UNIVERSITY OF MACEDONIA
FACULTY OF ECONOMIC AND REGIONAL STUDIES
DEPARTMENT OF BALKAN, SLAVIC AND ORIENTAL STUDIES
MASTER'S DEGREE IN POLITICS AND ECONOMICS OF CONTEMPORARY EASTERN AND SOUTH-EASTERN EUROPE

DISSERTATION THESIS

Economic Development & Growth in Western Balkans. The case of Serbia

CHRISTOS DASARGYRIS

Student Registration Number: **mpe18004**

Supervisor: *Dimitrios Kyrkilis, Professor of Economic Development and Investments in Eastern Europe and the Balkans*

Evaluation Committee Member: *Christos Paraskevopoulos, Professor of Political Science and European Public Policy*

Evaluation Committee Member: *Athanasios Koulakiotis, Associate Professor of International Economic Relations*

Thessaloniki 2022

"The approval of Master's Thesis by the Department of Balkan, Slavic and Oriental Studies of the University of Macedonia does not necessarily imply that the Department shares the author's opinions."

I hereby declare, that all the data used in this work, have been obtained and processed according to the rules of the academic ethics as well as the laws that govern research and intellectual property. I also declare that, according to the above mentioned rules, I quote and refer to the sources of all the data used and not constituting the product of my own original work. **Christos Dasargyris**

Table of Content

Abstract

It is late 1980’s early 1990’s. Soviet Union has fallen along with the other Socialist states. One of them was Yugoslavia; at its place, various different states start to emerge. The emerging of all these states was not peaceful; on the contrary there were conflicts both political and military. When these tense conflicts had come to an end, the newly formed independent states started another arduous internal battle: the battle of transformation from a centralized to a liberal economy.

Despite the fact that, transfiguration of the economy in Western Balkans started approximately at the same time with the rest of ex-socialist states in Eastern Europe, Western Balkans still remain behind in terms of economic growth. What it could be a reasonable explanation for that? However, we should mention that, Western Balkans taking some serious initiatives as independent states separately in order to catch up with the other advanced EU economies.

Last decade, Western Balkans has been in the spotlight for these initiatives. Tremendous step forward has been made and the first tangible results starting to appear. They had attracted not only the interest of Europe but also outside of it; since they seem to leaving behind their socialist past and opening up their economy to possible investors. The policy of opening up their countries to possible investments seems to be bringing fruitful results and the region in general can hope in a prosperous future.

*Keywords**:** Western Balkans, Growth, Reforms, Serbia, Business Opportunity*

Introduction

The Soviet Union has fallen, all the communist/socialist states has fallen into debris. Poverty, corruption and a massive exodus of people towards to more advanced economies dominate these countries in general. Luckily, this situation would not be last long. Countries of the former-so called- Eastern Bloc; start to reconstruct their economies and soon see tangible results in growth rates. The same strategy seems to be implemented in the Balkan neighbourhood. The former Yugoslav fall into pieces and its place emerged 6 totally different –both culturally and economically-independent states, known as a Western Balkans.

The last decade Western Balkans, seems to be doing fast-paced steps forward in reforming their economies. They have detached from their communist past and put some serious efforts in advancing their economies in order to catch up with more prosperous European economies. Rebuilding their economies goes hand in hand with the capital flow in state's treasury. For that higher purpose it was crucial-if not necessary- to open-up their border for foreign investors and implementing business friendly-laws which working in favour of the investor. Western Balkans counties started to implementing-every country in a different extent-unprecedented large privatization programmes of ex unprofitable state companies; either by selling them to foreign investors or internal ones. The ultimate purpose of attracting investors was-and still is- to catch up with the European advanced economies. Therefore, Western Balkans offers strong macroeconomic stability, strategic geographic location, diverse economies, favourable tax regimes and low unit labour costs. All these, combined with a relatively well-educated population, making an investor to have a better look in the region.

Nevertheless, Western Balkans seems to be facing some difficulties in catching up. Despite the fact that, Western Balkans has the same background with Eastern European countries and started from the same position. Eastern European countries seem to be doing better off and catching up with the rest of the Europe in a faster way than Western Balkans. Possible explanations on that issue have been given in this paper but if we want to mention some here briefly; probably would be the lack of infrastructure and innovation, the absence of incentives for a long-term productivity, the flexibility on how doing business (given the fact that the Western Balkans are not the most easy-of-doing- business region) and lack of know-how.

The layout of this paper gives an extensive knowledge on the topic. The first chapter gives a general idea regarding the transition from centralized to liberal economies and reforms that have been taken in order to catch up. In the second chapter we deepening in Western Balkans and explore the financial structure of the region. Additionally this chapter provides incentives that exist in the region in order to attract more investors. In the third chapter we investigate the case of Serbia. Serbia is taking steps forward but still hanging behind, even from Western Balkans states, like Croatia and Slovenia. Therefore in the last chapter I present some key point that would transform Serbia and making the country to catch up faster.

Chapter 1

1. From centralized to free-market economy

After the fall of Berlin Wall and consequently the fall of the Soviet Union, Balkans has been the field of tremendous changes, both politically and economically. The whole process of the financial transformation started in the decade of 1990's. This decade was the turning point of the Balkan economies; their leaders preferred applying more liberal financial measures that was leading towards to free-market economy rather than measures that have been tested in the past and obviously failed. These measures characterized by the intervention of the government in the economy and the relentless resistance to opening their economy in the world. In that particular direction, they moved towards to privatization of -up to this point-, state-owned banks and corporations, adopting a new liberal banking system and putting emphasis in the extroverting character of their economy; making an opening in the so called Western World. All these new measures had a significant positive impact in their economies. The growth rates started increasing, the international trade was making its appearance and the standards of living were improving for the majority of population, compared with the previous situation.

However, the transition to a market economy and multiparty democracy in the Balkan region and especially in the Western Balkans started in the 1990's, seems that the region is still behind in comparison with countries in Central and Eastern Europe (CEEB) and the Baltics, which have been in the past under the same regime. The same phenomenon is even more obvious with developed European economies. Most Balkan countries are today lagging behind in their level of economic development, economic and institutional reforms, and integration with the European Union[1].

In this framework we can identify three main reasons that delay the transition of the Balkans to a liberal economy during the 1990's. Political events and military conflicts where all successor states directly or indirectly involved. These conflicts had as a result some serious economic implications such as: high inflation, fall of GDP and rise of unemployment. Secondly, inappropriate economic policies, which have been implemented -mainly- from the successor Yugoslav states. These measures had as a result for the Balkans, in general, to be seen as an unattractive place for Foreign Direct Investment (FDI). Only exemption was Croatia which has attracted the most FDI in comparison with the other Balkan countries[2]. Last but not least, limited EU initiatives to facilitate transition. It was clear, within the European political cycles, that the EU was setting as a priority the smoothly transition of the CEEB and the Baltics countries.

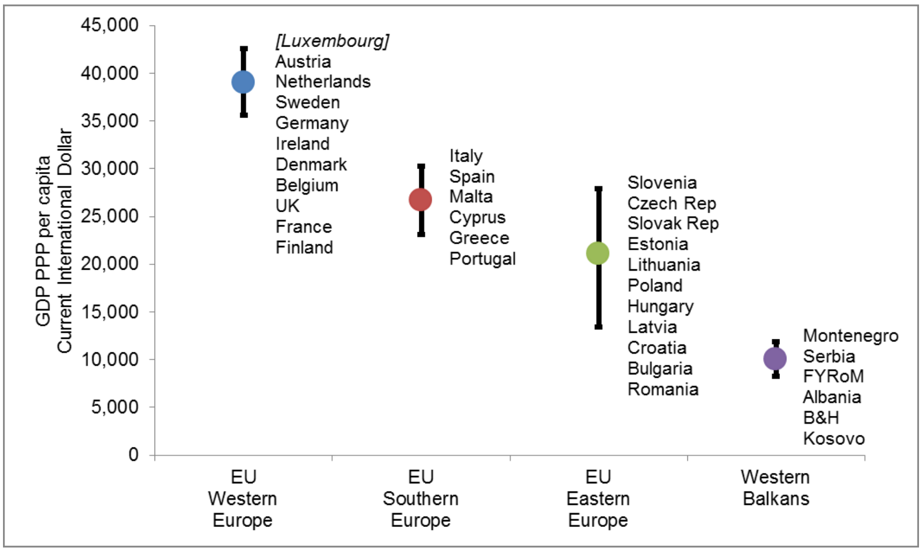
[1] Milica Uvalić,Vladimir Cvijanović, 2018, SOE. Towards A Sustainable Economic Growth and Development in the Western Balkans.

[2] Estrin, S. and M. Uvalic (2008), "From Illyria towards Capitalism: Did Labor-Management Theory Teach Us Anything About Yugoslavia and Transition in its Successor States?", Comparative Economic Studies,50th Anniversary Essay, Vol. 50, pp. 663-696.

The pre mentioned factors above played a significant role in the crawling development of Balkans especially of Western Balkans which was the region suffered the most from the socio-economic changes of the 1990's. Nevertheless, we must not ignore the progress that has been made in the region both in the economy and trade, which we are going to extensively examine in the coming chapters.

As it has been interjected above, Balkans and especially Western Balkans seems to be having a creeping progress despite all the remodelling they have done in the fiscal system. Despite all these alterations, still are abaft in comparison with other western, eastern and southern countries in the continent. Growth rates have been in bottommost single digits at best and negative at times in some countries. Levels of unemployment and poverty are persistently high. Supplies of foreign credit and capital from private sources – plentiful in the pre-crisis years – have largely dried up. Meanwhile, banks in the region remain preoccupied with the legacy of the crisis, especially the high levels of non-performing loans (NPLs), rather than lending to the real economy. At the same time, governments face severe limits in what they can do to tackle these problems[3]. The graph below illustrates the under-performance in Western Balkans by presenting the GDP in PPP in Western, Southern and Eastern Europe in Comparison to the Western Balkans.

Source: World Economic Outlook, IMF, October 2015.

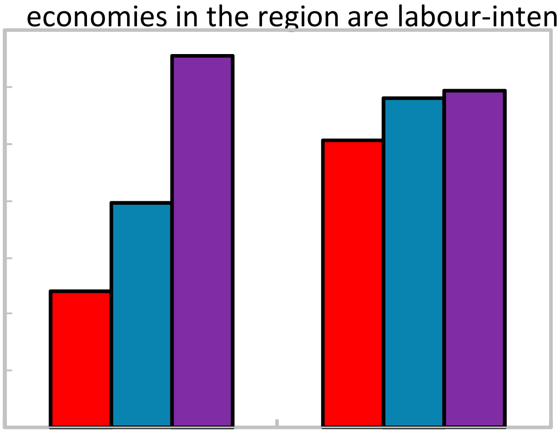


As we observe in the graph the GDP in PPP in Western Balkans is roughly the half of their Eastern Europeans the one third of the Southern Europeans and a quarter of the rich Western Europeans. This is a small idea on what is going in the region. The big question is: what must happen in order for the region to catch up? A close related question with WB perspective EU candidacy, question that will be answered in the following chapters.

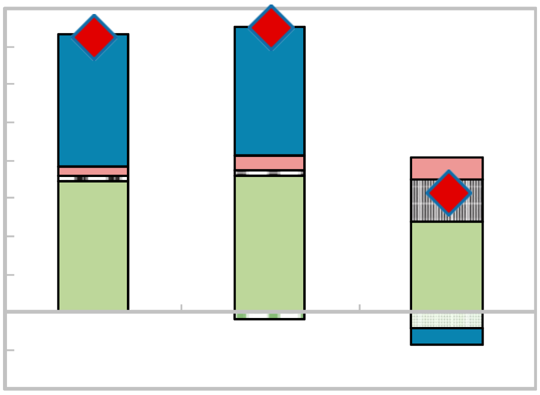
3 Sanfey P, Milatovic J, Kresic A. 2016, EBRD. How the Western Balkans can catch up.

1.1 Convergence and Growth, still way to go?

In the Western Balkans we see tremendous efforts for economic restructuring worth mentioning. But in terms of convergence and growth how the situation really is? It is a fact that Western Balkans saw a huge economic development in 2000's, along with the rest of New Member States. The reasons behind this are the capital inflows and the total productivity gains[4]. The capital inflows came along with the investment boom during 2000's and the productivity gains came from the transformation from central to market economy. The small number of labour inputs and the importance of productivity could explain why many economies in the region are labour-intensive[5].



Gross Fixed Investment (Percent of GDP) 2000-2011[6]



GDP Growth and Contribution 2000-2011 %[7]

Yet despite the limited contribution of labour input the force for progress from other factors was so strong that generated significant results on the standards of living. It is worth mentioning to say that Western Balkans had reduced the gap in GDP in PPP in comparison with the advanced EU economies by 30% as the graph shows below.

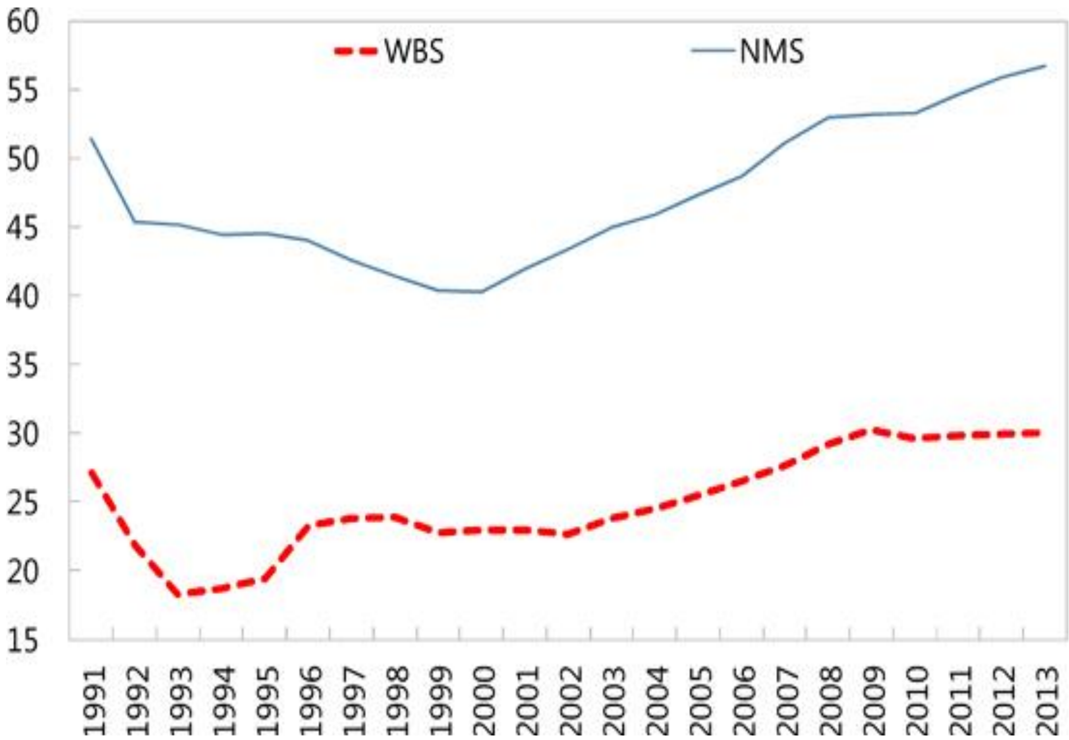
[4] Zuzana Murgasova, Nadeem Ilahi, Jacques Miniane, Alasdair Scott, Ivanna Vladkova-Hollar, and an IMF Staff Team. 2015. The Regional Economic Issues (REI) The WESTERN BALKANS- 15 Years of Economic Transition. ISBN: 978-1-49835-651-0

[5] Gerxhani, Klarita. 2004. "The Informal Sector in Developed and Less Developed Countries: A Literature Survey.'' Public Choice 120: 267-300.

[6] With red:Western Balkans, Blue: New Member States,Purple: EU-17. On the left is 2000 and on the right 2011.

[7] With blue: Total Factor Productivity Growth, Pink:Human Cpital, Grey: Change in average hours worked, White: Labour input, Green: Capital accumulation, Diamond: GDP growth. From left to right: WB, NMS, EU-17.

