

# Barriers to Business

## Serbia, Albania, North Macedonia

### Socio-Economic Context

Albania, Serbia, and North Macedonia are diverse countries with hopes of EU ascension. Held back by macroeconomic problems, each are struggling to compete in the world marketplace. The region is notorious for corruption, violence, and instability. It has suffered from consistently high unemployment rates and low GDP growth rates since 2008. Lack of relevant education has left the general population ill equipped to provide competitive advantages for international investors. All three of the considered countries run public deficits from 50 to 60 percent of their GDP. Much of the spending of these governments comes at the national level, even though recent efforts have been made to decentralize fiscal spending as well as territorial governance.

Each of these countries include substantial minority populations from their neighbors, as well as deep religious divides. While Serbia and North Macedonia are dominated primarily by Orthodox Christianity, Albania is mostly made up of Sunni Muslims. This further complicates the opportunities for peaceful and sustainable solutions to the problems which face them. Local political issues have a history of violence, with Russia representing a constant threat militarily, such as in their attack on Crimea. The Balkans themselves also have a history of ethnic conflict which has risen to levels of genocide, especially during the 1990's after the dissolution of Yugoslavia. Tensions remain between racial groups, well evidenced by a UEFA soccer match between Serbia and Albania, which in 2014 was the overtly racist chants and small-scale violence.<sup>1</sup>

However, this is not to dismiss the incremental but consistent progress made over the past 30 years. Growth in GDP before the 2008 Financial Crisis was consistently higher than it is today. USAID

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<sup>1</sup> <https://www.theguardian.com/football/2014/oct/14/serbia-albania-euro-2016-flag-halted>

has worked in each of these countries before, implementing projects to assist in with local and national reforms in a variety of areas. Individual aspects of governance show promise from recent changes and efforts.

## Cross-Border Trade

A vital part of Balkan economies is integration in the global marketplace. In trading across borders, all three of the countries in question score highly, ranking from 23 to 32 overall. This implies that international trade between neighbors is already streamlined. Doing business indicators show that border protocols for both importing and exporting in each country cost less and are quicker than OECD high income and E&E averages by wide margins.

However, global integration will still play a tertiary role in economic development for the Balkans in the future. The European Union represents the largest trading partner for these countries, accounting for about half of these countries imports and exports.<sup>2</sup> Moreover, each of the countries in the Balkans are attempting to gain EU membership, which has been shown to have significant positive impacts on trade and development. (Mitrovic et al. 2014)

According to the European Commission, there are three main obstacles to EU ascension for the Western Balkans in general. First noted is the rule of law and quality of governance, with a problematic judicial system and rampant corruption, each of these nations have a way to go before they are qualified for ascension. However, steady progress has been made over the previous two decades. The document in particular calls out public procurement as a section of governance in need of additional transparency. Improving these aspects should allow for further foreign investment and business.

Another barrier to joining the EU is the weak economy endemic to many Western Balkan nations. The European commission specifically labels the Western Balkans as “inefficient and rigid markets,

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<sup>2</sup> <https://oec.world/en/>

(with) low productivity, limited finance, unclear property rights and a cumbersome regulatory environment, leading to low competitiveness and high unemployment.”<sup>3</sup>

## Trade Barriers

A key reason for the motivation of EU membership is the reduction of trade barriers both inter-regionally and internationally. All three countries are part of the Central European Free Trade Agreement, but it still allows for significant trade barriers that hinder access between these different markets, especially with respect to imports.

Instances of these countries voluntarily erecting trade barriers for both political and economic reasons are recent. Jusufi et al. describe how tariffs on imported cement in Kosovo had resulted in retaliatory ones by North Macedonia and Albania in 2012, which were then dissolved later that year diplomatically. Another, more recent incident occurred in 2018, when Kosovo added 100% tariffs to Serbian imports in response to the contested country’s attempt to join Interpol. <sup>4</sup> Note that these tariffs were revoked in 2020.<sup>5</sup>

The Economic Development, Governance, and Enterprise Growth Project (EDGE) is currently a project being conducted by IDG. The activities involved include assisting with compliance to the rigorous standards and competition of the EU market, assisting in compliance with the WTO Trade Facilitation Agreement (TFA), and a COVID-19 SME impact report, as well as value chain and workforce assessments to better judge the place of the Western Balkans in the international economy. Sectors that received special attention as having potential for comparative advantage include fruit and vegetable production, rural and adventure tourism, textiles, and wood processing/furniture products.

