

REGIONAL COOPERATION IN SOUTHEASTERN EUROPE

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Abstract. *Among the countries of Southeastern Europe, despite the geographical proximity, there is a very low level of economic integration. Since the economic status of these countries is very poor, a revival of regional economic cooperation through intensification of trade, realization of regional investment projects and greater inflow of FDI, could foster economic growth in these countries. This would reduce the income gap in relation to those countries which will join EU earlier, and create conditions for a faster integration of Southeastern Europe with the EU. In this paper we shall analyze the existing level of economic integration of Southeastern Europe and try to argue why economic cooperation should be actively encouraged.*

INTRODUCTION

Among the countries in Southeastern Europe (in future text SEE), despite the geographical proximity, there is a very low level of economic integration. Such low level of economic integration before transition has been determined by non-economic factors to a large extent: historical, political, geostrategic and ideological (including the existence of the CMEA, the specific position of SFR Yugoslavia and the autarkic policy of Albania). The transition of centrally-planned to market economies caused important political and economic changes which affected the foreign trade orientation of these countries. The recent military conflicts, sanctions, etc., contributed to an introduction of restrictions on foreign trade. These restrictions directly influenced trade among the countries of SEE and lead to a considerably lower level of exchange in comparison with the level which would exist without the presence of these factors. In this paper we plan to analyse primarily economic aspects of regional cooperation in SEE. Our analysis will include seven transition countries: Albania, Bosnia and Herzegovina, FYR Macedonia, Romania, Bulgaria, Serbia and Montenegro. We will first examine the level of economic integration of the SEE region in the past and than try to argue why economic cooperation should be actively encouraged.

1. CAUSES OF REGIONALISATION

By elimination of the artificial barriers for the flow of goods, services, capital, knowledge and people across the borders, globalization enabled many countries to achieve rapid growth and raise their living standards. However, despite a considerable reduction of foreign trade restrictions (tariff and non-tariff), protectionism is still present. The reduced level of the world income, instead of stimulating liberalization of trade, further contributed to protectionism.

Developed countries have, on average, lower custom tariffs but they are concentrated exactly in areas in which less developed countries have comparative advantages, such as agriculture and labor intensive industries. According to some estimates, rich countries' protectionism costs less-developed countries more than \$100 bn a year, which is twice the flow of aid from developed to less-developed countries. At the same time, in less-developed countries the level of protection is three times higher than in OECD countries and represents an obstacle primarily for trade with other less-developed countries. It is estimated that its elimination would bring about another \$50 bn net benefits. One way to realize these benefits is regionalization of exchange.

During the last ten years there has been a revival of regionalism. In the USA, the new Common Market of the South (MERCOSUR) in 1991 and the North American Free Trade Association (NAFTA) in 1994 were created. At the same time, old Preferential Trade Agreement (PTAs) like the Andean Pact (ANDEAN) and the Central American Common Market started a process of renewal. In Asia, countries in the Association of Southeast Nations (ASEAN) formed in 1992 the ASEAN Free Trade Area (AFTA). These are some of the examples of regional trade integration, but there are many more. Nearly every country in the world is either a member of – or discussing participation in – one or more regional integration. In 1999 regional agreements notified to World Trade Organization (194) were a greater number than that of its members (140). Regional agreements exist between high developed, undeveloped, and recently (started with NAFTA) between developed and undeveloped. More than half of world trade now occurs within actual or perspective trading blocs.

The earlier attempts of regionalisation were limited largely to trade and just a few other areas. The new regionalism is more global in scope and involves integration not only of trade but also of finance and foreign direct investment.

Both political and economic considerations are involved in every regional economic integration. Every attempt of regional economic integration is motivated with political and economic factors, but the relative importance of economic and political factors differs in each. Whereas the movement toward integration in Western Europe has been motivated primarily by political consideration, the motivation for North American and Pacific Asian regionalism has been principally, but not entirely, market driven. However, in the case of North American regionalism some political motives, such as strengthening North America's position vis-à-vis Western Europe and reducing illegal Mexican migration into the United States, have also been factors.

In addition to the differing mixture of political and economic goals, regional arrangements vary in their institutional form. For example, Western Europe is attempting to create an integrated political/economic entity, has erected an external tariff, and has become highly institutionalized, while the Pacific Asian regionalization has no external tariff, has

a very low level of institutional development, and every economy in the region has retained high tariffs. North American Free Trade Agreement created a free trade area without an external tariff, does not have a common market, and has only a few formal institutions.

