

BUILDING COMPETITIVENESS IN SOUTHEAST EUROPE AS A PREPARATION FOR WIDER EUROPE

1. Competitiveness of Southeast European Economies

Competitiveness of national economies is a concept so often praised and criticized that came in focus of all studies dedicated to analysis of position of countries in the world economy. For all of us it is normal to think about competitiveness of companies but when we use this concept to compare national economies we are not that convinced. In contemporary world economy countries are competing for scarce resources and their ability to attract foreign investments and use these resources is seen as their competitiveness. When we observe competitiveness in this manner it is clear that we look only at economic competitiveness and all other dimensions of countries competitiveness are abstracted. Macroeconomic competitiveness is a relative concept that means that we have to compare countries to determine their individual competitiveness and it is often referred as international competitiveness.

There are many methodologies today available for measuring international competitiveness of countries but most regarded are index measures developed by World Economic Forum (WEF) and Institute for Management Development (IMD). Since there two institutions have work together in the beginning and have a same preposition that microeconomic competitiveness determine macroeconomic competitiveness, and vice versa, their methodologies are quite similar. But only WEF in its Global Competitiveness Index analysis includes countries of West Balkans (WB) so we will present their findings in this paper. In table 1 we can observe that only Montenegro from the region is in the upper half of the list where countries are rank by their global competitiveness score and last year it was Montenegro and Croatia in the upper half of the list.

Table 1: World Economic Forum Ranking of Economies by Global Competitiveness

2009-2010	<i>Rank</i>	2008-2009
Switzerland	1	United States
Sweden (4)	10	Sweden (4)
United Kingdom (13)	20	France (16)
Ireland (25)	30	Ireland (22)
Slovenia (37)	40	Czech Republic (33)
Italy (48)	50	Slovenia (42)
Hungary (58)	60	Russia (51)
Montenegro (62)		Croatia (61)
-----	70	Montenegro (65) -----

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Croatia (72)	80	Bulgaria (76)
Macedonia (84)	90	Serbia (85) Macedonia (89)
Serbia (93) Albania (96)	100	Albania (108)
Bosnia and Herzegovina (109)	110	Bosnia and Herzegovina (107)
Venezuela (113)	120	Tajikistan (116)
Tajikistan (122)	130	Kyrgyz Republic (122)
Burundi	133	Chad

Source: World Economic Forum, Global Competitiveness Report 2009-2010, Davos, 2009, p.13

Main factors that make WB economies less competitive are according to WEF study:

- Corruption, problematic for all WB economies and very obstructive for doing a business in these economies;
- Inefficient government bureaucracy, problematic for five out of total six WB economies;
- Policy instability, problematic in majority of WB economies;
- Access to finances;
- Tax regulations and rates, problematic in half of the observed WB economies.

Other country specific factors include inadequate infrastructure, government instability, low educated workforce and bad work ethics.

All policies of individual WB economies adopted in the near future aimed at increasing its competitiveness in world economy must include measures to combat corruption, increase efficiency of government bureaucracy, improve policy stability, make access to finances more easy and improve fiscal policy. Since many of the WB economies have problems with similar factors of uncompetitiveness regional cooperation must be enhanced in all areas so these economies can easily resolve many of problematic factors in joint action.

If we focus just on **trade competitiveness** of WB countries we must point out that some institutions focus their research on this segment of competitiveness and they are more profound in their analysis of competitiveness of national economies. International Trade Center, an international organization parented by United Nations and World Trade Organization, uses two methods - Trade Performance Index (TPI) to estimate competitiveness of economic sectors in international economy and National Export Performance (NEP) which estimates global competitiveness of individual products in export of each economy. The TPI index results denote the sectors dominating export structure and the numbers in brackets signifies the rating of sectors' competitiveness at the global level. Both analytical instruments possess the static (current) and dynamic (future) versions.

