Wiener Institut für Internationale Wirtschaftsvergleiche

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Study presentation and expert discussion

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The long way round: Lessons from EU-CEE for improving integration and development in the Western Balkans

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The current EU strategy for the Western Balkans has not been very successful, to put it mildly

- Western Balkan countries are waiting far too long to enter EU (sometimes even to start the negotiations)

North Macedonia is waiting 18 years to start the negotiations, Albania 13

TABLE 2 **Timeline of applications for EU membership and waiting times for the Western Balkan countries**

Country	Date of application for EU membership	Beginning of accession negotiations	Years since application for EU membership
Albania	28 April 2009		12.5
Bosnia and Herzegovina	15 February 2016		5.5
Montenegro	15 December 2008	29 June 2012	13
North Macedonia	22 March 2004		17.5
Serbia	22 December 2009	21 January 2014	12

Note: Kosovo has not yet applied for EU membership | **© Bertelsmann Stiftung and wiiw.**

Note: Waiting times in the tables are from 6 months ago

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This is in stark contrast with the CEE countries, which entered EU after waiting for 9 years, on average

TABLE 1 **Timeline of applications for EU membership and EU accession in CEE**

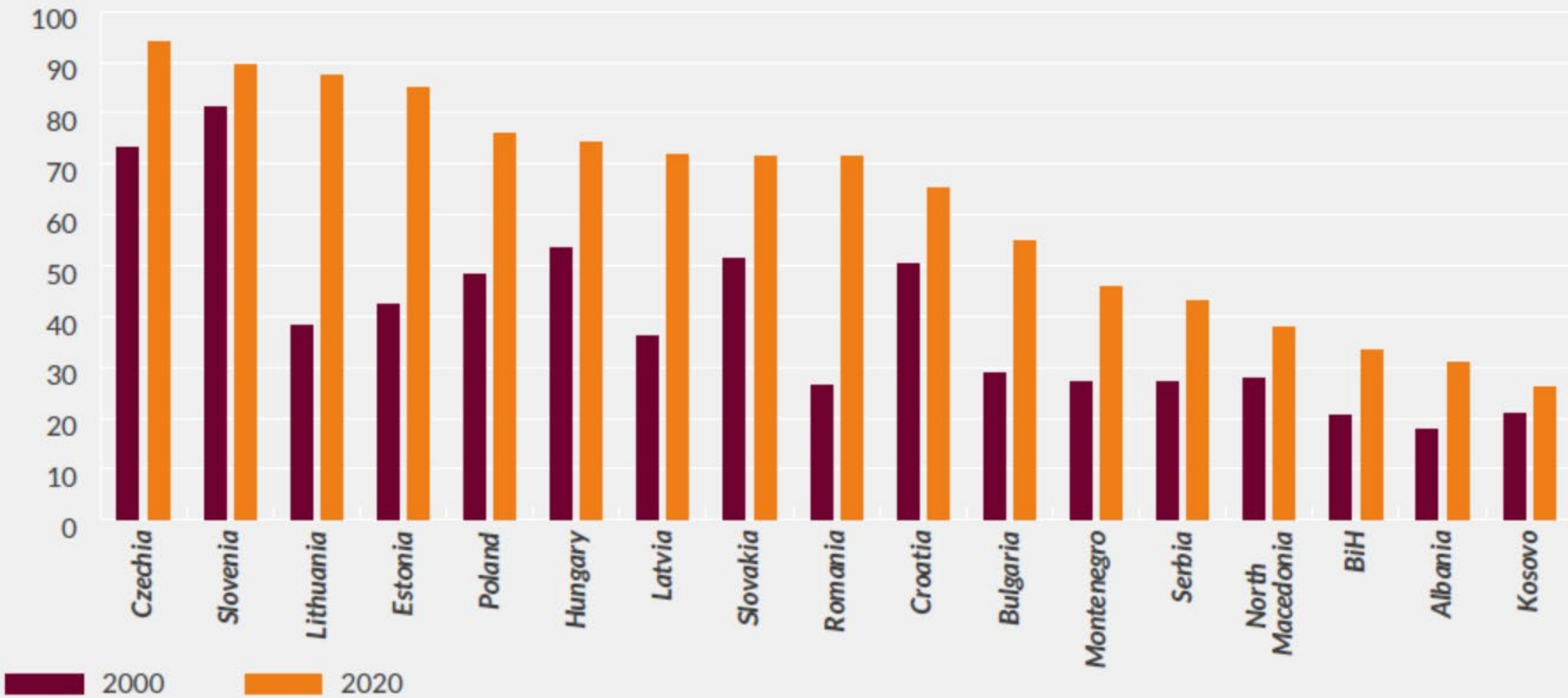
Country	Date of application for EU membership	Beginning of accession negotiations	Date of EU accession	Years between application and accession
Hungary	31 March 1994	31 March 1998	1 May 2004	10
Poland	5 April 1994	31 March 1998	1 May 2004	10
Romania	22 June 1995	15 February 2000	1 January 2007	11.5
Slovakia	27 June 1995	15 February 2000	1 May 2004	9
Latvia	13 October 1995	15 February 2000	1 May 2004	8.5
Estonia	24 November 1995	31 March 1998	1 May 2004	8.5
Lithuania	8 December 1995	15 February 2000	1 May 2004	8.5
Bulgaria	14 December 1995	15 February 2000	1 January 2007	11
Czechia	17 January 1996	31 March 1998	1 May 2004	8
Slovenia	10 June 1996	31 March 1998	1 May 2004	8
Croatia	21 February 2003	3 October 2005	1 July 2013	10

Source: Based on CVCE.EU | **© Bertelsmann Stiftung and wiiw.**

The current EU strategy for the Western Balkans has not been very successful, to put it mildly

- Western Balkan countries are waiting far too long to enter EU (sometimes even to start the negotiations)
- Convergence to EU levels of income has been very slow

FIGURE 1 **GDP per capita in purchasing power standards as a percentage of EU-27 GDP (in 2000 and 2020)**



Sources: wiiw, Eurostat, national sources | **© Bertelsmann Stiftung and wiiw.**

The current EU strategy for the Western Balkans has not been very successful, to put it mildly

- Western Balkan countries are waiting far too long to enter EU (sometimes even to start the negotiations)
- Convergence to EU levels of income has been very slow
- Support for EU membership in the region declined for the first time in 2022, to 60%, from 62% in 2021 (Balkan Barometer 2022)

Why has the EU strategy for the region failed?

