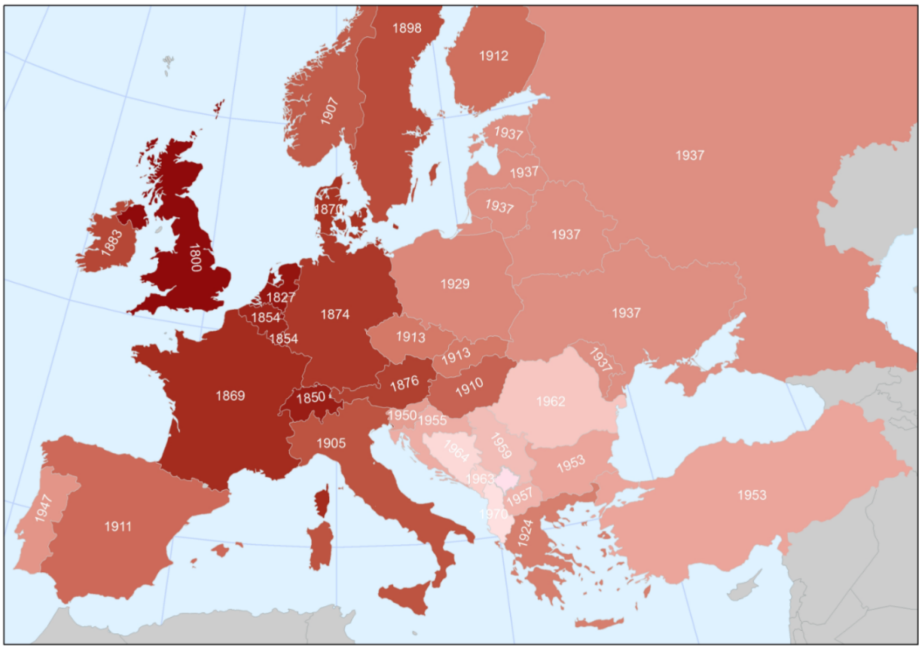
Core railway network in Europe, 1870, 1910 and 2010



Source: HGISE Railways Historical Database.

Figure 10 / Industrial Revolution's slow trickle down

Year of surpassing 2000 USD in GDP per capita (1990 Int.$ at PPP)

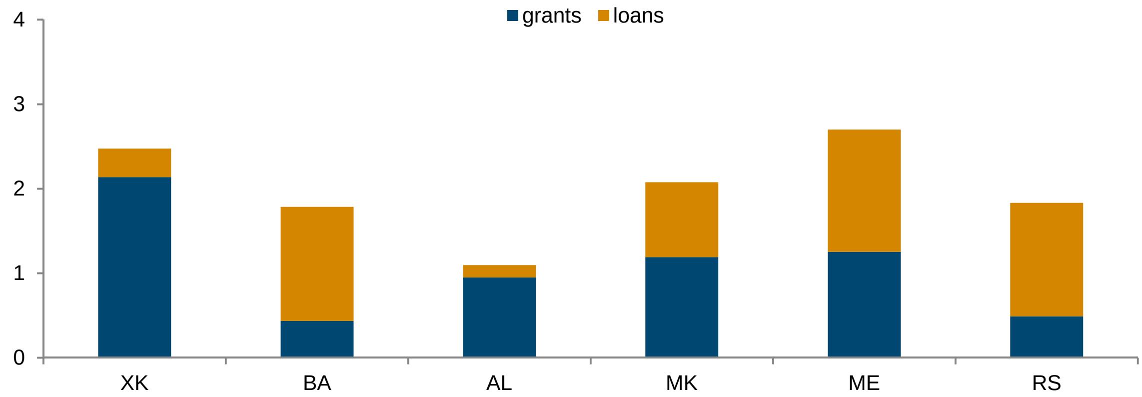


Note: Interpolation for Ireland; extrapolation for Slovenia; Kosovo 2002 estimate based on wiiw data; Czechoslovak observation for Czech and Slovak Republic; Belgian observation for Luxembourg, Soviet observation for Russia, Estonia, Latvia, Lithuania, Belarus, Ukraine and Moldova.
Source: The Maddison-Project, wiiw, own estimates.

This long-term historical deficit was then compounded by the wars of the 1990s, and the (linked) delayed accession to the EU. This had three important implications for connectivity in the region. First, physical infrastructure was destroyed in the wars, including infrastructure connecting what would become different countries in the former Yugoslavia. It is emblematic that so many bridges were destroyed. This ranges from the destruction of the historic Old Bridge in Mostar in Herzegovina to the NATO bombing of Serbian bridges across the Danube. Second, even after the wars ended, political relationships remained at best strained (if not outright non-existent), limiting the willingness of countries to develop physical transport connections between them.

Figure 11 / The EU's financial support is modest in per annum terms

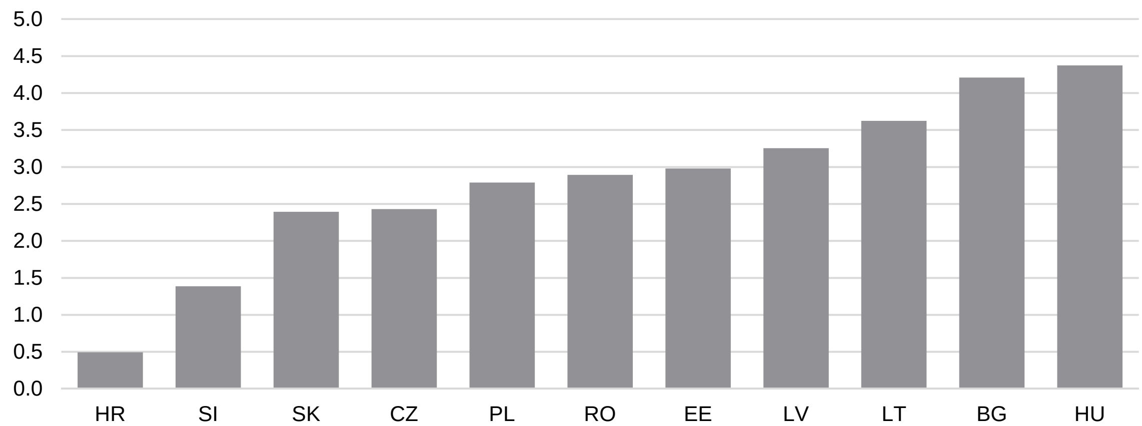
IPA and WBIF grants and EIB loans, in % of GDP per annum