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<sup>3</sup> [https://ec.europa.eu/info/sites/default/files/communication-credible-enlargement-perspective-western-balkans\\_en.pdf](https://ec.europa.eu/info/sites/default/files/communication-credible-enlargement-perspective-western-balkans_en.pdf)

<sup>4</sup> <https://www.bbc.com/news/world-europe-46287975>

<sup>5</sup> <https://www.dw.com/en/kosovo-lifts-all-tariffs-on-serbian-bosnian-goods/a-52975561>

## Credit

Another aspect of integration comes from access to overseas finance, which remains a vital resource for the Balkan nations. Studies have found that high levels of FDI are preconditions for sustainable economic growth (Popovic et al 2018). Previous potential members have relied on EU investment to support export-led businesses. Jirasavetakul et al. find through literature review that stability, legal rights, and quality domestic suppliers are important for growth through FDI. When conducting empirical analysis, they find that there is a great deal of potential for future growth via FDI through “closing the gap related to institutional quality, participation in vocational training, and higher public investment”.

Access to credit is of moderate effectiveness between the three countries, with Serbia and Albania ranking 67 and 48 while North Macedonia ranks 25<sup>th</sup>. The difference comes from institutional coverage of the adult population. Serbia has 100 percent Credit Bureau coverage, but 0 percent coverage through Credit Registries. Albania has 56.2 percent coverage from Credit Registries, but 0 percent coverage from Credit Bureaus. Compare this with North Macedonia, which boasts both 100 percent coverage of individuals through Credit Bureaus, as well as 41.7 percent coverage through Registries. Before EDGE, USAID conducted the Regional Economic Growth Project (REG) in 2013. This mission focused on providing European and Eurasian countries opportunities for greater economic growth and integration with the world economy.

REG focused on a sector-by-sector empowerment of competitiveness, enterprise development, and financial access. For the previously defined countries, there were several sectors that showed promise. In particular, the ICT sector was well developed, and a performance evaluation report studied the effects of REG on this part of the economy. In this area, REG was successful anecdotally in providing opportunities for business networking both domestically and abroad, while also providing new skills to workers. Another focus of the project was Agribusiness, with 40 percent of activities booked in the

project devoted to this sector. In this sector, REG assisted in building effectiveness in marketing and operations.<sup>6</sup>

In the final performance evaluation report (prepared by IDG LLC), several recommendations were made for next steps. IDG called out each of Serbia, Albania, and Macedonia, suggested continuing work in these regions “where bilateral budgets for economic growth activities have been reduced or eliminated”. It also suggests aggregating common needs across the region as opposed to a bilateral basis, providing regional support for other issues, a “buy-in mechanism for technical expertise”, explicitly prioritizing different objectives, communicating “relationships between Bilateral and Regional Programs and Implementers”, and providing rapid response for future mission needs.<sup>7</sup>

Other lessons learned included a priority on geographic boundaries for each mission, as well as determining sub-region interventions. There should also be substantial expertise available on the ground, with contractors ready to help. Also, responsibilities must be clearly defined for both regional and bilateral implementers. Finally, performance indicators should be agreed upon before-hand, with only a single metric defining success. The report also mentioned the possible value of tourism and trade facilitation as priorities for the region.

## Education

Previous studies have mentioned the need for education to help prepare Balkan citizens for the international workforce. Brajkovic (2016) studies recent trends in higher education, and finds that again governance, corruption, and short-term decision-making are key obstacles for effective reform in this sector. Even when they are effectively educated, they often leave for developed nations as found in Dinkovski et al. and Radonjic et al., providing yet another challenge. However, note that both Serbia and

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<sup>6</sup> [https://pdf.usaid.gov/pdf\\_docs/PA00N298.pdf](https://pdf.usaid.gov/pdf_docs/PA00N298.pdf)

<sup>7</sup> [https://pdf.usaid.gov/pdf\\_docs/PA00N298.pdf](https://pdf.usaid.gov/pdf_docs/PA00N298.pdf)

North Macedonia actually experience brain gain as a result of international students returning from abroad.