- Because it has conditioned EU accession on improving regional cooperation
- And has assumed that regional cooperation improves with regional economic integration
- Bilateral Investment Treaties, Free Trade Agreements, Berlin Process, Common Regional Market, Multi-annual Action Plan for a Regional Economic Area
- “Wandel durch Handel” (Change through Trade)

But prerequisites for this have never been present in the Western Balkans

- Institutional – rule of law, control of corruption
- Structural – infrastructure, low income, poverty, low public spending on public goods and services
- Political incentives – lack of local ownership of the idea
- Economic fundamentals – the region is not big enough for significant economic gains

What do we do in this study?

- We re-assess the EU strategy for the Western Balkans
- Trying to derive lessons from the EU accession of the EU-CEE for the Western Balkans

More precisely…

- We investigate to what extent regional economic integration improved in EU-CEE after EU accession
- Identify the reasons for this
- Draw recommendations for the Western Balkans on the grounds of this

Three types of economic integration

1. Intraregional trade in goods
2. Intraregional trade in services
3. Intraregional direct investment

- All defined as proportion of overall trade/investment in a country, that is due to regional trade/investment

Three hypotheses how EU accession can affect regional integration

1. **Income hypothesis** - EU accession increases incomes in the region, which boosts demand for, and supply of, products coming from the region, which in turn leads to greater intraregional trade and investment
2. **Foreign firms hypothesis** - EU accession leads foreign companies to enter the region, which creates trade and services supply chains within the region
3. **Previous linkages hypothesis** - EU accession creates opportunities for broken business linkages to be re-established as well as for existing business linkages to flourish further

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Econometric approach

- We first see whether EU accession has affected the three measures of regional economic integration
- We then see whether variables measuring the three hypotheses are significant or not

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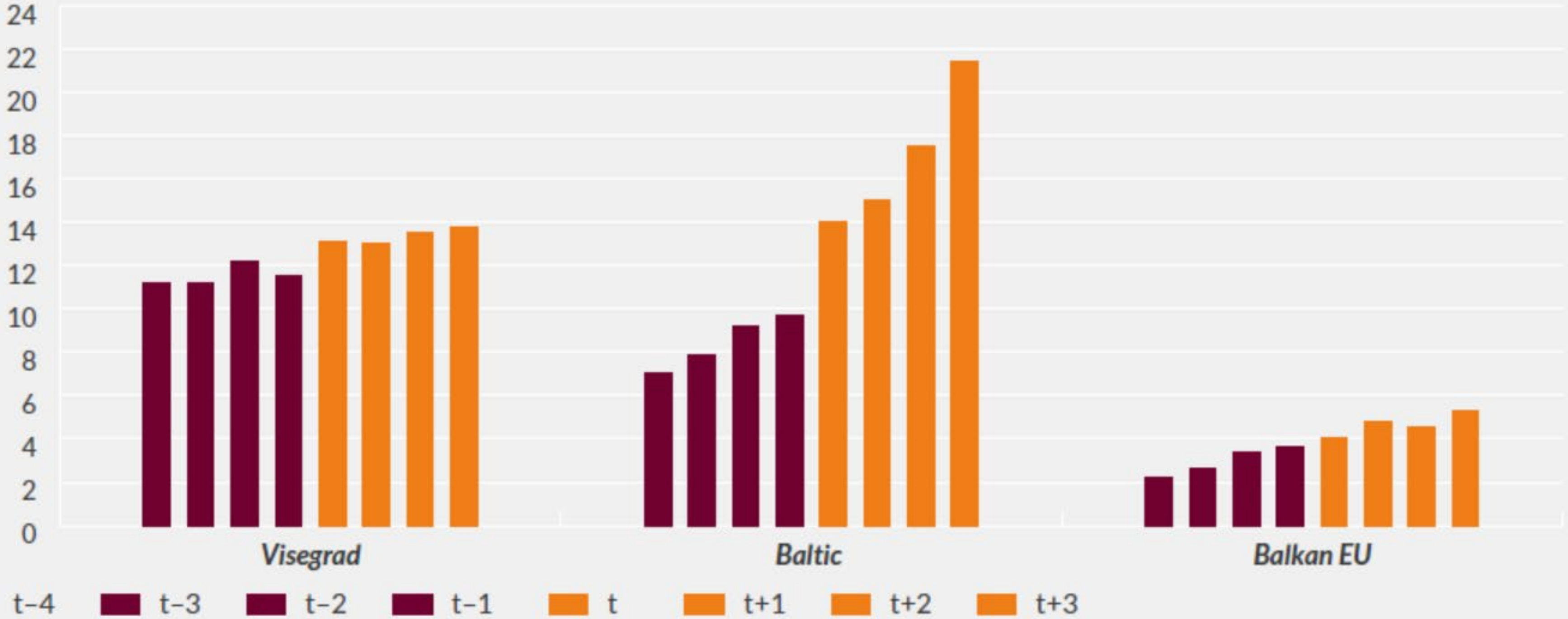
Main findings (1)