Note: IPA pre-accession funds are earmarked for the period 2007-2020. WBIF (Western Balkans Investment Framework) data is for the period 2009-2017. This is also the observation period for the loans of the European Investment Bank (EIB).
Source: EC, wiiw Annual Database, wiiw calculations.

Figure 12 / EU budget net operating balance

% of GNI, 2012-16 average

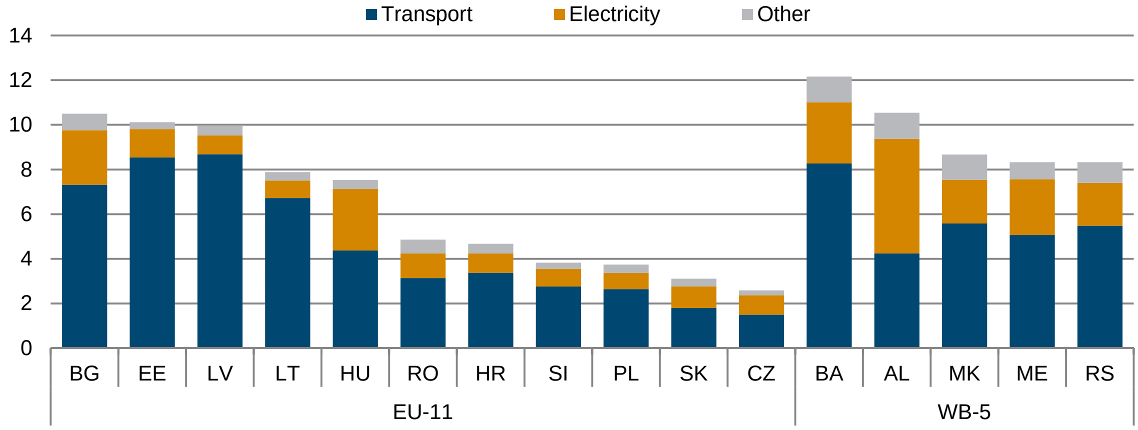


Sources: European Commission, wiiw.

Third, the wars contributed heavily to the delay in the region joining the EU, which has meant the Western Balkan countries missed out a huge amount of funds available to their regional peers for infrastructure upgrading (Figure 11). Eight formerly Communist countries joined the EU in 2004, and another two in 2007, with Croatia arriving in 2013. Over this period, these countries have had access to full EU funds, something that remains largely unavailable to the Western Balkan countries (Figure 12).

Figure 13 / Substantial investment needs

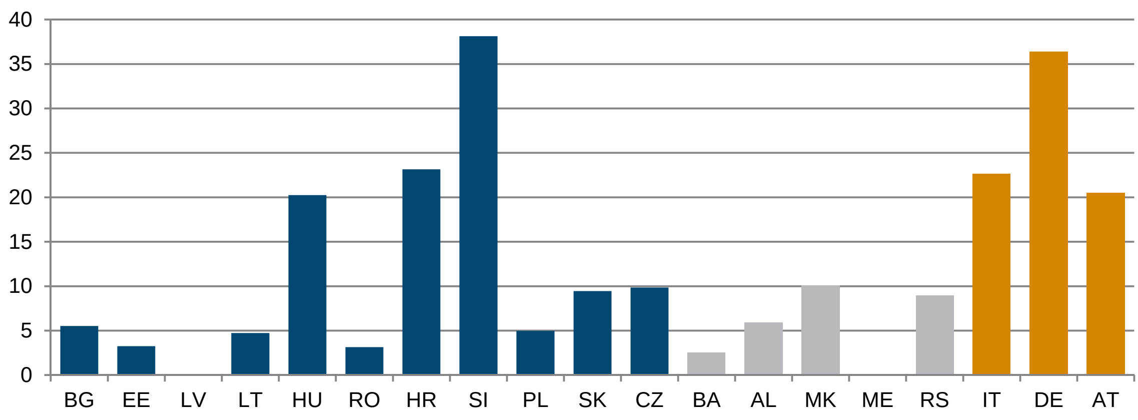
Infrastructure investment needs 2018-2022 in % of GDP per year



Note: CZ extrapolated from relationship between PL and SK; all data in % of 2015 GDP at 2010 prices.
Source: EBRD Transition Report 2017-2018, own calculations.

Figure 14 / Low motorway density in the Western Balkans

Motorway density in km per 1000 km² land area, 2015



Note: AT, BG, IT 2014; AL own estimate.
Source: Eurostat.

These factors have meant that the region's existing infrastructure deficit has, if anything, grown wider. Infrastructure investment needs in the Western Balkans are estimated by the EBRD to be between 8% (Serbia) and 12% (Bosnia) of GDP per year over the period 2018-2022, significantly higher than for most EU member states (Figure 13). Railway and motorway density in the region remains far below that of neighbouring EU member states such as Bulgaria, Croatia, Hungary, Romania and Slovenia (Figure 14).