Education in the Western Balkans in general is inequitable, with regional differences playing a huge role in the success of individuals. Findings from the Programme for International Student Assessment (PISA) in 2018 show that academic success assessments may be structurally biased against certain socio-economic backgrounds, with a focus more on the lecturer than the student. Helping provide additional resources to under-provided schools, as well as encouraging flexible and student-centered learning programs are mentioned as potential improvements.<sup>8</sup>

## Access to Electricity

Electricity is vital in the modern global economy. For sponsoring export-based SME's, an ability to consistently acquire cheap power can be the determining factor between success and failure. Serbia and North Macedonia each primarily use dirty, non-sustainable sources for power, while Albania has the luxury of relying mostly on hydropower.

However, state owned companies are the norm with respect to electrical utilities, leaving markets uncompetitive and vulnerable to consistent power outages. Serbia and Macedonia each have heavy reliance on unsustainable energy sources like Coal and Oil, presenting potential future challenges as well.<sup>9</sup>

## Governance

Each of these countries have histories of poor governance and systematic protection for individuals. Judicial systems often make inexplicable decisions when regarding influential individuals, further hampering the potential for healthy democracy and growth in the future. Transparency

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<sup>8</sup> [https://www.oecd-ilibrary.org/education/education-in-the-western-balkans\\_764847ff-en](https://www.oecd-ilibrary.org/education/education-in-the-western-balkans_764847ff-en)

<sup>9</sup> <https://www.iea.org/countries/north-macedonia>, <https://www.iea.org/countries/serbia>

International stated that these nations have powerful heads of state, coupled with dysfunction at other levels of governance, which in turn makes a consistent and strong justice system difficult. Other actors in their respective countries are not equipped with the necessary resources to provide oversight.<sup>10</sup>

However, the governments of each nation have made serious commitments toward decentralization and reform. The Planning and Local Governance Project (PLGP) was a partnership between USAID and the Government of Albania (GoA) to decentralize governance and allow for more efficient local borrowing. This was successful, with many regions experiencing a 20-30 percent growth in tax revenues, as well as resulting in the creation of “one-stop shops” for local administrative issues.

## Issues that especially affect Albania

Albania ranks much lower in several categories than the other two countries. While Serbia and North Macedonia rank 9<sup>th</sup> and 15<sup>th</sup> in the world with respect to construction permits, Albania ranks 166<sup>th</sup>. When deconstructing the factors mentioned in Doing Business, the timeframe required is over three times as long, while costs as a percentage of warehouse value are almost twice as much.

Similar yet smaller disparities occur in protecting minority investors, registering property, and paying taxes. This implies that Albania is lagging in many crucial factors necessary for a healthy private sector. These seem to show a specific need for reforms in Albania, which may help with inter-regional trade as the other two countries gain access to a better functioning market. Moreover, Albania was hit with a 6.4 magnitude earthquake in 2019, which caused 844 million Euros worth of damage, as estimated by the Albanian government.<sup>11</sup>

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<sup>10</sup> [https://images.transparencycdn.org/images/NISWBT\\_EN.pdf](https://images.transparencycdn.org/images/NISWBT_EN.pdf)

<sup>11</sup> <https://balkaninsight.com/2020/02/05/earthquake-reconstruction-would-cost-more-than-1-billion-albania-gov-says/>

## Other Possible Paths Forward

The European Commission has published Economic Reform Programmes for each of the Western Balkan nations for the time period of 2021-2023. Both Serbia and Albania weathered the COVID-19 better than expected, while North Macedonia saw its economy contract after a period of growth. Each of the economies are expected to rebound towards pre-crisis levels of consumption, before reverting to traditional growth rates around 4-6%. In each, timely fiscal and policy measures were taken which protected their potential for future growth, with high government expenditures projected to be replaced by broad, private sector activity.

Key points of improvement necessary for robust future growth include the education system, transparency in fiscal policy and private sector support, general policy, and governance reforms, and reducing the size of informal economies. Addressing any one of these issues may present a viable, incremental change that can further economic development and private sector growth in the Western Balkans.

