

THE FUTURE OF THE WESTERN BALKANS IN THE SHADOW OF THE WAR IN UKRAINE

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Russia's invasion of Ukraine has brought a new sense of urgency to the question of the Western Balkans' Euro-Atlantic future. The stoking of ethnic tensions in Bosnia and Herzegovina and Kosovo by the Kremlin has fuelled fears of a spillover of tensions into the region at large. Serbia's refusal to implement EU sanctions on Russia is yet another example of the EU's weakened influence in the region. All of these factors have highlighted the mounting challenges standing in the way of successful integration of the Western Balkans in the Union. Most notably, the EU must balance credible accession prospects with a hard line on rule of law and democracy standards, while simultaneously counteracting the advancing authoritarian currents already present in the region.

State of Play and Short-Term Challenges

Countries in the region still face serious economic, societal, and governance challenges which require comprehensive reforms. This brief summarises these challenges and identifies the methods by which the EU could support national governments and civil society across the region in overcoming them.

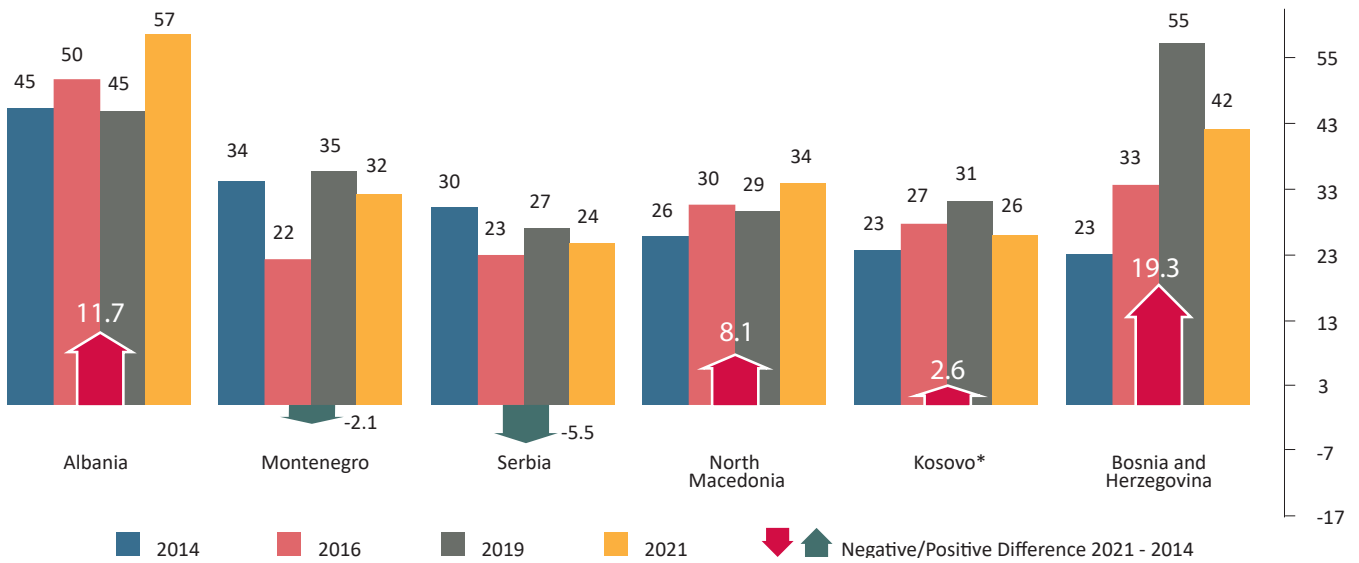
Turning the Tide against Corruption

Despite longstanding reforms, high levels of corruption and governance gaps across a variety of sectors remain among the region's greatest challenges. Administrative corruption is pervasive in the Western Balkans, with between 20% and 46% of the region's population admitting to having paid a bribe in exchange for services or favourable treatment. Cor-