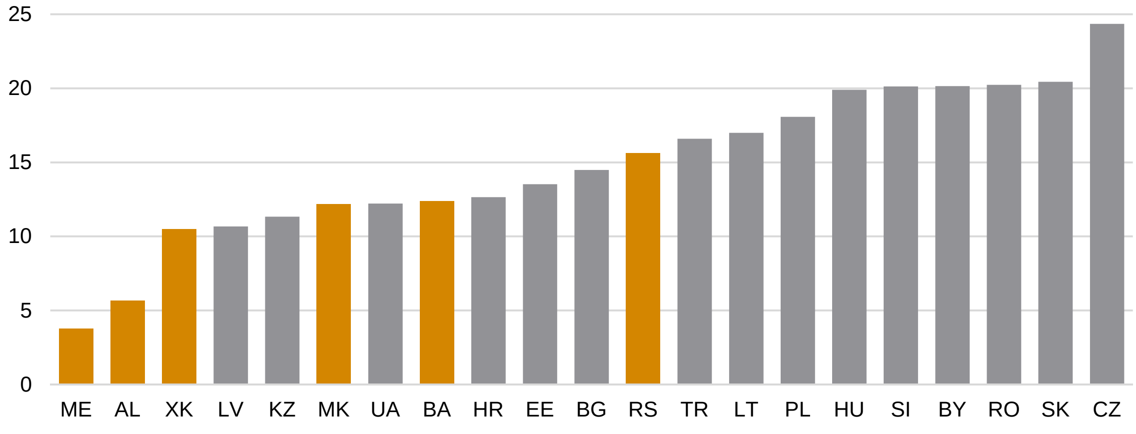
In this context, the Berlin Process is a welcome development. Annual meetings with a focus on connectivity mean that the issue stays at least on the agenda. According to our calculations, announced projects in the Berlin Process, if realised, will add 1 percentage point per year to GDP in all Western Balkan countries over a 15-year time horizon. Moreover, around 200,000 jobs would be created, equivalent to around 4% of the region's workforce.[7]

4. The lack of an industrial base

The fourth main challenge that we see is the very small industrial base of most countries in the region. Even before transition, the region was not very highly industrialised, and has if anything only fallen further behind other CESEE countries since. The lack of a manufacturing base has contributed to the weakness of intra-regional trade flows, limited demand for services and R&D, and a poor record on innovation. All of the Western Balkans non-EU members are comfortably below the regional average for manufacturing as a share of GDP except Serbia (Figure 15).

Figure 15 / Manufacturing, % of GDP

2016 data



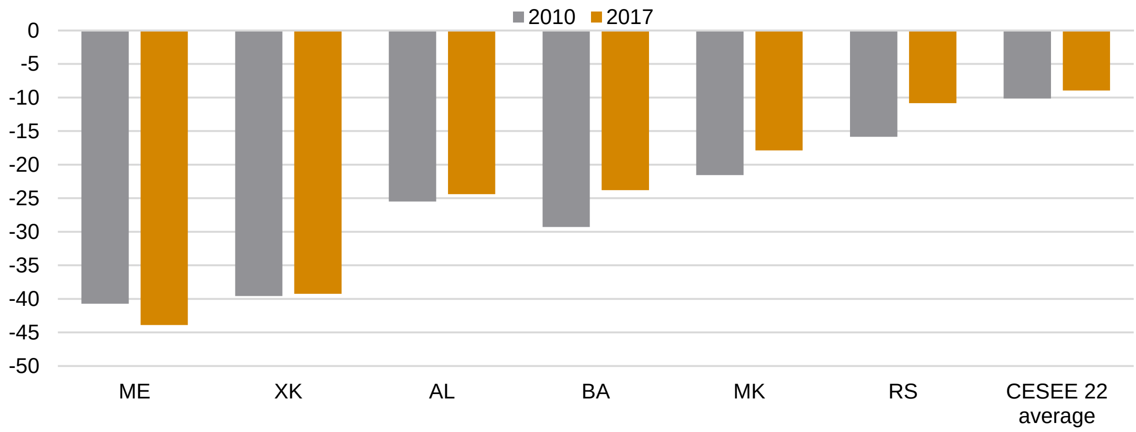
Sources: Eurostat, wiiw.

Small industrial bases have also been a key factor behind the massive trade deficits and consequence macroeconomic imbalances that countries in the Western Balkans face (this is highlighted as an issue across the Commission progress reports). Only Serbia has a trade shortfall anywhere close the regional average (Figure 16). This has held back productivity growth and per capita income convergence. The Western Balkans countries have struggled to integrate into global value chains, and attract a much lower level of (manufacturing) FDI per capita than their peers in the EU. This is also partly the reason for the region's low employment rates.

7 https://wiiw.ac.at/infrastructure-investment-in-the-western-balkans-p-3661.html

Figure 16 / Merchandise trade balance

% of GDP

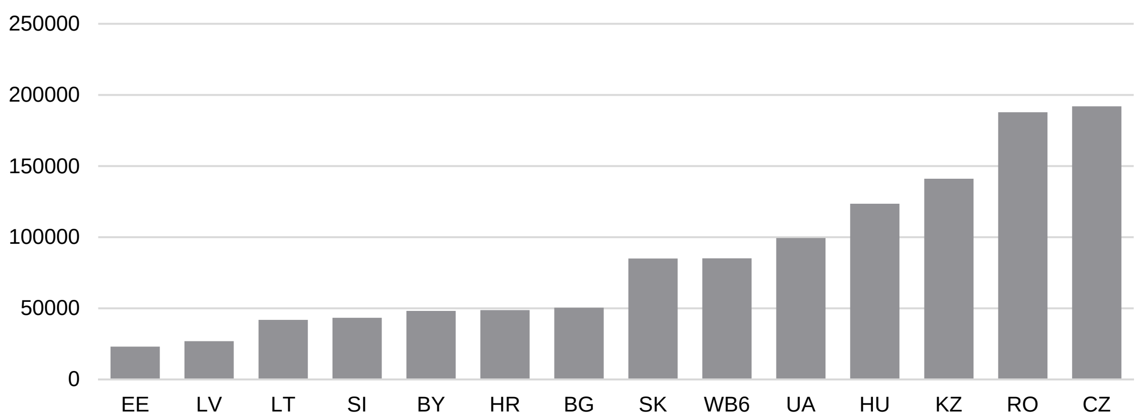


Sources: National central banks, wiiw.