From IDG's perspective, potential future projects might include a focus on continuing to help firms integrate into the international market, with special emphasis on the EU. Previous projects have seen success from connecting firms with international businesses. Engaging younger individuals and providing them opportunities to get into the workforce may help avert them from the informal economy, while finding ways to improve the education system may help future generations more broadly. Possible interventions to the education system would involve making the system more equitable, focusing on regions with underperforming schools as well as rethinking assessments and teaching.

Further help is required by domestic firms as the market integrates, with serious issues arising from the competitive nature of the EU market. Assisting businesses adhere to the rigorous standards and regulations involved presents a way to improve integration and development into the future. Assisting with regional governance in the face of decentralization efforts may improve regulatory environments and



allow for more targeted assistance of SME's, while also strengthening democracy and anti-corruption measures in the region. Assisting Serbia and North Macedonia in renewable energy production, notably hydropower, may also provide future benefits in terms of carbon emissions and sustainability.

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## Annex: Visuals

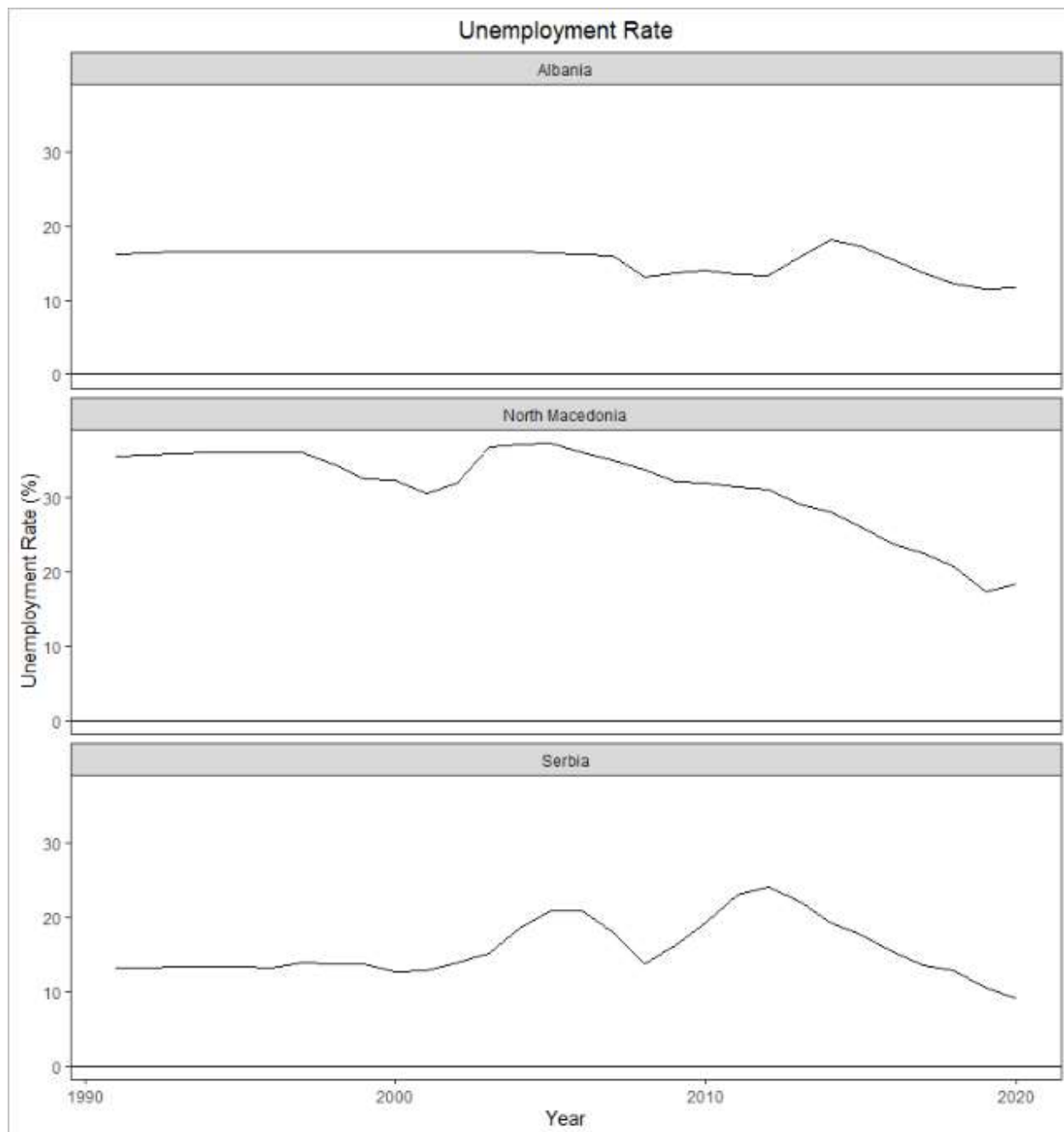


Figure 1 Unemployment rates by country, Source: <https://data.worldbank.org/indicator/SL.UEM.TOTL.ZS?locations=RS>