KEY POINTS

- The Western Balkans is facing **an uphill struggle in its aspirations to join the European Union**. The EU, for its part, is attempting to maintain a **hard line on rule of law and democracy standards** while keeping the prospect of accession credible.
- High levels of administrative corruption in the region are compounded by **the inability of the judiciary to effectively enforce anticorruption laws**.
- Labour productivity in the region is low; there is **high monopolisation in a number of sectors**, regulations are burdensome for business, and taxation policy is erratic. This has resulted in the emergence of a **flourishing hidden economy**.
- Western Balkan economies also suffer from significant **competition deficiencies**, which make them vulnerable to monopolisation pressures.
- The deterioration of the media landscape has led to **widespread media capture**. In turn, this has allowed a **proliferation of disinformation and pro-Russian propaganda** across the region, spread by both state-owned and private media channels. Accordingly, the accession process should devote more attention to media freedom in order to strengthen the EU's ability to use **conditionality mechanisms** to tackle capture.
- Economic cooperation within the region must prioritize **tackling business capture**. The EU and other Western partners, notably the United States, must offer **meaningful alternatives to Chinese and Russian investments** in critical infrastructure.
- The EU and international financial institutions must work closely with governments in the region to help them **counter the damaging effects of illicit financial flows**.

Figure 1. Corruption Pressure in the Western Balkan Countries Has Risen Since 2014/2016



*Percentage of the population 18+ who have been asked to give and have given a bribe/money/favour/gift

Source: SELDI Corruption Monitoring System, 2021.

ruption pressure (reported instances of solicitation of bribes) is similarly high.¹ The adoption of regulatory anti-corruption standards on conflict of interests, whistleblower protection, and mandatory asset declarations for public officials, although notable, has done little to address those issues, and has been plagued by poor enforcement. As a result, a majority of citizens in the region are highly sceptical of their governments’ ability to meaningfully tackle corruption, and have largely lost faith in the effectiveness of anti-corruption measures.²

High levels of administrative corruption are compounded by the inability of the judiciary to effectively prosecute corruption-related offenses, and consecutive rounds of reforms have been similarly ineffective in insulating the judicial branch from political interference. The executive and legislative branches maintain formal levers of influence, including with respect to personnel decisions and budget allocation, as well as mechanisms for informal pressure, enabled by weak integrity and anti-corruption protocols. As a result, cases of successful prosecution of politicians and senior civil servants on corruption-related offenses remain exceedingly rare. When they do occur, they are

more often the result of partisan politics or intended to appease international partners by demonstrating quick results than a sign of genuine commitment to punishing those who perpetrate corruption. This ongoing trend highlights the difficulties associated with externally supported anti-corruption efforts in settings where corruption risks stem from the very top of the political system.

Unsurprisingly in this context, opinion polls reveal that 60% of people in the region distrust the judiciary, while less than 30% of people consider it to be politically independent.³ This is a stark indication of the level of social disillusionment with the political establishment and reform efforts to-date. Addressing these institutional deficiencies must be the core focus of EU conditionality mechanisms, in order to reinstate the social contract between societies and their governments across the region.

