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Regional Trade and Investments Integration Results within the South East Europe 2020 Strategy⁵

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Abstract: *The aim of this paper is to analyse the level and the dimensions of implementation of trade and investment integration targets in South East Europe (SEE) 2020 Strategy in SEE countries (Albania, Bosnia and Herzegovina, Croatia, Kosovo, Macedonia, Montenegro and Serbia). The main defined targets in SEE 2020 Strategy are to increase the intra-regional trade in goods more than 140% and to increase the overall Foreign Direct Investments (FDI) annual inflow to the region by at least 160%. Regional cooperation is one of the essential factors that should create new relations in SEE, enabling political stability and economic development, as an important preconditions for the countries in their EU accession process. The research methodology for this paper is a comparative analysis of quantitative data and review of the last years' published official reports and scientific articles. Authors will provide updated situation overview in the countries of SEE with critical analysis of different respective actions and projects needed for achieving the SEE 2020 targets for the Integrated Growth Pillar. This research*

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adds value as a scientific research in the area of trade and investments and provides recommendations for further policy makers' activities.

Keywords: *South East Europe 2020 Strategy, trade, investment, economic growth, competitiveness, integrated growth.*

Regionalni trgovinski i investiciono-integracijski rezultati u okviru Strategije Jugoistočna Evropa 2020

Sažetak: *Cilj ovog rada je da se analizira nivo i dimenzije sprovođenja trgovinskih i investiciono-integracijskih ciljeva u Strategiji Jugoistočna Evropa (JIE) 2020 u zemljama Jugoistočne Evrope (Albanija, Bosna i Hercegovina, Hrvatska, Kosovo, Makedonija, Crna Gora i Srbija). Glavni ciljevi definisani Strategijom JIE 2020 su povećanje intraregionalne trgovine robom preko 140% i povećanje ukupnog godišnjeg priliva Stranih Direktnih Investicija (SDI) u regionu za najmanje 160%. Regionalna saradnja je jedan od važnih elemenata u stvaranju novih odnosa u Jugoistočnoj Evropi, koja će doneti političku stabilnost i ekonomski razvoj, koji su važni preduslovi za zemlje ovog regiona u njihovom procesu pristupanja EU. Metodologija istraživanja ovog dokumenta je komparativna analiza kvantitativnih podataka i pregled proteklih godina objavljenih zvaničnih izveštaja i naučnih članaka. Autori će obezbediti ažurirani pregled situacije u zemljama Jugoistočne Evrope sa kritičkom analizom različitih odgovarajućih akcija i projekata neophodnih za postizanje ciljeva Strategije JIE 2020 za stub integrisani rast. Ovo istraživanje ima dodatnu vrednost kao naučno istraživanje u oblasti trgovine i investicija i daje preporuke za dalji rad kreatora politike.*

Ključne reči: *Strategija Jugoistočna Evropa 2020, trgovina, investicije, ekonomski rast, konkurentnost, integrisani rast.*

1. Introduction

Seven South East European countries (Albania, Bosnia and Herzegovina, Croatia, Kosovo, Montenegro, Serbia and the Republic of Macedonia) under auspices of the Regional Cooperation Council (RCC) have developed and adopted the South East Europe 2020 Strategy ('SEE 2020' or 'Strategy'), in November 2013. This strategy is a document of commitment and interest for political and economic cooperation of the region in order to enable economic growth of the countries, as well confirming and emphasizing the importance that these countries are interested in European perspective. All countries not only geographically, but also economically are linked with the European Union (EU) economy and see their future within EU.

The SEE Strategy followed the concept of EU's Europe 2020 Strategy, in terms of the issues addressed and the concept of enhancing cooperation of the region in areas that are of common interest.

SEE Strategy 2020, outlines approach and sets out a vision for a new development pathway that is focused on economic growth and greater prosperity, as well strengthening the ties with the EU.

In accordance to Kersan-Škabić I. and Tijanić L., (2009), the vision of the SEE Strategy and their targets are based on bigger regional cooperation necessary to develop capacities in order to compete with other larger markets. In this way, the stability and prosperity of the region will be secured.

2. Literature review

Further political and economic cooperation of the region as it is stated in the SEE 2020 Strategy should stimulate the key long-term drivers of growth such as innovation, skills, FDI and the integration of trade. The SEE 2020 Strategy is centred on a set of five interlinked pillars: integrated growth, smart growth, sustainable growth, inclusive growth, within a good governance framework. They are followed by 11 targets as numerical values for these dimensions and 77 national targets.