There is no universal theory which could explain all regional integrations, because they are very different. However, we could point to some very important common elements in all regional integrations. First, every attempt of regionalisation include political motive. Although interest groups could affect regional integration, these arrangements are produced primarily by national interests as defined by the ruling elites of the states involved. Second, growing numbers of participants and the increasing complexity of the problems in international negotiations also encourage the movement toward regional arrangements. For example, the large number of participants in GATT/WTO trade negotiations has led many states to seek easier solutions on regional level. Third, emergence of new economic powers, intensification of international economic competition and rapid technological developments also contributed to regionalisation. During 1970s, many countries responded to such challenges with restoration of protectionism i.e. with the use of non-tariff barriers. Since that approach prove ineffective, states in Western Europe and North America and many others turned down to custom unions and free trade areas to protect themselves from the rapidly industrializing and highly competitive economies of Pacific Asia. Forth, economic regionalism is also motivated by economic security problem. Strengthening of the European Union forces USA to support North American Free Trade Area. Japan, fearing exclusion from both of those regional blocs, stimulated Asian Pacific regionalism. Fifth, increasing importance of oligopolistic competition in world trade and economies of scale additionally contributed to regionalisation. Many businessmen and political leaders believe that protected regional arrangements enable local firms to achieve economies of scale and increase their competitiveness vis-à-vis foreign firms. Then when the firms are sufficiently strong, they will be able to compete more successfully against established oligopolistic firms in global markets.

The world bank official line is critical of regional trade blocs formation (3, p.14). Although these blocs enable member countries to achieve progress in the area of liberalization, in general they induce an increase in the real cost of their imports, reduce the technology flow and raise export dependence on particular markets. Moreover, countries that are involved in these forms of integration have not grown faster than the other once , when investment differences are taken into account. Regional trade blocs were mainly formed between neighboring countries, which are naturally referred one to another.

It is impossible to understand the formation and growth of regional trade blocs without reference to the costs and benefits of globalization, and the lack of global governance institutions that might reduce or compensate such costs. Regional governance institutions of trade blocs fill this institutional vacuum and provide a good, perhaps the best explanation of trade blocs diffusion. From that aspect, existence of regional trade blocs is not a brake to globalization, for trade blocs complement it, filling a systemic vacuum.

2. LEVEL OF ECONOMIC INTEGRATION IN SOUTHEASTERN EUROPE

Before transition, at the end of 1980s, the political and economic picture of SEE was considerably different. Five countries in the SEE region (Bosnia and Herzegovina, Croatia, FYR Macedonia, Slovenia, Serbia and Montenegro) were part of the Socialist Federative Republic of Yugoslavia. SFRY was the most developed and the largest country in the SEE (both in territory and population) and because of its specific position in international economic relations it was, in comparison to its neighbours (Bulgaria and Romania), less dependent in trade with other socialist countries. Among the republics of the former SFRY existed strong economic links, i.e. a high level of economic integration. According to the available data, more than a half of the gross material product of former SFRY had been realized in exchange with other republics. For Serbia, the foreign trade share in gross material product (defined as an average of export and import) was 17,8% in 1987, while the share of intrarepublican trade was 40,3%. Appropriate shares for Croatia were 15,6% and 49,4%, Slovenia 22,4% and 56%. For other republics foreign trade share were between 16,1% and 19,4%, but the share of intrarepublican trade was on a much higher level – between 58,3% and 91,8% (5, p.10). For every republic, value of the delivery to other republics was greater than the export of these republics, and the value of import was lower than the value of purchase from other republics (1, p.43).

Bulgaria and Romania had been members of the CMEA (Council for Mutual Economic Assistance) for several decades and therefore had a higher proportion of trade with other socialist countries. Exchange with other SEE countries was a negligible part of their overall exchange. In the case of Bulgaria, exchange with other SEE countries constituted 13,4% of exports and 6,5% of imports. For Romania, this share was even lower: 3,2% of exports and 4,4% of imports. In the case of SFRY, exchange with other countries of socialist block constituted 2,1% of exports and 2,2% of imports (6, p.4). Albania was the most closed economy in Europe. After abandoning CMEA in the early 1960s, it followed its own autarchic development strategy form many years and had limited economic links with the rest of the world, including its closest neighbours. The low level of exchange between SEE countries, despite geographical proximity, points out to the low level of economic integration, except for the countries of the former SFRY. At that time, the SEE region actually consisted of two sub regions: the first, relatively integrated, consisted of the republics of the former SFRY; and the second, consisted of Bulgaria, Romania and Albania, characterized by very weak mutual trade links. Trade flows between the two SEE sub regions were negligible.