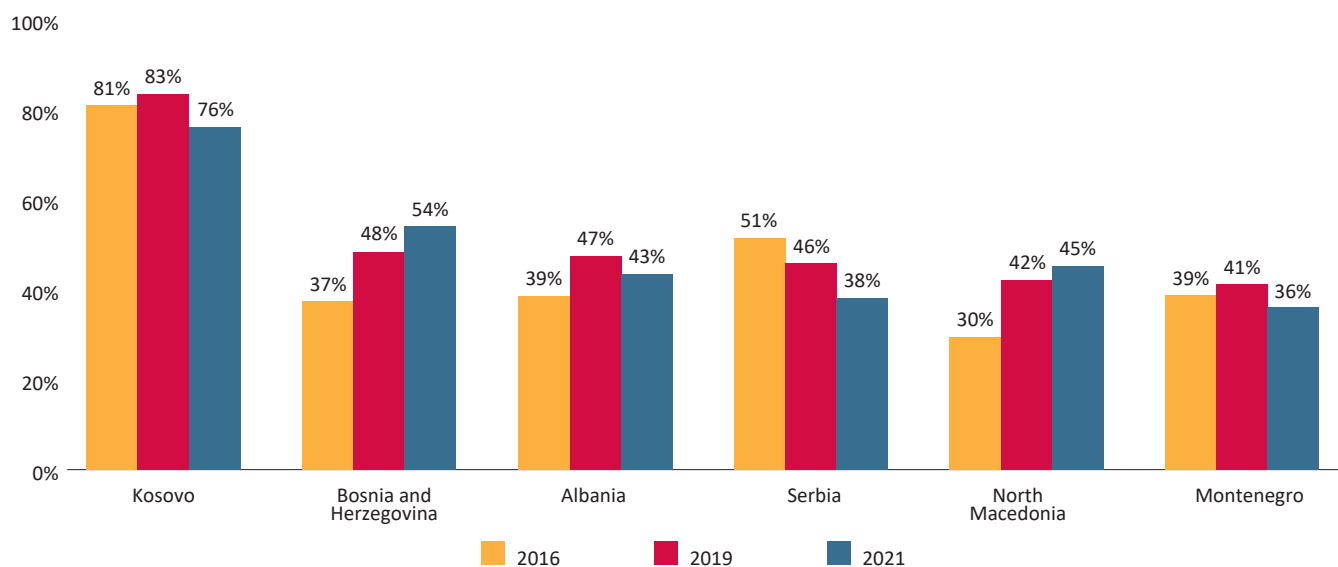
Tackling the Hidden Economy

Despite relatively strong GDP growth over the past two decades and steady improvement in key econom-

¹ SELDI, *Corruption in the Western Balkans Not Abating: What’s Next.* SELDI – Southeast-European Leadership for Development and Integrity, Policy Brief No. 13, January 2022.

² Ibid.

³ Regional Cooperation Council, *Balkan Barometer 2022: Public Opinion – Analytical Report*, Sarajevo: RCC, 2022.

Figure 2: Hidden Employment Index 2016-2021

Source: SELDI Corruption Monitoring System / Hidden Economy Monitoring System, 2021.

ic indicators such as unemployment rates, economies in the Western Balkans still lag far behind the EU average. Labour productivity is low, high monopolisation persists in a number of sectors, regulations are burdensome for businesses, and taxation policy is erratic. This has resulted in the emergence of a flourishing hidden economy. The size of the informal economy varies across the region, but remains alarmingly large in most countries, even if some improvement is visible in comparison to 2019 levels. Even in Montenegro, the best-performing country in the region, 36% of people report at least some level of informality in their employment, while this reaches a staggering 76% in the case of Kosovo.⁴

The presence of a sizeable hidden economy has a number of adverse effects: It hampers competition, leads to the proliferation of corruption, and deprives the state of tax revenues while depriving individuals from adequate social security and labour protection. The effects of this informality were particularly strongly felt during the COVID-19 pandemic, when many engaging in undeclared work were left without access to health-care or state financial support.

⁴ SELDI, *Hidden Economy in the Western Balkans 2020: Trends and Policy Options.*, Policy Brief No. 11, November 2020.

Reversing Monopolisation Resulting from State Capture

Western Balkan economies also suffer from significant and persistent competition deficiencies, which leave them vulnerable to monopolisation pressures. The lack of capacity among public institutions, combined with weak and poorly enforced anti-trust regulations and inefficient corporate governance practices, are all environmental factors which increase local economies' vulnerability to state capture.⁵ While the trend towards oligarchisation of local economies is most pronounced in Albania, Kosovo, and Bosnia and Herzegovina, it remains strong across the region, and appears to be accelerating.⁶ State capture and monopolisation dynamics are especially pronounced in sectors such as energy, telecommunications, pharmaceuticals, and construction, where powerful private interests have successfully established control over a sizeable share of the available assets. This has allowed local oligarchic networks to penetrate state regulatory and governance mechanisms and co-opt them in service of private business interests.

⁵ Mineva, D. et. al., *Rolling Back State Capture in Southeast Europe: Implementing Effective Instruments for Asset Declaration and Politically Exposed Companies*, Sofia: Center for the Study of Democracy, 2023.

⁶ SELDI, *State Capture Assessment Diagnostics in the Western Balkans 2020: Risks and Policy Options*, Policy Brief No. 10, October 2020.

