

workshop report

# South East European Studies *at Oxford*

## *Redefining convergence in South East Europe: Implications of changes underway in the EU and Euro Area*

*June 2013*



St Antony's College  
University of Oxford

**seesox**

South East European Studies at Oxford

CELEBRATING 10 YEARS 2002—2012

# Redefining convergence in South East Europe: Implications of changes underway in the EU and Euro Area

SEESOX-Bank of Albania Workshop, in association with the EBRD



*This report draws on discussions at the Workshop on “Redefining convergence in South East Europe”, which was held at St. Antony's College, Oxford University, on 8 March, 2013. The participants included academics and officials from Albania, the United Kingdom, the EBRD, and the region of South East Europe. The report represents SEESOX's interpretation of discussions at the workshop and does not purport to reflect the views of any of the participants.*

---

## **Preamble**

The seminar was preceded the day before by the launch at the European Studies Centre of two highly relevant SEESOX books - *Growth in Albania and South East Europe: the Way Ahead*, by Ardian Fullani, Bank of Albania & SEESOX, 2013; and *Defining a New Reform Agenda: Paths to Sustainable Convergence in South East Europe*, edited by Othon Anastasakis, Peter Sanfey and Max Watson, SEESOX, 2013. These two studies underscored a need for South East Europe to focus more on strengthening institution building at home, while rebalancing the region's reliance on the European Union (EU) as its principal political and economic anchor with a broader international trading perspective, especially with Turkey, the Middle East and Asia. This book launch set the scene for the workshop, as the attending delegates deliberated on the implications for further integration of the region with the EU

in light of the ongoing crisis in the Euro Area (a.k.a. Eurozone).

## **Competition and economic catching up**

The first session addressed the need for new ways of thinking in terms of the economic development of South East Europe. Delegates heard that reforms based on traditional transition economic theories had failed to offer a sufficient response to the challenges of the last twenty years. As the region enters a new transition phase in the wake of the global crisis, a new paradigm will be needed; this new approach should seek to identify the region's specific comparative advantages, and exploit its proximity to Western Europe by linking into the latter's production chain as well as its markets. The former transition countries of Central Europe had successfully tapped into manufacturing bases in Western Europe via the outsourcing of different stages of production tailored to the capabilities of that region.

These countries were now moving up the value-added scale. Delegates were advised that South East Europe could do the same and eventually become quality suppliers in a Pan-European value chain. To complement this process, a new set of supportive policies should be developed, focusing on industrial upgrading, technical regulations, sector-specific regulatory regimes and innovation structures. There would need to be continued efforts to remove structural obstacles to convergence, including the lack of cooperation between stakeholders, the misallocation of educational resources, and the slow implementation of governance reforms.

In addition to structural barriers, this session highlighted the many other hurdles that lay in the path of sustainable economic growth in South East Europe. Business and consumer confidence in the region was below the EU average (which was hardly a high bar in the prevailing Eurozone gloom), although there were some signs that business confidence was finally picking up. There was a serious and growing problem with non-performing loans, and a large private debt overhang from the boom years. Opacity in property rights remained an obstacle to economic incentives, financial intermediation (collateral), and investment. There was still much work to be done in overhauling and improving the region's infrastructure, including intraregional connectivity.<sup>1</sup>

---

<sup>1</sup> The new road linking Tirana to Pristina was hailed as a major step toward improving trading links in the region. If the route were to be extended further to Belgrade, Serbia

Delegates discussed the potential for foreign direct investment (FDI) in South East Europe. There was a degree of scepticism about the operationalization of “picking winners”, whereby policymakers are enjoined to identify the sectors which regional economies should target for incoming FDI. There was a danger, in small economies, that such a process would favour existing dominant firms and thereby solidify an inherited industrial structure that may be suboptimal. It would be advisable to bring in outsiders in the selection procedure to help avoid such an outcome. Nevertheless, some discussants saw the potential for FDI in the agribusiness and clothing sectors. There was also a debate regarding the feasibility of requiring FDI to be in the form of joint ventures with foreign firms, as well the likely incompatibility of such requirements with EU law. Lastly, the discussion focused on the role of investment promotion agencies and the potential for regional cooperation between them. More generally, delegates saw the potential for greater intra-regional trade in South East Europe, if cross border non-tariff barriers could be eased.

### **Political institutions and convergence**

The second session addressed the region's progress in achieving convergence from a political point of view. This was much harder to measure than economic convergence. Arguably, all the countries in the region have met the minimal political

---

would also obtain a direct link to the coast for its products, for export potential to the rest of the world.

convergence criteria of at least having functioning democracies. There has also been progress in strengthening the rule of law, albeit to different degrees across the region. Delegates were reminded, however, that one area given insufficient attention by EU conditionality is the independence and quality of the media.