Catching up with Advanced Europe (Average country GDP per capita as percent of average EU17 GDP per capita)



Sources: Penn World Table; and IMF staff calculations.

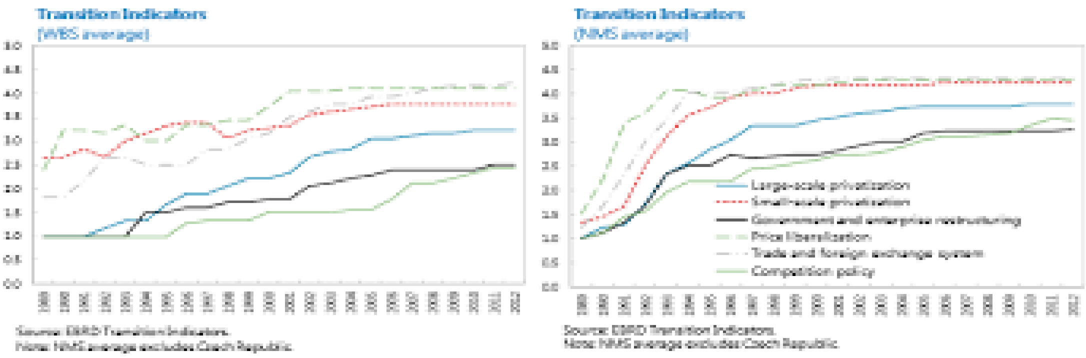
But the pace of convergence of Western Balkans is stagnant compared to New Member States. What is hiding behind that? One possible explanation is that the New Member States have better access to knowledge. Since they are located closer to EU advanced economies; are way easier to be offered opportunities in terms of access to markets and investments. Another reason is the internal changes in the financial sector that each country has been made in order to speed-up convergence[8]. Additionally, some evidence suggests that the labour force playing an extremely significant role in the economic development[9]. Finally, some surveys have concluded that policies which promote market liberalization and give incentives to the private sector have a significant footprint in the economic prosperity[10]. Having that in mind; next section going to examine reforms and the progress has been made in Western Balkans in the long road of economic transformation.

[8] Aghion, Philippe, Peter Howitt, and David Mayer-Foulkes. 2005. "The Effect of Financial Development on Convergence: Theory and Evidence ''The Quarterly Journal of Economics (February):173-222.
[9] Fung, Michael K. 2009. "Financial Development and Economic Growth: Convergence or Divergence?''Journal of International Money and Finance 28: 56-67.
[10] Campos, Nauro F., and Fabrizio Coricelli. 2002. "Growth in Transition: What We Know, What We Don't and What We Should ." *Journal of Economic Literature* 11: 783–836.

1.2 Significant Reforms

Predominately, Western Balkans followed the same pattern of economic restructuring with New Member States. This process involved, price liberalization, trade and foreign reforms that enforce privatization and -later on- competition policies. However, the whole restructuring means was significant slower that New Member States as graphs illustrate below.

Transition Indicators (WBS)



Source: EBRD Transition Indicators

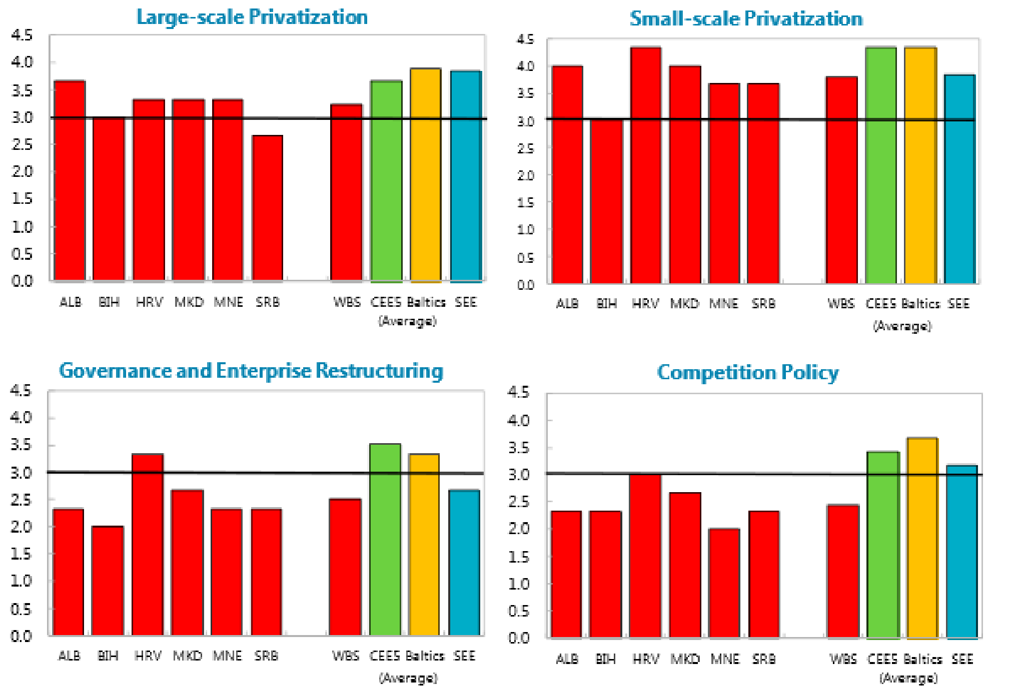
Despite the difficult decade of 1990's Western Balkans reached in a satisfactory point of the pre-mentioned sectors by 2000. Although, measures for large-scale privatizations and competition policies has not been introduced because of their degree of difficulty. In a socialist state with the absence of any kind of ownership, how would it be possible to convert to private ownership? In this process of privatization each state followed its own policies more or less[11].

The progress in ***large-scale privatization*** was not the same among Western Balkans. Countries like Bosnia and Herzegovina, Montenegro and Serbia implemented way later these kinds of privatizations. Something, which other countries on the region started in the late 1990's. Additionally, there were considerable variations in the privatization of different sectors. For instance, the banking, telecommunications and the energy sector moved forward but large public corporations such as: metals, shipyards and railways; proven difficult to privatize.

Regarding ***corporate governance and enterprise restructuring*** of the former socialist states remain a challenge across the region. For instance in Bosnia and Herzegovina the management of privatized corporations was blocked because of the ill-arrangement of the ownership. In FYROM most of the former state-owned corporations were given to insiders rather than useful investors, holders of huge capital and the experience on setting businesses. The result of all these was, many corporations survived but they were underperformed. In Serbia, weak government

11 Hashi **I,** Krasniqi A. B, 2008, ''Entrepreneurship and SME Growth: Evidence from Advanced and Laggard Transition Economies'', International Journal of Entrepreneurial Behaviour, Vol 17 will in price control leaded in large scale corporate losses and huge fiscal cost. In Croatia, the state persisted by subsidizing various sectors, particularly the agricultural sector and the shipbuilding up until EU accession. In Montenegro, the privatization of aluminium and steel enterprises causing significant loses of public money.

Selected Transition Indicators, 2012



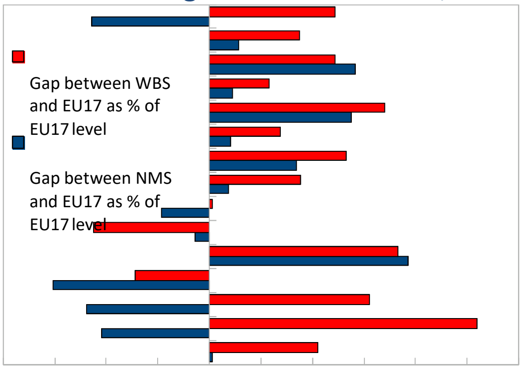
Source: EBRD Transition Indicators and IMF staff calculations.
Note: The scales range from 1 to 4+, where 1 represents little or no change from a rigid centrally planned economy and 4+ represents the standards of an industrialized market economy. A value of 3 indicates an advanced stage of transition. Data for Czech Republic and Kosovo is not available.

The Western Balkans made a compelling progress in the elimination of bureaucracy and in the improvement of the business environment during the decade of 2000’s. The general image is that, the business environment continues to block foreign investors but, despite that, there are some success stories. Measures were taken in order to lighten the regulatory burden. Many countries, took the initiative to remove unnecessary regulations, set up one stop shops for starting a business and obtaining construction permits, reduced non-tax fees, strengthened bankruptcy procedures, improved investor protection, introduced or expanded the coverage of real estate cadastres, introduced or improved investment promotion laws, and set up entrepreneurial zones with good infrastructure and land free of ownership uncertainty. Large infrastructure projects were initiated to fill critical gaps[12]. World Bank’s Doing Business Indicator reveals that significant progress has been made in registration of property. Registration in Western Balkans is way cheaper that the advanced EU economies. Additionally, taxation is lighter across the region. However,

[12] Zuzana Murgasova, Nadeem Ilahi, Jacques Miniane, Alasdair Scott, Ivanna Vladkova-Hollar, and an IMF Staff Team. 2015. The Regional Economic Issues (REI) The WESTERN BALKANS- 15 Years of Economic Transition. ISBN: 978-1-49835-651-0

business and investors still suffer from bureaucratic time- consuming issues such as: pay taxes, solve insolvency, it is still takes a lot of time for businesses to trade or enforce contracts. Last but not least, the region lacks in infrastructure in transportation and energy.

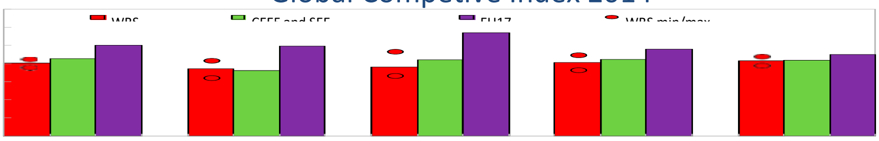
Selected Doing Business Indicator, 2012



Source: World Bank, Doing Business Indicators; and IMF staff calculations

A formidable challenge facing the region is reforming governance. While better governance facilitates higher per capita incomes, empirical evidence does not point to a virtuous cycle whereby higher growth automatically brings about improvements in governance[13]. This shows that there is a huge need of government improvement. Western Balkans is hanging behind compared to New Member States and EU in rule of law, political stability and corruption control. The quality of such institutions depends on several factors, particularly openness—that is, countries with greater openness to trade and finance tend to have better economic institutions[14].

Global Competive Index 2014



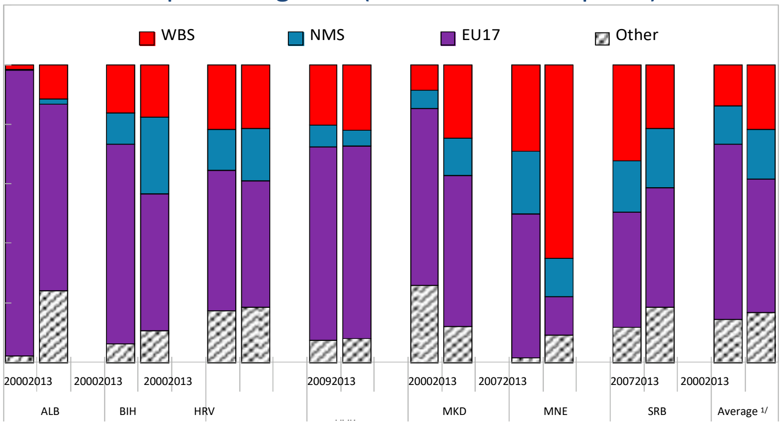
Source: WEF Global Competiveness Indicators and IMF staff calculation

Trade openness is commonly associated with higher economic growth and efficiency; we now turn to an assessment of the progress of the Western Balkans in this area. While the region has gradually moved toward greater openness, the Western Balkans average share of exports stands at under half of the New Member States average of 60% of GDP. The average share of exports to GDP increased by 8 percentage points between 2000 and 2013, albeit representing disparate cross-country dynamics: a twofold and threefold increase in export shares took place in relatively closed economies like Bosnia and Herzegovina and Albania, in contrast with limited gains in export shares in Montenegro. The EU has been the largest export market for the region for some time, and continues to absorb about 60% of

[13] Kaufmann, Daniel, and Aart Kraay. 2002. “Growth without Governance.” World Bank Policy Reaserch, Working Paper No. 2928. Washington: World Bank.
[14] EBRD 2013, Transition Report.

Western Balkan exports, with the notable exception of Montenegro. Yet trade among the Western Balkan countries themselves has become more important as well since 2000.

Exports of goods (share of total exports)



Source: Direction of Trade Database and IMF staff calculations

The evolution of the structure of export goods in the Western Balkans as a group has broadly mirrored the experience of New Member States, which saw a rise in higher-value-added exports accompanied by an increase in agricultural exports and minerals. However, this masks large heterogeneity across the region. Whereas FYR Macedonia and Serbia have augmented their shares of exports of machinery and transport, mineral exports have increasingly dominated the export structure in Albania, Bosnia and Herzegovina, and Montenegro. The latter lags behind the rest of its Western Balkan peers in export diversification, whereas Serbia has made significant progress, and Croatia has preserved its relatively more favourable starting point.

1.3 Picking up the pace

It is commonly accepted that ambitious structural reforms can boost economic advancement. But which specific reforms would deliver the strongest growth dividend in each of the Western Balkan countries? This question is tackled in this section by first identifying country-specific reform gaps, and then comparing the performance of the Western Balkan economies along a wide set of competitiveness indicators with the performance of New Member States and the average EU country[15]. Growth regressions are then used to rank reforms according to their

[15] The analysis is based on data from the World Economic Forum's Global Competitiveness Report. Competitiveness is defined as the set of institutions, policies, and factors that determine the level of productivity of a country. The database covers 144 countries, including six of the seven Western Balkan countries under consideration. Data for Kosovo are not available.

importance for growth. The results allow for proposing country-specific reform priorities in areas where both the competitiveness gap is large and the estimated growth impact of reform is high.

Set of factors that are in IMF report[16] that determine productivity and growth, encompassing 10 broad areas such as institutions, infrastructure, and innovation, among others[17]. Along a few dimensions the Western Balkan states have closed the distance with New Member states, but those most gaps are still negative. When assessed against EU averages, however, the pending reform agenda looms large. Where do the main gaps lie?

Relative to NMS, Montenegro and, to a lesser extent, FYR Macedonia compare relatively favourably: most of the estimated gaps are small, and a few are slightly positive—meaning that in these specific areas the competitiveness profile of these two countries is similar to that of NMS. The results for Albania, Bosnia and Herzegovina, and Croatia are more mixed—while the gap is relatively small in some areas, in others they lag behind significantly. For Albania and Bosnia and Herzegovina, the notable gaps are in infrastructure and financial market development; for Croatia, the gaps are in goods and labour market efficiency. Serbia generally faces more formidable structural challenges, as it compares unfavourably to NMS along all 10 indicators.

