

STABILIZATION AND ASSOCIATION AGREEMENTS IN THE WESTERN BALKANS: MANAGEMENT CHALLENGES OR ECONOMIC GROWTH?

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ABSTRACT According to EU enlargement policy, the main objective of the Stabilization and Association Agreements (SAAs) is not only economic growth and export promotion, but also law enforcement, including various market reforms. In addition to SAAs, the European Union (EU) also supported the Balkans with bilateral Free Trade Agreements (FTAs), followed by general trade preferences and multilateral free trade agreements (CEFTA 2006). This paper examines whether SAAs have been able to accelerate export growth, investment and economic development in the Western Balkans. Based on an empirical analysis of panel data, the main findings confirm that SAAs have not been sufficient to increase exports and consequently reduce the trade deficit of the Western Balkan countries. In addition, a special section is dedicated to Kosovo's management issues, such as firm development, export promotion, the relationship between management characteristics and export performance and other relevant topics, as Kosovo is the last country in the Western Balkan that is still implementing an SAA.

KEYWORDS: *Stabilization and Association Agreements (SAA), Western Balkans, EU, Management, trade.*

1. INTRODUCTION

The post-war transition in the Balkans has been rapid and extreme due to the political and institutional challenges facing the region. Since the countries of the Western Balkan (WB) were not institutionally prepared for the radical challenges of liberalization and democratization, political, social and economic reforms have taken a long time. The EU has institutionally supported the economic and political stability of the WB countries. Free trade agreements were concluded with the help of the EU. In doing so, the EU has supported political and institutional cooperation aimed at reviving economic growth and achieving long-term peace in the region. Although the EU's Free Trade Agreements have been proclaimed successful,

their implementation has shown that trade liberalization is not sufficient for economic development.

According to Qorraj (2010), CEFTA 2006 was the first practical step to measure or test regional cooperation in the region. To overcome the challenges associated with the functioning of CEFTA, countries also attempted to adopt European standards for production and trade. Authors such as Schiff and Winters (2003), Kaminski and De La Rocha (2003) and Trivić and Klimczak (2015) have reported that regional trade agreements have not been effective for economic growth. The SAA forms the relationship between the EU and the Western Balkans for the implementation of the Stabilization and Association Process. According to the European Commission (2020), these agreements are designed according to the specific

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situation of each partner country.

In addition, the agreements within this framework provide institutional support for the implementation of the integration path and have brought the countries of the Western Balkans closer to the EU by strengthening economic and institutional relations with the EU institutions. One of the most important points of the agreement is the commitment of the WB countries to accelerate reforms and thus alignment with the EU *acquis* and to continuously advance market reforms. The EU is the most important trading partner and by far the largest investor in the Western Balkans. However, most WB countries have trade deficits in their relations with EU countries. It is evident that local businesses in the Western Balkans have not yet fully exploited the opportunities offered by SAAs (Međak, 2018).

This article begins with a literature review of trade liberalization in the Western Balkans. It also analyzes the impact of SAAs on various economic indicators. In addition, it will address the management challenges that limit the benefits of SAAs.

The paper will test the following hypotheses:

- H1: SAA agreements could increase the volume of trade and foreign direct investment (FDI) in WB.*
H2: SAA agreements could accelerate EU reforms despite political challenges in the region.

2. THEORETICAL BACKGROUND: TRADE LIBERALIZATION AND REGIONAL RECONCILIATION

The question of whether free trade promotes economic development is one of the key questions in economics and has yet to be decisively answered by existing theories. Authors such as Grossman and Helpman (1990) analyzed the role of the external environment, trade and industrial policy in determining long-term growth rates. Sachs and Warner (1995) presented evidence for less developed countries and their economic policies. Greenway and Sapsford (1994) analyzed the efficient allocation of resources that can lead to higher growth through trade liberalization, while Rodrik (2003) analyzed the social and economic side of trade liberalization. However, these authors were not able to draw definitive conclusions about the impact of free trade on economic development.

Ocampo and Taylor (1998) and Frankel and Romer (1999) claimed that the geographical characteristics of countries are important determinants of their success in trade and that the impact of trade liberalization can therefore only be understood through

an institutional and historical analysis at the country level. These authors argued that trade liberalization contributes to economic growth. According to Harrison (1996) and Tavares and Wacziarg (2001), greater openness is associated with higher growth, while trade openness affects development mainly through an increase in domestic investment relative to GDP. They also argue that trade liberalization is an important determinant of export promotion, even if its effect varies from country to country.

These authors argued that trade liberalization had the potential to boost economic growth. The impact of free trade on imports, particularly in developing countries, has been the subject of studies by authors such as Melo and Vogt (1984), Bertola and Faini (1990) and Santos-Paulino (2002). Different countries are generally able to pursue development policies geared towards restrictive trade, allowing them to replace domestic production with imports. In addition, the new trade theories focus on economies of scale and external linkages. Proponents of these new theories, such as Ethier (1982), Helpman and Krugman (1985) and Brander and Spencer (1984), have reported that protectionist measures should be used for certain "infant" industries so that these industries can dominate the world market.