Table 2: Sectors and products dominating the export of observed national economies

ECONOMY	SECTORS (TPI)		PRODUCTS (NEP)	
	Current index (static)	Change index (dynamic)	Stars (static)	Champions (dynamic)

SERBIA	Non-electric machinery (43), transportation equipment (44), leather products (56) and electronic components (56)	Minerals (1), fresh food (9) and transportation equipment (11)	Panty hose and tights, frozen fruits and walnuts, and pneumatic tires	Petroleum oil, flat-rolled products of iron and seats
CROATIA	Non-electrical machinery (29), leather products (40) and IT and consumers' electronics (42)	Leather products (12), IT and consumers' electronics (15) and non-electronic machinery (21)	Instruments for automatic regulation, sweaters, pullovers, etc. and seats	Oil gas, seats, sweaters, pullovers.
BOSNIA AND HERZEGOVINA	Leather products (45), products made of wood (48) and clothing (67)	Fresh food (5), products made of wood (8) and processed food (9)	Footwear, unwrought aluminum	Electricity, waste and scrap iron and steel, seats
MACEDONIA	Basic processing industry (44), clothing (46) and products made of leather (50)	Transportation equipment (35), processed food (37) and leather products (51)	Non-alcohol beverages, ladies shirts and ladies apparel	Non-alcohol beverages, petroleum oil and ferrous alloy

Source: International Trade Center data published in: Jefferson Institute, Konkurentnost privrede Srbije 2006: dijagnoza rasta, Beograd, 2006, p.39.

Results shown in table 2 are product of the ITC analysis carried out in 2005 using the data from the period 1999-2003. At first glance, it becomes apparent that more developed economies in WB, such as Croatia and Serbia, possess more sophisticated sectors and products which dominate their export structure, as opposed to less developed countries, Bosnia and Herzegovina and Macedonia, where primary products (raw and partially processed materials) dominate their respective export structure. But this gap in sophistication of export sector is not so significant since the gap in development of observed economies is not huge and observed economies of WB were all part of former Yugoslavia and its single market with long-term mutual growth and similar foundations in terms of resources. *The general problem of WB economies is that they export products with low value added.*

The ranks shown in the brackets in the TPI columns represent the global competitiveness rank of each export sector. For example, both Serbia and Croatia have non-electric machinery sector as their competitive export sector but this Serbian sector is ranked 43 in the world among same sector of all other economies observed in this analysis while the same Croatian sector is 29th most competitive non-electric machinery sector in the world. *The most competitive export sectors of all WB economies are rank around 45th place on the list which present competitiveness ranking of a particular sector in global terms among 189 observed economies.*

But dynamic versions of both indexes show that rise in competitiveness is possible in the future, but different sectors will surface as most competitive in export of respective WB economies. Serbia can expect to have most competitive minerals sector in the world and Croatia and Bosnia and Herzegovina can have globally competitive leather products and fresh food sector, respectively.

2. Regional trade integration of West Balkans countries

In global economy regional trade integration is an important factor of competitiveness of member economies. These integrations serve as a larger national market and represent a good base for development of economies of scale reasonably protected from foreign competition. As multilateral trade liberalization came to a stop after the conclusion of GATT Uruguay round multilateral trade negotiations regional trade liberalization become a dominant trend in trade liberalization across the globe.

All regions in the world had established regional trade integration and countries are grouped by economic interest but also similar cultural heritage and way of life of its citizens. The territory of former Yugoslavia was a single market until dissolution that started in 1991. This region will not be trade integrated again until 2000 when the initiative for integration came from abroad. The fully functional trade integration in WB was achieved in 2006 with the creation of **Central European Free Trade Agreement (CEFTA 2006)**. The completion of free trade area for goods in envisaged at the end of 2010 but we have to acknowledge some problems in functioning of CEFTA 2006 like:

- Misapplication of CEFTA 2006 rules and adoption of certain protectionist measures by members;
- Existence of non-tariff barriers in intraregional trade;
- Status problems of certain CEFTA 2006 members connected with political and legal meters.