Given the low savings rates in the region, the funds for a bigger industrial base will have to come from FDI. Last year, wiiw complied a major FDI report for CEFTA (Hunya et al 2017). We found that FDI inflows into the Western Balkans relative to their GDP size was actually no lower than EU-CEE countries on average. However, this primarily reflects their small size (put together in nominal GDP terms they are roughly the size of Slovakia, see Figure 17). Most have struggled to attract investment into higher value added sectors in the tradeable sector. Our study identified weak governance and infrastructure deficiencies as key barriers to attracting a better quality of FDI. [8]

Figure 17 / Nominal GDP

EUR million, 2017 data



Sources: wiiw, national statistics offices, Eurostat.

To a certain extent, Macedonia shows the way for the rest of the region. Along with (to a lesser extent) Serbia, Macedonia has bucked the regional trend in developing a relatively big export-oriented

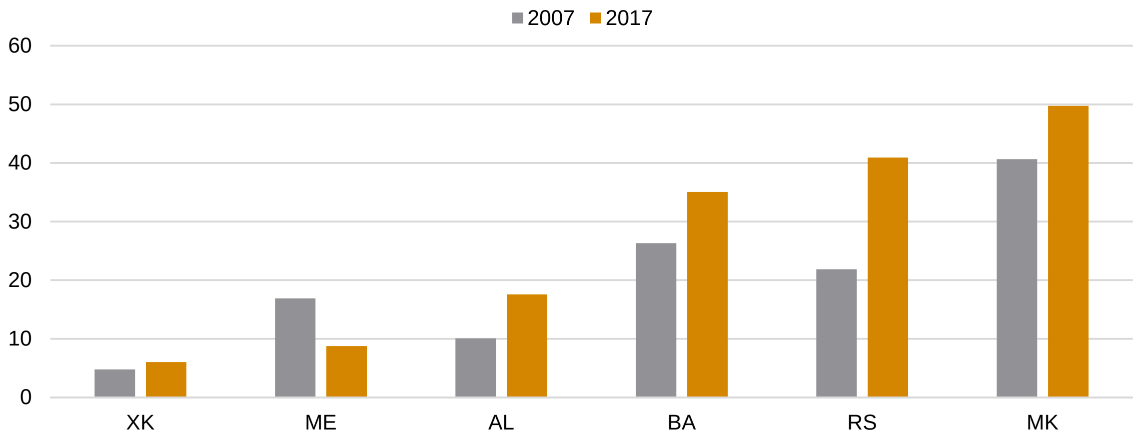
[8] https://wiiw.ac.at/wiiw-prepares-first-regional-investment-report-for-cefta-n-284.html

manufacturing sector[9]. Merchandise exports were equivalent to 50% of GDP in 2017 in Macedonia, and 41% in Serbia. These levels were still far below those in the manufacturing powerhouses of central Europe (especially the Czech Republic, Slovakia and Hungary), but otherwise roughly in line with levels seen in the rest of CESEE. However, Albania, Kosovo and Montenegro lag significantly behind (Figure 18).

Moreover, even in Macedonia, the process is far from complete. Our research on the Macedonian tradeable sector finds that it is not sufficiently diversified and internationalised, with a dominance of larger firms, and not appropriately innovative. We found that policy should focus on supporting innovation, easier access to the product market in support of entrepreneurship, and support for the internationalisation of economic activities. Both public policies and the financial system should be supportive of these improvements in the product market.

Figure 18 / Merchandise exports

% of GDP



Sources: wiiw, national statistics offices.

III. ADDITIONAL ECONOMIC CHALLENGES … IT'S ALL CONNECTED

The four issues described above are not the whole story. However, in our view addressing them would go a long way to helping to solve others, notably the lack of employment opportunities. Regional labour markets improved last year, but remain beset by high unemployment and low activity rates (Figure 19), especially among young people according to a major study undertaken by wiiw and the World Bank[10]. Continued large-scale emigration reflects a lack of opportunities at home.

A previous wiiw study found that much better employment conditions could be achieved via several policy steps[11]. A more widespread use of collective bargaining would ensure cooperation between labour and industry in maintaining competitiveness. Better quality vocational training, and

9 https://wiiw.ac.at/macedonian-exports-p-4275.html

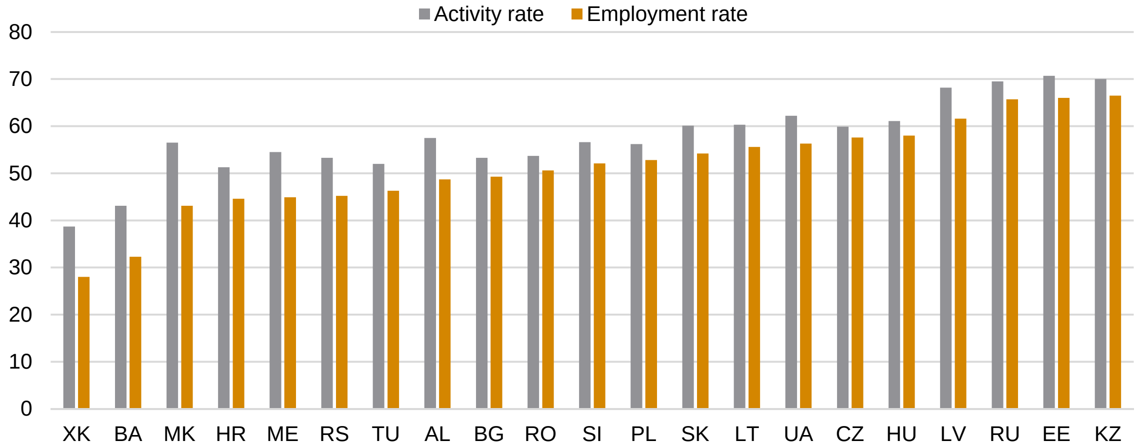
10 https://wiiw.ac.at/further-improvement-in-western-balkan-labour-markets-last-year-n-292.html

