INSIGHTS INTO BALKAN ECONOMIC INTERDEPENDENCIES

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Introduction

The Balkans has a broad but poorly defined development agenda. Factors that support and are likely to support the search for development and prosperity in the near future are the following:

• In most countries the transition to market economy and democracy has become irreversible;

• Leaders express commitments to follow the path of sustainable growth and prosperity combined with a vision of (re-) building their nations. In a response to this the international community launches a number of supporting initiatives;

• They all justify the need for an explicit local "ownership" and the inclusion of Balkan social capital in global competition.

There are factors, however, that are likely to counteract the seeds and efforts of development. For example, political wishes still need to be translated into practicalities and policy measures. It is already a conventional wisdom that long-lasting Balkan controversies stem from the unfinished formation of nation-states in the region (a process, which in other parts of Europe occurred between the 17th and 19th Centuries) and that this process contributes to intra-regional economic disparities. Kosovo is undergoing such nation-state formation. FR Yugoslavia is "defending" its national pride and territory. Montenegro is embarking on the nation-state path. Macedonia faces the challenge of defending its status quo.

Many constitutions in the region prevent flexibility on ethnic issues in their concept of statehood, envisage a constituent nation[1], ban autonomy[2], restrict foreigners from owning land, or prohibit political representation of ethnic and religious minorities.[3] To this list one should add constitutional provision for inefficient government machinery, protected monopolies and the ambiguous manner of imposing duties on citizenry through minor government acts.

In the 20th century most countries have used some form of “soft” ethnic cleansing; e.g., the last pre-Yugoslavian case was the expulsion of Bulgarian ethnic Turks in May-June 1989 to neighbouring Turkey (after they were deprived of their property rights). Similar events or negotiated “exchanges” of population, not very different from cleansing and deprivation, have been reoccurring in the last 120 years or so. Memories are alive while there is no critical mass of orientation towards the future.

While economic and political links between Balkan countries and the international community improved in the second half of 1999 and 2000, in 2001 the attempt of the UN and NATO to contain conflict within the borders of Kosovo failed and the aggression “leaked” from this UN protected territory into neighboring Macedonia, a country that originally had no formal involvement with the conflict in the province. In the light of prospects for economic cooperation and prosperity, it does not matter whether the territory is perceived as merely a “logistics site” for the politically dissatisfied Albanian minority in Macedonia or whether it is considered as a home base for “terrorist raids” of armed troops.[4] The fact of the matter is that the undecided status of Kosovo and the failure to organise (legitimate) representative democracy is reproducing the model of chetnik (i.e. guerilla) tactics of late 19th and early 20th Century national movements in the Balkans. These tactics revitalise political rhetoric and interethnic attitudes of the past, jeopardize fragile trust that business and trade opportunities would eventually make a difference, and scare away private sector and foreign investment in the region. Last but not least, the failures of democratic policies ensures the dominance of semi-legal and semi-informal economic interests in vast sub-regional territories, diminishing the chances of peace and order.

Problems

The idea of this paper is to provide some insights as to what extent transition Balkan economies represent indigenous roots of integration. International initiatives such as the Stability Pact assume that economic freedom, prosperity and rooted democracy would bring normality back to the region and would integrate it. There is a tacit believe that if economies are more interdependent, governments and people are less likely to resort to violence, since companies and citizens have much to loose. At the same time, both the Stability Pact and the EU Stabilisation and Association Agreement failed to prevent the March to May 2001 crisis in Macedonia.

Global economic divisions are different from those the world lived in even a decade ago. Reform leaders coped with the legacies of COMECON and re-oriented their capital and trade flows. These economies seek a niche in the global economy. The political process of building a nation state in a mid to late 19th Century manner, when homocentric European alliances were presumed as a territorial expansion of economic influence, is rather odd. Then, territorial identity was perceived as a precondition of prosperity, to be used as a governments' bargaining chip to seek rents from one alliance or another. Balkan nations, then, had fallen victim to these notions, fighting several wars with one another. Now, prosperity depends on competitiveness and innovation, on whether a national economy falls into the group of technology producing or technology consuming economies. If in the 19th Century it was somehow politically justifiable to fight for territorial influence in the Balkans, at the end of the 20th Century it was not. The region does not provide natural resources on which other economies depend, so there is no need to protect investment and trade routes.