Significant state capture and failure to reduce the size of the informal economy obstruct economic growth and undermine trust in public institutions. Tackling these issues is central to the fulfilment of the Copenhagen economic criteria and to Western Balkan countries' successful accession to the EU. To this end, the EU and other international partners must act in concert with reform-minded political actors and civil society representatives in order to develop and safeguard robust mechanisms for prevention and control.⁷ Successfully addressing these issues has become even more pressing in light of rapidly rising commodity and energy prices and soaring inflation rates, which cast a grim shadow on the region's prospects for economic growth. Without effective and timely intervention, these prospects will likely only grow bleaker as the war in Ukraine continues, further deepening the economic disparities between the Western Balkans and the EU.

Halting the Decline of Human Capital

High levels of outward migration, also known as "brain drain", present another major challenge for the region. Dissatisfaction with public institutions, poor living conditions, and high levels of inequality, coupled with relatively easy access to EU labour markets with substantially higher wages, have resulted in a steady stream of workers, many young and highly skilled, moving abroad in search of better employment opportunities. Estimates suggest that over 150,000 people emigrate from the region to OECD countries every year.⁸ Although recent studies indicate that some circular movement is present in the patterns of migration, many of those who emigrate do not return.⁹ The trend does not seem to be abating – the number of people willing to consider relocation outside the region remains very high, ranging from 37% in Serbia to 49% in Albania.¹⁰

The adverse effects of high volumes of emigration have been felt most keenly in sectors such as healthcare, secondary and higher education, engineering, IT, and skilled manual labour.¹¹ High levels of emigration and related labour shortages at home further hamper the region's ability to increase its economic competitiveness, foster innovation, and increase productivity, all of which remain vital for convergence with EU development levels.

Resisting Subversive Authoritarian Influence

The region's geostrategic importance, the ongoing uncertainty surrounding its European prospects, and persistent governance deficits have made the countries of the Western Balkans particularly **vulnerable to foreign malign influence**. Such pressures have only intensified since the outbreak of the war in Ukraine, further strengthening existing authoritarian trends across the region.

Russia has long been the main subversive foreign presence in the region, which remains central to the Kremlin's effort to reassert its great power status internationally. This campaign of influence has been defined by a concerted effort to penetrate and establish control over strategic industries such as energy, infrastructure, mining, telecommunications, and banking. Estimates suggest that Russian-linked capital directly or indirect controls up to 10% of the region's economy, although the true extent of financial penetration is likely much higher due to concealment by opaque corporate ownership.¹² Moreover, Russia's corrupt corporate networks tend to have greater leverage than the on-paper size of the trade or capital relations suggest.

Moscow's strategic involvement in the region extends well beyond economic levers of influence. Russia's economic pressure has been accompanied by a

⁷ Center for the Study of Democracy, *Making Democracy Deliver in the Western Balkans: Strengthening Governance and Anticorruption*, Policy Brief No. 77, May 2018.

⁸ Omic, E., and Handeland, C., *Social Infrastructure in the Western Balkans. Increasing the Region's Economic Resilience, Enhancing Human Capital and Counteracting the Effects of Brain Drain*, Research Papers Series, Paris: Council of Europe Development Bank.

⁹ Leitner, S. M., *Net Migration and Its Skill Composition in the Western Balkan Countries between 2010 and 2019: Results from a Cohort Approach Analysis*, Vienna: Vienna Institute for International Economic Studies.

¹⁰ Regional Cooperation Council, *Balkan Barometer 2022: Public Opinion – Analytical Report*, Sarajevo: RCC, 2022.

¹¹ Vračić, A., *The Way Back: Brain Drain and Prosperity in the Western Balkans*, European Council of Foreign Relations, Policy Brief, May 2018.

¹² Stefanov, R., and Vladimirov, M., *The Kremlin Playbook in Southeast Europe: Economic Influence and Sharp Power*, Sofia: Center for the Study of Democracy, 2020.

targeted campaign combining soft, sharp, and hard power instruments aiming to exploit and intensify social tensions and undermine the stability of democratic governance. The ultimate goal of this strategy is to cultivate a favourable environment for advancing Moscow's strategic business and political interests, all while weakening support for further Euro-Atlantic integration and tarnishing the EU's appeal in the region.¹³