11 https://wiiw.ac.at/infrastructure-investment-in-the-western-balkans-p-3661.html

stronger links between industry and the education system would also help.[12] The region has generally been slow to adapt to changing circumstances in the labour market, owing to factors including resistance to reform, corruption in the education system, a lack of quality control in private institutions, and low incentives for new providers of vocational training (Arandarenko and Bartlett, 2012). Even in countries with relatively high levels of enrolment in vocational training (such as Serbia and Bosnia), this is not matched by professional skills acquisition[13]. One caveat here, however, is the point made recently by Ivan Krastev at wiiw's Spring Seminar, that improved education in CESEE simply leads to increased outward migration[14].

Figure 19 / Labour market indicators

LFS data, %



Sources: wiiw, national statistics offices, LFS.

IV. HOW MUCH OF A THREAT DO OUTSIDE ACTORS REALLY POSE?

Concerns about the influence of outside actors in the Western Balkans from the likes of Russia, Turkey and China, and the potential for these countries to seriously compete with the EU for influence, have grown louder in recent years. However, at least in an economic sense, we see these concerns as being often overplayed. From the perspective of trade and FDI, for example, it is difficult to overstate the dominance of the EU in the Western Balkans (and consequently the much smaller role of other powers, see Figures 20 and 21).

Russia's investment in the region tends to be motivated by political and security factors. Russian FDI in the Western Balkans is chiefly focused on the energy sectors in Serbia and the Republika Srpska in Bosnia, along with private real estate in Montenegro. Russia accounts for 11% of the inward FDI stock in Montenegro, and 6% in both Serbia and Bosnia, but effectively nothing anywhere else. Turkey's FDI in the region tends to be more commercially-driven, and is more diverse in terms of sectors and partner countries. However, its highest level is 14% of the total in Kosovo, followed by 8% in Albania, 5% in

12 https://wiiw.ac.at/2017-western-balkans-summit-in-trieste-the-quest-for-a-common-market-n-236.html

13 http://blogs.lse.ac.uk/lsee/2014/06/05/vet-balkans/

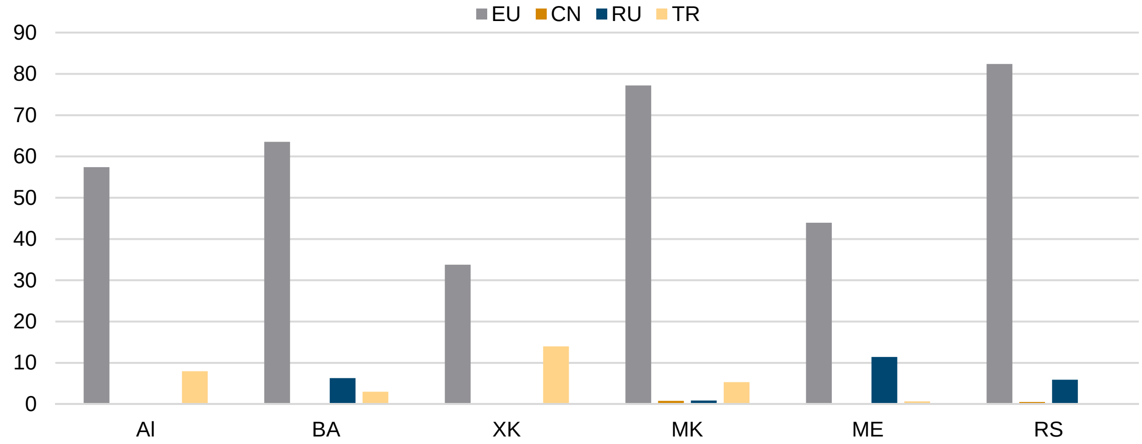
14 https://wiiw.ac.at/exit-noise-and-disloyalty-n-302.html

Macedonia, 3% in Bosnia and 1% in Montenegro. All of these levels are dwarfed by the EU, which accounts for an average 60% of the total FDI stock across the six countries (see chart below)[15].

The situation with trade is similar: the EU is overwhelmingly dominant as an external partner, with others only playing minor roles. On average 60% of exports from the six Western Balkan countries go to the EU, compared with 1.7% for Russia, 1.9% for Turkey, and 2% for China. The highest share of exports that any of the six Western Balkan countries send to these three is 5.8% from Montenegro to China.

Figure 20 / Inward FDI stock by source

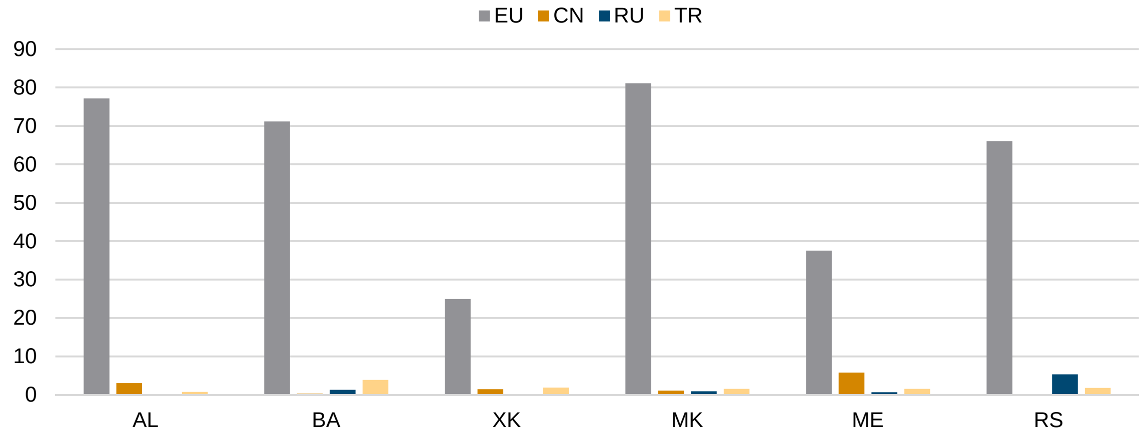
% of total



Sources: wiiw, national central banks.