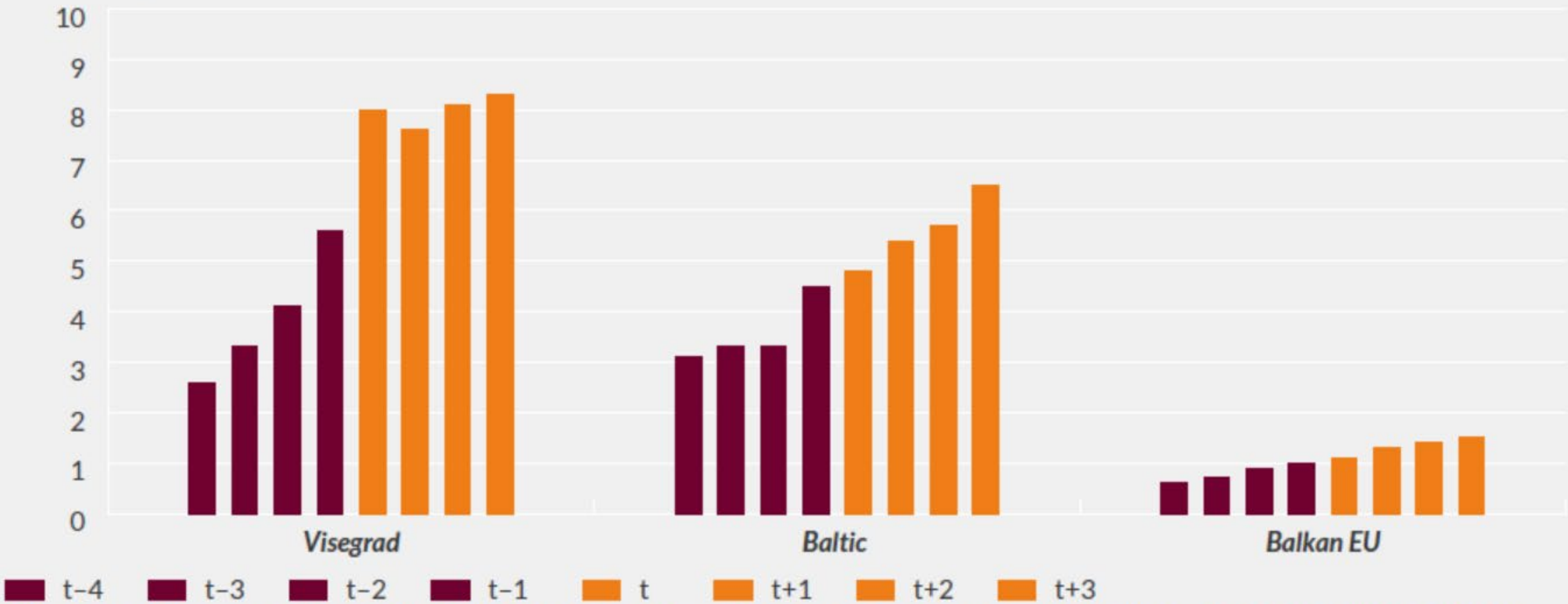
- EU accession has improved regional economic integration in EU-CEE, especially in trade
- Trade in goods and services with each other increased by approximately 50 percent due to EU accession
- Integration in terms of FDI also improved after accession, but not that much, and we find no evidence that EU accession directly affected it

FIGURE 6 **Intraregional exports of goods for Visegrad, Baltic and Balkan EU countries, pre-accession and post-accession (as % of total exports)**



Note: "t" denotes the year of EU accession, "t+1" the first year afterwards, and so on. Concretely, "t" is 2004 for Visegrad and Baltic countries, 2007 for Bulgaria and Romania, and 2013 for Croatia.
Source: UN Comtrade | **© Bertelsmann Stiftung and wiiw.**

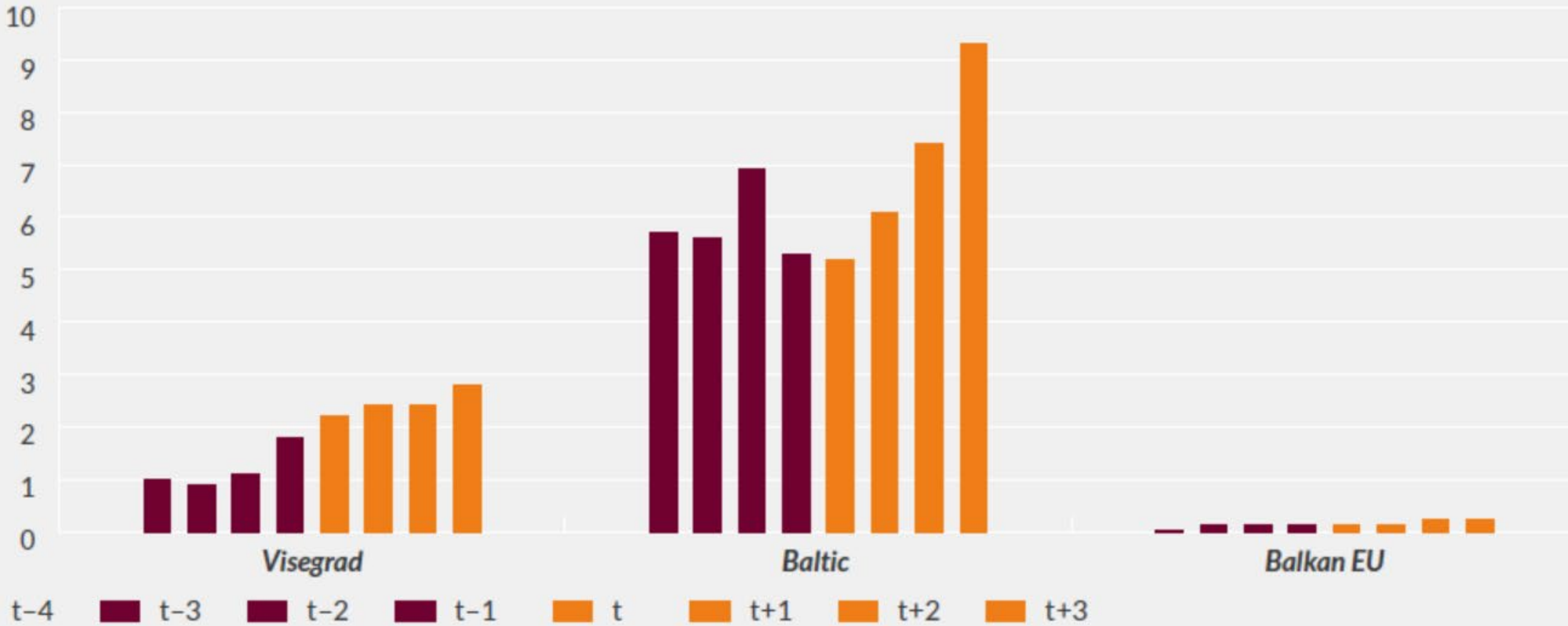
FIGURE 9 **Intraregional exports of services for Visegrad, Baltic and Balkan EU countries, pre-accession and post-accession (as % of total exports)**



Note: "t" denotes the year of EU accession, "t+1" the first year afterwards, and so on. Concretely, "t" is 2004 for Visegrad and Baltic countries, 2007 for Bulgaria and Romania, and 2013 for Croatia.