Transition from centrally-planned to market economies caused important political and economic changes, including dissolution of the CMEA in 1991, fundamentally changed foreign trade orientation of Bulgaria and Romania. These two countries successfully re-oriented a great deal of their exports from CMEA to the market of EU.

The disintegration of SFRY in 1991-1992 has led to the creation of five independent states which, quite contrary to the general trend of trade liberalization elsewhere, introduced restrictions on trade with their former trading partners. These developments reduced the level of foreign exchange among former SFRY republics. Disintegration of common market caused great losses in production, employment and other macroeconomic aggregates. Estimates of economic damages caused by disintegration of the common state is very complicated and hard task and therefore was and will always be the subject of po-

lemics among economists. Nevertheless, it is completely clear that economic subjects and citizens of the former republics suffered considerable damages from the disintegration of the common state. In the short run, all republics suffered great damages on the basis of interruption of organic ties between enterprises and sectors, which evolved during many years. It resulted with reduction and in drastic cases with complete cessation of production. The reasons were twofold: first, the lack of raw materials and spare parts; second, sudden loss of market.

Under the influence of these changes, during the last decade EU became the most important trading partner for the majority of SEE countries. Albania, Bulgaria and Romania very quickly reoriented trade from their traditional partners primarily towards the EU, while trade links between them have become even weaker. For these countries, trade with other SEE countries in 1998 was of marginal importance. On the other hand, for the countries of the former SFRY trade with other SEE countries represents a significant portion of the overall trade. Despite several military conflicts, the introduction of trade and other barriers, embargoes etc., which all contributed to a drastic reduction of the overall level of trade among the newly created states, most successor states of the former SFRY have maintained some trade with their former trading partners. During the second half of the 1990s there was a revival of trade, especially between Croatia and the Bosnian Federation, and between FRY and the Serb part of Bosnia and Herzegovina. In 1998, the share of trade with other SEE countries in the overall export and import was 67% and 53% for Bosnia and Herzegovina, 35% and 16% for FRY, 24% and 33% for FYR Macedonia. For Croatia, export to other SEE countries was 25% of the overall export, and import from these countries was only 12% of the overall import. Exchange with other SEE countries was of negligible importance for Slovenia.

Today, the SEE region is economically less integrated than a decade ago. This low level of integration has been determined mainly by non-economic factors: historical, political, geostrategic and ideological (including the existence of the CMEA, the specific position of Yugoslavia and the autarchic policy of Albania). Similarly, the economic interest may not be the primary factor determining trade flows in SEE today. In addition to historical factors that once divided SEE, we should point out to the recent military conflicts, embargoes and politically-motivated trade wars, which have had a direct impact on trade among SEE countries, contributing to a much lower level of trade than otherwise could have been the case.

3. PERSPECTIVES OF REGIONAL ECONOMIC COOPERATION IN SOUTHEASTERN EUROPE

Historically, the south eastern part of Europe has always been among the least developed regions in Europe. The long term changes in *per capita* income levels of SEE countries relative to a control country or a group of countries are probably most indicative of the changes in the relative economic position of this group of countries. According to some estimates, the relative income position of SEE as a whole vis-à-vis EU 15 is considerably worse in 2000 than it had been in 1950. A similar trend can be observed comparing the income *per capita* between Central European (CE) and Southeast European countries during the same period. It means that the difference in average GDP *per capita* (on PPP basis) between SEE and CE is comparable to that between CE and EU average (4, p.2-3).

The time required for catch-up is alarming. Unless the current trends in economic performance are decisively broken, it will take decades, even in the more optimistic scenarios, for SEE to reach only the mediocre level of the *per capita* income of more advanced CE countries. In other words, the SEE have as much to do to catch-up with the current CE average income level, as the CE have to do in order to catch-up with the EU average. The time required for catch-up of income level of the least developed EU economies is measured by decades, not to mention catching-up of the income level of most developed EU economies.

The relative position of this region in relation to the income level of developed European countries has remained unchanged during a relatively long period, which points out to the lack of convergence. Although there have been periods of reducing the absolute lag, the relative position has remained stable and there has been no convergence. By intensifying trade and other links among SEE countries regional economic cooperation could contribute to economic recovery and growth and thus help SEE region to pull out of this vicious circle of economic backwardness.

One of the first steps is to increase mutual trade on the basis of removal of trade barriers. Liberalization of trade could stimulate regional trade, and thus create strong impulses for economic development, with both static and dynamic gains. The potential for expanding trade exists primarily between successor states of former Yugoslavia.

The expected increase in trade may turn out to be transitory, but it could certainly be beneficial. If we consider that over the last few years, SEE exports to the EU have been stagnating or declining (with the exception of Romania) this fall could be compensated by increasing exports to SEE countries.