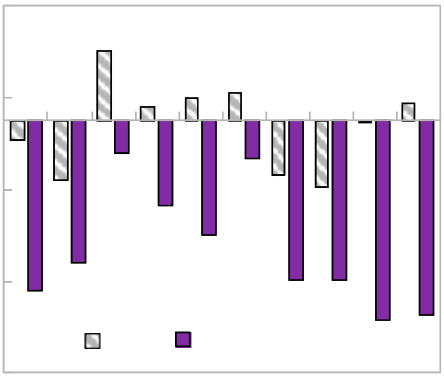
Relative to the EU average, the gaps in all Western Balkan countries tend to be wider, highlighting significant structural reform needs in almost all areas. This is also true for Montenegro and FYR Macedonia, which compare reasonably well to the New Member States. Overall, the major gaps throughout the region are in institutions, infrastructure, goods market efficiency, and financial market development. The estimated gaps in business sophistication and innovation are particularly large compared to the EU, both relative to other reform areas and in contrast to generally good performance of the region along this dimension relative to New Member State peers. In the graphs below Peers illustrated with white and EU Average with purple

[16] Zuzana Murgasova, Nadeem Ilahi, Jacques Miniane, Alasdair Scott, Ivanna Vladkova-Hollar, and an IMF Staff Team. 2015. The Regional Economic Issues (REI) The WESTERN BALKANS- 15 Years of Economic Transition. ISBN: 978-1-49835-651-0

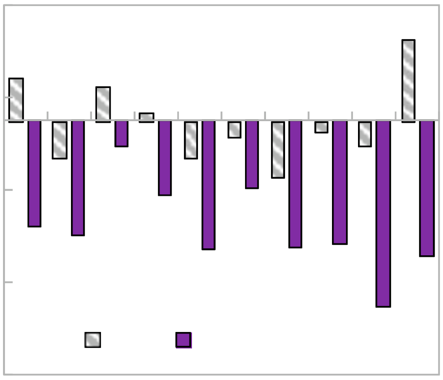
[17] While the Global Competitiveness Report covers 12 reform areas (pillars), we omit two: Macroeconomic Environment and Market Size

Main Reform Gaps in the Western Balkans

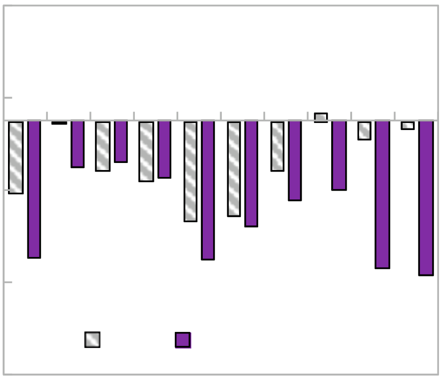
Albania



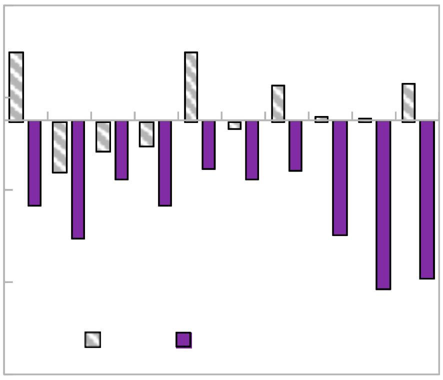
BIH



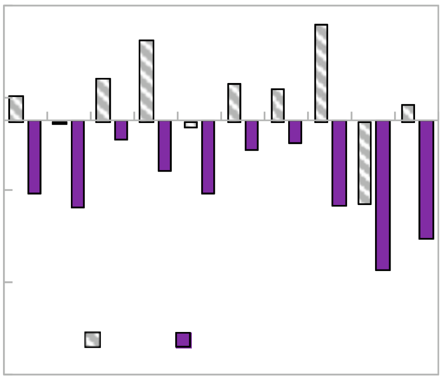
Croatia



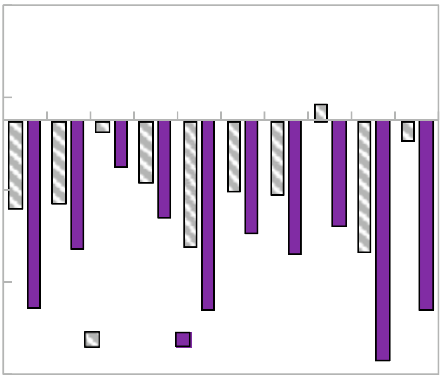
FYROM



Montenegro



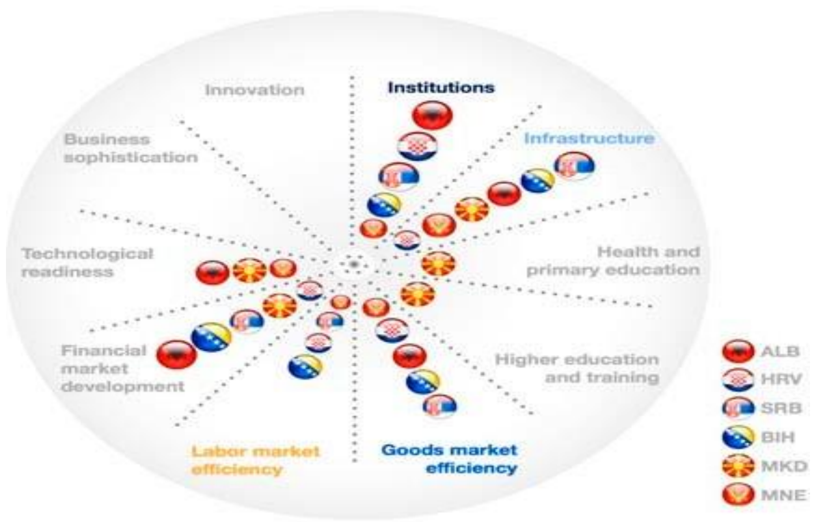
Serbia



Sources: World Economic Forum, *Global Competitiveness Report*; and IMF staff calculations

If all structural reforms were equally important for growth, the size of the reform gap would signal reform priorities. However, the growth impact of reform areas differs. There is a study that suggests[18] that while reforms in all areas are expected to have a positive impact on growth, reforms in institutions, financial markets, and infrastructure has, on average, a larger impact on growth. Results also suggest that the growth impact of reforms varies with income levels— institutions and infrastructure are estimated to be relatively more important for lower- and middle-income countries, whereas innovation and business sophistication appear relatively more important for high-income countries.

Top 5Reform Priorities for Each of WB States[19]



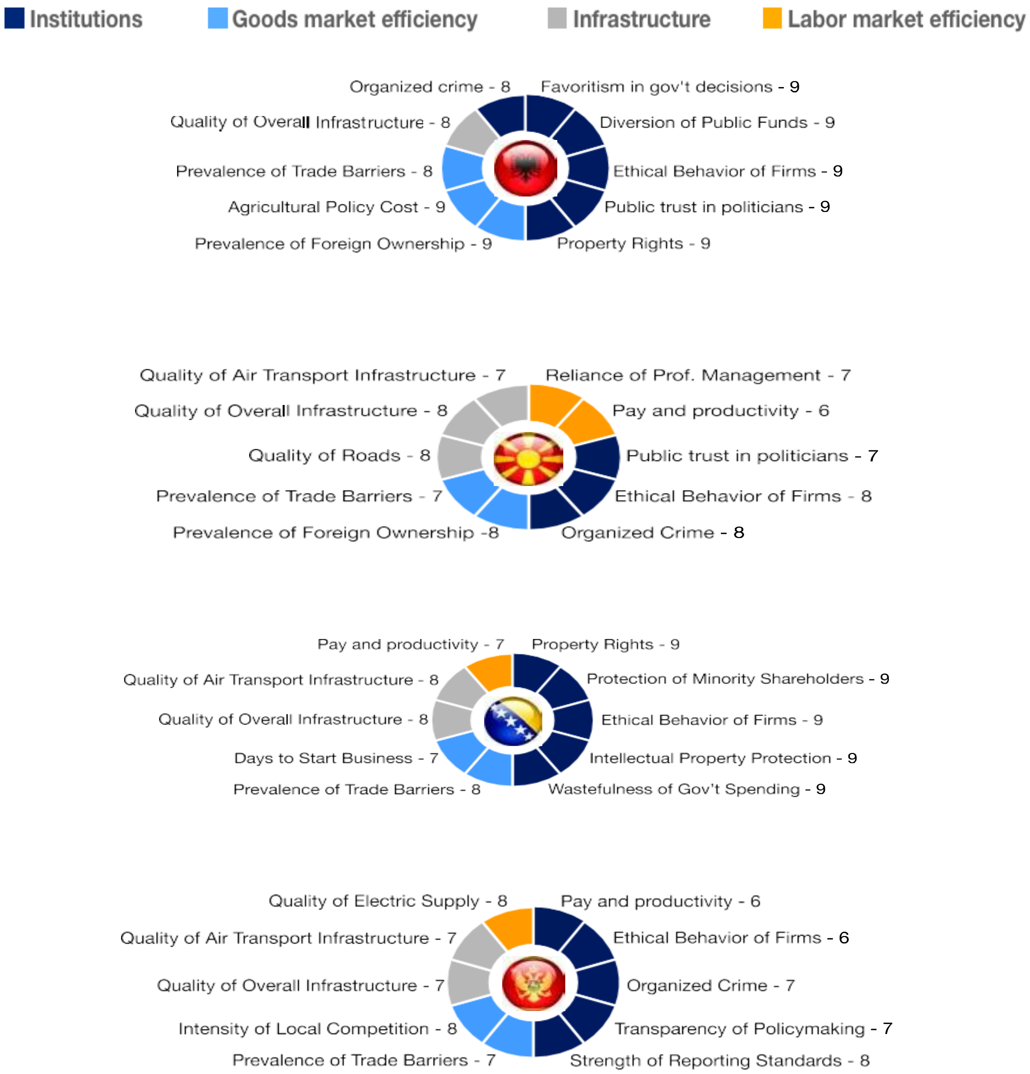
Leaning on these findings by combining reform gaps and the relative importance of each reform area for growth, we can identify reform priorities. According to our methodology, the reform priority is higher the more important the specific reform area is for growth and the larger the corresponding reform gap is. This derived structural reform map serves to provide an indicative overview of where reform priorities may be. Furthermore, results suggest that, compared to New Member States, reforms across the Western Balkans are particularly needed in the areas of institutions, infrastructure, goods market efficiency, labor market efficiency, and financial market development. Each of those areas is found to be among the top five reform priorities for at least four of the six Western Balkan states; infrastructure was identified as a top reform priority in all six countries.

[18] Zuzana Murgasova, Nadeem Ilahi, Jacques Miniane, Alasdair Scott, Ivanna Vladkova-Hollar, and an IMF Staff Team. 2015. The Regional Economic Issues (REI) The WESTERN BALKANS- 15 Years of Economic Transition. ISBN: 978-1-49835-651-0

[19] Note: Reform priorities are assessed relative to the NMS in each of the 10 main pillars of the Global Competitiveness index. Larger bubbles represent reform areas that receive a higher rank ordering. Analysis for Kosovo not included as the relevant data are not available.

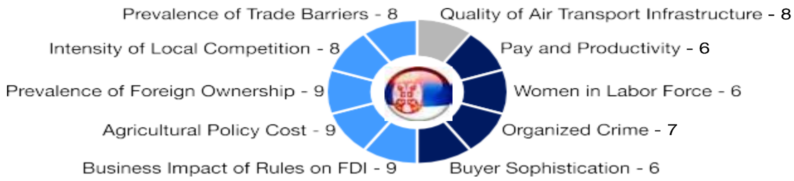
Identifying reform priorities at the more granular level, the study combines the analysis of reform gaps with their estimated growth impact, focusing on the 10 most important reform priorities for four subpillars.[20] Reform priorities remain broadly the same whether New Member States or EU countries are taken as the comparator. In most countries reforms related to the quality of institutions dominate the priority list, followed by goods market efficiency and infrastructure. Of the labor market indicators, pay and productivity enters the top 10 reform priorities in half of the Western Balkan countries.

Top 10 Reform Priorities For Each of the WB States[21]



[20] The detailed analysis at the disaggregated level is indicative. Results at this level are more sensitive to the quality of data, potential measurement errors, estimation results, and the classification scheme.

[21] These are assessed relative to the NMS along four sub-pillars of the Global Competitiveness Index (Institutions, Goods Market Efficiency, Labor Market Efficiency and Infrastructure). 2/ Numbers indicate the priority, with 9 pointing to the highest priority.



Chapter 2

1. Western Balkans: new business opportunities arise

As far as this thesis has reviewed, Western Balkans put some serious efforts in reconstruction of their economies, of course there are still flows, but things seem to be changing. In this chapter we will examine what Western Balkans can provide to possible investors, how competitive the region is. Additionally, we are going to examine the financial system of the region. It is vital; in order to attract more external investors the stability of this sector is a crucial index.

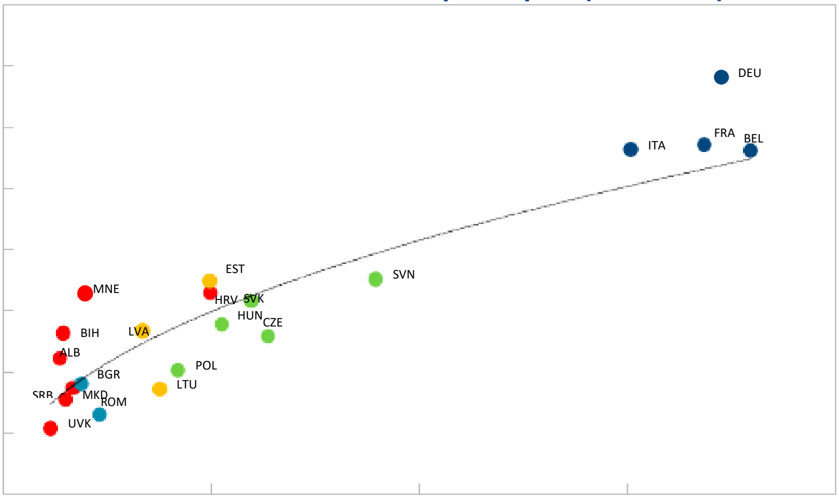
1.1 Financial Deepening

Deep financial systems support sustained economic growth and macro-financial stability mainly through efficient allocation of resources between savers and borrowers, and by allowing economic agents to smooth consumption and overcome risks[22]. Financial depth indicates the amount of financial services available in an economy, and is often proxied by the magnitude of assets or liabilities of financial institutions relative to the size of the economy. It tends to increase with economic growth and development, though it can also vary among countries at similar levels of income and market size, because of differences in macroeconomic stability, institutional strength, or the impact of past events, such as crises or wars. Over the course of economic development, financial deepening first occurs through the spread of banking services, and then involves increasing use and provision of nonbank financial services— capital, pension, and insurance markets. Nonbank deepening begins to takes place once challenges related to information, enforcement, and coordination are overcome and there is sufficient demand for

[22]Levine, Ross. 2005. "Finance and Growth: Theory and Evidence." In *Handbook of Economic Growth Vol. 1A,* edited by Philippe Aghion and Steven Durlauf. Amsterdam: Elsevier.

sophisticated financial services[23]. The evolution of financial deepening in the Western Balkan countries so far appears to be following the standard pattern. These countries have advanced rapidly with bank deepening, perhaps more so than the New Member States at a similar stage of economic transition. However, the Western Balkan countries have lagged behind their peers in deepening their nonbank financial sector, as capital markets (equities and bonds), pensions, insurance, and other financial markets remain nonexistent or severely underdeveloped in many of the Western Balkan countries, except perhaps in Croatia.

Bank Assets and Income per capita (200-2011)



Source: World Bank Financial Development Database (GFDD)

The process of bank deepening in Emerging Europe in the 1990s was not smooth. Countries found it challenging to establish market-based financial systems because of the need to simultaneously undertake macroeconomic stabilization as well as financial and operational restructuring of banks and firms. New legal and institutional frameworks also had to be put in place[24]. As transition progressed, these countries began to open up their banking sectors through privatization, in many cases by applying liberal licensing criteria and insufficient supervision. Not surprisingly, the outcome was a wave of banking crises in a number of these countries[25], with fewer but more costly crises in the Western Balkan countries than in the New Member States. Nonetheless, one positive outcome of the turbulent 1990s was a round of banking consolidation and increasing penetration of foreign banks, which brought professionalism, know-how, and arm's length relations with borrowers. Not surprisingly, this set the stage for sustained financial deepening in the subsequent decade.

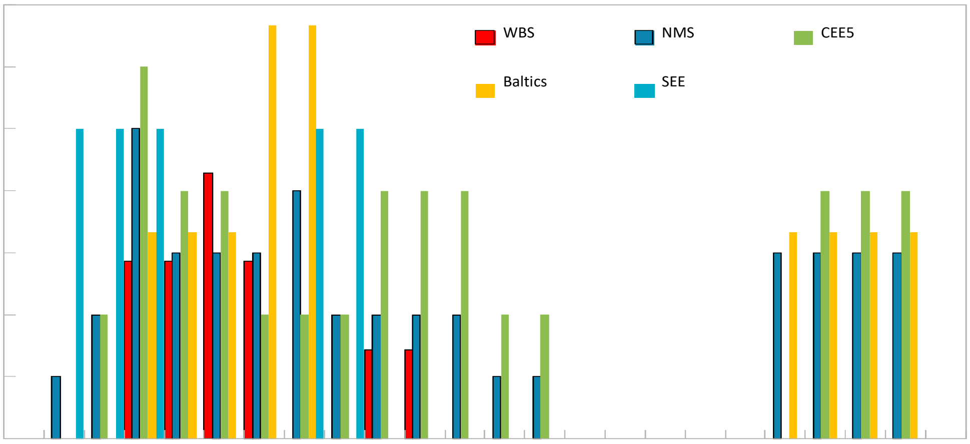
---

[23] Pagano, Marco. 1993. "Financial Markets and Growth: An Overview." *European Economic Review* 37: 613-22.