In order for a regional trade integration to be beneficial to its members the substitution trade linkages must exist between member countries of one regional trade integration. *Trade data of CEFTA 2006 members from 2008 show that this integration is important for all its members except Moldova where trade with CEFTA 2006 countries is only few percents of total trade of Moldova.*²

In the table 3 we have presented the shares of WB economies in CEFTA 2006 intraregional trade flows. Concerning CEFTA 2006 intraregional exports we can observe that *most developed CEFTA 2006 members, Croatia and Serbia, have largest share of intraregional export*, which combined are above 60% in 2007 and above 70% in 2008. Bosnia and Herzegovina and Macedonia have significant shares in CEFTA 2006 intraregional export flows while all other CEFTA 2006 members have small shares in intraregional exports. But concerning shares in CEFTA 2006 import flows member economy that is dominant is Bosnia and Herzegovina with approximately 44% share in total CEFTA 2006 imports in 2008. Kosovo (UNMIK), Serbia and Montenegro have also significant shares in CEFTA 2006 import flows. That means that *less developed CEFTA 2006 members have significant shares in intraregional import flows*.

Table 3: WB Economies Share in CEFTA 2006 Intraregional Goods Trade (percentage)

Customs Territory	EXPORT		IMPORT	
	2007	2008	2007	2008

² Data by Chambers of Commerce from publication: To European Integration Through Regional Economic Cooperation, Chamber of Commerce of Montenegro, Podgorica, October 2009.

Albania	0.70	1.03	3.42	2.26
Bosnia and Herzegovina	17.59	15.07	36.25	43.93
Croatia	32.44	39.66	16.65	9.83
Macedonia (FYR)	11.74	11.26	7.87	4.99
Moldova	0.10	0.1	0.09	0.08
Montenegro	2.96	2.12	15.98	10.53
Serbia	33.68	29.12	19.42	11.84
Kosovo (UNMIK)	0.79	1.54	0.32	16.49

Source: Calculations based on EUROSTAT data and national statistical offices

The data from the table 3 pictured an *important problem of trade relations of CEFTA 2006 members and that is uneven trade balance*. While Croatia and Serbia have large trade surplus in its trade with CEFTA 2006 members, all other CEFTA 2006 members are recording huge trade deficits in its trade with these large and developed economies. This situation is not sustainable in the long run since all partners are supposed to have some product to export so they will be able to import products. Sometimes the problem is ruted in the application of non-tariff barriers that affect intraregional trade. These measures are more applied by developed member economies of CEFTA 2006 or are caused by existence of outdated regulations and burdensome administrative procedures. Main categories of non-tariff barriers present in CEFTA 2006 regional trade are technical barriers to trade and administrative barriers. *All regional policy initiatives in development of trade in CEFTA 2006 region should address the removal of non-tariff barriers in intraregional trade*. First a scientific inventory of all present non-tariff barriers in intraregional trade must be carried out and then adopt an action plan on removal of these barriers.

One of the solutions of great trade imbalances in intraregional trade can be promotion of foreign direct investment in the CEFTA 2006 region. It is important that CEFTA 2006 economies do not exchange only goods but also capital. Usually more developed countries in the region invest their capital in less developed regional economies and import products from its foreign affiliates changing trade imbalances between countries. *Work should be done on creating a free investment area in CEFTA 2006 region*. Some initiatives have been adopted in this direction but their are really bilateral since the proposition is to complete the network of bilateral investment treaties (BITs) in the CEFTA 2006 region with the conclusion of missing BITs between CEFTA 2006 member economies.

The question that should be addressed regarding the functioning of CEFTA 2006 is the problem of existence of multilateral regional trade agreement that contains bilateral trade preferences. This means that CEFTA 2006 agreement only absorbed the bilateral trade concessions exchanged between WB economies resulting from the network of their bilateral trade agreements negotiated under Stability Pact. This can be a problem for a customs clearance since all customs administrations have to apply trade preferences for each individual partner from CEFTA 2006. Also the treatment of agricultural products in CEFTA should be better addressed.