The turn-out point in the regional cooperation between SEE countries has been an adoption of the Stability pact for SEE in 1999. During the same year EU opened the process of stabilization and association for Croatia, Bosnia and Herzegovina, Albania, FYR Macedonia, Serbia and Montenegro. Basic instrument that EU applies in this process is Stabilization and Association Agreement which, among other things, establishes obligation of deepening the regional cooperation with countries which signed the Agreement, with other countries included in the process of stabilization and association, as well as with candidates for affiliation to EU. On that basis, SEE countries signed the Memorandum of liberalization and facilitation of foreign trade and thus accepted the obligation to complete the network of agreements on free trade up to the end of 2002. By establishing a free trade area – the South European Free Trade Area (SEFTA) - SEE countries for the first time, but with the active help of EU, create an institutional basis for deeper economic cooperation in the region.

It is the question that certainly will preoccupy attention concerned with depth and width of institutional forms of cooperation in the region. Before mentioned Memorandum, beside network of bilateral agreements on free trade imply mutual cooperation in different areas: in custom procedure, commercial law, standards, industrial property law, etc. In this region a number of common problems exist (many of them have emerged especially after the 1999 military conflict in FRY) which could be solved only jointly, with the participation of all SEE countries as a part of the economic, as well as political and social, reconstruction of the region. Therefore, closer cooperation between these countries in the following fields: infrastructure, transport, Danube issues, migration, energy, ecological damages etc., is needed. These problems should be addressed and solved on the basis of

close cooperation of all SEE countries, otherwise they will be only partially resolved. Regional transnational projects are needed to rebuild railways, highways, other transportation routes and the communications network. The promotion of trade and economic development also depends to a great extent on efficient regional infrastructure networks, wherein reintegration of regional infrastructure could lead to important economies of scale.

If the SEE countries begin cooperation in the liberalization of trade, implementation of joint investment projects, intensification of other forms of cooperation, it can contribute to economic and political stability and thus substantially improve investment climate in this region. Low level of FDI is a regional problem that will remain unresolved unless more permanent political and economic stability is achieved through SEE.

Regional cooperation in SEE could facilitate future integration with the EU. By facilitation of mutual trade, implementation of large investment projects and greater inflow of FDI faster growth could probably be achieved. This would reduce the income gap with respect to those who will enter the EU earlier, leading to faster future integration of SEE with EU. But, SEE countries must not have great illusions about quick entry into the EU, because during the past decade EU enlargement proceeded very slowly.

There are also strong non-economic motives for intensifying the regional cooperation. The undefined status of Kosovo and poor prospects for its early resolution posing concrete political and economic security is a problem for the SEE region. The need to establish more permanent conditions for security, stability, peace and development in the region should be a major stimulus for closer cooperation in all fields. For SEE countries there are no alternatives in the medium run but to intensify regional cooperation.

CONCLUSIONS

Historically, the South eastern part of Europe has always been among the least developed regions in Europe. Situation has not changed during transition. Output fall in these countries has been deeper than in CE countries, and many of them has not managed to reach pre-reform output level yet. By facilitation of mutual trade, implementation of large investment projects and greater inflow of FDI, faster growth could probably be achieved. Therefore, regional economic cooperation among SEE countries is very important. All inclusive regional strategy for SEE is needed, which should include many fields - economy, politics, culture etc. – and all SEE countries. Necessity for such a strategy stems from the fact that the most important problems of this region (stability, democracy and development) are closely intertwined. Whereas closer cooperation in each of the areas would be beneficial in itself, an all – inclusive regional strategy could generate various spillover effects – closer cooperation in one area could facilitate and reinforce closer cooperation in others.

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REGIONALNA SARADNJA U JUGOISTOČNOJ EVROPI**Nataša Golubović, Srdjan Golubović**

Između zemalja Jugoistočne Evrope, uprkos geografskoj bliskosti, postoji nizak stepen ekonomske integrisanosti. Imajući u vidu slabe ekonomske performanse ovih zemalja, jačanje regionalne ekonomske saradnje kroz podsticanje međusobne razmene, realizaciju regionalnih investicionih projekata i veći priliv SDI, može da podstakne brži privredni rast u ovim zemljama. Time bi se smanjio jaz u dohotku u odnosu na zemlje koje će ranije pristupiti EU i stvorili preduslovi za bržu integraciju zemalja JIE u EU. U radu ćemo najpre analizirati stepen ekonomske integrisanosti regiona Jugoistočne Evrope u dosadašnjem periodu, a zatim pokušati da argumentujemo neophodnost jačanja ekonomske saradnje među zemljama ovog regiona.