Source: World Input-Output Database | **© Bertelsmann Stiftung and wiiw.**

FIGURE 12 **Intraregional inward FDI stocks for Visegrad, Baltic and Balkan EU countries, pre-accession and post-accession (as a % of total inward FDI stocks)**



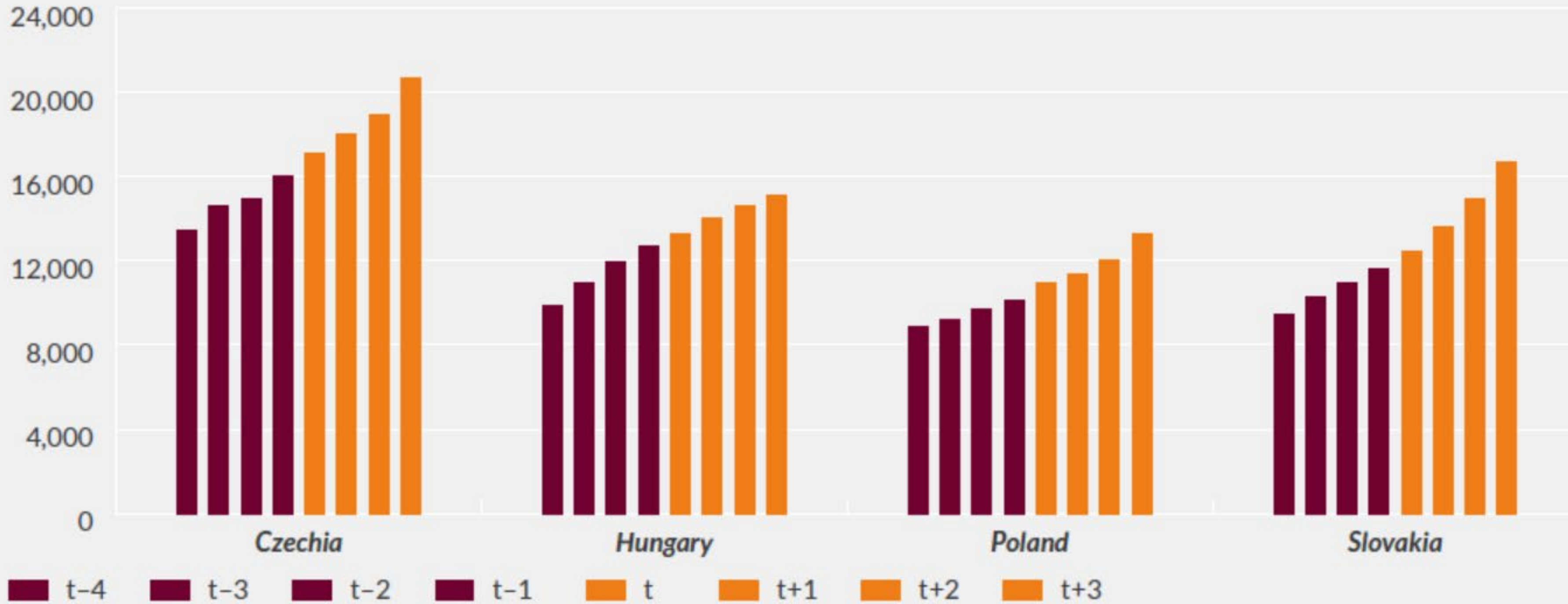
Note: "t" denotes the year of EU accession, "t+1" the first year afterwards, and so on. Concretely, "t" is 2004 for Visegrad and Baltic countries, 2007 for Bulgaria and Romania, and 2013 for Croatia.

Source: wiiw FDI Database | **© Bertelsmann Stiftung and wiiw.**

Main findings (2)