Balkan countries faced different challenges. Slovenia from day one has 60% trade with the EU. Bulgarian COMECON trade in the 1970s and 1980s averaged around 60%, in Czechoslovakia it was over 50%, in Romania less than 30%, Hungary 40% and in Poland 50%.[5] The non-transition Balkan states, Greece and Turkey, are also different, one being a part of the EU single market, and the other in a free trade agreement with EU and a virtually free trade relationship with the Middle East (and Israeli) markets. The issue is whether and how it is possible to convert this diversity into mutual benefit. The Balkans do not constitute an economic notion, rather a political one.

Policy Objectives

Declared objectives of Balkan economic recovery fall into the area of socio-political engineering of a "neighbour-success" development pattern, which intends to compensate to a certain extent for the declining share of the region and individual countries in the global economy, and be a vehicle for enlarging individual countries' markets, and constitute a path to better competitiveness.

Table 1: Per Capita GDP as a %age of the West - 1870-1989

	1870	1913	1938	1973	1989
Western Europe	44	44	44	45	40
Overseas West	32	30	35	38	32

Source: Ivan T. Berend, From Plan to Market, From Regime Change to Sustained Growth in Central and Eastern Europe, Economic Survey of Europe, UNECE, 2000, No 2/3, p. 49, a quotation of A. Madison, Monitoring the World Economy 1820-1992, OECD, Paris, 1995, p. 212.

GDP per capita comparisons suggest that between 1870 and 1989, neither market nor central planning could generate prosperity at best available standards. CEE countries did not change their relative position vis-à-vis Western Europe and the West in general. The situation of the Balkan countries is likely to be worse than in CEE.

Trade Conditions

Like elsewhere, a critical mass of publicly supported orientation towards prosperity requires that there is a political consensus for structural change and exports to sophisticated markets. This consensus is expected to contribute to higher flexibility and lesser dependence on export receipts from physical access to major trade partners when conflict and/or non-tariff barriers interrupt traditional trade routes. In other words, regional integration alone is no substitute for general reform and restructuring efforts.

In terms of trade to GDP, there is a significant difference between Bulgaria, Bosnia and Herzegovina (B&H), and Macedonia with the highest ratios of trade to GDP, the medium ratios of Croatia and Romania, and the smaller international exchanges of Albania, and FR Yugoslavia (FRY). In Albania, reasons for this are the small size of industries, low productivity levels and wide spread economic informality. In the FRY, the ratio reflects distortions due to embargoes, sanctions and military conflicts.

Table 2: Trade Openness - 1998 (%)

	Exports+Imports as % of GDP
Albania	34
B&H	83
Bulgaria	91
Croatia	61
Yugoslavia	40
Macedonia	91
Romania	58

Source: World Bank[6]

The greater openness of Bulgaria and Macedonia is evidence of having got some fundamentals right, such as establishing trade contacts and cooperation links with a potential to cluster internationally.

The EU is the biggest trading partner for all SEE economies. On the other hand, in 1998, transition Balkans together had merely 1.6% of EU imports and 4.4% of exports. It is thus clearly no major market for the EU. Excluding Bulgaria and Romania, it is less than 1% of EU imports. The alternative Balkan market has its own peculiarities. **Tables 3** and **4** below show the distribution of main trade partners in 1998.

Table 3: Balkan Ranks of Trade Partners (Imports, % in 1998)

PARTNERS/ RANKS	AL	B&H	BG	CR	FRY	MK	RO	Balkans
Balkans (incl. Slovenia)	6.9	43.4	3.4	12.1	17.4	28.9	1.5	11.5
EU	79	41.5	44.6	58.1	72.6	52.8	56	56.1
I	38.7 (Ita)	14.7 (Ger)	13.9 (Ger)	20.5 (Ger)	25.2 (Ger)	14.4 (Ger)	17.5 (Ita)	
II	24.4 (Gre)	11.8 (Ita)	7.9 (Ita)	19 (Ita)	22.7 (Ita)	13.8 (Ita)	17.4 (Ger)	
III	7.9 (Ger)	4.9 (Aus)	6.4 (Gre)	5.1 (Fra)	8.8 (Aus)	8.9 (Aus)	6.9 (Fra)	
Industrial world	81.9	44.8	53.4	71.1	78.9	57.7	65.4	65.1

Source: IMF Direction of Trade, own calculations.