While South East Europe has been trying to escape its endemic nationalist parochialism, delegates were warned that the region is now being confronted by the irony of the growing risk of the “Balkanization” of the EU (with the forthcoming Scottish independence referendum, a promised UK in/out of EU referendum, and ongoing risks of Eurozone disintegration). The appearance of populism, nihilistic political figures and extremist parties in some of the countries most severely affected by the Eurozone crisis is worrying, and sets a bad example for countries trying hard to forget such temptations. These developments have combined with the EU's failure to resolve the economic problems of the Eurozone to undermine the region's faith in the “democratic capitalism” model and the EU path of political and economic convergence.

Notwithstanding the fading allure of the Western European model, it is hard to see how the region can self-start on its own. The resolution of its remaining ethnic minority problems, for example, is unlikely to be completed without the broader EU glue to put matters in perspective. But as the early prospect of EU accession recedes, so does the political value of

accession for governments imposing difficult reforms while also seeking re-election to tight timetables. The likely effectiveness of EU conditionality can therefore be overstated. This accentuates the need for a stronger domestic political will and for stronger mandates for home-grown reform. Without strong and inclusive political support, economic reforms will fail to generate long term gains.<sup>2</sup>

### **Regional challenges and cooperation**

The third session comprised a panel of central bank governors and officials who explored the advantages of enhanced regional cooperation. These possibilities differed depending on the definition of the region. In view of the continuing goal of accession, which was now a multispeed process, institutionalized arrangements risked fracturing as individual members joined the EU and changed their status. Nevertheless, there was considerable support for greater regional cooperation, not least to strengthen the region's standing through the eyes of outsiders. There was clearly scope for more institutionalization of the existing cooperation between Central Banks in South East Europe. The key role played by the Central Bank of Albania in promoting such cooperation was

---

<sup>2</sup> This is the Acemoglu dilemma - economic inclusion cannot sustain economic growth without inclusive political institutions (*Why Nations Fail*, Daron Acemoglu & James Robinson, Profile Books, London, 2012). It was observed during the Workshop that many institutions which had tried to eschew political interference, e.g., central banks adopting inflation targeting, have found their non-political mandates too narrow to deal with the global recession. Technocrat governments appointed (e.g., in Italy) for crisis management in the Eurozone, have meanwhile had to surrender to elections in short order, notwithstanding their hard won achievements.

acknowledged by all. From an operational perspective, discussants expressed their commitment to the memoranda of cooperation signed between the Central Banks of South East Europe, while they declared their intention to set up various working groups at a technical level. Participants also discussed the potential for closer co-operation in a number of policy areas beyond financial stability, including (inter alia) the possibility of establishing a regional Council of Ministers. It was emphasized that intra-regional trade could be an engine of regional growth, for which greater cooperation in infrastructure development (especially in road and rail networks, and port facilities) could be very helpful.

### **The role of the EU as an anchor in changing times**

The final session focussed on the future role of the EU in relation to the region. The argument was put forward that countries in the region could still benefit from EU membership, notwithstanding the ongoing turmoil in the EU. The basic political model offered by the EU remained the one that could most effectively deliver regional prosperity—there is really no credible institutional alternative for the future of the region. But those seeking accession should be clear about what membership of the EU (and preparations for that) really implies, from both the political and economic perspective. Problems following from the accession of the Bulgaria and Romania have prompted a more

rigorous approach for the accession of the other countries of the region.

The accession process and associated EU conditionality could (inter alia) help countries overcome the legacy of ethnic conflicts in the region. There were a number of bilateral political issues (namely the Serbia-Kosovo, Croatia-Serbia, and Greece-former Yugoslav Republic of Macedonia disputes) which could benefit from unbiased EU pressure. However, these issues will need to be resolved before accession, not after. The EU will have learnt an important lesson from the political problems of Cyprus at the time of its accession, and will want to avoid situations where EU member-states manipulate their membership against the constructive resolution of their bilateral issues with non-EU countries in the region.

In the subsequent discussion, participants debated the extent to which the EU and the European Commission (EC) has lost leverage and credibility in the region. It was noted that the EC has become the junior partner in the Troika (EC, ECB & IMF), which has been charged since the onset of the Eurozone crisis with attending to its casualties (and will likely continue to operate in some form in the future under the European Stability Mechanism). Non-EU countries in the region and in similar circumstances are no doubt relieved that they had to endure the ministrations of only one doctor (the IMF) rather than the witches' brew of the Troika reserved for the blessed members of Eurozone. Delegates were also reminded that key

European initiatives are no longer being pursued through EU institutions, but rather through certain key EU member-states (especially Germany). This points to a profound change in the power structure within the EU membership. The region's changing relationship with the EU has also brought into focus the scope for greater influence in the region from Russia, and more especially, Turkey, both of which offer strong cultural links, geographic proximity, and commercial opportunities.