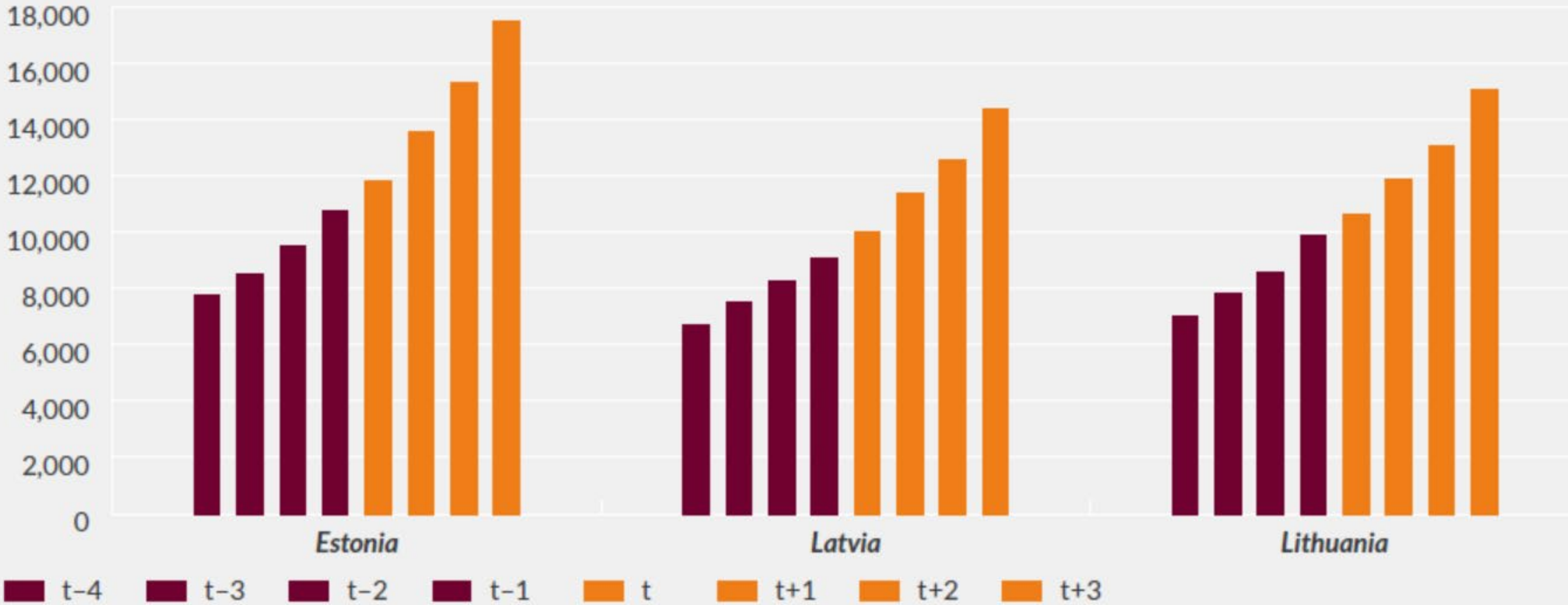
- The dominant means by which EU accession improved intraregional trade integration was the income channel.
- By increasing incomes in the region, EU accession boosted demand for and the supply of goods and services from the region, which in turn increased intraregional trade.

FIGURE 13 **Real GDP per capita in terms of purchasing power standards for the Visegrad countries, pre-accession and post-accession (in €, 2020 prices)**



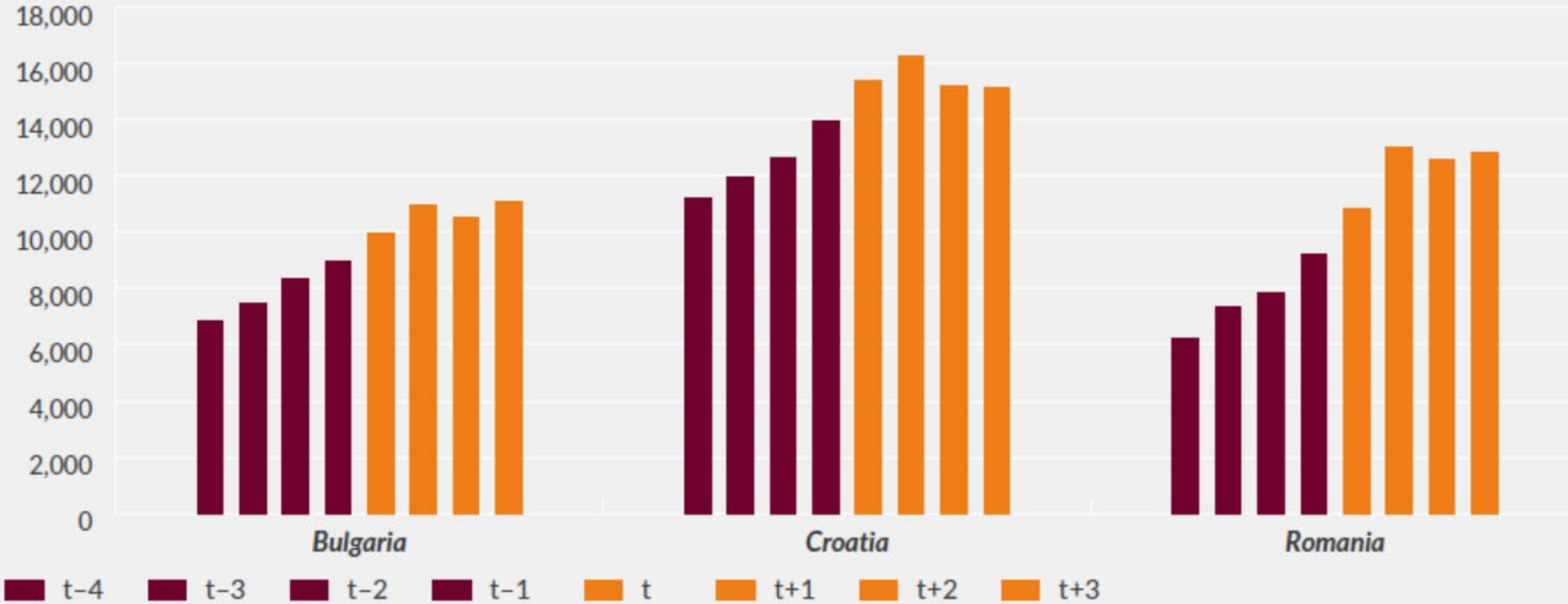
Note: "t" denotes the year of the EU accession, "t+1" the first year afterwards, and so on. Concretely, for Visegrad countries, "t" is 2004.
Source: wiiw Annual Database | **© Bertelsmann Stiftung and wiiw.**

FIGURE 14 **Real GDP per capita in terms of purchasing power standards for the Baltic countries, pre-accession and post-accession (in €, 2020 prices)**



Note: "t" denotes the year of the EU accession, "t+1" the first year afterwards, and so on. Concretely, for Baltic countries, "t" is 2004.
Source: wiiw Annual Database | **© Bertelsmann Stiftung and wiiw.**

FIGURE 15 **Real GDP per capita in purchasing power standards for the Balkan EU countries, pre-accession and post-accession (in €, 2020 prices)**