The integrated growth pillar focuses on regional economic integration through increased trade and investment flows. The smart growth pillar aims to upgrade human capital and foster a knowledge economy in the region, the sustainable growth addresses issues pertaining to the environment and national competitiveness, including infrastructure. The inclusive growth tackles employment and health issues and governance for growth address the cross-cutting issues including strengthening the capacity of public administration, the rule of law and reducing corruption.

The efficiency of the Strategy is strongly related to the trade increase, so four of the targets (as part of overall targets and within different pillars) are showing the increase of trade in different aspects as an indicator for competitiveness, growth and prosperity of the region: Total trade in goods and services in million EUR; Trade balance % of GDP; Intra regional trade in goods in million EUR; Exports of goods and services per capita. The progress in all five pillars is required for SEE economies to reach the overall developmental goals presented in the strategy. To attain these ambitious SEE headline targets, key precondition is the macro-economic stability and prosperity.

2.1. Integrated growth

One of the key pillars related to regional economic integration and economic growth is based on the expectations for increased trade in the region and larger inflow of FDI. Within this pillar under 3 dimensions are promoted actions aimed at: development of free trade area, development of competitive business environment - increasing FDI and further integration of the region into the European and global economy. The headline targets are ambitious, so by 2020 the region should achieve the following:

- Increase SEE intraregional trade in goods by more than 140% (from 12459 million EUR, to 30500 million EUR)
- Increase by at least 160% the overall annual FDI inflows to the region (from 3396 million EUR to 8800 million EUR)

Being among the SEE 2020 priorities and prerequisites for growth, the SEE region must establish a free and open investment regime by removing intra-regional investment barriers, facilitating the free flow of goods, services, and human capital, pursue policies that support the attraction and inflow of FDI, as well as intra-regional investments, and promote further integration of the regional markets. The removal of barriers to regional trade and investment offers the opportunity for economies of scale, geographically diversified businesses, and an overall more efficient allocation of resources within the regional markets.

At the firm level, this means the potential for investor subsidiary networks, as firms seek efficiency gains through a fragmentation of their production process allocating individual segments of value addition in places of comparative economic advantage. Progressive liberalization of cross-border transactions reduces time and cost to trade and invests within a region. It fosters development of regional value chains and leads to increased diversification and sustainability of economic growth.

2.2. CEFTA 2006 focus

Main goals of CEFTA 2006 are to increase the intra-regional trade and competitiveness of the region as a whole. CEFTA 2006 provides a much more comprehensive framework for development of mutual relations and economic cooperation among the SEE countries and builds their competitiveness (Petrevski, 2013). This conclusion is based on the fact that it encompasses a much larger number of issues than the individual bilateral agreements that were regulating this area to present, as well as than the original CEFTA. The new opportunities for cooperation pertain to the following areas: trade in goods and services, investments, public procurement and protection of intellectual procurement.

CEFTA 2006 opens opportunities for development of cooperation among its members so as to achieve progressive liberalization and mutual opening of their markets for preferential access. It also provides opportunities for initiating concrete negotiations for liberalization of the trade in services among the members. CEFTA 2006 mandates that its members shall encourage mutual investment initiatives through promotion of the conditions and shall facilitate investment administrative procedures in order to create a transparent regional environment for the investors. In this context, members are obligated to provide a just and equitable treatment, as well as full protection and security for investments coming from other members, that is to provide them with the same favourable treatment as for domestic investors and investors from third countries. In order to avoid any contradiction with the existing international agreements, CEFTA 2006 provides that its provisions on investments shall not affect nor disturb the relations among its members previously agreed with the bilateral agreements governing investments.

2.3. FDI as a driver for economic growth

Attracting FDI is one of the key strategies and pillars for enabling economic growth. They contribute to creation of jobs especially in times of great crisis, it enables inflow of new skills, knowledge and technology spillovers, diversification of export, boost aggregate productivity and raise GDP growth, etc. The countries from SEE region also identified attracting FDI as one of the key pillars in the development strategies. The competition between SEE countries for attracting FDI is strong.