For Bulgaria, proximity matters in trade with Greece, a third partner since 1994 and EU member. Bosnia and Herzegovina, FR Yugoslavia and Macedonia have around one-fifth or more of their trade with a neighbouring country from the Balkans.

Table 4: Balkan Ranks of Trade Partners (Exports, % in 1998)

PARTNERS/ RANKS	AL	BiH	BG	CR	FRY	MK	RO	Balkans
Balkans (incl. Slovenia)	3	39.3	7.7	25.3	25.9	22.8	3.3	11.5
EU	88.8	50.9	47.9	45.8	71.7	51.8	62.8	58
I	58.9 (Ita)	22.3 (Ita)	13.1 (Ita)	18.4 (Ita)	28 (Ita)	22.4 (Ger)	22.3 (Ita)	
II	12.8 (Gre)	18.8 (Ger)	10.9 (Ger)	17.3 (Ger)	25.5 (Ger)	11.4 (Ita)	19.5 (Ger)	
III	8.3 (Ger)	4.5 (Aus)	9.2 (Gre)	2.3 (Fra)	5.3 (Fra)	3.7 (Bel)	5.9 (Fra)	
Industrial world	94	54	56.7	53.4	71.7	65.9	70.7	65.6

Source: IMF Direction of Trade, own calculations

With exports, the situation is basically the same. But it is obvious that Croatia exports rather extensively to neighbouring countries. Again Bosnia & Herzegovina, FR Yugoslavia and Macedonia have relatively high neighbour shares in their exports. Data for other years do not suggest a different picture.[7] At the same time it is obvious that these three countries experienced internal civic conflict and violence. A possible explanation for this coincidence of larger regional trade exposure and internal conflict is that the greater the trade, the greater the temptation to resort to physical (direct) control over trade roots and territories in order to extort taxes.

In general, however, Balkan countries trade over 60% with EU and the industrialised West, but not with one another. This fact might be justified by following reasons:

• Regional integration of a low-income economy with low-income countries usually makes an economy poorer;

• Demand is weak and relatively unsophisticated, and competitive companies chose more complex markets;

• The countries in the region have relatively similar product and quality structures;

• Instability of the regional markets in monetary and political terms;

• Inefficient contract enforcement and dispute resolution; tariff and non-tariff barriers; companies also avoid risks related to civic conflicts and insurgencies.

Economic Sizes and Balkan Cooperation

Economies and company structures are not well positioned to prevent external constraints to regional and indigenous development. Most economies are led by private sectors and services, which are rarely competitive. Foreign direct investment is negligible in absolute and in per-capita terms. The level of foreign ownership in Spain is 42%, in Poland 12%, and in Romania 6%.[8] Economic interdependence (besides Croatia in Bosnia-Herzegovina) is no factor. Mutual penetration of bank sectors is zero, with the exception of some Turkish and Greek banks. Foreign ownership in banking sectors used to be a rare phenomenon until recently. The presence of foreign (international) banks ranks from more than 80% of the respective sectors of Bulgaria and Bosnia & Herzegovina to zero in FR Yugoslavia and Kosovo. A common practice used to be transferring payments to a neighbouring country via international correspondent banks or using cash, and, in FR Yugoslavia, to have an account in part of the ex-republic from where to carry in cash. Domestic, not to mention regional (or of regional significance) commodity exchanges, do not exist or function badly. Links between capital markets are at the level of irregular correspondence. Cross-border clusters are the exception, even between countries never torn by recent wars and conflicts (e.g. Bulgaria and Romania).[9]

The dependency on international initiatives, constellations and agreements and the inability to cope with past legacies in Balkan countries is jeopardized by the fact that these are low income economies. Bulgaria's GDP per capita is just one-fifth of the EU lower rank economies. The average SEE GDP per capita at market exchange rate in 1998 was US$1,793. Lowest GDP per capita is Albania (US$1,110) and the highest Croatia (US$4,635). The total SEE GDP was US$94.92 billion, only 0.32% of the value of 1998 world output. If we exclude Romania (which is roughly 40% of the total SEE), remaining SEE GDP for 1998 is US$58.12 billion, i.e. 0.2% of the world output. Thus (excluding Romania) total SEE GDP was roughly one-twelth of the combined 1998 public procurement budget of the EU member states.