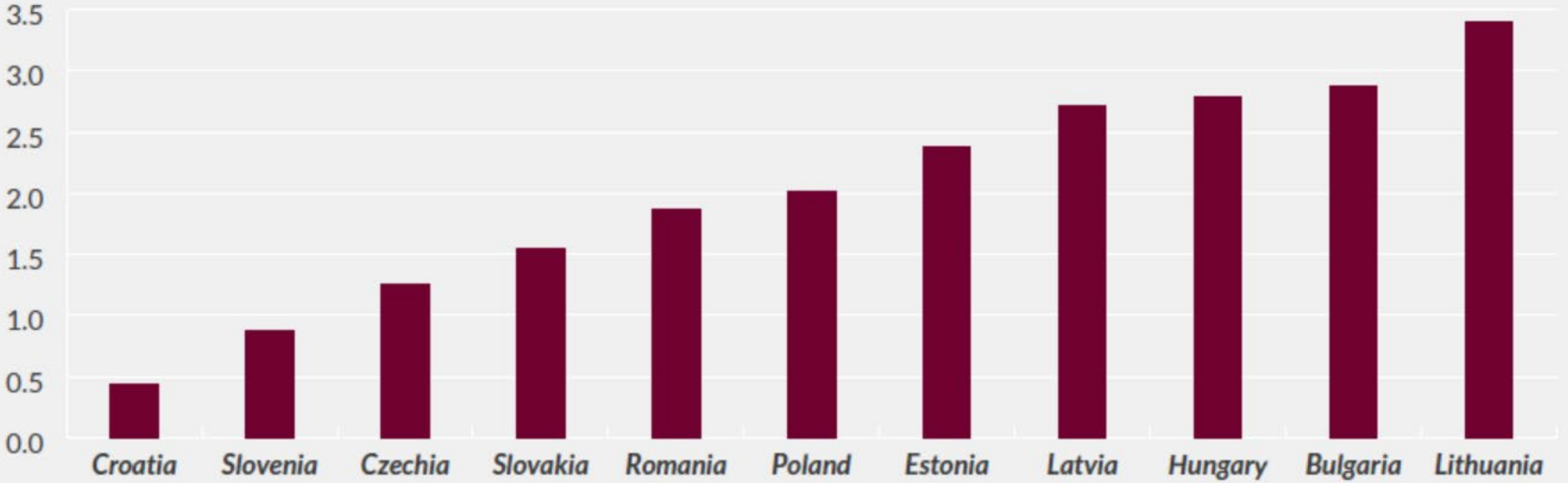


Note: "t" denotes the year of the EU accession, "t+1" the first year afterwards, and so on. Concretely, "t" is 2007 for Bulgaria and Romania, and 2013 for Croatia.
Source: wiiw Annual Database | **© Bertelsmann Stiftung and wiiw.**

Main findings (3)

- The most direct way that EU accession has increased incomes in EU-CEE has been through the EU budget transfers.
- On average, these countries have received transfers from the EU budget equivalent to 2 percent of their GDP per year (more in recent years).
- Our analysis points out that doubling the annual transfers (i.e. increasing them from 1 percent to 2 percent of GDP) leads to an overall increase in GDP of 14 percent, which is very sizeable.

FIGURE 16 **EU budget transfers to EU-CEE countries between 2004 and 2018, averages per country (in % of annual GDP)**



Source: European Commission | **© Bertelsmann Stiftung and wiiw.**

FIGURE 17 **EU budget transfers to all EU-CEE countries between 2004 and 2018, averages per year (in % of EU-CEE GDP)**

Source: European Commission | **© Bertelsmann Stiftung and wiiw.**

Main findings (4)

- Initial conditions were important for integration.
- Countries and industries that had greater regional integration in 2000 also integrated faster after EU accession.
- Our explanation for this is that EU accession opens up space for existing trade and investment linkages to develop further.

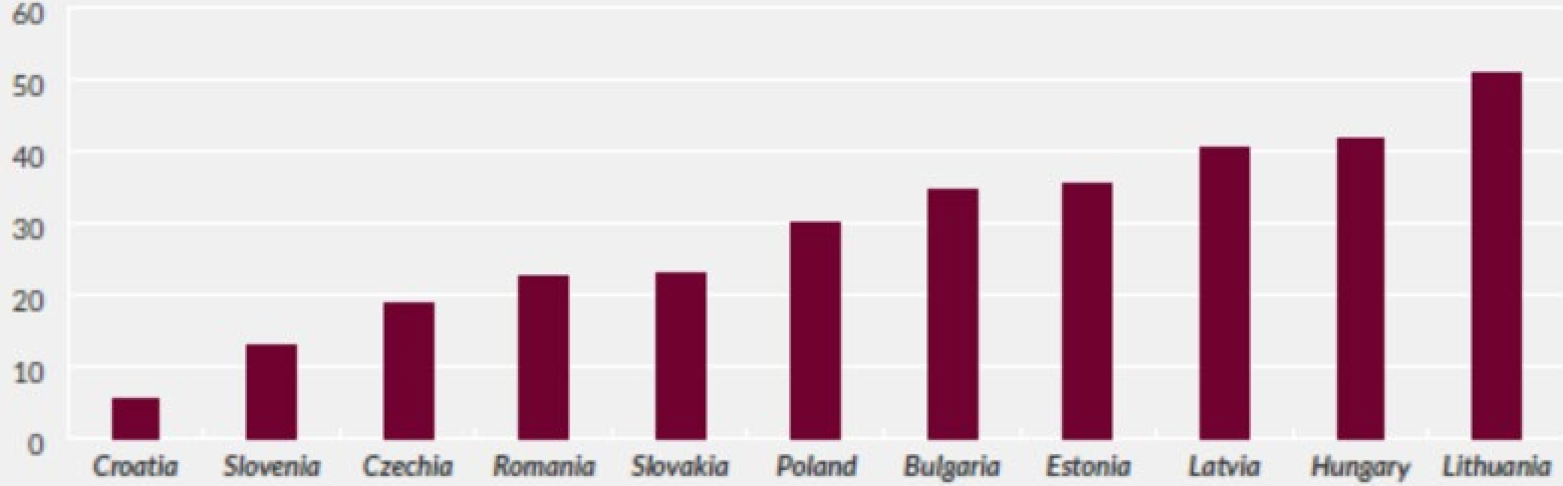
Main findings (5)