The Kremlin has also made a concerted effort to gain a significant foothold in the **media landscape** across the region.¹⁴ This has been achieved through a combination of tools including formal media ownership, direct capital control, and the use of indirect financial incentives such as advertising revenues and the provision of free content, targeted towards already cash-strapped media outlets. Powerful state-owned Russian enterprises such as Gazprom and Lukoil have effectively become the largest advertisers in Western Balkans' media space, securing significant informal influence.¹⁵ This media capture has led to the seamless proliferation of disinformation and pro-Russian propaganda in the region spread by both state-owned and private media channels. In some countries, Russia exploits shared Orthodox and Slavic cultural heritage as well as the population's frustration with the status quo in order to push Moscow's preferred line on issues of strategic interest. The Kremlin's information war has only intensified since the breakout of the war in Ukraine, with many pro-government outlets parroting Moscow's narrative. Such efforts appear to have been highly successful in countries like Serbia, where nearly two-thirds of the population believe that NATO is to blame for Russia's invasion, in stark contrast to the prevailing view across most of the EU.¹⁶

The authoritarian pressures present throughout the region have recently been exacerbated by the increased involvement of **China** and its tacit underwriting of Russia's malign behaviour.¹⁷ Beijing has sought to leverage its Belt and Road Initiative (BRI) and exploit the region's dire need for capital in order to lock many

Western Balkan countries into costly and questionable infrastructure projects which cultivate economic dependence. This "debt trap diplomacy" is perhaps best illustrated by the case of Montenegro: The country received a €800 million from China's Exim Bank in 2014 for the construction of a section of a highway from the coast to the border with Serbia, which remains unfinished. The loan, which is equivalent to approximately 20% of the country's GDP,¹⁸ caused Podgorica's debt to balloon to 103% of the country's GDP and has fuelled fears of default, which would allow the bank to seize land inside Montenegro.¹⁹ While the government was able to secure assistance from EU and U.S. financial institutions to refinance the loan, it will remain a significant strain on Montenegro's already fragile economy for decades to come, and leave the country vulnerable to political pressure from Beijing.

Although the Montenegrin case is perhaps the most striking, it is by no means the only example of this strategy. China is estimated to have invested €32 billion in the region between 2009-2021, with at least €5.7 billion loaned to Serbia alone.²⁰ In addition to the damaging economic and political dependence which such investments impose, they are also often associated with significant human rights and labour violations, as well as environmental damage. As such, they directly undermine local governments' compliance with EU standards, and thus jeopardise further integration with the Union.²¹ The content and conditions of these projects' contracts are usually not made public, and in some cases, they are even falsely portrayed by pro-government media as gifts or foreign direct investments (FDI) instead of loans.²²

This expanded economic footprint in key industries has allowed Moscow and Beijing to establish significant influence over political decision-making, a development which has largely come at the EU's expense. The penetration of authoritarian forces intensified significantly during the pandemic, when both Russia and China engaged in intense and successful 'mask diplomacy' and

¹³ Ibid.

¹⁴ Center for the Study of Democracy, *Policy Agenda for Countering Media Capture in Europe*, Policy Brief No. 116, October 2022.

¹⁵ Filipova, R., Vladimirov, M., and Gerganov, A., *Tackling Kremlin's Media Capture in Southeast Europe: Shared Patterns, Specific Vulnerabilities and Responses to Russian Disinformation*, Sofia: Center for the Study of Democracy, 2021.

¹⁶ Savic, M., "EU Rejected by Serb Majority as Poll Shows Putin Well Regarded", *Bloomberg Online*, June 29, 2022.

¹⁷ Vladimirov, M., and Gerganov, A., *Chinese Economic Influence in Europe: The Governance and Climate Conundrum*, Sofia: Center for the Study of Democracy, 2021.

¹⁸ Monstat, "Gross domestic product of Montenegro for period 2010 – 2014", Statistical Office of Montenegro Official Website. September 1, 2022.

¹⁹ Standish, R. et al., "No Clear Option for Montenegro As It Tries To Repay \$1 Billion Highway Debt To China" *Radio Free Europe*, April 14, 2021.

²⁰ Stojkovski, B., et al., "China in the Balkans: Controversy and Cost" *Balkan Insight*, December 15, 2021.

²¹ Ibid.

²² Shullman, D., *China's Growing Influence in the Western Balkans*, Hearing at the U.S. Senate Committee on Armed Services Subcommittee on Emerging Threats and Capabilities Washington, D.C., 2019.