Another issue that various authors have examined is the impact of free trade agreements and trade liberalization on FDI. Raff (2004), Waldkirch (2008) and Moon (2009) analyze the impact of Free Trade Agreements (FTAs) on vertical FDI. From another perspective, trade liberalization is often seen as a first step towards political integration and reconciliation. This is particularly important for the Western Balkans, where countries could improve political relations with their neighbors mainly through trade and economic cooperation (Qorraj, 2016).

Authors such as Bartol and Bennik (2004) believe that reconciliation is a social outcome based on structural and social issues, such as the development of free trade, cooperative economic projects and other economic activities. Gündüzet al. (2006) have extended these studies by examining the role of the private sector in reconciliation between countries. In this case, the private sector could support peacebuilding and economic cooperation and thus reduce conflict-related market failures. Paszkiewicz (2012) argued that since the WB is a small market with low economic development, it needs to intensify its cooperation, also considering the low industrialization in these countries; trade liberalization has brought limited economic growth but supported regional cooperation between these countries.

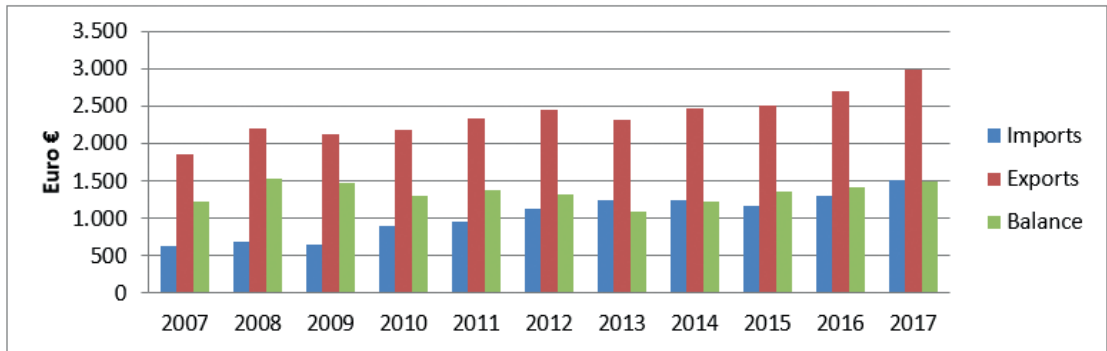


FIGURE 1. EU-North Macedonia Trade 2007-2017 in Euros (Millions)

SOURCE: European Commission and state statistical office of North Macedonia online data

3. THE EU- SAA AND WESTERN BALKANS

The EU concluded SAAs with all WB countries between 2001 and 2016. In addition to providing a legal instrument for aligning the laws of these countries with those of the EU and supporting the countries in implementing the necessary reforms, the SAA promotes trade flows and political stabilization in the region. In addition, the EU created the Interim Agreements between the EU and the WB countries by lifting restrictions with few exceptions (European Commission, 2018).³ The following sections describe the impact of these agreements on various WB countries.

3.1 North Macedonia

With the signing of the SAA, the EU lifted all trade restrictions with North Macedonia, except for wine and beef.⁴ North Macedonia also lifted all restrictions on most products imported from the EU (Tosevska, 2007).

Figure 1 shows EU exports to North Macedonia and EU imports from North Macedonia. Like other WB countries, North Macedonia has a negative trade balance with the EU; however, compared to other countries in the region, export growth is faster. However, the analysis of the above data shows that North Macedonia's export growth has been slower than its import growth. Even in recent years, North Macedonia has recorded a higher trade deficit with the EU despite its export growth. According to Samonikov and Veselinova (2013), North Macedonia was an attractive

country for foreign investors thanks to its comparative advantages, provided it pursued well-designed and effective policy.

However, between 2007 and 2017, FDI in North Macedonia fluctuated significantly (Table 1). In terms of GDP, the global financial crisis severely impacted the country's economic growth after 2007 (Table 1). Looking at North Macedonia's economic growth between 2007 and 2017, it can be seen that SAAs have accelerated the positive effects. North Macedonia had the largest growth trend in 2007, but since then the effects of the global financial crisis have significantly affected this growth.

3.2. Albania

In 1999, the EU liberalized trade with Albania under the Autonomous Trade Preferences, while in 2009 the SAA came into force⁵. In addition, Albania committed to a gradual reduction of tariffs until 2019, when all industrial tariffs will be liberalized (Zahariadis, 2007). Figure 2 shows that Albania's exports grew slowly in 2007, 2008 and 2009. In 2009, the country's exports to the European Union decreased significantly due to the crisis that affected all EU countries, especially Italy and Greece, Albania's main trading partners. From 2010, trade with the EU increased again. However, EU imports always exceeded Albanian exports, which further increased the trade deficit.

The 2007 SAAs between the EU and Albania aimed to ensure the free movement of capital for direct investment by companies in the territory of the other party and to create opportunities for the

3 Within the framework of SAA, the EU launched different trade facilitation instruments with the region of WB.

4 North Macedonia was the first country which signed and implemented the agreement. The agreement was signed with North Macedonia during 2001 (Secretariat for European Affairs of Macedonia, 2014).

