

## Southeast European Times

### Which way ahead for the Western Balkans?

**Daniel Daianu** Southeast European Times

July 17, 2006

**Although the overall situation remains positive, issues such as unemployment, "aid addiction" and the need for investment must be addressed if the Western Balkans are to continue along the right path, writes former Romanian Finance Minister Daniel Daianu.**

In general, recent developments in the Western Balkans have prompted more than a few pundits to sound alarm bells concerning the relative neglect of the region by Brussels and the main European capitals. The last report of the Amato Commission -- which is made up of top European politicians -- sent a strongly worded message in this regard. Several times lately the European Stability Initiative, an NGO whose work is dedicated to the western Balkans, has issued similar warnings.

Various factors are influencing the course of events in the Western Balkans, some which move things in the right direction, and others which keep the region in the grip of serious traps -- whether political, economic or interethnic. In the recent past, one could sense a more forceful march in the right direction. The attraction of joining the EU, though a distant goal, played a decisive role. Good economic signs multiplied: Inflation was coming down dramatically all over the region and, more importantly, economic growth was picking up strongly.

The referendum in Montenegro captured the attention of many European chancelleries. Some hailed it, while others were cautious. Would it help find a solution to the Kosovo issue? Would it put other forces into motion that would enhance the quest for EU accession in the region? These are questions that automatically come to mind.

The banking sectors in the region were being cleaned up and able, after a long time, to fund growth via investment and consumption credits. Intra-regional trade started to grow, as local politicians acknowledged that Chinese walls do not make sense for their small economies. Domestic politics strengthened the hand of democratic forces.

What about the situation now? Economic data, at least on the surface, does not indicate a worsening of the overall state of affairs. Economic growth has continued, apparently unabated. During 2005, the rise in GDP was 5 per cent in the Western Balkans, except in Macedonia (where it was 3.5 per cent). Inflation has been in the single digits, at the very low end of the range -- except in Serbia, where it stood at over 16 per cent in 2005. And the strengthening of banking sectors has continued, owing to the enforcement of better prudential regulations and the inroads made by Austrian, Greek and Italian banks.

However, there are areas where the data looks less bright, illustrating an eye-catching variety of circumstances.

Aid addiction has not diminished in Bosnia-Herzegovina (BiH), where the current account deficit totalled almost a fourth of GDP, while FDI amounted to less than 4 per cent of GDP. In Kosovo, the current account deficit has been even higher -- over 30 per cent of GDP last year.

Remittances are high in the province (over 14 per cent of GDP). But as an economist would point out, they do not cover the current account deficit; the latter needs stable capital inflows in order to be sustainable.

Unemployment remains high in BiH, Kosovo and Macedonia, although local economists and officials dispute the numbers and cite the vibrant informal sector. What is not in dispute, however, is the propensity among citizens -- especially youth -- to migrate and seek work abroad, due to the high wage differentials. Substantial economic fragility exists in the region and inward FDI, though increasing in recent years, is not yet a driving force for creating jobs and underpinning stability. Can the current positive trends be sustained unless they are backed by a strong capital formation process? Probably not. Furthermore, domestic investment hinges on the prospects for joining the EU in the not too distant future.

Across the region, the message is the same: The only game is EU accession. The rationale for this quest is economic, political and geopolitical. At a time when Montenegro has broken loose completely, when Kosovo's status is heatedly debated, when the economic fragility of BiH poses a continuing headache, the heavyweights of the Union should pay more attention to the region.

According to some Western policymakers, the Salzburg EU summit again pledged the Union's support for the region, renewing the commitments made in Thessaloniki. And yet it is not unfair to say that the support shown in Salzburg was more tepid. Western politicians have had to respond to the change of mood in their electorates. The referenda in France and the Netherlands signalled considerable anguish regarding immigration, globalisation and the fate of the welfare state.

The irony is that the EU enlargement of 2004 has not been, on the whole, a nuisance to the old EU member states; the latter are running trade surpluses with the former communist economies and have relocated factories there so they can compete better in world markets. In addition, whatever some say about the "Polish plumber", the fact is that workers from Poland, Bulgaria, Romania and so on fill important niches in western labour markets and help those economies function better.

Still, it is hard to deny that fatigue exists in the West. Several top-notch politicians are lame ducks, and not a few governments are reluctant to undertake painful reforms. On the other hand, it is important not to misread the themes of public debate. In truth, it is not the last wave of enlargement that has triggered the fatigue in the "Old EU". Rigid labour markets, unreformed educational systems, under funded welfare systems, insufficient spending on R&D, and an inability to come to grips with

the reality of a global economy are the real root of the problem.

Romania and Bulgaria will most likely join the Union in 2007, in spite of critical reports from the European Commission. This should embolden Paris, Berlin, London and others to be more forthcoming when it comes to

the prospects for Western Balkan states. A substantially eased visa regime, more assistance for boosting the capacity to absorb EU funds, and more clearly formulated messages would help greatly to this end. How Brussels approaches these issues will prove a key test of EU statesmanship.