'vaccine diplomacy' targeting the region. Although the size of Moscow and Beijing's pandemic-related assistance was ultimately symbolic compared to the comprehensive support provided by the EU, it was given disproportionate publicity by captured media outlets and co-opted political actors.²³ Authoritarian assistance was contrasted with the EU's slow reaction at the early stages of the pandemic, and framed as evidence of the Union's lack of solidarity with the region. This eagerness of local elites to underplay the support received by the EU while falsely contrasting it with the apparent generosity of authoritarian regimes is another worrisome trend which exacerbates popular frustration with the bloc. This trend further erodes the EU's credibility in the region, and empowers illiberal political actors in their pursuit of nationalist and anti-democratic policies.

Ensuring Energy Security and Green Transition

Energy security has long been an important concern for Western Balkan countries, but the current energy crisis has brought it to the forefront of political agendas across the region. With energy poverty remaining a major concern across the region,²⁴ the Western Balkans have been disproportionately hard-hit by soaring energy prices. The crisis has highlighted the inability of the region's inefficient electricity systems to guarantee security of supply, and has demonstrated the urgent need for a swift shift towards more economically and environmentally sustainable technologies.

The energy sector across the Western Balkans is generally inefficient and relies on outdated infrastructure; these problems are worsened by significant dependence on fossil fuels, particularly coal, limited take-up of renewables, and a lack of political and social demand for decarbonisation. As a result, local populations are also exposed to some of the highest rates of air pollution and particulate matter emissions in Europe; the main source of these harmful pollutants is aging lignite-fired thermal power plants.²⁵ The economic and healthcare costs associated with this pollution are estimated in the range of €11.5 billion,

with a significant proportion borne by neighbouring EU Member States.²⁶ The region's successful transition to low-carbon energy sources would be a vital step not only towards its further Euro-Atlantic integration, but also the broader achievement of European climate ambitions. Failure to advance towards meaningful decarbonisation could potentially jeopardise the achievement of Europe-wide targets for carbon emission reduction and climate neutrality by 2050.

In this context, the significant financial involvement of authoritarian powers, especially China, in the energy sectors of Western Balkan countries represents a serious concern. The vast majority of large-scale infrastructure projects funded by Beijing focus on the energy sector, and promote outdated and polluting technologies such as coal-fired power generation, which are not aligned with the countries' priorities or market realities. Such projects not only introduce significant market distortions, as they often benefit from extensive state aid, but also frequently directly undermine the EU's decarbonisation agenda, to which the Western Balkan countries have formally committed by signing the Sofia Declaration in 2020.²⁷

These ill-advised investments will likely have long-lasting negative effects on the local energy markets by locking Western Balkan countries into continuous reliance on polluting and carbon-intensive energy production, while simultaneously preventing the region's transition towards low-carbon energy sources. All of these factors are likely to obstruct the region's further integration with the EU and implementation of the EU acquis, as such projects do not comply with the Union's environmental or competition standards.

What's Next

- A revised **EU enlargement policy** should offer a clear roadmap for each candidate country, spelling out concrete targets, monitoring mechanisms, and sanctions for non-compliance or reversal of reforms, as well as deadlines for the completion of key milestones.

²³ Tzifakis, N., "The Geopolitics of Pandemic-Related Assistance to the Western Balkans", Barcelona: European Institute of the Mediterranean, 2021.

²⁴ Colovic-Daul, M., Kryzanowski, M., and Kujundzic, O., *Air Pollution and Human Health: The Case of the Western Balkans*, United Nations Environment Programme, 2019.

²⁵ Ibid.

²⁶ Matkovic, V., and Gierens, R., *Chronic Coal Pollution: EU Action on the Western Balkans Will Improve Health and Economies across Europe*, Brussels: H HEAL, CAN Europe, Sandbag and CEE Bankwatch Network and Europe Beyond Coal.

²⁷ Center for the Study of Democracy, *The Chinese Economic Footprint in Central and Eastern Europe: Impact on Energy Transition and Climate*, Policy Brief No. 97, January 2021.