[24] Barisitz, Stephan. 2009. "Banking Transformation 1980-2006 in Central and Eastern Europe—From Communism to Capitalism." South-Eastern Europe Journal of Economics 2: 161-80.

[25] Roaf, James, Ruben Atoyan, Bikas Joshi, and Krzysztof Krogulski. 2014. "25 Years of Transition. Postcommunist Europe and the IMF. "Regional Economics Issues Special Report. International Monetary Fund, Washington.

Banking Crisis Incidence (1989-2011) in %



Source: EBRD

How does the pace of credit deepening Western Balkans compare with that in the New Member States? Such a comparison requires controlling for the stage of economic transition. As the two sets of countries began transitioning to a modern economic system almost a decade apart, a comparison of their relative progress necessitates putting them on an appropriate timeline. We use the EBRD's transition index to determine when these countries reached a "fairly advanced stage of transition." This is defined as a country having achieved macroeconomic stability and progressed with structural economic reforms. Fairly advanced transition was broadly under way in the median New Member States by around 1994. The Western Balkan countries reached a similar level of transition much later with a sizable intra-group variation. While advanced transition began prior to the 2000s in Croatia and FYROM , it began only in 2002 in the rest of the Western Balkan countries, after conflicts in the region had been settled. The analysis of the study comparing the evolution of financial deepening in the two sets of countries thus uses 1994 and 2002, respectively, as the starting years of advanced transition for the two country groups (i.e., for setting time t =0)[26]. As can be seen in the text table, the median Western Balkan country had slightly lower domestic banking asset depth than the New Member States at the same stage of transition (excluding the Baltics), but also lower comparable GDP per capita (except Bulgaria and Romania).

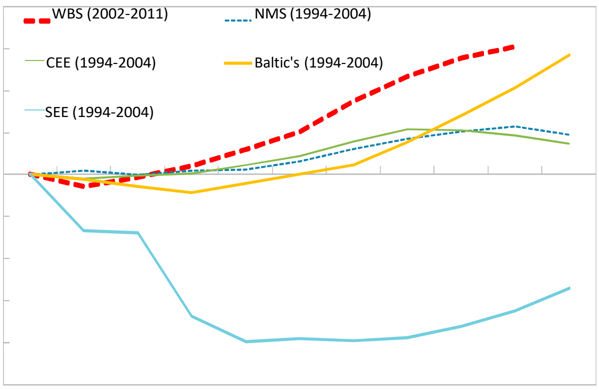
The transition threshold analysis (Murgasova 2015) suggests that the Western Balkan countries' banking systems deepened more rapidly than did those of the New Member States in the respective period following the beginning of advanced transition. The ratio of bank credit to the private sector as a percent of GDP, a widely-used measure of credit depth, grew relatively slowly in the New Member States in the five years following the start of advanced transition (i.e.,

[26] Exogenous global factors in the 1990s and the 2000s complicate the comparison somewhat. The emerging market crises of the 1990s are likely to have exogenously dampened the pace of financial deepening in the New Member States, while the global creditboom in the post-2002 Great Moderation period may exaggerate the extent of financial deepening in the Western Balkans

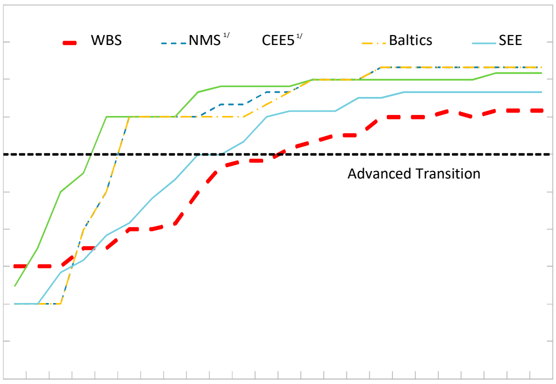
during 1994–99)[27]. On the other hand, Western Balkan countries' private credit-to-GDP ratio grew briskly after these countries had reached advanced transition and increased by a cumulative 30% of GDP in 10 years.

	WBS	NMS	Baltics	CEE	SEE
Year reached fairly advanced transition [2/]	**2002**	**1994**	**1994**	**1994**	**1994**
EBRD Transition Index [3/]	**3.2**	**3.5**	**3.5**	**3.5**	**2.1**
GDP per capita (constant 2000 U.S. dollars)	2,570	4,866	3,545	7,314	2,899
GDP per capita (current U.S. dollars)	1,827	2,410	1,903	3,891	1,236
Bank assets to GDP	28.2	33.0	16.5	36.5	96.0
Bank credit to the private sector to GDP	19.8	20.3	14.5	22.6	48.3
Bank deposits to GDP [4/]	39.0	30.9	17.0	44.6	44.6

Credit Deepening



State of Transition (1989-2011)



Source: World Bank FinStat Database

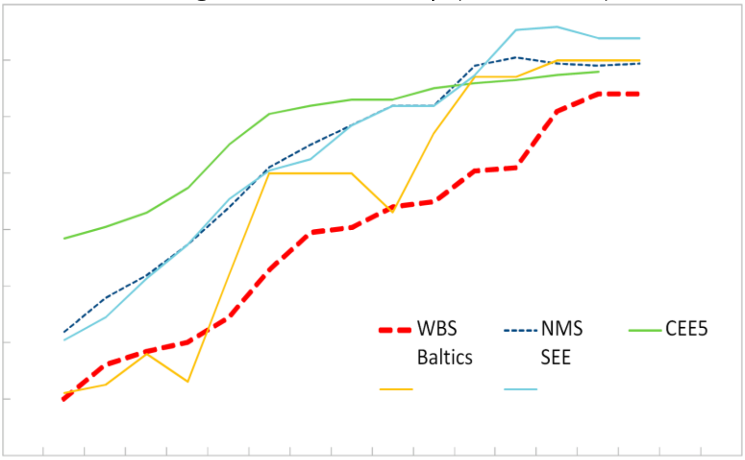
The rapid credit deepening in the Western Balkan countries also coincided with the global financial boom of the mid-2000s, which raises the question of whether credit growth was excessive and resulted in the buildup of vulnerabilities. A number of factors suggest that there was a lesser buildup of vulnerabilities and a milder boom-bust cycle in the Western Balkan countries than in the New Member States (the latter issue is discussed in fuller detail in the next section). First, much of the credit growth in Western Balkan coincidence with a rapid widening of the domestic deposit base-faster than the New Member States experienced in the period following their advanced transition-. Large inflows of remittance from abroad along with high interest growth, may explain –partly- the deposit growth[28]. More importantly, the rapid entry of foreign banks and the introduction of deposit

[27] The 1996 banking crisis in Bulgaria was particularly severe. There were also banking crises in Lithuania and Latvia (1995) and the Czech Republic (1997). Romania had a currency crisis in 1997, and growth in many countries was also affected by the 1998 Russiancrisis (IMF 2013).

[28] The higher real interest rates in some Western Balkan countries are related to declines in inflation, which serve as a proxy forgreater macroeconomic stability.

insurance scheme in 2000s likely helped to boost the confidence of depositors in the regional banking sector and attracting more deposits.

Foreign Bank Ownership (1994-2011)



Source: EBRD

1.2 Competiveness in Western Balkans

In the introduction I suggested that the Western Balkans lag behind the rest of Europe because economies in the region have been less competitive than others. The notion of "competitiveness" can mean different things to different authors. In this paper we deem a country to be highly competitive if it has the right combination of institutions and policies, such as effective governance and an enabling business environment, and factors of production to achieve high levels of productivity. To understand why the region finds itself in its current state, and to assess the potential for catch-up, it is important to see where these countries stand across a range of indicators vis-à-vis its comparators in the European Union.

How competitive are the Western Balkans countries? The natural starting point to answer this question is the World Economic Forum's *Global Competitiveness Report* (GCR), a publication that bills itself as the "world's most comprehensive assessment of national competitiveness". But the GCR by no means captures all aspects of this concept. Other surveys and studies can complement the report by providing greater insights into specific aspects of the business environment and governance that hold back private sector development and deter investment.

This section of my thesis gives a comprehensive analysis regarding the competitiveness of each Western Balkan country in comparison to EU. The table below illustrates the 2015-16 GCR global rankings for each country (excluding Kosovo, for which data are not available), along with three benchmark comparators: the European Union, the EU-15 (the 15 member states prior to the 2004 expansion) and the EU-11 (the 11 countries in central Europe, the Baltic states and south-eastern Europe that joined in 2004 or later.

Rankings in Global Competitiveness Index 2015-16

		ALB	BIH	MKD	MNE	SRB	WB	EU-11	EU	EU-15
Basic requirements	1st pillar: Institutions	84	127	52	70	120	91	72	47	30
	2nd pillar: Infrastructure	88	103	78	73	75	83	52	33	18
	3rd pillar: Macroeconomic environment	118	98	47	79	125	93	47	59	66
	4th pillar: Health and primary education	52	48	76	33	62	54	45	30	20
Efficiency enhancers	5th pillar: Higher education and training	47	97	46	54	71	63	40	30	20
	6th pillar: Goods market efficiency	63	129	33	70	127	84	53	39	29
	7th pillar: Labour market efficiency	97	131	84	74	118	101	68	54	45
	8th pillar: Financial market development	118	113	52	44	120	89	56	53	48
	9th pillar: Technological readiness	89	79	63	55	51	67	37	26	16
	10th pillar: Market size	104	97	108	131	75	103	66	54	37
Innovation and sophistication factors	11th pillar: Business sophistication	95	125	72	102	132	105	63	39	19
	12th pillar: Innovation	118	115	58	69	113	95	58	37	20
Global Competitiveness Index		93	111	60	70	94	86	50	36	23

Source: World Economic Forum's Global Competitiveness Index Historical Database.

The graph illustrates the huge competitiveness gap between the Western Balkans region and the European Union. On average, the region is ranked 86th (ranging from FYROM in 60th to Bosnia and Herzegovina in 111th place), compared with an average 50th place for the EU-11 and 36th for the European Union as a whole. The gap is particularly large with respect to the EU-15, where the average ranking is 23rd.

The GCI is made up of three broad categories, which are divided into 12 pillars, and the rankings of the five Western Balkans countries by categories and pillars are also contained in Table 1. The rankings differ widely, both within and across countries. The region scores reasonably well on indicators associated with health and primary education, as well as higher education and training (except for on-the-job training), electricity and telephone infrastructure and information and communications technology (ICT) use. However, the most problematic areas are: efficient use of talent, that is, capacity to attract talent from abroad and retain talent, as confirmed by the brain drain problem; and reliance on informal (family and friend) relationships rather than on professional management. The second area dragging down the overall ranking is business sophistication. Despite the high heterogeneity, on average countries lack well-developed business clusters and are characterized by shallow value chains. Transport infrastructure ranks badly mostly due to the limited passenger-carrying capacity in airline traffic, but also because of the poor quality of overall infrastructure, including roads, railways and ports.

On the other side, the graph below, shows the 2007-08 GCR scores compared with the latest available (2015-16), suggests that there has been a gradual improvement in competitiveness since the pre-crisis years. In contrast, scores of the

EU countries have remained on average almost the same as before. The biggest jump in competitiveness is in FYR Macedonia, where the score has improved by 0.6 points (on the GCR's 1 to 7 scale) and now lies just behind the EU-11 average. Notable advances have also occurred in Albania and Montenegro, but less so in Bosnia and Herzegovina and Serbia. In an important sense, therefore, the Western Balkans economies are converging with EU comparators in terms of competitiveness.

Global Competitiveness Index, evolution of the scores

	2007-08		2015-16		Difference in scores
	Score	Rank	Score	Rank	
Albania	3.5	109	3.9	93	0.44
Bosnia and Herzegovina	3.6	106	3.7	111	0.15
FYR Macedonia	3.7	94	4.3	60	0.55
Montenegro	3.9	82	4.2	70	0.30
Serbia	3.8	91	3.9	94	0.10
WB	3.7	96	4.0	86	0.31
EU-11	4.4	48	4.4	50	0.05
EU	4.7	34	4.8	36	0.03
EU-15	5.1	21	5.1	23	0.01

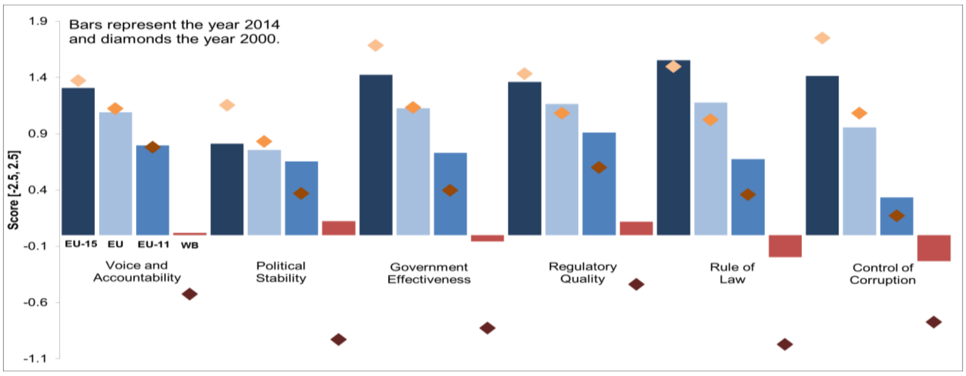
Source: World Economic Forum's Global Competitiveness Index.

The GCR scores are a useful starting point for investors who wish to get a sense of how competitive a country is. However, other cross-country surveys and reports can provide complementary perspectives and insights, especially when it comes to economic governance and the overall quality of the business environment. To shed further light on these two areas, we draw on three other surveys and reports: two from the World Bank (Governance Indicators and *Doing Business* scores) and the joint EBRD-World Bank *Business Environment and Enterprise Performance Survey* (BEEPS).

The World Bank's Governance Indicator scores are shown in the graph below. As with the GCR scores, there is some distance to go for Western Balkans countries to match EU standards. But again, a look at the scores over time suggests that the gap is, on average, narrowing steadily. The biggest increase over the past 15 years has been in political stability, which is an indication of the region's growing political maturity. However, due to a low starting point, on present trends it would take several decades before Western Balkans countries catch up with EU members in terms of governance. Still, this convergence is expected to speed up in the process of EU approximation[29].

[29] Scores range from -2.5 for weak governance performance to 2.5 for strong governance.

The Worldwide Governance Indicators, 2014



Source: The World Bank's Worldwide Governance Indicators database.

The World Bank's annual *Doing Business* scores provide further insight into the obstacles faced by enterprises in the region[30]. The latest rankings on overall ease of doing business vary widely, from 12th (FYR Macedonia) to 97th (Albania) out of 189 countries. The width of this range exaggerates the differences among countries of the region. The rankings therefore need to be interpreted cautiously: few would argue that it is really easier to do business in FYROM than in Canada or Germany, for example, despite their relative positions in the overall scores. However, as with other indicators considered here, the sub-components and their trends over time can be more revealing. Common problems across the region include: dealing with construction permits (Albania ranks in last place globally on this measure)[31] getting electricity; and paying taxes, despite recent improvements in some cases. On the other hand, all countries made notable progress in ease of starting a business, registering property and trading across borders.

To gain further insight into the obstacles, as perceived by businesses, we turn lastly to the EBRD-World Bank *Business Environment and Enterprise Performance Survey* (BEEPS). The BEEPS, carried out every three to four years since the first round in 1999, is a face-to-face survey of top managers that looks at various aspects of the business environment through both quantitative and qualitative questions. One of the parts of the survey is an opinion-based question that asks respondents to grade areas according to their perception of how severe an obstacle is. The responses range from "not an obstacle", which can be scored at 0, to "a very severe obstacle", scored 4.