5 Albania like other countries of the region exploited different trade instruments before SAA implementation.

TABLE 1. GDP Growth and FDI of North Macedonia, 2007-2017

Years	GDP Growth (Annual Percent)	FDI
2007	6,4	733.466.879
2008	5,4	611.688.378
2009	-0,3	259.530.321
2010	3,3	301.441.681
2011	2,3	507.920.732
2012	-0,4	337.911.248
2013	2,9	402.458.309
2014	3,6	60.879.915
2015	3,8	296.604.200
2016	2,8	549.371.101
2017	0,2	380.738.977

Source: The World Bank online data

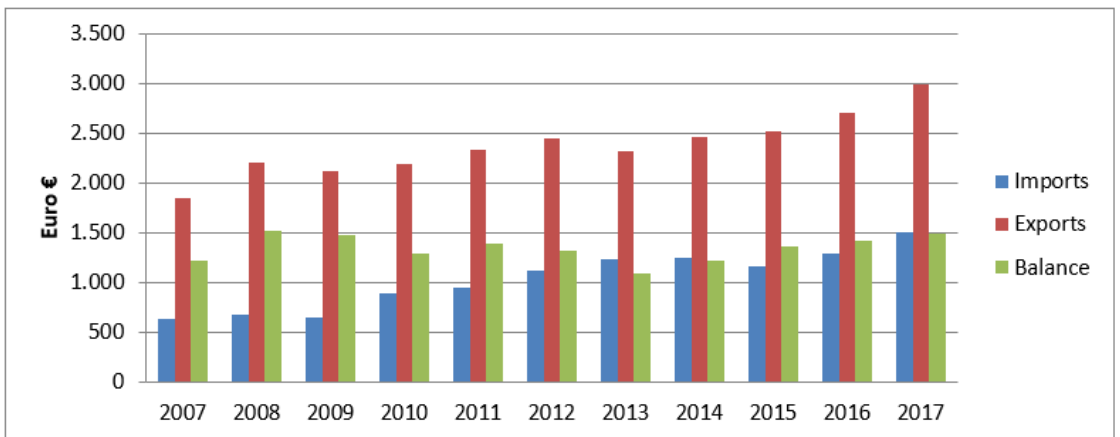


FIGURE 2. EU-Albania Trade, 2007-2017 in Euros (Millions)

Source: European Commission online data

repatriation of these investments and the resulting benefits (Official Journal of the European Union, 2009). Table 2 shows the FDI development Albania since 2008. They follow the same pattern as in North Macedonia. In 2008, Albania's FDI amounted to 1,253 million dollars; in 2012, Albania recorded a decrease in FDI. In 2017, the value of Albanian FDI amounted to 1,022 million dollars. The start of the implementation of the SAA thus had a positive impact on the growth of FDI in Albania.

Albania's growth before the global crisis was one of the highest in the Western Balkans at 5.5 percent from 1997-2008; after the crisis, growth fell to the regional average of 2.4 percent in 2009-2014 (IMF, 2016). These data reflect an unsatisfactory increase

in Albanian GDP growth after the start of SAA implementation. The conclusion is that the global crisis must have affected Albania's GDP growth and that SAAs played only a limited role in the regeneration of growth rates during the implementation process from 2009 onwards.

3.3 Montenegro

Montenegro signed the SAA on October 15, 2007 and it entered into force in 2010 (European Union, 2017). Despite an increase in exports after the signing of the agreement, Montenegro has a constant deficit in foreign trade in goods.

Figure 3 shows the trade relations between the

TABLE 2. FDI and GDP Growth in Albania 2009–2017 in U.S.Dollars

Years	FDI	GDP Growth (Annual Percent)
2007	652.275.603	5,9
2008	1.253	7,5
2009	1.344	3,3
2010	1.09	3,7
2011	1.048	2,5
2012	918.313.370	1,4
2013	1.254	1,0
2014	1.15	1,7
2015	989.278.987	2,2
2016	1.044	3,3
2017	1.022	3,8