In general the level of FDI inflow of the country is indicator that shows the attractiveness of the market, favourability of the business environment, stability of the economy, realized reforms, potential of the market for growth and access to other markets, availability of attractive and free capacities, incentives that are offered as well efficiency of the promotion activities in order to convince the investors to come in the country. There are also other factors like: geographical factors (size of the market, landlocked vs. sea side), existing natural resources, industries and facilities, quality and price of the labour force, political stability, predictability of the economy etc. Foreign investments are coming in the region through privatization process especially in Bosnia and Serbia, where this process still is not completed, as well by so called brownfield and Greenfield investments, investments in free economic zones or by increasing the capacities of existing investments.

According to Mehic et al. (2013), one of the key objectives of the governments of transition economies in the course of transition has been attracting FDI. The government policies focus on regulatory frameworks by removing legal barriers and regulatory obstacles to foreign capital inflows as well institutional settings by creation of public agencies to promote and attract FDI. The

governments in order to attract FDI offer set of fiscal privileges like tax concessions, tax exemptions.

FDI policies in the region are focused on improving investment environment; active promotion, image building, creation and promotion of free economic zones and industrial zones and parks.

3. Research methodology

The research methodology is a comparative analysis of quantitative data and review of the last years' published official reports and scientific articles. The following part analyses the sustainability of targets and ability for fulfilment, by country and as a region. The targets that are given in the SEE 2020 Strategy are for 2020, and the baseline data is for 2010. Within the process of collecting data for FDI from different sources, it can be concluded as a general remark that FDI statistic data are not unified in: Vienna Institute for International Economic Studies (WIIW), United Nations Conference on Trade and Development (UNCTAD), World Bank (WB) sources etc.

Table 1. FDI by countries in mil. EUR - SEE 2020 and Baseline data

Country	2010 - baseline	2011	2012	2013	2020 - target	% of growth 2020/2010
Albania	793	717	727	741	2200	177
Bosnia and Herzegovina	174	342	273	320	500	187
Croatia	326	1087	1066	437	1500	360
Kosovo	366	379	213	286	800	119
Macedonia	160	337	72	252	600	275
Montenegro	574	495	634	479	700	22
Serbia	1003	1827	242	756	2500	149
Total	3396	5184	3227	3271	8800	160

Source: SEE 2020 Baseline Report, Towards Regional Growth, 2014, Publisher, Regional Cooperation Council, page.89, and authors calculations

The SEE countries have identified different targets for FDI inflow in 2020 presented in the table 3. The expected average growth of FDI in the region is 160%, the lowest projections are recorded by Montenegro 22% of growth, and highest expectations were projected by Croatia 360% and Macedonia of 275% growth. The indicator for overall FDI inflow is based on one-off annual data and therefore it is difficult to extrapolate a clear trend. Actual data for FDI up to 2012/2013 shows slower than expected convergence towards the 2020 targets. The annual values for FDI for 2010-2013, compared to the 2020

targets, seem to be very ambitious. The regional 2020 target inflow is 169% higher than the 2013 inflow.

Most of the FDI into the region is coming from the EU. The risks for achieving the projected amount of FDI are possible EU and World recessions, EU internal problems, political instability in SEE region, worsening the image of the region, etc. Having compared the targets it seems that Montenegro will attract much more FDI than it was projected, while Macedonia has projected too ambitious number.

4. Results and discussion

Statistical data in Table 1 regarding total trade of SEE countries by 2012/2013 shows that the convergence towards the 2020 targets is slower than expected. For example, the increase of total trade annually in the period 2010/2013 is by 7%, 1.5% and 2%, while the gap between the projections for 2020 in relation to 2013 is very large, 100%. Difference according to the trend in the first three years of implementation of the Strategy SEE 2020 is difficult to be realized.

Table 2. Total trade of goods of SEE countries (Eur. Million)

Country	2010	2011	2012	2013	2020
Albania	7695	8154	7596	7498	17500
Bosnia and Herzegovina	12138	11418	11323	11609	24500
Croatia	35400	37092	37752	36701	80000
Kosovo	3321	3681	3576	3573	6000
Macedonia	7834	9670	9683	9747	15500
Montenegro	3118	3489	3555	3530	6000
Serbia	24907	27557	29093	32004	60000
Total	94413	101061	102578	104662	209500
% of increase of total trade annually		+7	+1,5	+2	

Source: CEFTA intra-regional trade, <http://www.cefta.int/statistics>

Around 14% of total SEE countries trade volume is intra-regional trade. In Table 2, intra-regional trade showed increase in 2011, but then a slight decrease in 2012 and 2013. There is a very large gap between the 2013 value and 2020 target of 120%. The country-by-country comparison shows that the 2020 targets compared to 2012 projected growth between 102% in

Republic of Macedonia and 170% in Serbia. The growth is projected very high for all economies, except for Montenegro, which has modest 15% gap between 2012 and 2020 target.