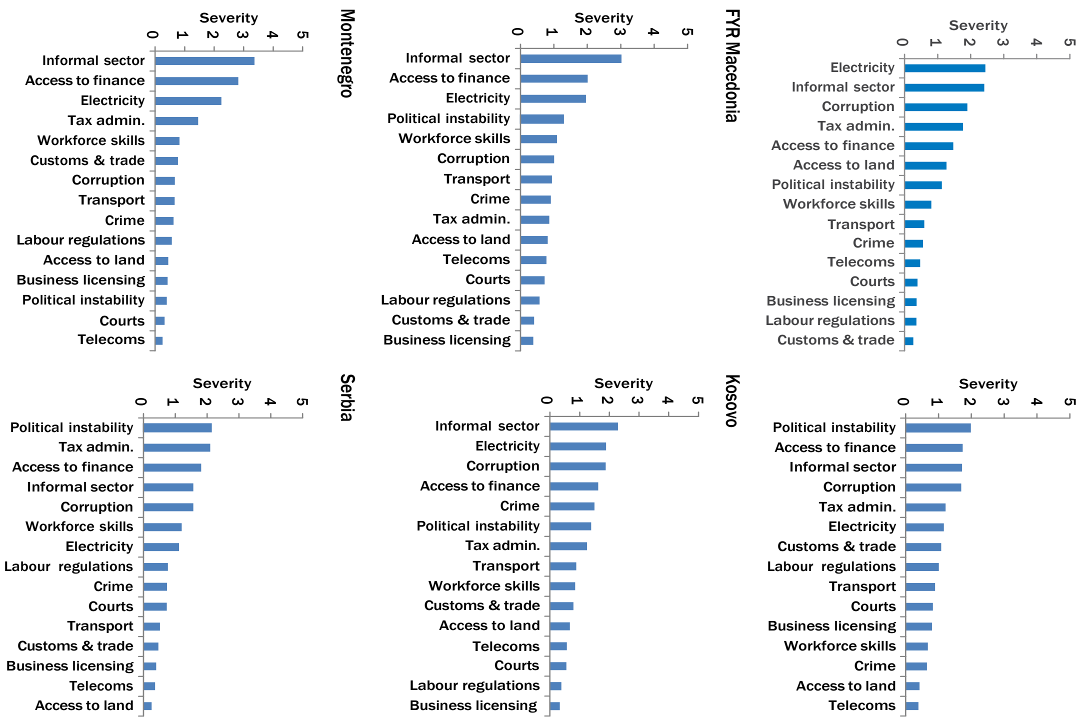
The graph below highlights the main obstacles, ranked by severity, for a hypothetical "average" firm in each country. In virtually all countries, competition from the informal sector stands out as a key constraint. This is a long-standing problem in the region and efforts to address it have been sporadic at best. The

[30] All scores are available at: www.doingbusiness.org.

[31] Albania's overall ease of doing business ranking was downgraded by 35 places to 97th. This was almost entirely because the country's position in the category relating to construction permits dropped, caused by the government's decision to suspend the issuing of construction permits during the territorial reform process until urban plans are in place.

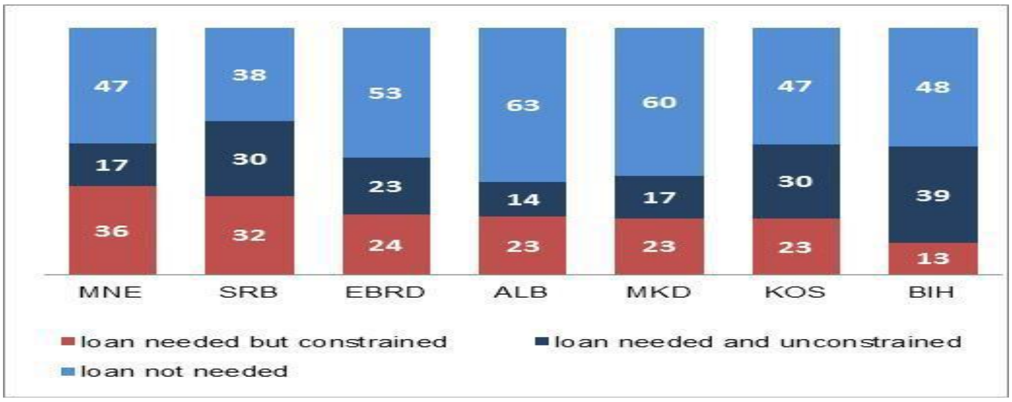
Albanian government's recent initiative to tackle the problem is welcome and may yield concrete results. Having reliable access to electricity is also identified by many businesses in Albania and Kosovo as a major obstacle, consistent with the analysis of the World Bank's *Doing Business* report.

Access to finance is another major obstacle to doing business, according to many respondents to the BEEPS. A quarter of all surveyed firms across the EBRD region described themselves as credit-constrained, meaning that they need a loan but are either rejected when they apply for a bank loan or feel discouraged from applying, something that illustrated in the graph called 'Share of credit-constrained share' . In the Western Balkans, this share is highest in Montenegro, where more than one-third of all surveyed firms feel credit-constrained, and lowest in Bosnia and Herzegovina (13%). In addition, overall demand for bank credit has decreased significantly in the post-crisis period. The percentage of interviewed firms that needed additional bank credit (including both the "credit-unconstrained" and "credit-constrained") declined from 61% in 2008-09 to 47% in 2013-14 across the EBRD region. The decline was even higher in the Western Balkans; from 15% points in Serbia to 20-25% points in the rest of the region. This is not surprising because, in the presence of slow economic growth, fewer firms needed loans to expand their production capacity and this has been only partially offset by increased demand for working capital on the part of firms negatively affected by the financial crisis.



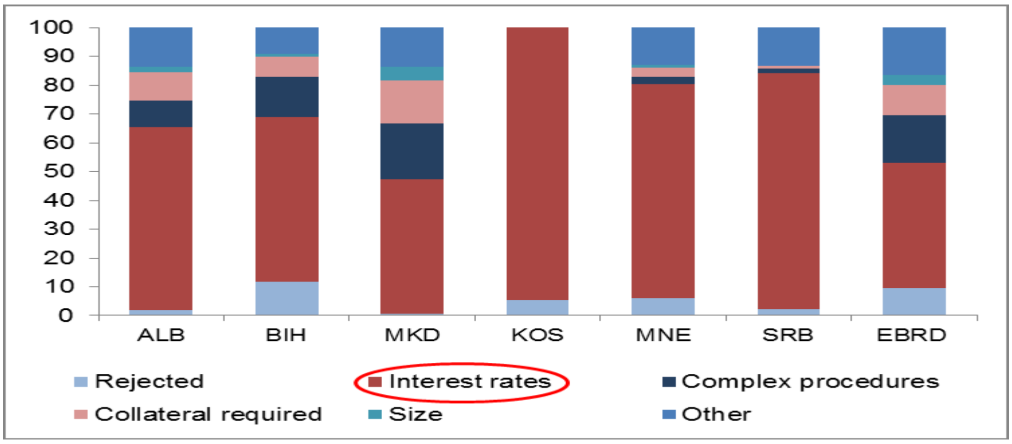
Source: EBRD-World Bank BEEPS V, 2013.

. Share of credit-constrained firms



Source: EBRD-World Bank BEEPS V, 2013

Reasons why firms are credit-constrained



Source: EBRD-World Bank BEEPS V, 2013

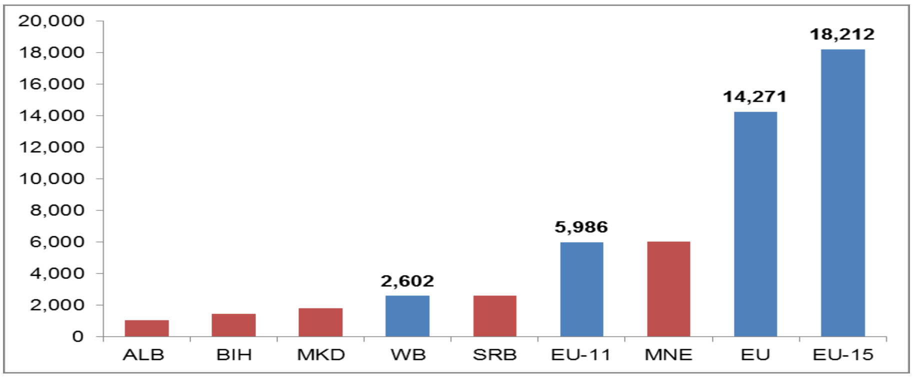
But what is driving these constraints? The graph above illustrates additional insights. Overwhelmingly in the Western Balkans region the main driver is the discouraging level of interest rates. Despite the high number of banks in the region, competition among lenders appears to be limited and small and medium-sized enterprises (SMEs) in particular struggle to get the funds they need to grow their businesses. Other reasons that discourage firms from applying for bank credit include: complex procedures, collateral requirements and size of the loan.

To conclude this section, it is fair to say that the Western Balkans region lies behind western European comparators in terms of competitiveness, governance and ease of doing business. But there are plenty of reasons to be optimistic about future trends. In particular, institutions and governance standards are being slowly but steadily improved, especially in the EU candidate countries.

1.3 FDI in Western Balkans

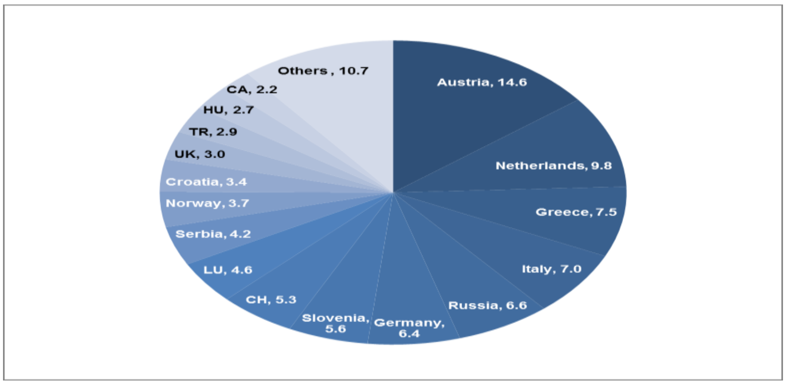
One of the most visible impacts of the global crisis in the Western Balkans has been the sharp drop in FDI to the region followed by a stagnating trend. While Serbia is the biggest recipient of FDI in aggregate terms, Montenegro received the biggest share of foreign capital in each of the last seven years in per capita terms. Still, the region lags significantly behind the European Union in terms of FDI stock per capita received; average FDI stock per capita in the Western Balkans is around €2,600 while in the European Union it is around €14,300, more than five times higher as the graph illustrates below. Even compared with the EU-11 average, the region's average FDI stock per capita is less than half. The catch up potential is obvious.

FDI stock per capita (€), 2014



Source: IMF World Economic Outlook.

Biggest FDI stock owners in Western Balkans (%), 2014



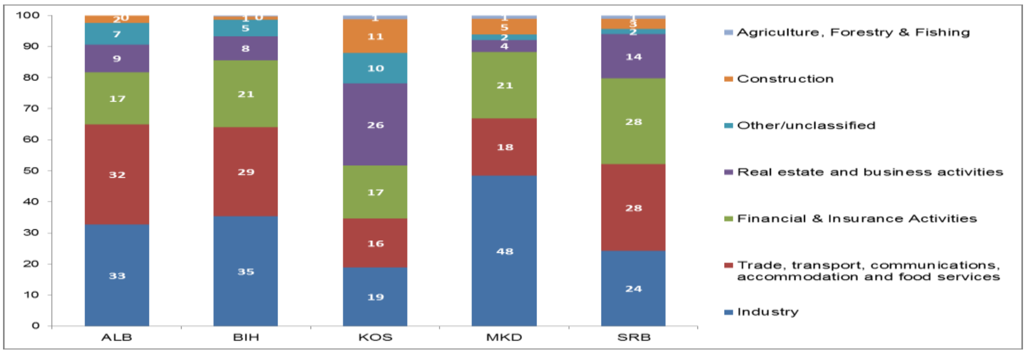
Source: EBRD 2013

The above graph delineates the main sources, by country, of the stock of FDI to the region. Traditionally, the most important investors have been the EZ countries, including Austria, followed by the Netherlands, Greece and Italy. However, an examination of FDI into individual countries of the region reveals important differences. Greece holds 26 % of FDI stock in Albania, Austria is the top investor in Bosnia and Herzegovina and Serbia (21 and 17 % respectively), Turkey is the biggest investor in Kosovo (10%)[32], the Netherlands has 22% in FYROM, while Russia holds 17 % of the stock in Montenegro.

Intra-regional FDI is limited, although Serbia is an important player in Bosnia and Herzegovina (second biggest investor) and in Montenegro (sixth biggest). Slovenian and Croatian investors are relatively active in the region; the former country is among top 15 FDI sources in all of the Western Balkan countries, while Croatia has invested notable capital in three countries of the region (Bosnia and Herzegovina, FYROM and Serbia).

Western Balkans countries have a fairly diversified structure of FDI stock per activity as the graph below illustrates[33]. The highest shares are in transport, storage and communication (Albania and Serbia), manufacturing as a part of industry (Bosnia and Herzegovina and FYROM), financial intermediation (Serbia, Bosnia and Herzegovina and FYROM) and real estate, renting and business activities (Kosovo). Some countries, notably Albania, have attracted FDI into natural resources. Much of the FDI in all countries has happened in the context of privatizations in sectors intended primarily for domestic consumption, such as financial services and telecommunications. As this source has largely dried up, countries in the region are focusing more on attracting FDI in tradeable sectors, which contribute to export capacity rather than domestic consumption.

FDI stocks per activity, 2014



What can the region do to attract higher levels of FDI? For starters a good solution is to offer fiscal incentives to investors. In the Western Balkans these are usually part of a broader package of investment incentives of each country, which are usually administered through national investment promotion agencies. Common

---

[32] The sources of FDI into Kosovo are somewhat unclear as more than 40% of the stock is attributed to an “not specific” source.

[33] Activity is classified as follows: Agriculture, forestry and fishing; Industry (mining and quarrying; Manufacturing; Electricity, gas, steam and air conditioning, water supply and disposal); Construction; Trade, transport, communications, accommodation and food services (Wholesale and retail trade; Motor vehicles repair; Transport, storage and communications; Accommodation and food services); Financial and insurance activities; Real estate and business.

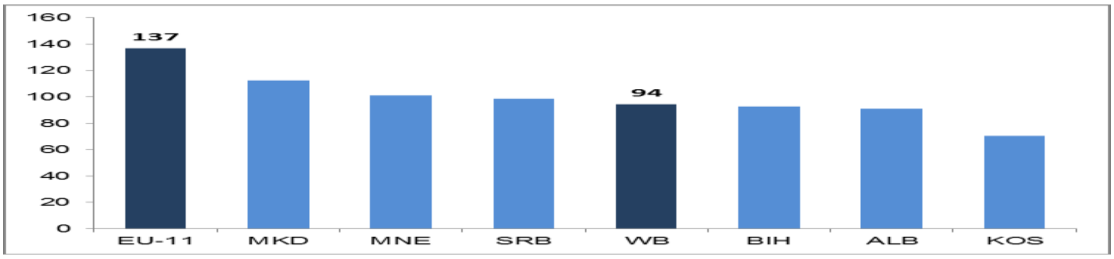
fiscal incentives include tax holidays, with either tax exemptions or reductions under some conditions, concerning corporate income tax, VAT or import/export duties, and tax loss carry forward exemptions. All of these countries have set up economic zones, business parks, trade zones and other similar concepts, which offer tax exemptions as one of the benefits, though not all of them are fully functional yet.

1.4 Trade in Western Balkans

All countries in the Western Balkans realise that sustainable growth must be built on an improved export performance, rather than on cheap and plentiful supplies of foreign capital and credit, much of which has gone into non-export-oriented sectors. But how realistic is it to expect enhanced trade and export activity in the region in the coming years? In order to answer this question it is important to understand that these countries currently trade less than one would expect when one takes into account size, level of development and geographical location.