But the dominant trade integration on the european continent is **European Union** (EU) and all WB countries have the ambition to join this integration as soon as they fulfill set EU entry requirements. The CEFTA 2006 is only a transitory integration with main aim to prepare economies members for a full EU membership, as it was the

case with original CEFTA members. But this can pose a problem since CEFTA 2006 economies are on different levels of their approach to EU. As some of CEFTA 2006 members approach EU membership before others this will influence the trade relations in WB if trade cooperation is not synchronized in this two integrations. *The policy action is needed that will harmonize simultaneous trade cooperation in CEFTA 2006 and EU.* This is especially important in relation to different trade regimes set by two trade integrations which play important role in production specialization and boost of competitiveness of national economies in WB region.

3. Regional trade integration and improvement of Competitiveness

The fact is that companies from WB are not competitive in comparison to the most of the companies that operate in same sectors on a single european market. CEFTA 2006 as a subregional trade integration is a good chance for companies from WB to raise their competitiveness in interaction with other WB companies in a framework of free trade area created by CEFTA 2006.

Only in completely free trade system trade specialization is defined by comparative advantage. Free trade in global economy is an ideal and the reality is existence of managed trade. Every national economy is faced with many diverse trade regimes – national, regional and multilateral. Every trade regime is a framework that defines product and trade specialization of each national economy. Due to the creation of specific regional trade regimes some trade flows with third countries get diverted to intraregional trade flows.

Countries in transition are at a specific phase of its economic development and the change in economic system will lead to restructuring of the economy. *In order to create a new economic structure fully based on international trade specialization principles one economy has to now which trade regime will be prevalent in the future.* Economies in WB are creating CEFTA 2006 trade regime but this framework will be temporary so companies from WB must realized that the framework of their business activities will be trade regime set by a Common EU Trade policy. CEFTA 2006 is not closed integration but it is in a way shielding companies established in its members from a full foreign competition including EU based company.

Usually companies can export using regional trade benefits only if their export products have local origin but CEFTA 2006 rules envisaged the use of regional rules of origin. *This means that inputs produced in other CEFTA 2006 members can be processed and exported as finish products with regional origin in all CEFTA 2006 members.* This will raise the number of potential products in intraregional CEFTA 2006 trade.

But companies from WB must realize how EU accession of CEFTA 2006 economies to the EU can affect their business activity. They must capitalize on all possibilities, like the use of inputs of a european origin, which can be processed in CEFTA 2006 economies and in that state exported to EU using the rules on diagonal cumulation of origin. The domestic origin is accepted for products with high content not only CEFTA 2006 inputs but also EU origin inputs, including European Economic Area EFTA country members. There are many non-tariff obstacles when companies from WB countries export products to EU single market and this problems need to be addressed in near future as a part of SAA process.

The creation of CEFTA 2006 investment zone can enhance the concentration of capital in CEFTA 2006 economies and effective production making this companies more competitive in EU and other foreign markets. There are many products that can be produced in regional production chains, with the engagement of companies from several CEFTA 2006 members producing parts of finished products, and after finalization this products can be exported to third markets as very competitive products using extra favorable trade regimes. Serbia has a very favorable free trade agreement with Russian Federation, which can be used by affiliates of companies from other CEFTA 2006 members. *For this to be possible CEFTA 2006 must widen its regional cooperation to the investment zone with national treatment of investments from other CEFTA 2006 members and insure domestic status from companies based in other CEFTA 2006 countries.*

Regional program for enhancing competitiveness must be adopted which will gather all CEFTA 2006 in joint action for enhancing competitiveness and creation of favorable business environment in CEFTA 2006 area and trade link with EU. This program must be financed by all CEFTA 2006 economies and international donors and oversight by regional institutions. It must contain measures:

- ***That address joint problems in competitiveness of individual CEFTA 2006 economies;***
- ***That improve the structure of export products of CEFTA members;***
- ***That resolve trade imbalances in CEFTA 2006 region tackling non-tariff barriers and improving intraregional investments in CEFTA region;***
- ***That manage the restructuring of export sectors of CEFTA 2006 economies in view of creation of CEFTA 2006 trade integration and approaching EU trade regime;***
- ***That stimulate export oriented regional production networks and use of favorable foreign trade regimes.***