Source: The World Bank online data

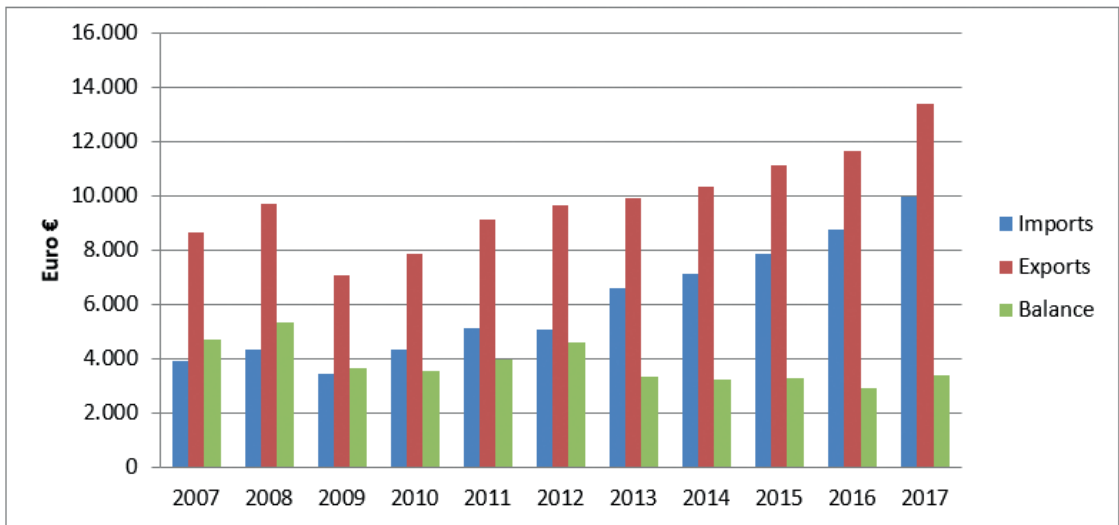


FIGURE 3. EU-Montenegro Trade, 2007-2017 in Euros (Millions)

SOURCE: European Commission online data

EU and Montenegro, i.e. exports and imports. Montenegro is an attractive country for foreign trade in services. The positive trends in foreign trade in services are probably a result of favorable developments in tourism and transport (Bjelić and Dragutinović-Mitrović, 2012). The discrepancy between Montenegro’s trade flows with the EU was relatively small from 2009 to 2011 and widened in 2012 and 2013 (Statistical Office of Montenegro, 2015). The trade deficit decreases in 2013 and remains relatively low until 2017 (European Commission, 2018).

The country has a high share of FDI in the ser-

vices sector; the main investors are Hungary, the UK, Austria, Slovenia and Russia (Government of Montenegro 2006). The FDI structure is mainly influenced by the privatization process and investments in real estate (Gardašević, 2018). Table 5 shows that Montenegro recorded the highest level of FDI in 2009 with 1,549 billion dollars. The FDI trend performed a positive impact on economic growth, as FDI was the main driver of the country’s economic development (Central Bank of Montenegro, 2008). However, the global crisis has affected FDI in Montenegro and the SAA has not had a serious impact on solving this problem.

TABLE 3. FDI and GDP Growth in Montenegro, 2009-2017 in U.S. Dollars

Years	FDI	GDP growth
2007	937.515.441	6,8
2008	975.105.642	7,2
2009	1.549	-5,7
2010	758.407.499	2,7
2011	556.257.883	3,2
2012	618.367.296	-2,7
2013	446.490.330	3,5
2014	496.716.255	1,7
2015	699.736.511	3,3
2016	226.666.592	2,9
2017	560.290.272	4,7

SOURCE: The World Bank online data

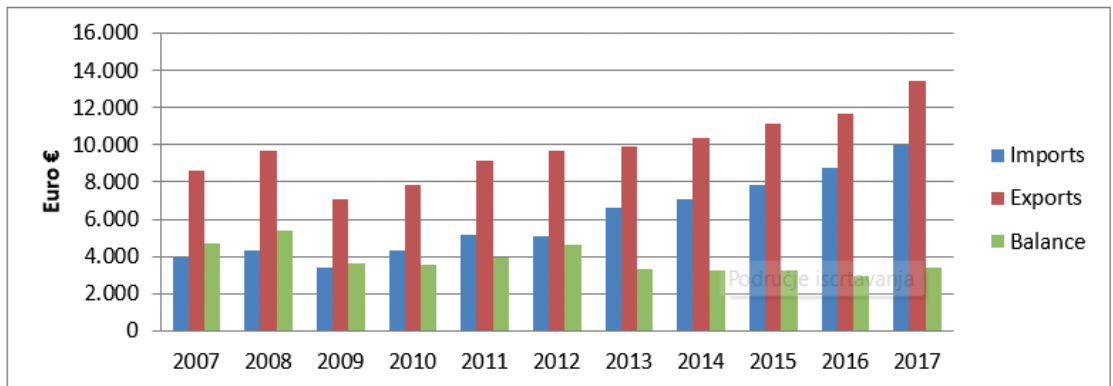


FIGURE 4. EU-Bosnia and Herzegovina Trade, 2007-2017 in Euros (Million)

SOURCE: European Commission online data

Table 3 shows the annual growth of the Montenegrin economy between 2007 and 2017. Montenegro's GDP growth in 2017 was the result of increased work on construction projects in the transport, tourism and energy sectors (Government of Montenegro, 2018). Like Albania and North Macedonia, Montenegro also experienced economic growth that was not due to the result of the SAA, but to other factors such as FDI, the business environment, the tourism sector and other relevant sectors (World Bank Group, 2018).

3.4. Bosnia and Herzegovina

Bosnia and Herzegovina (B&H) experienced constant political and economic crises⁶ due to the lack of

a sustainable political structure. Figure 4 shows the trade relations between the EU and BiH. According to the European Commission report, 2018, B&H faced trade imbalances; due to high imports, the trade deficit amounted to 23.6 percent of GDP in 2017.

Transfer inflows, such as remittances, largely finance the substantial trade deficit. Since the EU market is more competitive than the economy of Bosnia and Herzegovina and the negative impact of trade liberalization as a result of the SAA quickly became apparent, the positive effects could be achieved in the long term (Jerinić, 2017).