A company demographics of low-income economies might be considerd as typically consisting of three groups of companies:

• **Subsistence** firms, in which there is little distinction between household and company finance, and which have high “social” value added but little or no value for the economy as a whole;

• **Survival** companies, which are incorporated, niche filling, relatively immobile, dependent on “single” suppliers or markets;

• **Competitive** companies, which are driven by productivity and quality of operations and are mobile, adjustable to the demand of a sophisticated market.

From these three groups, it is likely that the first prevails in number while the share of the third group is negligible. In this demographics, sole proprietorship firms are more likely to belong to the first category. In Bulgaria, one of the relatively well established Balkan economies, the picture is the following. 85% of the registered enterprises are sole proprietorships; 150,000 (i.e. roughly one-third) might be considered active (i.e. pay taxes or report more profits than losses). The share of competitive companies of all registered is just 5-7%, although these produced 35% of gross value added in 1999.

It is difficult to underestimate the political impact of this situation. Subsistence companies could be a subject of welfare policies and usually in high-income economies of the EU they are. Votes are where the majority is and there is pressure to support survival and subsistence companies at the expense of competitive ones. In Bulgaria and the Balkans they advocate welfare-like policies, requesting subsidies and protectionism and their demands often serve as substitute for the economic rationale of domestic and international policies.

Political Pre-conditions of Economic Cooperation

Since there is no indigenous critical mass - at the level of the firm - for cooperation and thinking about the future, attention again must be directed to more or less pure political conditions. There are two main political pre-conditions to convert the region into the recovery and development path. The first is to avoid the legacy risks. Such risks may occur when new realities reproduce the heritage of the 1990s or when post-Kosovo initiatives, opportunities, policies and instruments are rejected by local or Western democracies, and fail to behave in an economically rational manner.

The second condition is to avoid deeper divisions of legitimate execution of power in the Balkans. It is likely that geographic location, meaning the proximity and availability of traditional (pre-1999) trade routes and markets, will have a predominant importance in the short and medium term. Companies from and economies in the Balkan countries will naturally seek diversity and alternatives to pre-WW1 links and routes. The philosophy of both governments and chetniks here has often been that nations (not companies) compete; seeking rents from others is a norm. As Arben Xhaferi said recently in an interview for IWPR: “I explain [the outbreak of violence in Macedonia] as ethnic competition: to whom does the state belong?”

Domestic and intra-regional conditions that would eliminate sticky political and economic divisions in SEE are as follows:

• To avoid consistent failures of Balkan countries, leaders must agree on long-lasting peace agreements and constitutional orders;

• To reduce discrepancies in economic rules of the game within the region[10] and between different speeds of market and democratic reforms, including those related to EU-accession;

• To re-address aspirations to build nation-states at the expense of others, combined with a lack of respect for human and minority rights.

There is no shortage of international initiatives as well as of desire to be a member of those initiatives and structures, as Table 5 below demonstrates.

Table 5:
Membership in International Organisations and Initiatives[11]

States	Key trade related organizations				Key agreements			South-East Europe Initiatives				
UN/ECE	WTO	WCO	OECD	ICC	European Union		EFTA	BSEC	CEI	SECI	SE Stabty. Pact	SE Trade Initve.
					TR	PECO						
Albania	(WTO)	WCO			GSP		(UTA)	BSEC	CEI	SECI	SESP	SETI
B&H					ATP		(UTA)		CEI	SECI	SESP	SETI
Bulgaria	WTO	WCO		ICC	EAA& invit.	PECO	FTA	BSEC	CEI	SECI	SESP	SETI
Macedonia	(WTO)	WCO		(ICC)	TCA	SAA	(UTA)		CEI	SECI	SESP	SETI
Croatia	(WTO)	WCO		ICC	ATP	SAA	(UTA)		CEI	SECI	SESP	SETI
Romania	WTO	WCO		ICC	EAA& invit.	PECO	FTA	BSEC	CEI	SECI	SESP	SETI
Yugoslavia				INCC NC		(SAA)	(UTA)				SESP	(SETI)

Notes: Brackets mean either a procedure to join (ratify) or status of an observer and/or unclearly defined membership.