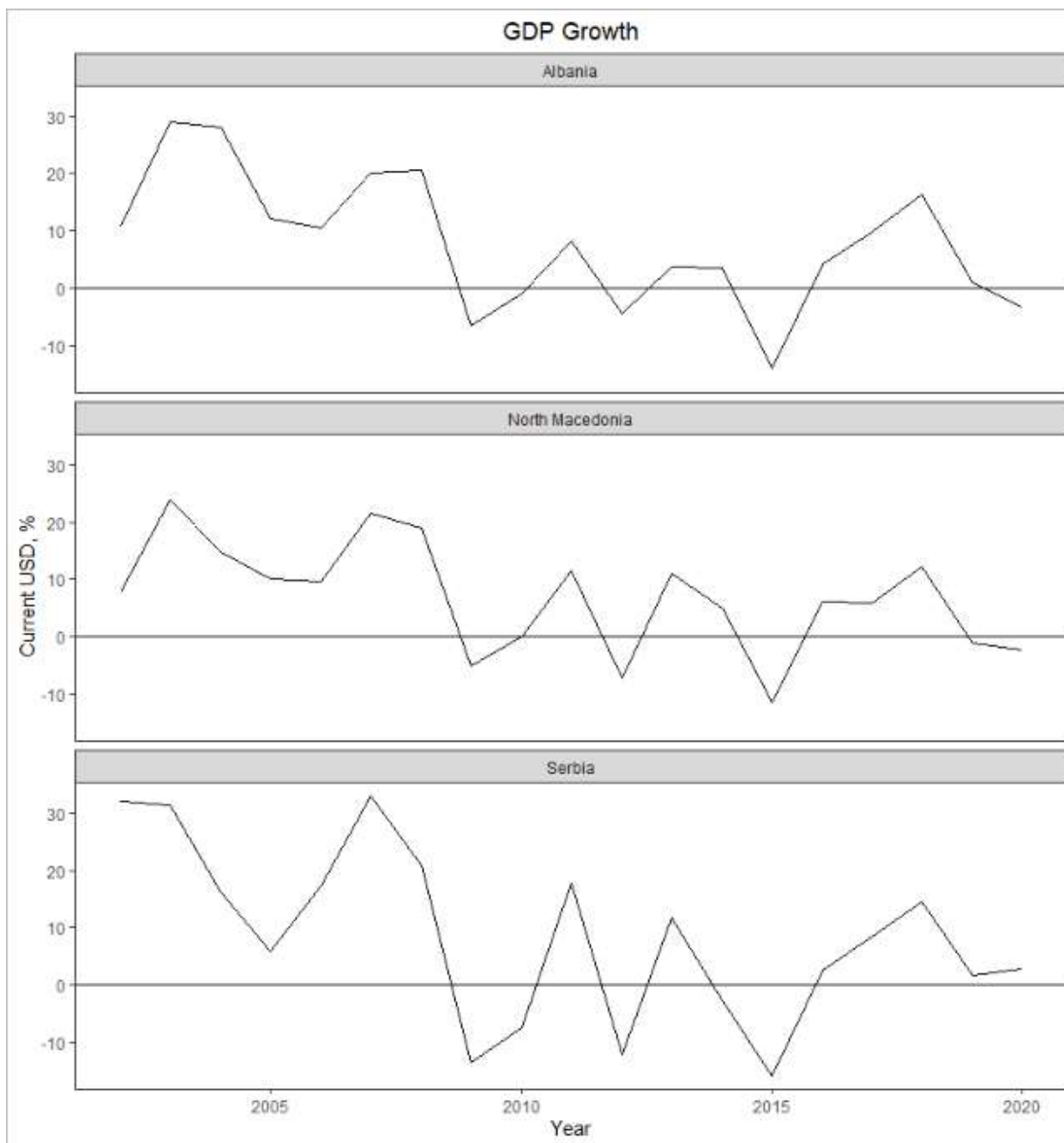


Figure 2 GDP growth by country Source: <https://data.worldbank.org/indicator/NY.GDP.MKTP.CD>