- The EU's involvement in the Western Balkans should be accompanied by clear political commitments by other **key strategic partners**, notably the **United States**, to the democratic future of the region. In this respect, the potential passage of the Western Balkans Democracy and Prosperity Act in the U.S. Senate could complement and strengthen the EU's engagement with the region. The EU should seek synergies between the funding, technical assistance, and conditionality requirements of different donors in order to maximise their impact.
- The EU must support Western Balkan governments in designing regulatory reforms of their taxation, social security, and labour policies in order to **improve the business environment and incentivise a transition towards formal employment**. This should be complemented by a reform in inspection procedures to make them more efficient in targeting high-risk sectors and enterprises. The EU could furthermore provide Western Balkan governments with concrete advice on tackling informality-related issues by including recommendations in its annual Joint Conclusions. Local gaps in relevant skills could be addressed systematically through the establishment of mechanisms for structured and ongoing cooperation between national oversight authorities and their EU colleagues, facilitating the exchange of information, expertise, and best practices.
- The EU and international financial institutions must work closely with governments in the region to help them **counter the damaging effects of illicit financial flows**, especially those linked to authoritarian governments. To this end, the resilience and capacity of local financial authorities must be improved in order to improve their ability to screen foreign investments, carry out strategic analysis, trace assets, counter money laundering, and vet the final beneficial ownership of FDIs. The operational authority of EU supervisory and enforcement institutions such as the European Public Prosecutor's Office and the future Anti-Money Laundering Authority should be expanded to include functional cooperation with aspiring member states, with the goal of integrating them into the European infrastructure for financial oversight. Such cooperation should focus on issues of mutual interest, such as sanction enforcement and information sharing.
- Economic cooperation with the region should prioritize **tackling business capture**. International partners, together with civil society actors and national governments, must analyse existing capture dynamics and the regulatory and governance deficits which enable them. Measures promoting corporate transparency and reporting as a way to **expose and tackle market concentration** should be prioritised. This should be accompanied by supportive measures targeting sectors with high monopolisation risk such as energy, where the EU could leverage its energy support package and the Economic and Investment Plan for the Western Balkans in order to promote diversification of the energy mix in the short-to-medium term, as well as a move away from overreliance on Russia.
- The EU and other Western partners, notably the United States, must offer **meaningful alternatives to Chinese and Russian investments** in critical infrastructure. The launch of the EU's Economic and Investment Plan for the Western Balkans is a welcome, albeit belated step in this direction. The delivery of such funds, however, should be optimised to ensure that they impart real benefit while still remaining attractive to local elites as alternatives to funding from autocrats, which is often favoured due to the fewer conditions attached. To this end, the EU should not lower its insistence on compliance with transparency, corporate governance, and competition standards, but should provide operational support to local administrators in tackling the additional burden created by such bureaucratic requirements. The Union should also actively support civil society actors in developing the capacity to monitor the utilisation of foreign funds, including through the creative use of technology, big data, and open source intelligence.
- **Investments originating from third parties such as China** should be subject to rigorous scrutiny, and must align with the countries' commitments under the Stabilisation and Association Agreements with the EU. It should be made clear to local partners that accepting investments which do not meet the EU's environmental, human rights, and competition standards is incompatible with the objective of EU membership, and would significantly derail their path towards accession. A concrete step in this direction could be the establishment of governance standards and guidelines for Chinese and other third-party investments, which could serve as a form of pre-approval.
- EU delegations and Member State embassies in the Western Balkans should assume a **more proactive role in countering Kremlin-sponsored propaganda**.

They should be prepared to address and debunk false claims spreading anti-Western sentiment in real-time through direct and regular engagement with local media outlets. EU missions should reinforce in-house communications capacities, make social media accounts more accessible and appealing to the wider population, and use them in a more targeted manner in order to counter false and anti-EU narratives in the information space.

- **Media freedom should receive more attention in the accession process** in order to strengthen the ability of the EU to use conditionality mechanisms

to tackle capture. One key step in this direction could be the inclusion of a media freedom initiative under the Berlin Process, requiring concrete commitments from Western Balkan governments. Such commitments could include the introduction of public registers of media ownership for online, broadcast, and print media, along with stronger licensing requirements and more transparent advertising regulations. The enforcement of those commitments should be monitored closely through a dedicated EU monitoring report on media freedom, whose findings should have bearing on access to EU funding.