Figure 21 / Merchandise exports by destination

% of total



Sources: wiiw, national statistics offices.

15 All data from the wiiw FDI database, https://data.wiiw.ac.at/foreign-direct-investment.html

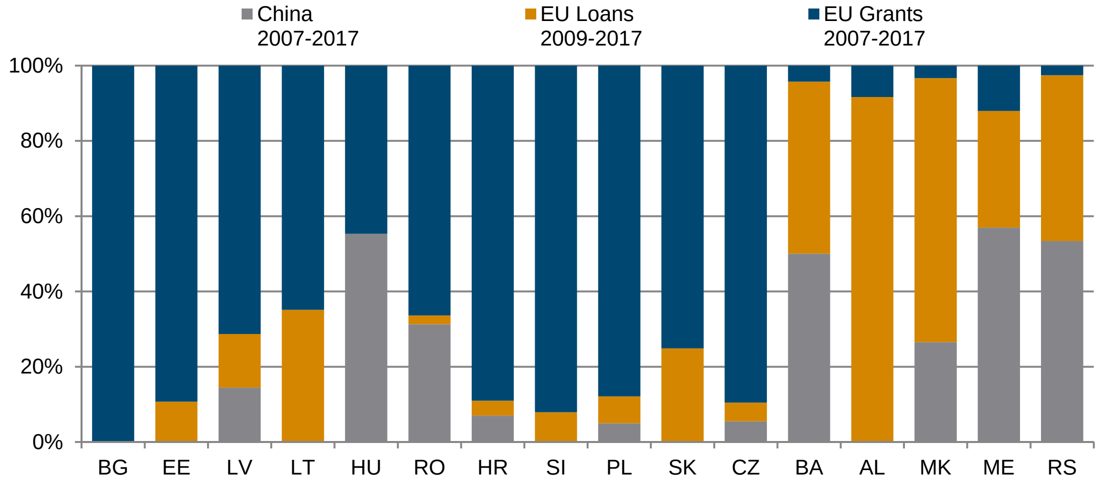
This is not to say, however, that the situation is static and that outside powers will not aim to increase their economic role in the Western Balkans in the coming years. One particularly significant development is China's Belt and Road Initiative (BRI), within which the Western Balkan countries will play an important role (Grübler et al. 2018). The Western Balkans has a particular importance for China as it lies between the port of Piraeus in Greece (67% of which was acquired by China in 2016) and the big markets of Western Europe. Announced Chinese construction projects as part of the initiative in 2007-17 were worth EUR 12.2bn in loans for 16 CESEE countries. Within these projects, the Western Balkans countries are quite dominant: 29.4% alone is earmarked for projects in Serbia, with a further 20.7% in Bosnia and 7.4% in Montenegro. The vast majority of the projects are either in energy or transport.

There are questions about the extent to which all planned projects will actually be realised, but if they are, it would certainly help to alleviate some of the region's infrastructure deficiencies. The upgrading of energy capacity would also be a highly welcome development, and help to drive economic expansion. In addition, Chinese activities in the region could increase demand, reduce transport costs and time, help with the diversification of exports, and strengthen regional connectivity and cooperation.

Nevertheless, we see material risks to the region as a result of Chinese involvement, some of which could have implications for EU accession[16]. First, Chinese money will arrive in the form of loans, creating risks of unsustainable debt burdens for some countries (Hurley et al. 2018). Second, there is a chance that Chinese activities in the region will add to the already existing problem of corruption (Makochi and Nechev, 2017). Third, there are justifiable concerns about greater dependency and political influence. Fourth, it is quite possible that infrastructure development will be undertaken by Chinese contractors, suppliers and workers, and using Chinese materials. This would significantly reduce the economic benefits for the region (Barisitz and Radzyner 2017).

Figure 22 / Loans from EU and China of greater significance in Western Balkans

Share of infrastructure funding by EU and Chinese sources



Source: European Commission ESIF, CEF, TEN-t, WBIF, EFSI data; China Global Investment Tracker; wiiw calculations.

16 https://wiiw.ac.at/western-balkan-countries-to-profit-from-belt-and-road-initiative-n-219.html

V. NON-WESTERN BALKANS BARRIERS TO ACCESSION

Even if the EU was waiting with open arms for the Western Balkan countries to be ready, the challenges would be enormous. However, considering the situation in the EU, and in Europe more generally, the difficulties these countries are set to face on the road to accession are even more daunting. We see four main external barriers to Western Balkan EU accession.

First, domestic political reality in many EU member states. Some countries, for example, will have to hold referenda on future enlargement. Particularly in the context of developments of the last few years, and the rise of populist parties across the EU, it is easy to imagine how electorates could reject the admission of additional countries to the EU. There may well also be a specific issue faced by countries in the Western Balkans with large or majority Muslim populations. One survey last year showed a clear majority of respondents in most European countries surveyed opposed to future immigration from countries with largely Muslim populations[17].