- We find no support for the “foreign firms” channel

Implications for the Western Balkans

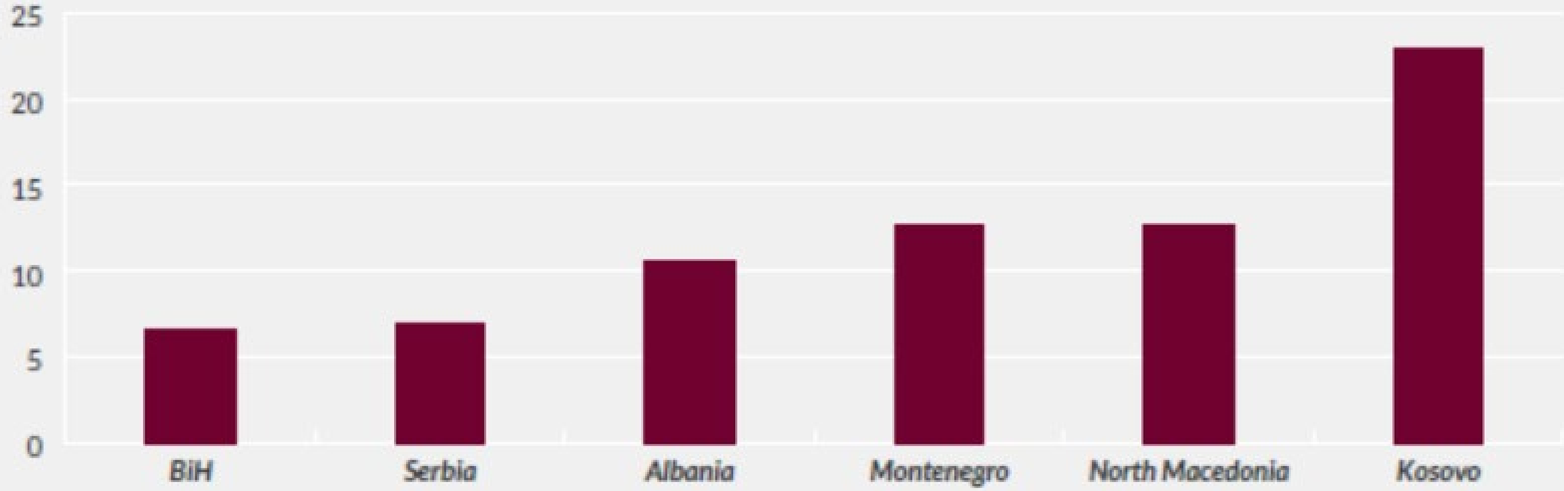
- The most effective way to improve regional cooperation in the region is to enact policies aimed at raising incomes.
- One direct way for the EU to achieve this would be to increase budget transfers to the Western Balkans. This could be done by granting the Western Balkan economies full access to the EU budget.

FIGURE 22 **Total EU budget transfers in EU-CEE countries between 2004 and 2018 (as % of GDP)**



Source: European Commission | © Bertelsmann Stiftung and wiiw.

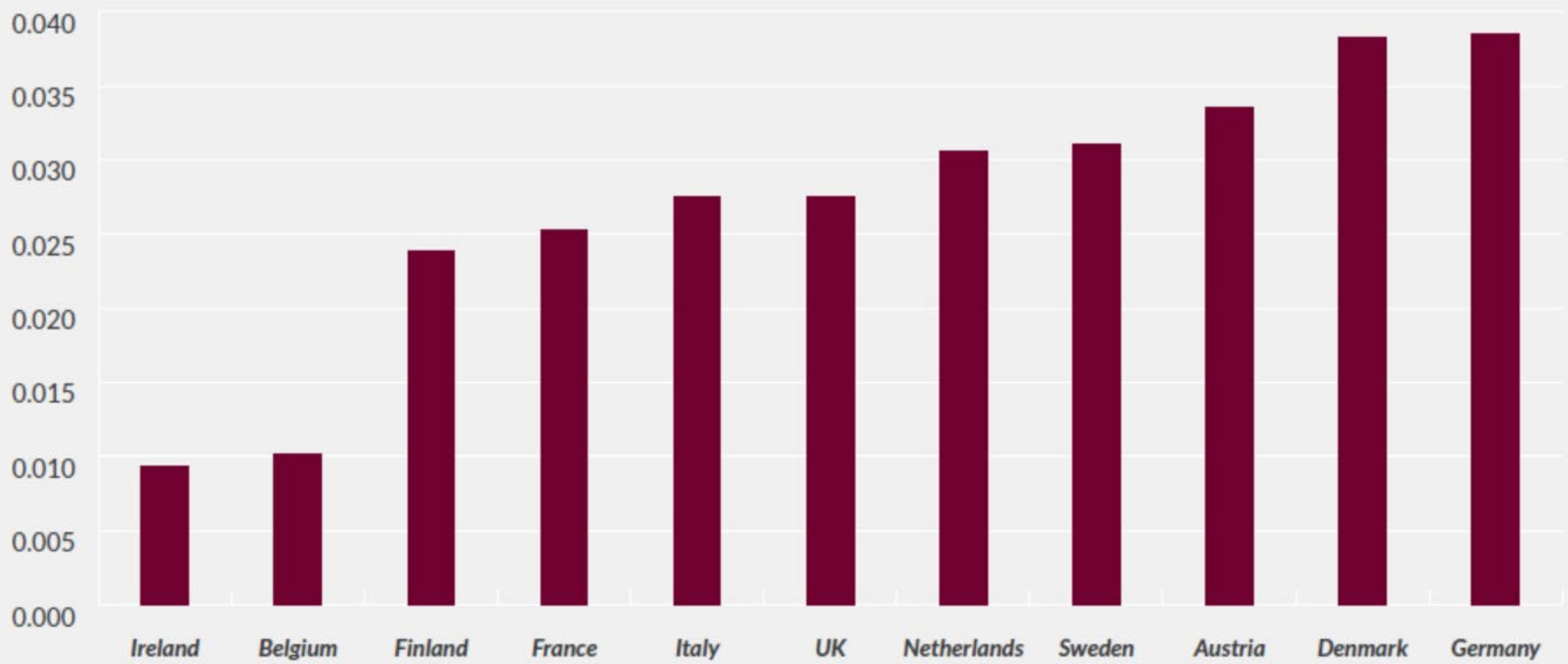
FIGURE 23 **Total IPA funds in Western Balkan economies between 2007 and 2018 (as % of GDP)**



Source: European Commission | © Bertelsmann Stiftung and wiiw.