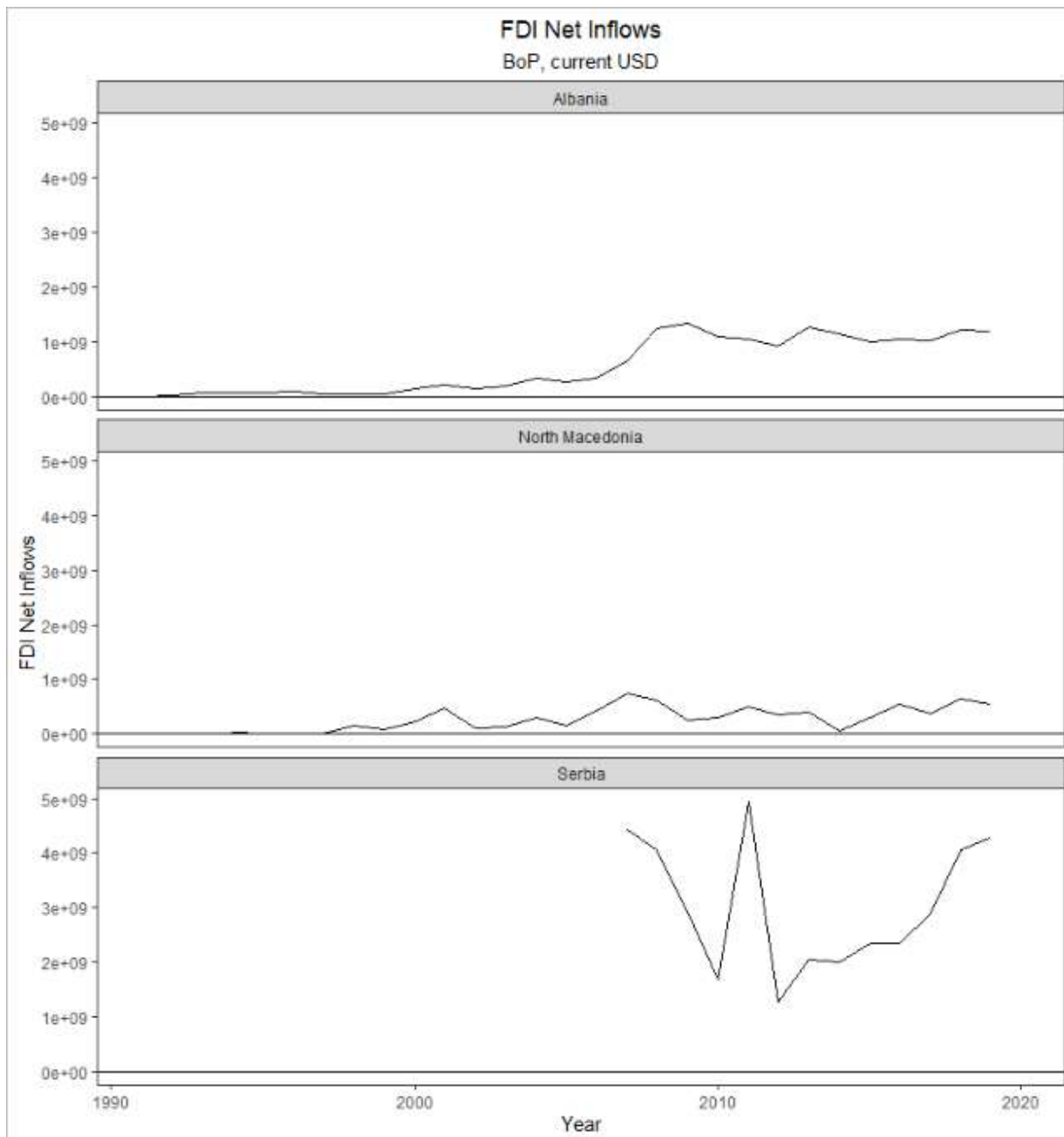


Figure 3 Source: <https://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD?locations=RS>