Notwithstanding the prevailing pessimism, the ultimate goal of the EU—of bringing harmony to Europe—seems as compelling now as when it was first conceived. The growth of the EU from its narrow industrial origins in 1952, to the Treaty of Rome in 1957, to the group of 12, and thence to 27 members over the past 60 years remains an extraordinary geopolitical achievement. The most recent enlargement push reached the very limits of the continent, and the Western Balkans only missed the boat because of the conflict in the region in the 1990s. A European destiny, if not as gilded as it was a few years ago, still beckons for this region.

## Participants

|                          |   |
|--------------------------|---|
| Othon Anastasakis        | Director of SEESOX; Director of European Studies Centre; Fellow, St Antony's College, Oxford  |
| Graham Avery             | Hon. Director General, European Commission  |
| Dimitar Bechev           | Head of European Council on Foreign Relations, Sofia  |
| Adam Bennett             | Associate of SEESOX; Senior Member, St Antony's College, Oxford   |
| Elvis Çibuku             | Advisor, Governor's Office, Bank of Albania   |
| Belma Čolaković          | Chief Economist of the Central Bank of Bosnia and Herzegovina   |
| Nigel Davies             | Managing Director, Wyn River Ltd  |
| Gillian Edgeworth        | Head of EEMEA Economics, Unicredito   |
| Ardian Fullani           | Governor, Bank of Albania   |
| Gani Gërguri             | Governor, Bank of Kosovo  |
| Tom Hashimoto            | Linacre College, Oxford; University of New York, Tirana   |
| Maja Kadievaska Vojnovik | Vice Governor, National Bank of the Republic of Macedonia   |
| James Ker-Lindsay        | Eurobank Senior Research Fellow, LSE  |
| Gramos Kolasi            | Director for Coordination, Governor's Office, Bank of Albania   |
| Dhori Kule               | Member of the Supervisory Council, Bank of Albania  |
| Ermir Maliqaj            | European Integration and Communication Department, Bank of Albania  |
| Genci Mamani             | Head of the Governor's Office, Bank of Albania  |
| Armela Mancellari        | Hub Economist, International Growth Centre Hub  |
| Christos Papazoglou      | Deputy Director, Economic Research Department, Bank of Greece   |
| Slavo Radošević          | Professor of Industry and Innovation Studies, University College London   |
| Peter Sanfey             | Deputy Director, Office of Chief Economist, EBRD; Associate of SEESOX; Senior Member, St Antony's College, Oxford                   |
| Jonathan Scheele         | ESC Fellow, St Antony's College, Oxford   |
| Marko Škreb              | Chief Economist, Privedna Banka Zagreb  |
| Teuta Starova            | Minister Counsellor, Embassy of Albania   |
| Altin Tanku              | Director of the Research Department, Bank of Albania  |
| Jovan Teokarević         | Associate Professor of Political Science, University of Belgrade  |
| David Vines              | Professor of Economics; Fellow, Balliol College, Oxford   |
| Max Watson               | Associate of SEESOX; Director of the Political Economy of Financial Markets Programme; Visiting Fellow, St Antony's College, Oxford |

# ABOUT SEESOX

---

## seesox

South East European Studies at Oxford

CELEBRATING 10 YEARS 2002—2012



If you would like to join our mailing list to receive information about our latest

SEESOX

European Studies Centre  
St Antony's College  
University of Oxford

Telephone: +44 1865 274537

Fax: +44 1865 274478

E-mail: [seesox@sant.ox.ac.uk](mailto:seesox@sant.ox.ac.uk)

**South East European Studies at Oxford (SEESOX)** is part of the European Studies Centre at St Antony's College, Oxford. It focuses on the interdisciplinary study of the Balkans, Greece, Turkey and Cyprus. Drawing on the academic excellence of the University and an international network of associates, it conducts policy relevant research on the multifaceted transformations of the region in the 21st century. It follows closely conflict and post-conflict situations and analyses the historical and intellectual influences which have shaped perceptions and actions in the region. In Oxford's best tradition, the SEESOX team is committed to understanding the present through the *longue durée* and reflecting on the future through high quality scholarship.

SEESOX has the following objectives:

- To support high-quality teaching and research on South East Europe;
- To organise conferences, workshops and research seminars;
- To promote the multi-disciplinary study of the region within the University of Oxford (e.g. politics, international relations, anthropology, sociology, economics) working in collaboration with other Centres and Programmes within the University, including student societies;
- To spearhead intellectual exchanges and debate on these issues among networks of individuals and institutions beyond Oxford;
- To foster cooperation between the academic and the policy making communities.

[www.sant.ox.ac.uk/esc/seesox](http://www.sant.ox.ac.uk/esc/seesox)