In addition to the listed initiatives and institutions, Bulgaria and Romania are also members of the Central European Free Trade Agreement (CEFTA). It seems, however, that these initiatives and domestic and regional policies proceed as if on two parallel, rarely interchangeable levels. Kosovo does not have and cannot have a place in the above table due to its undecided status. The membership of Macedonia in almost all relevant initiatives and institutions and the Stabilisation and Association Agreement with the EU seems not to contribute to the stability of the country.

In all SEE countries, domestic policies have been delaying reforms. Wars and conflicts aggravated and still prolong high country risks and worsen the ill effects of the lack of institution building. Therefore, regional initiatives and policies must not be perceived as a substitute for core market and democratisation reforms.

1. E.g., the Croatian Constitution says: "Croatia, the nation-state of the Croatian people and the state of other nationalities and minorities which are its citizens"; the Macedonian Constitution contains a similar statement: "Macedonia, the national state of the Macedonian people, which guarantees the complete civic equality and permanent cohabitation of the Macedonian people with the Albanians, Turks, Roma, and other nationalities living there." The Bulgarian Constitution states that "the official language is Bulgarian" (Article 3), while 10% of the citizenry has the Turkish as mother tongue.

2. E.g., Article 21 of the Bulgarian Constitution.

3. E.g., in the Constitution of Bulgaria one may find the statement; "the traditional religion [in the country] is the Orthodox Christian congregation" (Article 13.2), and that political parties established on "ethnic, racial or religious lines" are not allowed (Article 11.4). While such parties exist de facto it is almost impossible to implement this provision de jure.

4. The former explanation has been recently used by Veton Surroi, the publisher of the main Kosovo newspaper, Koha Ditore (see "Renewed Ethnic Reform Would Defuse Macedonian Conflict", International Herald Tribune, March 27, 2001, p.10); the latter interpretation was suggested by the prime minister of Macedonia, Ljupco Georgievski, in a public statement on March 19, 2001 and has been used by Yugoslav officials to describe insurgencies in the Presevo region earlier this year; while US, EU and NATO officials used the enigmatic and less decisive definitions of "extremism" and "armed extremists".

5. Rumen Dobrinski, Transition Failures: Anatomy of the Bulgarian Crisis, Vienna, WIIW, 1997, p.7.

6. Trade Integration for SEE in the Context of the Stability Pact, World Bank, 2000, p. 55.

7. The constellations have changed with regard to Bulgaria: in 2000 its Balkan trade tripled, due to petroleum exports to FR Yugoslavia and the free trade agreement with Macedonia, which in 2000 equaled Russia in Bulgarian exports.

8. Source: Heriot-Watt University, UK, quoted by: Francis Harris, “Join at your Peril,” Business Central Europe, March, 1999, 12.

9. Petya Mandova, Krassen Stanchev, To Cluster or Not: Cross Danube Firm Level Co-operation, (http://www.ime-bg.org).

10. See: Krassen Stanchev, “Market Reforms in the Balkans: Barriers and Challenges,” Balkan Transitions, edited by Ivailo Dichev, (Sofia, ACCESS, 1997).

11. ECE - Economic Commission for Europe, Geneva; WTO - World Trade Organization, Geneva; WCO - World Customs Organization, Brussels; OECD - Organization for Economic Cooperation and Development, Paris; ICC - International Chamber of Commerce, Paris (important for setting rules of conduct and international dispute resolution); EU - European Union, Brussels; EFTA - European Free Trade Association, Brussels; BSEC - Black Sea Economic Cooperation; CEI - Central European Initiative; SECI - Southeast European Cooperative Initiative; SESP - Southeast Europe Stability Pact; SETI - Southeast Europe Trade Initiative (SETI is an advocacy group, securing businesses’ support for values and projects of SECI and SESP); SAA - Stabilisation and Association Agreement; EAA - European Association Agreement; TR - Trade Relations; PECO - Pan European Cumulation of Origin; FTA - Free Trade Agreement; CU - Customs Union ; ATP - Autonomous Trade Preferences; GSP - Generalized System of Preferences; TCA - Trade and Cooperation Agreement; UTA - Unilateral Trade Agreement (an EU model to liberalise tariffs for the western Balkans).