Like other signatory states, B&H has committed itself to attracting investment through the SAA. In 2007, the country attracted the highest level of in-

6 Bosnia's SAA came into force on 2015 (Ministry of Foreign Trade and Economic Relations, 2015).

TABLE 4. FDI and GDP growth in Bosnia and Herzegovina 2009-2017 in U.S.Dollars

Years	FDI	GDP Growth (Annual Percent)
2007	1.842	5,8
2008	1.005	5,4
2009	138.511.019	-3,0
2010	443.840.207	0,8
2011	471.610.992	0,9
2012	391.976.946	-0,8
2013	313.295.008	2,3
2014	544.866.345	1,1
2015	383.089.615	3,0
2016	282.754.349	3,1
2017	462.732.353	3,1

SOURCE: The World Bank online data

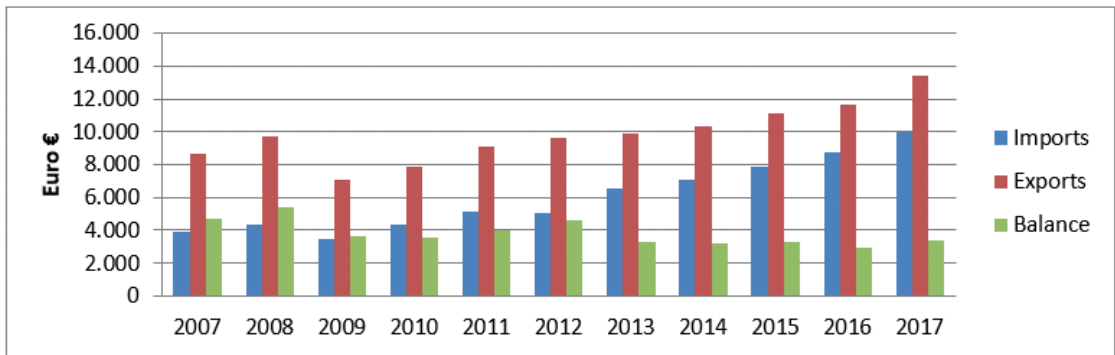


FIGURE 5. EU-Serbia Trade, 2007-2017 in Euros (Million)

SOURCE: European Commission online data

vestment, mainly due to the privatization process of large state-owned enterprises. In contrast, the global economic crisis led to a drastic decline in investment (Foreign Investment Promotion Agency of BiH, 2012). The ethnically and administratively divided status of Bosnia and Herzegovina has prevented a unified economic space, so trade with the surrounding regions has replaced the desired effect of “trade creation” between the entities. Private sector investment and political and social development are essential to the Bosnian economy (The Portland Trust, 2009). As a result, despite international support, B&H has been unable to accelerate sustainable growth due to political challenges.

3.5 Serbia

Due to the Autonomous Trade Measures, the trade balance between Serbia and the EU showed a pos-

itive trend between 2000 and 2008 (Holzner and Ivanić, 2012). According to Mitrović and Bjelić (2012), most of the trade benefits for the WB countries, including Serbia, were realized through the Autonomous Trade Measures.

In 2007, Serbia increased FDI, but over the years the level of FDI started to decrease, although there was an increase in 2011. Compared to other WB countries, Serbia recorded a stronger increase in investments. However, Serbia and the other WB countries were not able to significantly impact SAAs due to their low international competitive position. Serbia’s main partners from EU countries providing FDI are the Netherlands, Austria, Germany, Italy, etc. (European Movement in Serbia, 2018).

TABLE 5. FDI and GDP Growth in Serbia 2007-2017 in U.S.Dollars

Years	FDI	GDP Growth (Annual Percent)
2007	4.424	6,44
2008	4.055	5,65
2009	2.927	-2,73
2010	1.694	0,73
2011	4.927	2,03
2012	1.276	-0,68
2013	2.059	2,89
2014	1.999	-1,59
2015	2.342	1,77
2016	2.355	3,34
2017	2.893	2,04

SOURCE: The World Bank online data

The data shows that the value of FDI from the EU in Serbia has not changed significantly (World Bank Group 2018). Serbia's economic growth has also remained low since 2008, particularly in comparison to Hungary and Croatia (Zemniczky, 2015).

3.6 Kosovo

Based on previous findings and data from CEFTA 2006 and the Autonomous Trade Measures, Kosovo did not derive significant economic benefits from its trade liberalization. However, the SAA provided Kosovo with an additional trade framework and the opportunity for further cooperation with the EU. Kosovo started implementing the agreement in 2016. Subsequently, it fulfilled its obligations under the SAA, such as the approximation of legislation and trade issues (Council of Europe, 2015).

According to Qorraaj and Jusufi (2018), based on an analysis with exporting and non-exporting companies in Kosovo, the lack of benefits from free trade, the SAA and other EU instruments are mainly due to the following factors: lack of comparative advantages, the production capacities of local companies, lack of financial support for companies, the implementation of various market reforms, management problems and other challenges. In addition, the paper examines management problems as one of the obstacles to the use of free trade instruments.