To clarify this point, the graph below reveals the level of trade openness, measured as the sum of exports and imports divided by GDP, for each country and the region as a whole against the EU-11 comparator. In broad terms, the degree of openness recovered somewhat after the dip in 2009 at the height of the crisis, and it appears to have stabilized at close to or below pre-crisis levels. But the region lags behind central European and Baltic comparators on openness, perhaps unsurprisingly given that the latter region has been part of the European Union's large internal market for over a decade. The chart shows that the Western Balkans average trade openness is at 70% of the EU-11 one. Furthermore, the impact of net trade flows on GDP growth rates has generally been negative, as these countries have run persistent trade deficits. Reversing this trend is a key goal of all countries in the region.

Trade openness in 2014

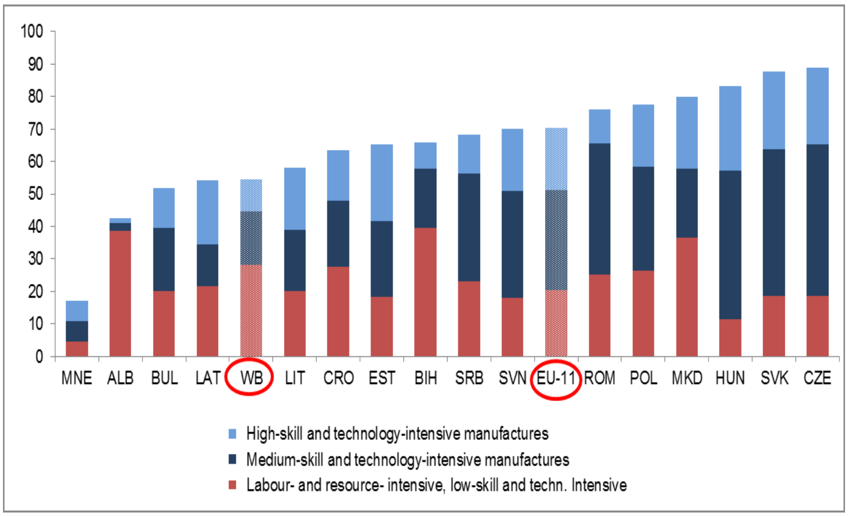


Source: the IMF's World Economic Outlook

Why is trade below potential? One reason is that it is a legacy of the break-up of Yugoslavia and conflicts in the region in the 1990s, and the many years of neglect and under-investment in infrastructure. But there are other related reasons associated with the product mix, inadequate inclusion in the European Union and global value chains and the obstacles faced by exporters.

Firstly, the average share of manufactured goods in total exports is much lower in the Western Balkans than in the EU-11 (55% versus 71%). However, this varies widely across the countries as the graph below illustrates, from only 20% in Montenegro to around 80% in FYR Macedonia (the latter due to the strong pro-FDI policies of the country in the previous years, mostly in tradeable sectors such as car components). This reflects the fact that the region is not well integrated into the European supply chains, as confirmed by a recent study by the OECD[34]. The results indicate that the Western Balkans is integrated mostly into the final stages of international supply chains in food, beverages and tobacco in addition to textiles and clothing, and mostly the intermediate stages of wood and cork, paper, printing and publishing, other non-metallic mineral products and fabricated metal products, as well as both first and intermediate stages of basic metals.

Manufactured goods by the technology level, % of total exports of goods, 2014



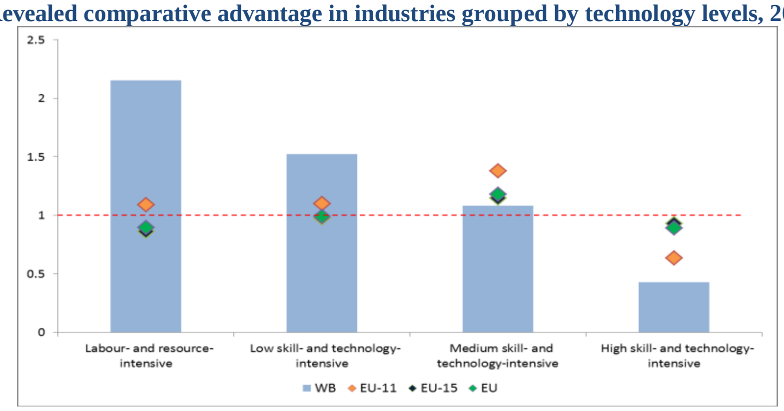
Source: UNCTAD's International trade database.

Not only is the role of manufactured goods on average smaller in the Western Balkans than in the EU-11, but the manufactured goods exported are also less sophisticated (as shown in Chart 19). Over 50 per cent of the region's manufactured goods are classified as "labor and resource intensive" or "low-skill and tech intensive", in comparison to about 30 per cent in the European Union. However, only 18 per cent fall into the category "high-skill and tech-intensive goods" in comparison to 27 per cent in the EU-11. Another way of seeing the Western Balkans region's dependency on labor-intensive goods is to look at the breakdown of revealed comparative advantage (RCA) by industries. The graph below illustrates that this region has developed a relative export specialization in industries that are labor- and resource-intensive and low skill- and technology- intensive. In contrast;

[34] See the OECD Trade in Intermediate Goods and International Supply Chains in CEFTA, 2013.

EU countries have the highest revealed comparative advantage in medium skill- and technology-intensive industries, and are above the Western Balkans in terms of high skill- and technology-intensive industries. A more detailed analysis by specific industries shows that the strong comparative advantages in the region are in industries such as beverages and tobacco, food, clothes and raw materials

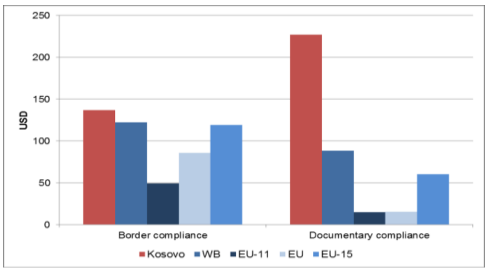
Revealed comparative advantage in industries grouped by technology levels, 2014



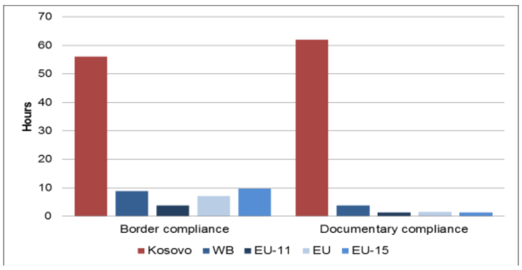
Source:UNCTAD’s International trade database

Secondly, exports in the Western Balkans typically face bigger obstacles to doing business than those in comparator countries. To see this, we can use once again the World Bank’s Doing Business report as the two graphs illustrate below. The main difference between this region and the EU-11 lies in the cost to export; with costs in the Western Balkans countries more than double that in the EU-11. Time to export is also longer although the differences are less pronounced. Any improvement over time on these measures has been slow.

Cost to export, 2015



Time to export, 2015



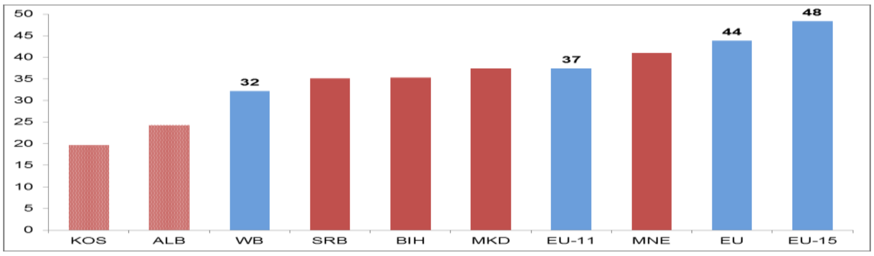
Source: *Doing Business*, The World Bank

1.5 Attracting investors

In this section of my thesis we are going to examine what Westerns Balkans can do or already have in their arsenal in order to attract external investors. I am presenting a couple of reasons below.

I am starting with one big advantage that Western Balkans have: the low labor cost combined with a well educated population. The graph below illustrates that all Western Balkans countries have lower labor cost in comparison to the EU average.

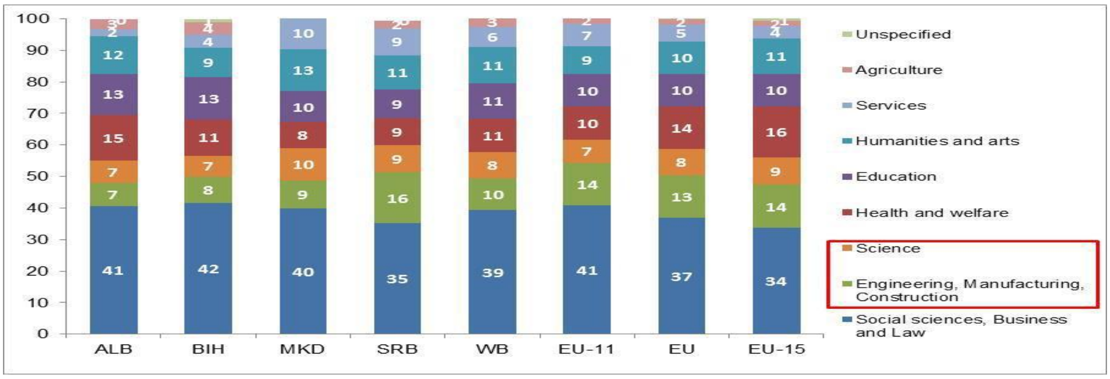
Unit labour costs, 2014



Source: Eurostat report, 2014

The advantage of low labor cost taking even more important role when it is combined with the education level of the population. Unesco's Education Database[35] shows that in Western Balkans those who had attending or currently attending tertiary education are approximately half of the EU average. However, the number of those who had taken a technology-science education, which is important in order to develop new technologies, is lower compared to EU average. This is not the case for Serbia though, which has approximately double students in this domain compared to other countries in the region.

Composition of tertiary education, 2014



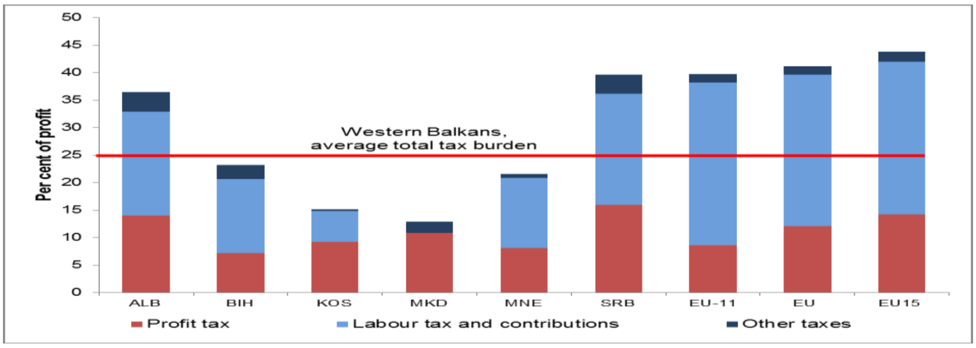
Source: UNESCO's Education database.

Another advantage which exists in all the countries of the region is the taxation system. Western Balkans have favorable taxes for those who interested in

[35] UNESCO: Education database, 2015

investing. The majority of the countries in the region had made huge progress in transforming their taxation system in order to be compatible with the international standards. During the past decade Western Balkans made efforts in order to keep stable the taxation system, to drop all obstacles in submitting taxes and widening the tax base. The total tax burden is obviously lower than the EU average. This is the result of lower tax profit smaller labor tax burden. As a matter of fact FYROM has one of the lowest tax burdens in the world, simply because there are no labor taxes. On the other hand Serbia and Albania have tax profits close to EU average which is around 40%.

Total tax burden in % of profit, 2015



Source: The World Bank's Doing Business database.

Last but not least, the geostrategic position of Western Balkans which is providing easy accessibility to EU advanced economies and markets. The favorable position of the region comes to boost the trade agreements that each country has already agree with the EU economies, something that gives an unimaginable opportunity to a potential investor. It is not given the name 'Getaway to Europe' randomly. The location of the region, which is lay between West and East justify this 'nickname'. Global superpower such as China they have seen huge potential in the region and they want to connect Europe and the Greek port of Piraeus, which has been taken by Cosco Pacific in a 35-years concession in order to transform the port in one of the biggest top containers port in Europe, through Balkans. The Balkan Silk Road will be based on the existing railway system and in the new train network that China develops in the region through subsides to each country government.[36]

Chapter 3

1. The case of Serbia

This section of my thesis will examine the development that has happened in Serbia after the collapse of the Soviet Union and the liberation of the economy. Will shed light in the reforms that took and taking place in Serbia in order to boost up the

[36] Wouter Zweers Vladimir Shopov Frans-Paul van der Putten Mirela Petkova Maarten Lemstra, Netherlands Institute of International Relations, 2020. China and EU in the Western Balkans. A zero-sum Game?

economy and transform it into a liberal economy which brings prosperity on its people.

Serbia's growth rates continuing to go up but still the standards of living are not approaching the average of the EU. Serbia's growth rate at the moment is 3% annually, and it seems that the country has already reached its peak[37]. In order for Serbia to reach the EU economical standards must implement a new agenda of financial growth which includes boosting investments in the country, building skilled workforce, financing growth, removing competition barriers, provide government expenditures for growth. Things that will be examined.

As a general picture Serbia has great potential to develop further the private sector which is the crucial for the economic convergence with EU. In Serbia the private sector has the 70% of the country's employment. Nevertheless, its profitability is way lower than the other Western and Eastern Balkans counterparts[38]. It is generally accepted that private sector is the most important index in boosting growth, which is why Serbia should focus on improving governance and enhancing more efficient practices of employment. Another 'bleed' of the Serbian economy is the State Owned Enterprises. These enterprises despite they are in crucial pillars of the economy which can bring a lot of capital flow are not the most appealing for investments[39]. Additionally, these companies can be proved very helpful to the private sector if operating efficiently. The reason of that is very simple: if these enterprises work more efficient will start generating income and will be re-invested in the form of subsidy in various sectors (education, health, etc) which supporting the private sector.

Fall of Soviet Union has leaded Serbia-along with other socialist states-into crumbles. Changes in laws have been made in order to democratize the new-formed state. Privatization of the state owned companies started, and an unprecedented restructure happened in the economy. Along with these Serbia improve its relations with the EU and searching access in the EU advanced markets. We must not forget that Yugoslavia was the only socialist state which was close to grand EEC (in the 70's) membership.

1.1 Boosting investments

As is the level of investment in Serbia it is impossible to sustain long term growth. Serbia's public investment is approximately one third lower than the CEE counterparts. It is worth mentioning that, if Serbia had started investing as much as these countries, now its GDP would have been 25% higher that it currently is. Still Serbia spends around 5% of its own budget to subsides, mostly to support inefficient state owned enterprises. Reducing inefficient spending and at the same time

[37] EBRD Report, 2018

[38] Peter Tabak and Sanja Borkovic, Serbia Diagnostics Assessing Progress and Challenges in Developing a Sustainable Market Economy, EBRD, 2018.

[39] These companies related more with the public gods (water, electricity, railway, public transportation)

increasing public investment would have an enormous positive impact on the rise of GDP. In order to transform public spending to more growth- directed, must maintain low fiscal deficit by keeping recurrent spending in a low level. The government must focus on projects that will give a positive boost to private sector. These kind of spending should be allocated to infrastructure, water, energy, transportation.

Source: Serbia Statistic Office

1.2 Labour market

Serbia. the past decade implementing reforms that boost job creation and in extense rise of employment. Serbia creating approximately 60.000 jobs per year, contributing in the drop of unemployment from 20% in 2014 to 13% 2019, which is among the lowest in the region40. It is a fact that the economy has the possibility to grow faster if more people find employment. Nevertheless, Serbia has more than a third of its working age population (15-65) that does not participating in the labour force; 60% of those are employed. A percentage which is 10% lower that the EU average. This has a serious impact in the economic growth. A male person that does not work means that Serbia loses 20 years of his productive lifetime and 25 for females. If females could work as much as male do, the income of its population could increase by 16, 2%[41]. If the 50 percent employment gap, as well as the gap in earnings, between the country's Roma minority and the general population in Serbia were closed, the total gains could be from 0.9 to 3.5 percent of GDP[42].