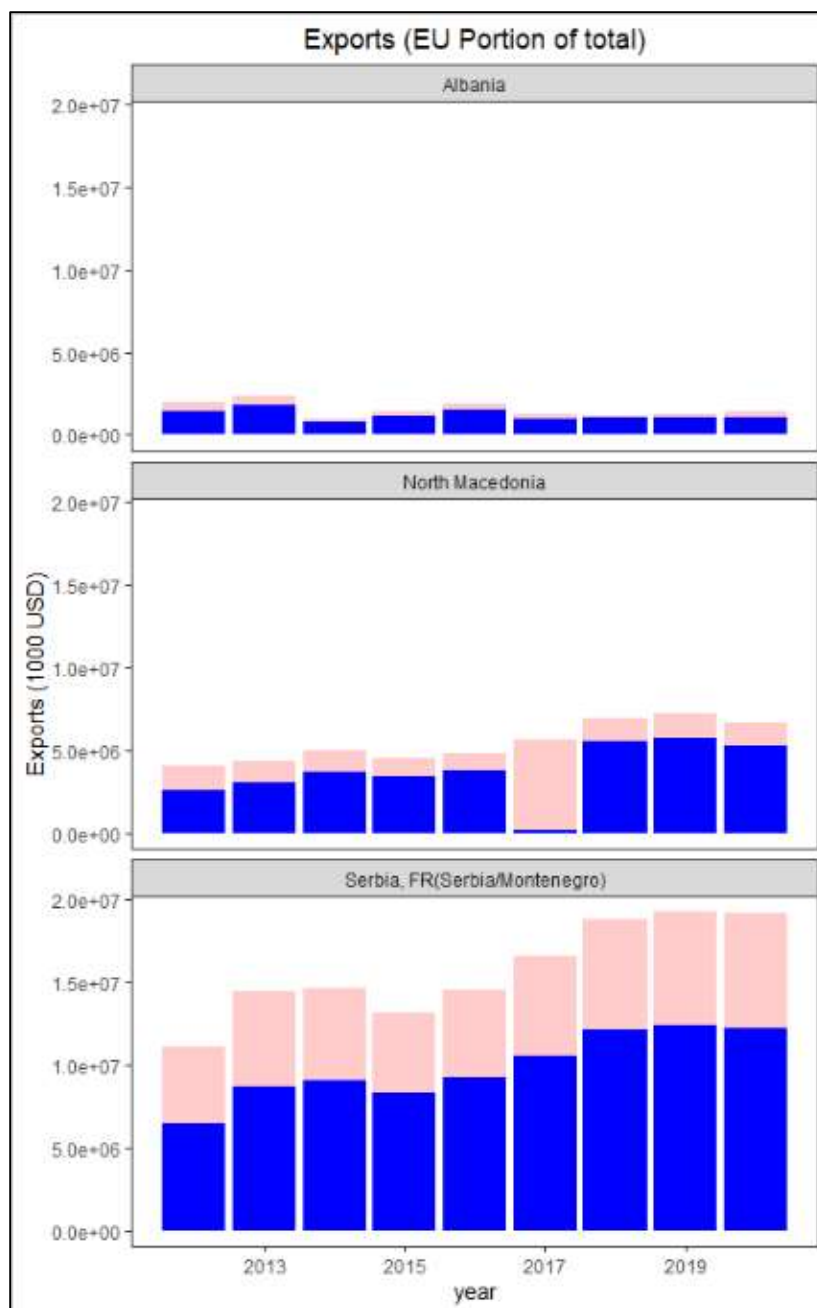


Figure 4 Source: WITS World Bank Database <https://wits.worldbank.org/default.aspx>