4. MANAGERIAL CHALLENGES

Since Kosovo, as the last country to implement the SAA, was not part of the previous analysis, this section will focus on Kosovar companies or their management challenges, followed by human resources and other issues that affect the ability of businesses to benefit from the SAA. A well-organized management structure of companies has an extremely large impact on the level of exports, so it makes sense to shed more light on this topic in this section of the paper. Kosovo is still in the transition phase, in which entrepreneurship and small business creation are expected to play an essential role on the way to a modern free market economy and thus to economic development and growth (MTI 2013). According to the results of the Kosovo government's SME development strategy for Kosovo 2012-2016, the large imbalance between exports and imports is mainly due to the fact that Kosovo's SMEs are not competitive at an international level.

Weak exporting SMEs hinder the further contribution of SMEs to GDP, job creation and economic growth. Exports are dominated by base metals and minerals produced by large companies. The continued dominance of metal products in total exports remains a concern, more so than the low base of total exports (Government of Kosovo 2017). More than 50% of all Kosovar SMEs operate in the commercial sector, which is characterized by small and unproductive investments. This model, followed by the "me too" approach of new businesses, limits the ability of the SME sector to create jobs.

According to the report on the business climate in Kosovo by the Riinvest Institute (2017), the number of SMEs per capita in Kosovo is lower than in other countries in the region. This shows that the entrepreneurial culture in Kosovo is developing slowly compared to other countries in the Western Balkans. According to a similar report, the vast majority of companies in Kosovo are owner-managed and most companies do not have boards of directors due to their structure and size. The share of women entrepreneurs in the total number of businesses is only 8.3, and according to Ramadani et al. (2015), most of these Kosovar women work in micro-enterprises, are well educated and mostly work in trade. In terms of their work experience, most of them have up to six years of work experience.

Kosovar businesses are mainly concentrated in the central region, which includes the largest city of Pristina, followed by the regions of Ferizaj, Peja and Prizren. The geographical structure of the companies has remained almost the same over the years. In terms of ownership, in 2022, 90% of companies were domestic companies, while only 10% were foreign or even joint (domestic+foreign) companies. Regarding the number of companies by sectors or industry, 2556 new companies were established in Kosovo in the first quarter of 2023. The preferred economic sectors in the first quarter of this year were: trade with 722 registered companies (28.2%), manufacturing with 316 (12.4%), construction with 266 companies (10.4%), accommodation and food services with 247 (9.7%), professional, scientific and technical activities 204 (8.0%).

In Kosovo, the need for entrepreneurship is emphasized instead of entrepreneurial opportunities. According to Block and Sandner (2009), Deli (2011), Fairlie and Fossen (2017), Qorraj and Jusufi (2019), entrepreneurs who are entrepreneurial out of necessity are oriented towards local markets, while entrepreneurs who are entrepreneurial out of opportunity are more oriented towards international markets. Authors such as Bernard and Jensen (1990), Bernard et al. (2007), Bernard and Jensen (1995) have concluded that high productivity, wages, the management structure of the company, employees and capital are important factors that enable a company to be successful in the foreign market. Similar results were presented by Wagner (2005). Damijan et al. (2004) concluded in their study of exporting companies in Slovenia that companies exporting to advanced markets are much more demanding in terms of corporate governance than companies exporting to regional markets and those targeting local markets.

Krasniqi and Desai (2014), in their study of the export activities of Kosovar SMEs, concluded that for

exporting companies in Kosovo, business experience, the size of the company and the qualification structure of human resources, especially managers, are factors that determine the export activities of these companies. Furthermore Krasniqi and Desai (2017) used panel data for 3 time periods in their research on institutions and export performance in 26 transition countries and used variables such as export performance (dependent variable), formal and informal institutions, enterprise size, enterprise age, human and managerial resources, government size, population (v.independent) have reached findings that suggest benefits from focusing on the positive part of non-linear relationships between the age or experience of the enterprise and exports. It should be emphasized that this research used country-specific averages for these variables.

Other authors such as Bajraliu and Qorraj (2023) have addressed the issue of digitalization in Kosovo and reported that the development of digitalization has changed the nature of work and opened up new opportunities for businesses to achieve sustainable human resource management in many ways. According to the report, managers of Kosovar companies lack advanced management knowledge. In addition, only a few exporting companies have managers with proven experience in the international market, while the majority of them only have access to the local market.

Other challenges related to management issues of Kosovar entrepreneurs are as follows:

Challenges related to technical, innovative and managerial skills: Lack of activities to utilize new technologies, followed by underutilization of electronic communication and adoption of e-business, e-procurement and computerized production.

Interdependence between universities and enterprises: The lack of professional centers that link universities and enterprises and contribute to the development process of SMEs by combining science or knowledge and innovation in a functional competence network. This process will enable SMEs to exploit their creative development potential, increase their competitiveness and establish cooperation with local and international partners from research and industry.

Management challenges: According to various analyzes and interviews, especially with managers of export companies, there is a priority need for practical training such as: management training (business plans, general business management, planning strategy and organization); financial management training (applying for EU funds); market assessment training (internal market assessment, access to import and import procedures, access to export procedures), etc.