To increase job creation, in order for employees to match better to firma, a more skillful plethora of workers would help. Serbia has already taken significant initiatives to change its work regulations and make its labour market more flexible in 2014-2015[43]. Additionally, reforms in labour market can bring an extra 0.1% in growth. Particularly, a more progressive income tax for employees with children and

[40] EBRD Report, 2019

[41] Cuberes and Teigner 2015 [2010 data]. "How Costly Are Labor Gender Gaps? Estimates for the Balkans and Turkey", World Bank Policy Research Working Paper 7319

[42] World Bank, 2015. "Roma in Serbia, A Generation of Opportunities: The Economic and Fiscal Benefits of Roma Inclusion in the Western Balkans." Background paper, World Bank, Washington, DC

[43] Reforms made labor regulations more flexible in many areas, including for example contracts, working arrangements, and employment termination. As a result, Serbia' employment protection legislation (EPL index) is generally in line with OECD countries.

subsidies through the social security system for the low-waged employees will encourage them to move into the formal sector.[44] Serbia can also boost job matching by monitoring these labour market policies, better skilled workers would be more productive and if the educational system produce workers that match modern labour market criteria, growth it is inevitable to increase[45].

To develop new applicable to modern labour market skills, a radical change in the educational system is required. In order for Serbia to deliver quality learning and demands that match skills that a modern economy needs, must modernize the curriculum. In a sense, connection of education with labour demands it is all that Serbia needs.

1.3 Release competition

Competition can boost productivity and as a result growth. That is because competition gives incentives for innovation and uses capital and workforce in the most productive way. Serbia, unfortunately, is among the countries with the most restrictive regulations to competition.46 That led to Serbia to change its regulations regarding competition fundamentally. A Competition Law was introduced in 2005, creating the Commission for Protection of Competition. The applicability of competition laws focused more in private firms and just recently started implemented in state owned enterprises. Additionally, in that effort Serbia has developed antitrust institutions which their appearance coincided with privatizations and corporatization of state owned enterprises. Despite a series of successful reforms, state ownership remains wide-spread and distortive along the value chains. Since the 1990s, Serbia has privatized or resolved over 2,000 state-owned companies. With about 600 enterprises remaining in the hands of the state, ownership by the state is still more widespread than in most countries covered by widely used indicators on competition in product markets. State-controlled companies operated in many sectors where private operations are most viable[47]. For example, SOEs were present in light manufacturing industries such as furniture, cables, and car parts. SOEs were also present in some network sectors, which are private in the majority of EU member states (such as mobile services). This presence often distorts prices and supply along the value chains, reducing exports and productivity growth in connected sectors. SOE governance reforms have not been completed.

---

[44]Informal employment represents about 20 percent of Serbia's total employment.

[45]For example, one area where the available workforce skills provide opportunities for the private sector is the ICT sector. Serbia ranks among the top 5 countries worldwide in ICT talent on the Startup Genome list.

[46]Drozd and Sipka (2019) "Removing Regulatory Barriers to Competition", background paper for this report. OECD PMR database and OECD-World Bank Group PMR database.

[47] Source: Wood and Furniture Industry Performance and Value Chain Analysis, CEVES and Chamber of Commerce, 2017; Note on Competitiveness and Jobs in Serbia's Wood and Wooden Furniture Sector, World Bank, 2017.

State aid is excessive and misallocated for the benefit of unproductive SOEs. State aid amounted to 6.4 % of general government expenditures and 2.2% of GDP in 2017, four and three times higher than the EU average, respectively. Some aid is not reported or reviewed in line with the State Aid Control Law. Between 2014 and 2017, SOEs accounted for 60% of state subsidies even though they generated 19% of value added during this time. A significant portion of these subsidies were given to cover operating losses of unproductive SOEs[48].

Drastically reducing state aid and improving control and measurement of impact would improve its growth impact. Reducing state aid to the level of EU countries would free up 1.5% of GDP for more productive use. It would also increase competition by leveling the playing field between state-owned and private companies. While direct support to firms is not recommended, the state should intervene when there are market failures (such as unequal access to finance). These firms could also benefit from horizontal policies that encourage innovation, combined with actions to reduce disproportionately high administrative burden on start-ups. Strategic changes would also be needed in how the state supports SMEs. In addition, while it has served well and helped create more jobs, the FDI attraction strategy could be re-focused on attracting better and more productive firms in sectors with high potential spillovers to the domestic economy.

Reforms that foster competition can have a significant impact on growth. In Australia, the implementation of the National Competition Policy increased GDP by at least 2.5% between 1992 and 1999[49]. In Ukraine, eliminating restrictions to competition in the services sector led to an increase of 3.6% in total factor productivity in the manufacturing sector[50]. In Serbia, leveling the playing field between SOEs and private firms would yield the most benefits. These changes would include a drastic cut in state aid, strengthening state aid control, privatizing or corporatizing the remaining SOEs, and insulating the rulemaking process from capture through wider stakeholder consultations and stronger impact assessment. Ongoing market reforms in network sectors, primarily energy, transport and telecom, and lower barriers in professional services could complement these changes and reduce input costs for firms. Finally, stronger enforcement of competition rules, particularly more efforts to detect cartels and anti- competitive agreements, would also help to limit overcharges.

[48]According to BRA, four out of top five loss-makers in 2018 are SOEs: the power generation company EPS, the natural gas supplier Srbijagas, Railways company, and furniture maker Simpo. See Business Registry Agency (2019) Annual Report on Performance of Businesses in the Economy.

[49]The Australian government implemented a broad range of economy-wide (e.g., corporatizing SOEs, changes in antitrust regulations) and sector-specific reforms (e.g., unbundling in electricity, tradeable water allocations). The estimate of 2.5 per cent is conservative and reflects productivity and price changes in key infrastructure sectors in the 1990s. Australian Productivity Commission. 2005. Review of National Competition Policy Reforms. Canberra.

[50]Shepotylo, O. and A. Vakhitov, "Services liberalization and productivity of manufacturing firms: Evidence from Ukraine," Policy Research Working Paper 5944, World Bank, 2012.

1.4 Improving business environment

Excessive or inefficient regulatory barriers and complicated procedures can limit new firm entry, investment, and job creation. In turn, this negatively affects productivity and competitiveness of firms. Such barriers can include high regulatory and administrative costs, as well as discretion in the implementation of business regulations. They can distort the playing field by giving unfair advantages to specific firms or creating an uncertain business environment. A regulatory environment that is most conducive to growth would be more streamlined, transparent and consistent, with an even playing field for all firms.

Serbia has been successful in reducing the time and cost of doing business. Given that excessive or inefficient regulatory barriers and complicated procedures can limit new firm entry, growth, innovation, and job creation, this is no small success. Serbia ranks 44th globally in the World Bank's Doing Business 2020 report, up from 93rd in 2013. Over the last six years, Serbia closed most of the gap with the other 7STEEs[51]. An example of Serbia's remarkable ability to reform is the streamlining of construction permitting. In five years, Serbia moved from the bottom five countries to the top ten globally by halving the time and reducing its cost by over 90%. However, Serbia has not addressed deep- seated structural and institutional issues with its business environment. For example, Serbia performs poorly on voice and accountability, rule of law and control of corruption[52]. On all these indicators, Serbia ranks significantly lower than the 7STEEs, and in fact on voice and accountability and control of corruption, Serbia has been backtracking over the last five years. Related to this, it performs less well than on other Doing Business scores such as on Enforcing Contracts, with a distance-to-frontier score of 63.1. Other areas that are lagging are registering property rights and simplifying/ digitalizing government services[53]. In all these areas, faster progress on EU accession would help Serbia upgrade its legislation and institutional environment, automatically helping businesses

There are opportunities for improvement through all the stages of regulatory processes. Businesses and international partners most often cite issues with predictability, as well as consistency of implementation[54]. Strengthening public consultation processes could help address issues with predictability. Laws are often

---

[51]Source : World Governance Indicators

[52] Source : World Governance Indicators

[53]For example, over 1.5 million structures have not been legalized, even though the necessary legal framework is in place. Similarly, the conversion of land use titles into ownership rights is moving slowly. As part of the e-Paper initiative, about 2,500 administrative procedures have been identified, and the Government plans to simplify/digitize 70 per cent of these procedures, but this process has not yet been completed.

[54] For example, the EU Progress Report from March 2019 in the section on Economic Governance notes: "The efficiency and predictability of the institutional environment is not yet ensured and does not sufficiently support long-term growth." FIC White Book for 2018 notes as one of the six priority areas in the previous year: "Improvement and a more consistent implementation of tax laws, including prevention of new para-fiscal charges."

adopted using expedited procedures, without proper public consultations.[55] Also, regulatory impact assessment mechanisms exist, however their actual use in informing legislative changes is limited and their quality could be improved, including with regards to how it will impact SMEs.[56] Some of these weaknesses have been recognized and the recently adopted Law on Planning System is aiming to introduce much more robust and clearer procedures of adopting and amending legislation. In addition, establishment of the public register of para-fiscal charges to eliminate double charges, and those by municipal utilities; another update to the labor legislation, to accommodate "mini" and part time jobs; and final clarity on lingering property ownership issues, would also help.

Wider use of digital and e-governance platforms could help when it comes to consistency of implementation. The latest Doing Business report notes that the economies that score the highest have different characteristics, but all feature widespread use of electronic systems and online platforms to comply with regulatory requirements. The Serbian government is making important steps in this regard, including through the e-Paper initiative. About 2,500 different administrative procedures have been identified, and 1,750 will be simplified, with a subset of these being digitized and moved on-line.

Some issues of existing law, both implementation and form, remain. For example, important amendments to the Law on Legalization of Properties were adopted in 2018. However, its implementation is hampered by a large backlog of over 1.5 million structures. Among other things, this prevents expansion of these assets (e.g. industrial plants and infrastructure). Similarly, Law on Land Conversion (from land use to land ownership rights) was adopted in 2016. Yet for most of the companies bought through privatization or bankruptcy, conversion is moving slowly. This delay prevents the productive use of significant assets. The Foreign Exchange Law, a complex provision with 33 by- laws, requires significant streamlining, which would make it easier to do business for MSMEs, as well as encourage investment in Serbia and from Serbia to other countries[57].

Curbing state barriers to business lets firms operate more freely, but it doesn't make them compete. Pro-competition reforms are complementary to reforms that cut red tape. They share the objective of reducing barriers to entry and other regulatory burdens. At the same time, pro-competition reforms address also

[55]The EU Progress Report from March 2019, section on Functioning of product markets: "Business-related laws continue to be adopted under urgent procedure without the necessary consultation of interested groups, reducing predictability and quality of legislation."

[56]The EU Progress Report from 2019 notes: "The regulatory impact assessment and the SME test need to be systematically performed when formulating laws and secondary legislation. In general, businesses need to be better informed about regulatory changes and be actively invited to provide input in the process leading up to this regulation."

[57]Recently a broad coalition of private sector organizations (including Chamber of Commerce, Foreign Investors Council, National Alliance for Local Development, American Chamber of Commerce and others) has been making a strong case that this law is a major impediment to business operations and needs to be replaced with a new law.

other types of government interventions, such as state aid or access to essential infrastructure, as well as privately imposed barriers to competition. Pro- competition reforms tackle problems of an unlevel playing field between firms and the distortion of markets.

1.5 Serbia's future in EU

In this third section, which is dedicated to the analysis of the possible ways in which the European Union might transform after Brexit and the many crises and challenges of the last decade, remarks are given concerning internal relations within the European Union (EU), the EU's position on the global stage and the power/embeddedness/vulnerability of the European system of values. Regarding all three aspects, the authors try to understand how the identified changes and revisions are reflected in the EU's enlargement policy and in its relations with the Western Balkans. It tries to answer the question of how the changes that occur on the European scene affect the position and prospects of the region, which for the first time in history is united by its joint aspiration to integrate with the EU environment. As the migrant crisis has shown, although the region is not on the external borders of the EU or in its back or front yard, it is still a largely disorganized inner yard.

This section represent a view from Serbia where different strategic options and different views on these issues intersect, which affect the character, depth and pace of the reform process and its true commitment to European integration. All will agree that the region has lost a lot of time and enthusiasm in the process of EU accession, and that after solemn promises of a certain European perspective made at the Thessaloniki EU Summit - WB, 2003, the expectations of most countries in the region (except for Croatia) concerning membership of the EU in the near future have not been met. The joint stabilisation and accession process, which was designed as a mechanism to integrate the region into the EU, did not have the adequate strength and pace to sufficiently accelerate the consolidation of the post-conflict regions and assist in their essential long-term stabilization, as recent tensions in the region show. However, it is about a policy which when all is weighed up it must be assessed as successful, because no matter how distant, the prospect of EU membership was the anchor of all the positive changes in the region.

In a number of areas the region has already integrated or is rapidly integrating into the EU - trade, investment, energy, transport, telecommunications, research and development, as well as police cooperation, the protection of European borders, etc. In some areas the process is underway and in others, in the early stages. The high degree of economic integration is just one of the causes of the economic crisis spill over from the EU to the Western Balkans. Following an initial recovery in the past decade, the region has entered a phase of recession and stagnation, which has resulted in the region continuing to lag behind, high unemployment, corruption and organized crime, as well as deterioration in the political climate in the region. In addition, in the absence of stronger involvement of the EU and its Member States, the door has been opened for many new actors

(Russia, China, Turkey, Saudi Arabia, etc.), who in the last decade have taken up considerable economic and political space in the region.

And then there was Brexit, another blow that triggered essential revision of the very foundations of European integration. Some believe that the departure of the United Kingdom will lead to the consolidation of the EU through new and inevitable reforms. If the forecasts prove to be true that the EU will reconstitute in several concentric circles and that in the last circle, which will represent a common/single market, this time Great Britain will remain with Turkey and possibly the Western Balkans, and we will get a kind of "asymmetric federation" (a comparison with the possible options during the breakup of Yugoslavia), an asymmetry which Great Britain has always campaigned for. And it would not have to be the end 1 President of the Forum for International Relations of the European Movement in Serbia. The future of the EU and the Western Balkans - a view from Serbia of the EU. If we look at the current structure of participation in the Eurozone, the Euro-plus pact, the Agreement on Stability, coordination and governance in the Economic and Monetary Union, and the Schengen visa regime, it can be seen that an "a la carte" system already functions within the EU, which in some areas includes European countries that are not EU members.

Others believe that Brexit is the beginning of the end of the EU and an indication of a flood of nationalist and populist political forces which will put pressure on other countries to leave the Union (The Netherlands, Denmark, Sweden, Slovakia, and even France and Italy which are founder states). There are no mechanisms within the EU which can prevent this. The only obstacle to this would be an open debate about the serious economic and social issues within the EU which so far have been ignored, and this has invoked dissatisfaction on the left, as well as on the right which is far more powerful.

Finally, on a global scale, the EU is weaker with the exit of the UK. In the US, Democrats expressed sorrow, while conservatives satisfaction with the outcome. At first, Russia expected sanctions to be softened and better relations with the EU. Turkey immediately after Brexit restored relations with both Russia and Israel on the same day, while China and India reviewed planed investment in the UK and the fate of existing ones.

The process of "withdrawal" will last at least two years according to the procedure set out in the Treaty of Lisbon. So far, this is the first case of withdrawal from the EU. Britons are in no hurry and EU officials want a speedy process, however, there are those who are calling for sobriety and reflection. The first fear a "domino effect", while the second seek the best solution for both sides, which needs time and a cool head.

In the Western Balkans the consequences of Brexit are unclear, although it has caused satisfaction among Eurosceptics who are on the increase. New EU members are concerned and they remind us that the EU is the most important peace project in Europe, that Britain is a major financier of the net EU budget, and that for some of these countries it was an important factor in the establishment of security and stability and economic support in the post-war period. However, the United Kingdom is not an important trade, investment and technological partner of the Western Balkans. This is to some extent a mitigating factor. But so far it has been an important advocate of the enlargement policy and a counterbalance to the dominant role of Germany, not only in the Balkans.