Second, there is a more general enlargement fatigue in the EU. Certainly, much of the enthusiasm for eastward expansion of the EU in the post-crisis years has gone. Eleven years on from accession, Romania and Bulgaria are still under special monitoring, mainly due to corruption[18]. This casts a long shadow over the prospects of future joiners.

Third, some Western Balkan countries face political conflicts with countries already in the EU, which could impede accession. Greece-Macedonia has been a long-standing problem (although here we are cautiously optimistic[19]), but other issues, such as Serbia-Croatia, may also become more prominent as accession approaches. The accession of Kosovo is a particularly tricky issue from the perspective of some EU member states, especially (but not limited to) Spain.

Fourth, it remains possible that outside actors could seek to block the accession of one or more Western Balkan member states to the EU. Russian alleged actions in Montenegro ahead of its NATO accession are an illustrative example[20]. Perhaps most crucially, Serbia will at some point have to make a choice between the EU and Russia. It cannot continue to have a free trade agreement with Russia when it joins the EU. Serbian President Aleksandar Vucic's visit to Moscow to mark the 73rd anniversary of the end of World War Two[21], for example, provoked irritation in Brussels.

Balkan regatta or Balkan express?

A key question is whether the countries of the region will join together ("express"), or 1-2 at a time ("regatta"). This is not an easy question to answer, but the emphasis on solving bilateral disputes before accession makes the latter more likely. The EU is keen to avoid a repeat of the Croatia-Slovenia case. Serbia, for example, has a major incentive to solve its dispute with Kosovo in this regard. If not, it

17 https://www.chathamhouse.org/expert/comment/what-do-europeans-think-about-muslim-immigration
18 https://www.euractiv.com/section/justice-home-affairs/news/bulgaria-romania-have-made-progress-but-still-more-needed-eu-report/
19 https://wiiw.ac.at/greece-and-macedonia-edge-towards-solution-to-name-dispute-n-276.html
20 https://www.rferl.org/a/montenegro-russia-serbia-coup-plot-witness-identifies-suspect-funding/28819658.html
21 http://en.kremlin.ru/events/president/news/57434

may have to wait for Kosovo to be ready for accession in economic and institutional terms, which could yet be some time away.

A further consideration is if countries are not ready for full membership in 2025, there may be alternatives beyond the status quo. For example, from an infrastructure perspective, we would strongly support non-EU members in the Western Balkans being given more accession to structural and cohesion funds: negligible amounts of money from the perspective of wealthier member states could make a big difference to infrastructure investment levels in the region.

VI. CONCLUSION

The timeframe announced by the European Commission for Western Balkan EU accession is highly ambitious, and it is far from certain that any of the countries will be ready for accession in 2025. However, in economic terms, the currently more advanced countries (Serbia and Montenegro) have a chance. Whether or not they make it will depend on both a concerted domestic reform effort, and the strong involvement of the European Commission, other EU institutions, and governments in the key member states such as Germany.

The challenges facing the region on the road to accession are numerous. wiiw believes that four are particularly pressing: resolving political disputes within the region, improving governance standards, upgrading infrastructure, and expanding the industrial base. Solving these in a comprehensive and timely manner will go a long way to helping countries in the region to meet their accession goals.

REFERENCES

Arandarenko, M. and W. Bartlett (eds) (2012), Labour Market Skills in the Western Balkans, FREN and LSEE, Belgrade, November.

Barisitz, S. and A. Radzyner (2017), 'The New Silk Road, part I: a stocktaking and economic assessment', Focus on European Economic Integration, Oesterreichische Nationalbank, Vienna, Q3/2017, pp. 8-30.

Gruebler, J., A. Bykova, M. Ghodsi, D. Hanzl-Weiss, M. Holzner, G. Hunya and R. Stehrer (2018), 'Economic Implications of the Belt and Road Initiative for CESEE and Austria', Research Report, forthcoming.

Holzner, M., R. Stehrer, H. Vidovic (2015), 'Infrastructure Investment in the Western Balkans', *wiiw Research Report No. 407* (September).

Holzner, M. (2016), 'Policy Options for Competitiveness and Economic Development in the Western Balkans: the Case for Infrastructure Investment', *wiiw Policy Note/Policy Report, No. 16* (June).

Hunya, G. et al. (2018), *CEFTA Investment Report 2017*, CEFTA Secretariat, Brussels.

Hurley, J., S. Morris and G. Portelance (2018), 'Examining the Debt Implications of the Belt and Road Initiative from a Policy Perspective', CGD Policy Paper No. 121, Center for Global Development, Washington DC, March.

Makocki, M. and Z. Nechev (2017), 'Balkan corruption: the China connection', ISSUE Alert No. 22, European Union Institute for Security Studies (EUISS), Paris, July.

SHORT LIST OF THE MOST RECENT WIIW PUBLICATIONS

(AS OF MAY 2018)

For current updates and summaries see also wiiw's website at www.wiiw.ac.at

---

WESTERN BALKANS EU ACCESSION: IS THE 2025 TARGET DATE REALISTIC?
by Richard Grieveson, Julia Grübler and Mario Holzner

wiiw Policy Notes and Reports, No. 22, May 2018
23 pages including 22 Figures
PDF only: free download from wiiw's website

STRUCTURAL CHANGE, TRADE AND GLOBAL PRODUCTION NETWORKS: AN 'APPROPRIATE INDUSTRIAL POLICY' FOR PERIPHERAL AND CATCHING-UP ECONOMIES
by Michael Landesmann and Roman Stöllinger

wiiw Policy Notes and Reports, No. 21, May 2018
33 pages including 10 Figures and 1 Matrix
PDF only: free download from wiiw's website

ESTIMATION OF AGGREGATE AND SEGMENT-SPECIFIC FINANCIAL CYCLES FOR A GLOBAL SAMPLE OF COUNTRIES
by Amat Adarov

wiiw Statistical Report, No. 7, April 2018
165 pages including 432 Tables, 137 Figures and 3 Boxes
PDF only: free download from wiiw's website