5. METHODOLOGY- Data and Model

In terms of methodology, it should be noted that Anderson was the first economist to create the theoretical economic basis for the gravity equation or gravity model under the assumptions of constant elasticity of substitution expenditure and product differentiation by country of origin (Shahriar et al., 2019). The methodology and analysis used panel data applied to six countries in the Western Balkans. According to Park (2011), the analysis based on a panel model offers more variability and allows more variables to be analyzed. This paper mainly focuses on a linear regression model and on balanced rather than unbalanced data to avoid unnecessary complications. A model looks as follows:

$$x_{it}, i=1, \dots, N, \quad t=1, \dots, T$$

This is the individual or country element and *t* is the time element. Furthermore, a general panel data regression model is represented:

$$y_{it} = a + \beta'x_{it} + u_{it}$$

Dynamic panel data describes the case where a lag of the dependent variable is used as a regressor:

$$y_{it} = a + \beta'x_{it} + \gamma y_{it-1} + u_{it}$$

In the present model and data, the authors used alternative techniques. It should be analyzed that the impact of SAA on FDI, GDP growth and trade balance is difficult to predict accurately as there are various factors (business environment, government support) that might have contributed to the increase or decrease in GDP or FDI. The most commonly used form of analysis to measure the impact of FTAs is the gravity model, which includes many explanatory variables in addition to distance and joint income. The gravity model is often used in foreign trade. According to this model, international trade between two countries is strongly influenced by the economic size of these countries, measured by GDP, and the geographical distance, expressed by the geographical distance between the capitals (Pere and Ninka 2017). In addition, the gravity model is applied:

$$\text{Bilateral trade between country } i \text{ and } j = \frac{\text{GDP of country } i \times \text{GDP of country } j}{\text{Distance between capitals of country } i \text{ and } j}$$

In the model applied, country (i) is Western Balkans; country (j) is EU. In the first model, the dependent variable represents Western Balkans exports to the EU. In the second model, the dependent variable represents Western Balkan's imports from the EU.

$$\begin{aligned} \text{LogExport}_{ij} &= \beta_0 + \beta_1 \log \text{GDP}_i + \beta_2 \log \text{GDP}_j + \beta_3 \log \text{Distance}_{ij} + \beta_4 \text{population} \\ \text{LogImport}_{ij} &= \beta_0 + \beta_1 \log \text{GDP}_i + \beta_2 \log \text{GDP}_j + \beta_3 \log \text{Distance}_{ij} + \beta_4 \text{population} \end{aligned}$$

Since the variables derived from the above models are the GDP of the Western Balkans and the EU, the distance between the capitals and the population of the Western Balkans and the EU, it is appropriate to apply the Beck-Katz (1995) method to estimate the gravity model. Kosovo is not included in the empirical model analysis due to the early stage of SAA implementation.

Gümüştan and Kahveci (2012); Anderson and Yotov (2017); Irshad et al. (2018); Jusufi and Ukaj (2021) have used the gravity model with the same objective as the present work to estimate bilateral trade between the Western Balkan countries. In their model, they used specific variables such as the existence of trade agreements, religion and the voting results of the Eurovision Song Contest. According to their results, the geographical distance and the similarity of the countries' demand structures, together with the difference in the countries' GDP per capita, contribute to the understanding of trade formation between the Western Balkan countries. According to research by Karagoz and Saray (2010), a country's trade is highly dependent on the size of the countries with which it trades. Geographical distance has a strong influence on trade between partner countries, as a large geographical distance reduces the opportunities for efficient trade.

Evenett and Keller (2002) claimed that only two important theories such as the HO model and increasing returns to scale are sufficient to explain the success of the gravity equation or model of trade between different countries. Sandalcilar (2012) used the gravity model and panel data to estimate Turkey's trade with countries that are similar in terms of their economic power and geographical size. The results obtained confirm that similar cultural traditions of the population and a common border positively affect free trade, while the geographical distance between the countries negatively affects free trade. Abbate et al. (2012) analyzed how the structure of international trade changes in a given geographical area and over time. They found that distance strongly influences the topology of international trade in a non-linear way. The structure of international trade is non-assortative over long distances, while it is assortative over short distances. The high level of international trade depends on geographically close countries. This means that the choice of trade partnership varies over different distances. This can be clearly seen over time and after controlling for the economic size and income of the trading partners.

TABLE 6. Estimation Results

	Model 1	Model 2
Intercept	-14.19 (5.32)	-26.74 (14.15)
GDP of the country (i)	0.86*** (0.33)	1.15*** (0.89)
GDP of the country (j)	0.89*** (0.09)	1.12*** (0.51)
Distance between country(i) and (j)	-0.96*** (0.23)	-1.53*** (0.19)
Population	2.71 (2.45)	-0.76*** (-0.49)
R ²	0.94	0.83

*** significance at 0.01 level. In parenthesis are robust standard errors.

SOURCE: Authors own work

6. INTERPRETATION OF THE RESULTS

The analysis conducted in the paper provided information on the trade balance, GDP growth and FDI, while furthermore, based on the variables analyzed and the empirical data, the impact of the SAA on the WB is analyzed.