The costs of this for existing EU members will be small

FIGURE VII.4 **Estimated costs of full Western Balkan participation in the EU budget, as a percentage of each net contributor member state's 2018 GDP**



Source: European Commission, Eurostat, wiiw, own calculations. | **© Bertelsmann Stiftung and wiiw.**

- Greater transfers should be accompanied by strict conditions for institutional reforms.
- Our proposal is not substitution for a fast EU accession. Fast accession must remain the first priority. This is just a complement to that, until countries become members.
- War in Ukraine reinforces these arguments. If EU doesn’t show a greater support for the Western Balkans, Russia might step in.

Thank you for your attention!

Questions? Comments?

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Additional slides

Econometric approach (1)

Regional economic integration = f (EU, FDI, regional income, initial conditions, EU transfers, euro, size of economy, exchange rate, labour costs, productivity) *(Eq. 1)*

Econometric approach (2)

Income = f (EU, EU transfers, euro, interest rate, inflation, government expenditure, loans, education, FDI, political stability, exchange rate) *(Eq. 2)*

FDI = f (EU, EU transfers, euro, GDP per capita, size of economy, political stability, exchange rate) *(Eq. 3)*

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TABLE 3 **Econometric results for regional integration in terms of exports of goods**

Dependent variable: Regional integration in export of goods	
EU membership	0.50*** (0.14)
Initial regional integration	3.78*** (0.27)
FDI stocks	–0.030** (0.015)
GDP per capita of region	1.18*** (0.28)
EU transfers	0.051 (0.042)
Euro	–0.016 (0.070)
GDP of economy	–0.13** (0.050)
Exchange rate	0.0034 (0.066)
Labour costs	0.026 (0.054)
Labour productivity	–0.042*** (0.010)
Constant	-11.7*** (2.91)
Observations	1,972
Pseudo R-squared	0.099
AIC	1,339.7

Note: Explanatory variables are shown in the first column, coefficients and standard errors in the second. *, ** and *** denote statistical significance at 10 percent, 5 percent and 1 percent, respectively | © Bertelsmann Stiftung and wiiw.

TABLE 4 **Econometric results for regional integration in terms of exports of services**

Dependent variable: Regional integration in export of services	
EU membership	0.47*** (0.13)
Initial regional integration	9.83*** (0.94)
FDI stocks	0.045* (0.027)
GDP per capita of region	2.84*** (0.36)
EU transfers	-16.9*** (4.66)
Euro	-0.089 (0.10)
GDP of economy	-0.096 (0.068)
Exchange rate	0.24 (0.17)
Labour costs	-0.33** (0.17)
Labour productivity	0.11 (0.080)
Constant	-29.3*** (3.45)
Observations	1,405
Pseudo R-squared	0.101
AIC	655.8

Explanatory variables are shown in the first column, coefficients and standard errors in the second. *, ** and *** denote statistical significance at 10 percent, 5 percent and 1 percent, respectively | © Bertelsmann Stiftung and wiiw.

TABLE 5 **Econometric results for regional integration in terms of FDI**

Dependent variable: Regional integration in terms of FDI	
EU membership	0.00042 (0.0047)
Initial regional integration	0.94*** (0.051)
GDP per capita of region	0.039*** (0.012)
EU transfers	–0.00042 (0.0026)
Euro	0.014 (0.0091)
GDP of economy	–0.0043 (0.0036)
Exchange rate	–0.0022 (0.0018)
Constant	–0.26 (0.19)
Observations	**180**
Pseudo R-squared	
AIC	**–879.7**

Explanatory variables are shown in the first column, coefficients and standard errors in the second. *, ** and *** denote statistical significance at 10 percent, 5 percent and 1 percent, respectively | © Bertelsmann Stiftung and wiiw.

TABLE 6 **Determinants of income in EU-CEE**

Dependent variable: Real GDP of the country	
EU membership	−0.001 (0.138)
EU transfers	0.14** (0.052)
Euro	−0.153 (0.14)
Interest rate	0.025 (0.066)
CPI inflation	−0.027 (0.050)
Government spending	2.35*** (0.61)
Bank loans to firms	−0.28 (0.17)
Education	−0.18 (0.46)
FDI stocks	0.71*** (0.085)
Political stability	0.34** (0.13)
Exchange rate	−0.12** (0.038)
Constant	8.12** (2.64)
Observations	**145**
Pseudo R-squared	
AIC	**−20.2**

Explanatory variables are shown in the first column, coefficients and standard errors in the second. *, ** and *** denote statistical significance at 10 percent, 5 percent and 1 percent, respectively | © Bertelsmann Stiftung and wiiw.

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TABLE 7 **Determinants of FDI into EU-CEE**	
Dependent variable: FDI stocks into the country	
EU membership	0.15 (0.13)
EU transfers	-0.01 (0.09)
Euro	0.14 (0.10)
GDP of economy	0.85*** (0.12)
Exchange rate	0.08*** (0.02)
GDP per capita	0.03 (0.48)
Political stability	-0.009 (0.24)
Constant	-11.7 (4.64)
Observations	177
Pseudo R-squared	
AIC	598.4

Explanatory variables are shown in the first column, coefficients and standard errors in the second.
*, ** and *** denote statistical significance at 10 percent, 5 percent and 1 percent, respectively |