Table 3. Intra-regional trade of goods of SEE countries (Eur. Million)

Country	2010	2011	2012	2013	2020
Albania	425	509	533	497	1150
Bosnia and Herzegovina	3100	3450	3231	3297	7100
Croatia	2474	2809	3004	2860	6200
Kosovo	872	955	946	853	2000
Macedonia	1243	1452	1336	1239	2700
Montenegro	800	1003	1040	984	1200
Serbia	3544	3818	3755	3837	10150
Total	12458	13996	13845	13567	30500
% of increase/decrease of total trade annually		+12	-1	-2	

Source: CEFTA intra-regional trade, <http://www.cefta.int/statistics>

The main objectives for development should focus on deepening the free trade area; implementation of further trade facilitation and improving intra-regional trade as well increasing the attractiveness of the region as a destination for FDI.

4.1. Analyses by countries

Albania projected growth of FDI for 177% from 793 million EUR in 2010 to 2200 million EUR in 2020. For the period 2010-2013 Albania have registered strong and stable inflow of foreign investment on average 745 million EUR, but they are far from the target of 2200 million EUR. The investments were mainly FDI in the energy sector. The projections of the WIIW are that FDI will slightly increase in the next period. Some of the additional FDI should be related to hydropower plant projects, as Holzner recognizes (2014). Albanian Investment Development Agency recognizes that Albania focuses on creation of favourable and attractive investment climate.

Bosnia and Herzegovina projected growth of FDI by 187 %, from 174 to 500 million EUR in 2020. The inflow of FDI in period 2010/2013 was on average 277 million EUR with some fluctuations due to privatization process, internal and external factors. However, if we take into account on-going projects, even with lower values of FDI in previous two years, we can be optimistic regarding

future FDI growth. Additional investments are expected in the energy sector due to the construction of a new and revitalization of the existing facilities and plants. Non-privatized state-owned capital, which is intended for sale, is estimated to 5 billion EUR in the sectors: energy, mines, telecommunications, etc.

Kosovo projected growth of FDI by 119%, from 366 million EUR to 800 million EUR. The average growth for the period 2010/2013 is 311 million EUR. This amount is also far from the projected 800 million EUR. FDI in 2013 increased by 15% and make some 286 million euro for the year. The largest part of the increases in FDI occurred in the transport sector. Further infrastructure investment was announced, such as in modern electric power grids and roads. In particular, the development of Kosovo's highway network is being pushed by the government. Holzner (2014) elaborates that in early 2014 the FDI was launched for construction of motorway projected for 600 million euro within 42 months. Diaspora will have a significant role in increasing the FDI inflow.

Macedonia projected growth of FDI by 275%, from 160 million EUR in 2010 to 600 million EUR in 2020. The 2020 target is very ambitious projecting a growth of 138% by 2020 in comparison to the 2013 value. The target is stated in the Governmental program, where one of the key pillars for economic growth was improving the business climate and attracting FDI. The Government realizes their program by nominating ministers for FDI, nearly 30 promoters abroad and leading very intensive promotional campaign in the international media and road shows headed by the highest governmental officials. FDI are coming mainly in the free economic zones. Companies that are active in free economic zones in 2014 have registered more than 1 billion EUR export. The 2015 projections indicate the increase of 10-15% export. Foreign Investors Council in Macedonia in the White Book (2014-2015), elaborates that after their strong decline in 2012, FDI inflows strengthened again in 2013 and, including reinvested earnings, accounted for some 3.2% of estimated GDP at the end of the year. The government has been pursuing a strategy of attracting foreign direct investment in higher-value added sectors, and, at the same time, supporting local companies in developing the necessary skills to work as suppliers to the foreign facilities. While there was some indication of a shift in the FDI structure in 2013, exports have diversified only incrementally from commodities to chemicals and manufactured products with higher value added, such as machinery and electronics, and local sourcing remains limited, as a result of lengthy licensing procedures, and often missing skills and capacities required by the foreign companies.