EU officials argue that expansion will continue, but it has certainly fallen even lower on their list of priorities. The changes that will occur in the EU should be carefully monitored and every opportunity should be used for faster partial/functional/sectoral integration - so the regulation of the EU's relations with the United Kingdom could pave the way for countries that are not yet members. The Berlin process in a way anticipated this path. It would be good if the countries of the region succeeded in their fight for it to continue in coming years, as its discontinuance was announced. It was precisely Great Britain who was supposed to host the WB 6 summit in 2018, after Italy in 2017. However, this is not expected to happen as it will no longer be a member of the EU then. And even though regular summit meetings between the EU and the countries of the region, as envisaged in the Thessaloniki agenda, were not realised, the Berlin process has taken on an important communication role at the highest level, although with a limited number of EU Member States. That is why it is of practical and symbolic importance to political leaders and the general public in the region.

Conclusion

Welfare of the Western Balkans countries depends on the long-run and dynamic G.D.P. growth. Continuous and efficient investment is required to achieve high rates of economic growth. Therefore, external sources are used for faster development, whereby foreign investments are particularly significant. Official development assistance that W.B. countries receive from the developed countries should be taken into account. This kind of assistance mostly comes from the European Union. Given the European orientation of the region and high level of mutual economic relations, the subject matter of this paper covers the European Union investments and the Western Balkans development. The paper attempts to determine investment factors, analyze investments and E.U. official development assistance and to evaluate the intensity of the relation between the key development factors and investment inflows from the Union. Notable participation of the Union in the total assistance provided to the region indicates the interest of the member states and common institution to help W.B achieve a higher level of development. Investments analysis indicates the dominance of the E.U. participation in all countries of the Western Balkans. Besides that, according to the World Bank data, the Western Balkans countries were developing faster in the year 2016 than in 2015. Economic recovery can be explained by structural and other reforms carried out, whereby great credit belongs to the E.U. The labor markets also recorded positive changes, but unemployment remains high,22% in 2016.

Countries of the region have to intensify their reforms. This would attract both foreign and domestic investments, accelerate economic growth and revenues for households, reduce poverty and stabilize the public debt. Economic welfare would grow, macroeconomic stability would be established and the Western Balkans countries would be better resistant to new shocks and crises. While recognising the challenge of improving the overall efficiency of spending, this report emphasizes that, at this stage, the major part of investment could be realised only through the debt increase. Growth can be (and should be) effectively stimulated trough investment but the capacity to borrow should be increased by adapting the concept of fiscal space to the shared development vision agreed by the donors and the final beneficiaries for the region. It is more than ever important to support investment in infrastructure and SME lending. Otherwise, there is an important risk for the region to be stuck in the vicious cycle of low growth, weak private investment, high unemployment and high debt level.To adress this challenge, the role of development finance is crucial. It is the only way to finance long-term projects needed to redesign economic and social structure of the Balkan countries. Official support coordinated by the WBIF and the National Investment Committees (NICs), though insufficient to cover all the needs, represents a critical mass (some [16%] of the estimated public and private investment needs) that, if suitably planned and coordinated, could also influence choices on the other.

The Western Balkan countries are small open economies linked by trade. The report shows that coordinated action on autonomous demand via increasing simultaneously public investment in several or all the countries of a regionally integrated area is more effective than isolated action by a single country. Coordination of investment policy, as promoted under the Western Balkans Investment Framework, is thus beneficial. These benefits can be achieved particularly, by focusing investment on a network of regional investment projects which can be financed in all countries at the same time and contribute to improve supply conditions. One should also bear in mind the geopolitical importance for the EU to maintain its influence in the strategic Western Balkans region as other competitors (China, Russia, etc.) are already widely present by conducting active investment policy often contradictory with EU policies[58].

[58] Cf. for example, Poulain (2011) for the overlook of China's strategy in the region.

References

- Adarov, Amat, Vasily Astrov, Serkan Çiçek, et al. 2015. “A Time of Moderate Expectations”, wiiw Forecast Report No. Spring 2015, Vienna Institute for International Studies, March 2015.
- Allais, Maurice. 1962. “The Influence of the capital-output ratio on the real national income”, *Econometrica*, 1962, Vol. 30, Issue 4 (October), pp. 700 – 728.
- Andrés, Luis, Dan Biller, and Matias Herrera Dappe. 2014. “Infrastructure Gap in South Asia. Infrastructure Needs, Prioritization, and Financing,” Policy Research Working Paper 7032, The World Bank.
- Antiochou, Effie. 2011. “Medium Term Projections of Investment in the Western Balkans”, EIB Working Paper, Sept 2011, 43 p.
- Astrov, Vasily, Vladimir Gligorov, Doris Hanzl-Weiss, et al. 2012. “New Divide(s) in Europe?”, wiiw Current Analyses and Forecasts, No. 9, Vienna, March 2012.
- Ayyagari, Meghana, Thorsten Beck, Asli Demirguc-Kunt. 2003. “Small and Medium Enterprises across the Globe: A New Database”, World Bank WPS 3127.
- Afonso, Antonio, Luca Agnello, and Davide Furceri. 2010. “Fiscal Policy Responsiveness, Persistence and Discretion.” *Public Choice* 145 (3): 503–30.
- Aghion, Philippe, Peter Howitt, and David Mayer-Foulkes. 2005. “The Effect of Financial Development on Convergence: Theory and Evidence.” *The Quarterly Journal of Economics* (February): 173–222.
- Agnello, Luca, Davide Furceri, and Ricardo M. Sousa. 2013. “How Best to Measure Discretionary Fiscal Policy? Assessing its Impact on Private Spending.” *Economic Modelling* 34: 15–24.
- Bakker, Bas, and Christoph Klingen, eds. 2012. “How Emerging Europe Came Through the 2008/09 Crisis, An Account by the Staff of the IMF’s European Department.” International Monetary Fund, Washington.
- Barajas, Adolfo, Thorsten Beck, Era Dabla-Norris, and Reza Yousefi. 2013. “Too Cold, Too Hot, Or Just Right? Assessing Financial Sector Development Across the Globe.” Working Paper No. 13/81, International Monetary Fund, Washington.
- Barisitz, Stephan. 2009. “Banking Transformation 1980-2006 in Central and Eastern Europe—From Communism to Capitalism.” *South-Eastern Europe Journal of Economics* 2: 161-80.
- Barro, Robert and Jong-Wha Lee (2013), "A New Data Set of Educational Attainment in the World, 1950–2010." *Journal of Development Economics*, 104: 184–198.
- Bartlett, W., and M. Xhumari. 2007. “Social Security Policy and Pension Reforms in the Western Balkans.” *European Journal of Social Security* 9 (4).
- Beck, Thorsten, and Erik Feyen. 2013. “Benchmarking Financial Systems: Introducing the Financial Possibility Frontier.” World Bank Policy Research Working Paper 6615. Washington: World Bank.
- Beck, Thorsten, Asli Demirguc-Kunt, and Patrick Honohan. 2008. *Finance for All? Policies and Pitfalls in Expanding Access.* Washington: World Bank.
- Beck, Thorsten. 2009. *Access to Financial Services: Measurement, Impact and Policies.* Washington: World Bank.
- Beck, Thorsten, Asli Demirguc-Kunt, and Maria Soledad Martinez Peria. 2006. “Banking Services for Everyone? Barriers to Bank Access and Use around the World.” World Bank Policy Research Paper 4079. Washington: World Bank.
- Beck, Thorsten, Erik Feyen, Alain Ize, and Florencia Moizezowicz. 2008. “Benchmarking Financial Development.” World Bank Policy Research Working Paper 4638. Washington: World Bank.
- Ball, Laurence M., Daniel Leigh, and Prakash Loungani. 2013. “Okun's Law: Fit at Fifty?”, *NBER Working Paper*, No. 18668.
- Barjaktarevic, Zaneta Ostojic. 2001. “Condition of the Serbian Railways Infrastructure and Chances for its Fair Inclusion in the European Railways”, UIC.
- Barro, Robert J. 1988. “Government Spending in a Simple Model of Endogenous Growth”, *RCER Working Papers* from University of Rochester - Center for Economic Research (RCER)

- Bartlett, Will, and Milica Uvalić. 2013. “Chapter 1. Introduction”. [ed] Will Bartlett and Milica Uvalić. *The Social Consequences of the Global Economic Crisis in South East Europe*. London: London School of Economics and Political Science, June 2013, pp.1-14.
- Baumol, William J. 1990. “Entrepreneurship: Productive, Unproductive and Destructive”, *Journal of Political Economy*, October.
- Bencivenga, Valerie R., and Bruce D. Smith. 1991. “Financial Intermediation and Endogenous Growth”. *Review of Economic Studies.* 1991, Vol. 58, pp. 195-209
- Brems, Hans. 1956. "A generalization of the foreign trade multiplier", *Kyklos*, 9, n. 4: 475-491.
- Business and Finance Consulting. 2016. “Assessment of financing needs of SMEs in the Western Balkans countries: country reports”, Business and Finance Consulting, Zurich, April 2016.
- Cingolani, Massimo, Nadia Garbellini and Ariel Luis Wirkierman. 2012. “Macroeconomic Developments and Medium Term Outlook for the Western Balkans and Croatia” in *European Integration Process in Western Balkan Countries*, Paulino Teixeira, Antonio Portugal Duarte, Srdjan Redzepagic, Dejan Eric, Saša Andrejevic (ed.), 91-113, Coimbra, Faculty of Economics.
- Cingolani, Massimo, Nadia Garbellini and Ariel Luis Wirkierman. 2014. "Multiplicateurs matriciels du commerce extérieur et coordination de la politique fiscale: une application aux Balkans Occidentaux", In: *La 'grande Europe' en devenir*, Claude Berthomieu, Jean-Paul Guichard, Elena Ponomarenko, Srdjan Redzepagic ed., 175-186, Nice: Cemafi International.
- Clark, Colin M.A. 1957. *The conditions of economic progress*, London: Macmillan & co ltd and New York: St Martin's Press, Third edition.
- Commission on Growth and Development. 2008. “The Growth Report. Strategies for Sustained Growth and Inclusive Development,” The International Bank for Reconstruction and Development / The World Bank, Washington.
- Calvo, Guillermo A., Fabrizio Coricelli, and Pablo Ottonello. 2012. “The Labor Market Consequences of Financial Crises with or without Inflation: Jobless and Wageless Recoveries.” NBER Working Paper No. 18480. Cambridge, Massachusetts: National Bureau of Economic Research.
- Campos, Nauro F., and Fabrizio Coricelli. 2002. “Growth in Transition: What We Know, What We Don’t, and What We Should.” *Journal of Economic Literature* 11: 783–836.
- Che, Natasha, and Antonio Spilimbergo. 2012. “Structural Reforms and Regional Convergence.” Working Paper No. 12/106, International Monetary Fund, Washington
- Coricelli, Fabrizio, and Riccardo Fiorito. 2013. “Myths and Facts about Fiscal Discretion: A New Measure of Discretionary Expenditure.” http://works.bepress.com/riccardo_fiorito/2.
- Cottarellli, Carlo, Giovanni Dell’Arrica, and Ivanna Vladkova-Hollar. 2003. “Early Birds, Late Risers, and Sleeping Beauties: Bank Credit Growth to the Private Sector in Central and Eastern Europe and the Balkans.” Working Paper No. 03/213. International Monetary Fund, Washington.
- Dabla-Norris, Era, Giang Ho, Kalpana Kochhar, Annette Kyobe, and Robert Tchaidze. 2013.
- “Anchoring Growth: The Importance of Productivity-Enhancing Reforms in Emerging Market and Developing Economies.” Staff Discussion Note 13/08, International Monetary Fund, Washington.
- De la Torre, Augusto, Erik Feyen, and Alain Ize. 2011. “Financial Development: Structure and Dynamics.” World Bank Policy Research Working Paper 5854. Washington: World Bank.
- Demirguc-Kunt, Asli, and Leora Klapper. 2012. “Measuring Financial Inclusion: The Global Findex.” World Bank Policy Research Working Paper 6025. Washington: World Bank.
- Easterly, William, and Ross Levine. 2001. “It's Not Factor Accumulation: Stylized Facts and Growth Models.” *World Bank Economic Review* 15 (2): 177–219.
- Easterly, William, and Sergio Rebelo. 1993. “Fiscal Policy and Economic Growth: An Empirical Investigation.”
- Estrin, S. and M. Uvalic (2008), “From Illyria towards Capitalism: Did Labor-Management Theory Teach Us Anything About Yugoslavia and Transition in its Successor States?”, Comparative Economic Studies,50th Anniversary Essay, Vol. 50, pp. 663-696.Studies,50th Anniversary Essay, Vol. 50, pp. 663-696. *Journal of Monetary Economics* 32: 417–458.
- European Bank for Reconstruction and Development (EBRD). 2013. *Transition Report.* London: European Bank for Reconstruction and Development.

- European Banking Coordination Vienna Initiative. 2012. "Report from the Working Group on NPLs in Central, Eastern and Southeastern Europe."
- European Investment Bank. 2014. CESEE Bank Lending Survey, H1-2014.
- Fatás, Antonio, and Ilian Mihov. 2003. "The Case for Restricting Discretionary Fiscal Policy." *Quarterly Journal of Economics* 118: 1419–447.
- Fatás, Antonio, and Ilian Mihov. 2003. "The Case for Restricting Discretionary Fiscal. 2006. "The Macroeconomic Effects of Fiscal Rules in the US States." *Journal of Public Economics* 90: 101–17.
- Gerard, Marc, and Alexander Tieman. 2013. "Financing Convergence", *FYR Macedonia Selected Issues*
- Fung, Michael K. 2009. "Financial Development and Economic Growth: Convergence or Divergence?''Journal of International Money and Finance 28: 56-67. *Paper, IMF Country Report 13/279.* International Monetary Fund, Washington, June.
- Gerxhani, Klarita. 2004. "The Informal Sector in Developed and Less Developed Countries: A Literature Survey." *Public Choice* 120: 267–300.
- Gligorov Vladimir, Anna Iara, Michael Landesmann, Robert Stehrer, and Hermine Vidovic. 2008. "Western Balkan Countries: Adjustment Capacity to External Shocks, with a Focus on Labor Markets." Wiiw Research Report No. 352. Vienna: The Vienna Institute for International Economic Studies.
- Hashi I, Krasniqi A. B, 2008, ''Entrepreneurship and SME Growth: Evidence from Advanced and Laggard Transition Economies'', International Journal of Entrepreneurial Behaviour, Vol 17
- Inklaar, Robert, and Marcel P. Timmer. 2013. "Capital, Labor and TFP in PWT8.0." Groningen Growth and Development Centre. The Netherlands: University of Groningen.
- International Labour Organization (ILO). 2012. *Global Employment Trend: Preventing a Deeper Job Crisis.* Geneva: International Labour Organization.
- Kuddo, Arvo. 2013. "South East Europe Six: A Comparative Analysis of Labor Regulations." Technical Note (August). World Bank, Washington.
- Kaufmann, Daniel, and Aart Kraay. 2002. "Growth without Governance." World Bank Policy Reaserch, Working Paper No. 2928. Washington: World Bank.
- Laeven, Luc, and Fabian Valencia. 2012. "Systemic Banking Crises Database: An Update." Working
- Milica Uvalić,Vladimir Cvijanović, 2018, SOE. Towards A Sustainable Economic Growth
- and Development in the Western Balkans.
- Paper No. 12/163, International Monetary Fund, Washington
- Pagano, Marco. 1993. "Financial Markets and Growth: An Overview." European Economic Review 37: 613-22.
- Sanfey P, Milatovic J, Kresic A. 2016, EBRD. How the Western Balkans can catch up.
- World Economic Forum (WEF). 2014 Global Competitiveness Report 2013–2014. Zurich: World Economic Forum.
- World Bank. 2013. Global Financial Development Report 2014: Financial Inclusion. Washington: World Bank.
- Zuzana Murgasova, Nadeem Ilahi, Jacques Miniane, Alasdair Scott, Ivanna Vladkova-Hollar, and an IMF Staff Team. 2015. The Regional Economic Issues (REI) The WESTERN BALKANS- 15 Years of Economic Transition. ISBN: 978-1-49835-651-0.