GDP plays an important role in both models, which shows that the volume of trade between the WB and the EU also increases with the rise in GDP. According to Nieto et al. (2014), free trade is considered a long-term growth strategy in developing countries. GDP growth depends not only on free trade, but also on the economic competitiveness of countries, the economic prosperity of the population and the functioning of institutions. The positive and significant effects of the SAA do not seem to materialize for the Western Balkan countries in the short term, as the nature of the agreement reinforces and magnifies the positive and significant effect of FTAs for EU exports to the region rather than the other way around. Geographical distance also represents a negative relationship. Accordingly, trade between the countries decreases when the geographical distance between the capitals increases. Population size is only a negative factor in the model of imports.

In addition, the country-specific analyzes have shown that North Macedonia, despite its trade deficit with the EU, has achieved an increase in exports through the SAA, while foreign direct investment has increased as a result of the EU reforms. In Albania and Montenegro, the situation was similar in terms of export development and the development of foreign direct investment. In Bosnia and Herzegovina, the economic impact of the SAA was even lower, as the

country faced additional political challenges on top of economic sustainability. According to the data, Serbia has seen a larger increase in its FDI compared to the other countries. As the last country in the Western Balkans to implement the SAA, Kosovo faces many challenges: internal challenges such as the lack of ability to take advantage of EU market opportunities, challenges due to negotiations and unresolved issues with Serbia and, in addition, the current geopolitical problems in the EU and the world.

7. CONCLUSION

Many authors have shared different findings on the free trade instruments and the economic impact of Stabilization and Association Agreements (SAAs). Some evidence suggests that trade liberalization affects economic development overall, while other analyzes show the opposite, especially for transition countries and infant industries. Since the early 2000s, the countries of the Western Balkans region have been part of various EU agreements, including SAA. Previous studies conducted in Kosovo have confirmed that local businesses have not been able to derive sustainable positive effects from trade liberalization due to business performance, lack of institutional support and lack of experience with international markets (Qorraj and Jusufi, 2019).

The review of data for all Western Balkan countries in this paper confirms that SAAs have accelerated a significant impact on the development of the entire region, especially on trade volumes and FDI as a result of market reforms and convergence with EU standards. Moreover, according to the analysis, the SAA has

not been a sufficient instrument to improve the trade deficits of the WB countries, as many of these economies are still infant industries due to the long-term deindustrialization of the region. As far as EU reforms are concerned, there are signs that the WB countries have further developed their legal framework, especially in the area of trade, as they expect these reforms to help them on their path to European integration.

Apart from the role of FTAs in export promotion, this paper also analyzes the management challenges of local companies with a special focus on Kosovo by examining the qualification structure of human resources, which is dominated by necessity-type entrepreneurs. In addition, a lack of innovative ideas of local entrepreneurs, a lack of networking between universities and companies, as well as challenges related to the digitalization process have limited the importance of FTAs and especially the role of the Sta-

bilization and Association Agreement.

The main conclusion of the paper is that in addition to the opportunities arising from the SAA, businesses in the Western Balkans, and Kosovo in particular, can only fully benefit from EU instruments if they improve the performance of local businesses and adopt a better management approach, followed by innovation, digitalization and networking.

Finally, the main recommendations are as follows: apart from using free trade agreements, governments should support local exporting companies and provide them with technical assistance to compete in EU markets. In addition, local companies should adapt to market changes and develop innovative products and services that could increase the quality of their activities and thus improve their export performance and the national trade balance.

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SPORAZUMI O STABILIZACIJI I PRIDRUŽIVANJU NA ZAPADNOM BALKANU: IZAZOVI UPRAVLJANJA ILI GOSPODARSKI RAST?

SAŽETAK Prema politici proširenja Europske unije, glavni cilj Sporazuma o stabilizaciji i pridruživanju (SSP) nije samo gospodarski rast i poticanje izvoza, već i provođenje zakona, uključujući različite tržišne reforme. Uz SSP-ove, Europska unija (EU) podržala je zemlje Balkana i bilateralnim sporazumima o slobodnoj trgovini (FTA), zatim općim trgovinskim povlasticama te multilateralnim sporazumima o slobodnoj trgovini (CEFTA 2006). Ovaj rad ispituje jesu li SSP-ovi uspjeli ubrzati rast izvoza, investicija i gospodarski razvoj na Zapadnom Balkanu. Na temelju empirijske analize panel-podataka, glavni nalazi potvrđuju da SSP-ovi nisu bili dovoljni za povećanje izvoza, a posljedično ni za smanjenje trgovinskog deficita zemalja Zapadnog Balkana. Dodatno, poseban odjeljak posvećen je upravljačkim izazovima Kosova, poput razvoja poduzeća, poticanja izvoza, odnosa između karakteristika menadžmenta i izvozne učinkovitosti te drugim relevantnim temama, s obzirom na to da je Kosovo posljednja zemlja Zapadnog Balkana koja još uvijek provodi SSP.

139

KLJUČNE RIJEČI: *Sporazumi o stabilizaciji i pridruživanju (SSP), Zapadni Balkan, EU, upravljanje, trgovina.*