Montenegro projected growth of FDI by 22%, from 574 in 2010 to 700 million EUR in 2020. On average the annual FDI inflow in the period 2010/2013 is 545 million EUR. Montenegro is implementing the Strategy for attracting

foreign direct investment 2013–2015, based on economic diplomacy. The concept of open market economy, clear EU and NATO perspective give a positive impetus towards attracting more FDI in the country. Montenegro became a leader in Europe according to the level of FDI per capita, for five years in a row. Montenegro has the comparative advantages in tourism, agriculture and renewable energy sectors. The tourism is a sector with great potential, with expected inflow in next period of more than 3 billion EUR of FDI. Agriculture also has big potential for development and attracting FDI.

Serbia projected growth of FDI for 149 % from 1003 to 2500 million EUR in 2020. Serbia attracted some 1.8 billion EUR of foreign direct investments in 2011, registering 80% growth compared to 2010, and with this amount became the best performer in SEE. According to the World Bank SEE Regular Economic Report (2012), 2011 was an exceptional year for FDI. Namely, FIAT's had large investment in the auto industry in Kragujevac and the FDI of Belgium Delhaise was nearly EUR 1 billion. According to Ernst & Young, European attractiveness survey (2013), nearly 90% of projects in Serbia came from European countries. In the latest Ernst & Young, European attractiveness survey (2014), Serbia was ranked among top 15 countries by FDI projects. As a potential for FDI is a new Privatization Law that was enacted in August, setting the end of 2015 as a deadline for completing the privatization process. More than 500 companies are subject to sale. Net FDI inflow of EUR 1.3bn was recorded in 2014. According to National Bank of Serbia, FDI at EUR 1.3 billion is projected for 2015. Major part of inflows will target the manufacturing and trade sectors, excluding potential privatization proceeds, some of which have been announced for 2015 (Macroeconomic Development in Serbia, 2015).

5. Conclusions

Analysing the data for trade in the region after the adoption of the SEE 2020 targets, and comparing the baseline data we can conclude that:

- The SEE Strategy 2020 target was to increase SEE intraregional trade in goods by more than 140%, from 12.46 billion EUR in 2010 to 30.5 billion EUR by 2020. The projected growth is too ambitious for some countries.
- CEFTA is the dimension coordinator and main driver for actions in this pillar, related to increased level of intra-regional and global trade.
- Mutual trade cooperation in SEE countries can further be enhanced by greater activity of business associations and chambers of commerce of the countries in order to improve the opportunities for bigger economic cooperation and increased intra-regional trade.

Analysing the data for FDI inflow in the region after the adoption of the SEE 2020, and comparing the baseline data with the targets we can conclude that:

- The SEE Strategy 2020 target was to increase the FDI levels from 3.4 billion in 2010 to 8.8 billion by 2020. It may imply that for some countries the 2020 targets are too ambitious
- Due to the global economic crisis, weak Euro zone economy and some internal factors, the region has so far performed well under the expectations; Actual data are showing heterogeneous country experiences, relatively small progress or reverse trends in 2010–2012/2013. In order to reverse the negative trend, countries will need to implement aggressive measures and to work together.
- SEE countries are relatively small economies that continue to undergo transition and have strong aspirations towards increasing integration into the EU. They compete for investors primarily based on cost efficiency. There is evidence that cost efficiency competition is encouraging the countries to engage in a “race to the bottom” in which they have been progressively offering more generous investment incentives with limited clarity on the opportunity cost.
- Regional integration on investment matters offers opportunities through a higher degree of market integration.
- The removal of barriers for regional trade and investment increases the market size and offers the opportunity for economies of scale, geographically diversified businesses, and an overall more efficient allocation of resources within the regional markets.
- The regional integration efforts lead to increased FDI and intra-regional investments by creating bigger market and attracting market-seeking investments; contributing to the development of stronger and wide-spread regional value chains attractive for efficiency-seeking investments; increasing connectivity among businesses thus reducing risks of conflict; and creating commitment mechanisms that positively influence domestic policy reforms.
- On a national level a favourable investment environment and successful implementation of reforms are vital and key prerequisites for attracting more FDI. Therefore the countries should continue to improve the conditions on national level and take an active role in regional projects and actions for promotion and attracting FDI.

To achieve the SEE 2020 targets it is necessary to increase the integration and collaboration in the region, by exploiting all potentials. Key areas should be focused on increasing the trade facilitation, liberalization and integration. The countries of the region are individually competing for FDIs but they also have to collaborate in order to attract more FDI in the region. By creating and

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promoting bigger market it will result with attracting market-seeking investments that will contribute too to the development of stronger and wide-spread regional value chains attractive for efficiency-seeking investments too. This will influence on re-branding the image of SEE.

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