GLOBAL AND REGIONAL VALUE CHAINS: HOW IMPORTANT, HOW DIFFERENT?
by Roman Stöllinger (coordinator), Doris Hanzl-Weiss, Sandra Leitner, Robert Stehrer,

wiiw Research Reports, No. 427, April 2018
97 pages including 21 Tables, 22 Figures and 2 Boxes
hardcopy: EUR 8.00 (PDF: free download from wiiw's website)

WIIW MONTHLY REPORT 2018/04
ed. by Vasily Astrov and Sándor Richter

› Graph of the month: People at risk of poverty, in % (2016)
› Opinion Corner: Reflections on the US trade policy and the rising role of China
› Minimum wages back on the agenda in Europe

- Unemployment rate and GDP wage share in the EU-CEE: a dynamic analysis
- Income inequality and individuals' and households' behaviour
- Monthly and quarterly statistics for Central, East and Southeast Europe
- Index of subjects – April 2017 to April 2018

wiiw Monthly Report, No. 4, April 2018
44 pages including 4 Tables and 24 Figures
exclusively for wiiw Members

THE DYNAMIC EFFECTS OF FISCAL CONSOLIDATION EPISODES ON INCOME INEQUALITY: EVIDENCE FOR 17 OECD COUNTRIES OVER 1978-2013

by Philipp Heimberger

wiiw Working Papers, No. 147, April 2018
29 pages including 2 Tables and 9 Figures
hardcopy: EUR 8.00 (PDF: free download from wiiw's website)

THE IMPACT OF CHINESE TECHNICAL BARRIERS TO TRADE ON ITS MANUFACTURING IMPORTS

by Mahdi Ghodsi

wiiw Working Papers, No. 146, March 2018
33 pages including 6 Tables and 6 Figures
hardcopy: EUR 8.00 (PDF: free download from wiiw's website)

FINANCIAL CYCLES AROUND THE WORLD

by Amat Adarov

wiiw Working Papers, No. 145, March 2018
109 pages including 41 Tables and 48 Figures
hardcopy: EUR 8.00 (PDF: free download from wiiw's website)

WIIW MONTHLY REPORT 2018/03

ed. by Vasily Astrov and Sándor Richter

- Graph of the month: Difference between GDP and GNI in EU-CEE countries, as % of GDP
- Opinion Corner: Are net capital importing EU CEE countries exploited by foreign direct investors?
- How much do direct investors earn in EU-CEE countries and where do they put it?
- Impact of technical barriers to trade on foreign direct investment in CESEE
- FDI in Eurasia: A comparison with selected EU CEE countries
- The editors recommend for further reading
- Monthly and quarterly statistics for Central, East and Southeast Europe
- Index of subjects – March 2017 to March 2018

wiiw Monthly Report, No. 3, March 2018
48 pages including 1 Table and 30 Figures
exclusively for wiiw Members

CORPORATISM AND THE LABOUR INCOME SHARE: ECONOMETRIC INVESTIGATION INTO THE IMPACT OF INSTITUTIONS ON THE WAGE SHARE OF INDUSTRIALISED NATIONS

by Mario Holzner

wiiw Working Papers, No. 144, March 2018
26 pages including 8 Tables and 2 Figures
hardcopy: EUR 8.00 (PDF: free download from wiiw's website)

STRUCTURAL CHANGE IN TIMES OF INCREASING OPENNESS: ASSESSING PATH DEPENDENCY IN EUROPEAN ECONOMIC INTEGRATION

by Claudius Gräbner, Philipp Heimberger, Jakob Kapeller, Bernhard Schütz

wiiw Working Papers, No. 143, March 2018
33 pages including 1 Tables and 9 Figures
hardcopy: EUR 8.00 (PDF: free download from wiiw's website)

COHESION POLICY MEETS HETEROGENEOUS FIRMS

by Loredana Fattorini, Mahdi Ghodsi and Armando Rungi

wiiw Working Papers, No. 142, March 2018
25 pages including 7 Tables and 4 Figures
hardcopy: EUR 8.00 (PDF: free download from wiiw's website)

MIGRATION AND FDI FLOWS

by Neil Foster-McGregor, Michael Landesmann and Isilda Mara

wiiw Working Papers, No. 141, March 2018
19 pages including 7 Tables
hardcopy: EUR 8.00 (PDF: free download from wiiw's website)

RUSSIA'S REFORM FAILURES AND PUTIN'S FUTURE CHALLENGES

by Peter Havlik

wiiw Policy Notes and Reports, No. 20, March 2018
17 pages including 5 Figures
PDF: free download from wiiw's website

IMPRESSUM

Herausgeber, Verleger, Eigentümer und Hersteller:
Verein „Wiener Institut für Internationale Wirtschaftsvergleiche“ (wiiw),
Wien 6, Rahlgasse 3

ZVR-Zahl: 329995655

Postanschrift: A 1060 Wien, Rahlgasse 3, Tel: [+431] 533 66 10, Telefax: [+431] 533 66 10 50
Internet Homepage: www.wiiw.ac.at

Nachdruck nur auszugsweise und mit genauer Quellenangabe gestattet.

Offenlegung nach § 25 Mediengesetz: Medieninhaber (Verleger): Verein "Wiener Institut für Internationale Wirtschaftsvergleiche", A 1060 Wien, Rahlgasse 3. Vereinszweck: Analyse der wirtschaftlichen Entwicklung der zentral- und osteuropäischen Länder sowie anderer Transformationswirtschaften sowohl mittels empirischer als auch theoretischer Studien und ihre Veröffentlichung; Erbringung von Beratungsleistungen für Regierungs- und Verwaltungsstellen, Firmen und Institutionen.

wiiw.ac.at