

Preface

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South-East Europe promises to be the next major focal region of European integration dynamics and modernization efforts. While not much research has been devoted to it so far, South-East Europe is now among the fastest-growing regions on the continent and possesses large potential yet to be tapped for further expansion. South-East Europe as we understand it and as it is generally defined in contemporary political geography comprises the following countries: Albania, Bosnia and Herzegovina, Bulgaria, Croatia, FYR of Macedonia, Romania, Serbia and Montenegro. Since Central Europe joined the EU in May 2004, the focus of the integration process has clearly shifted south-east. Apart from Romania, Bulgaria and Croatia, which are the candidates for the next accession rounds, all other countries of the region now have an accession perspective. Moreover, the Stability Pact for South-Eastern Europe has been assisting the difficult catching-up process of this region through various initiatives for years. Austria is a neighbour and intimately linked to South-East Europe by the Danube, by geography and by history. Today, economic links play a prime role, with trade volumes developing on a dynamic trajectory and Austrian investors being in the forefront of the microeconomic re-integration process of the region with the rest of Europe.

This book contains contributions made to the Oesterreichische Nationalbank's first Conference on European Economic Integration, which took place in November 2004. This event continued the tradition of our East–West Conferences, but with a new name chosen to reflect the growing-together of Europe that we have witnessed and the challenges we will have to meet in the future. After decades of Cold War and separation, we were recently able to welcome ten new member countries to the EU. But, as mentioned, the re-unification of our continent is not yet over. Further deepening and widening of the Union promises to be the focal point of efforts of economic policies in the next quarter of a century. The title of the conference, South Eastern EUROPEAN Challenges and Prospects, on which this book is based, highlights important regional

issues as well as the integration dimension. High-ranking representatives from government and international organizations, central and commercial banks, as well as universities and research institutes contribute their expertise to several key topics related to macroeconomic, structural and external economic and institutional relations of South-East European countries.

To single out a few topics, taking stock of where South-East Europe stands as a point of departure yields a fascinating variety of positions in a number of fields: while major catching-up efforts are necessary virtually everywhere, some countries seem to have already embarked on a path of steady economic expansion, whereas others have apparently not yet reached the point of take-off. Some countries are in the acceding process to the European Union, while others still have quite a way to go. Some have already been reaping benefits of industrial restructuring whereas others have yet to develop viable export sectors. Challenges include the necessity to overcome problems of corruption, weak judiciary systems and to improve the investment climate. Does the region more or less correspond to what Central Europe was ten years ago? What is the current state of relations between the EU and the individual countries of the region? How has the Stability Pact for South-Eastern Europe piloted and assisted modernization efforts? On this range of issues, this book compiles first-hand evidence and background information from authors from the region and experts on the region.

The heterogeneity of traits resurfaces in the domain of monetary and exchange rate policies. Most types of exchange rate regimes can be found in the region: the solutions adopted range from a majority of hard pegs (even including cases of unilateral euroization) to a loosely managed float. Heterogeneity notwithstanding, the broad picture of anti-inflationary performance has been quite bright in recent years, although further progress is needed. There appear to be various paths to a common goal. Whereas one may assume that overall monetary policy credibility and perseverance are the decisive ingredients, one may doubt whether this is sufficient to sustain performance in the long run, if monetary policy commitment is not flanked by fiscal awareness and structural reform. In any case, euro holdings and bank deposits of the populations of South-East Europe remain high, which underlines the attractiveness of the common European currency throughout the region.

All is not bright in South-East Europe. Macroeconomic imbalances, particularly current account deficits, seem to have become entrenched across the region. While the fiscal situation has improved recently in some countries, most of them continue to be plagued by 'twin deficits'. The majority of economies remain dependent on foreign grants and financial assistance.

But this support is on a declining trend. Perhaps the most serious challenges are high unemployment, poverty and brain drain. Despite the robust average growth rates of recent years, sluggish reforms, economic mismanagement and in some cases even armed conflicts, ethnic separations and political disruptions affecting the whole region imply that most countries have still not recovered far enough to have re-attained the GDP level of 20 years ago. As a reaction to the impoverishment, migration has increased. But is migration unequivocally bad for the countries of origin? What are the main causes for the stubbornly high joblessness?

For South-East European countries saddled with deep-seated structural problems and opting for a catching-up strategy that should be as swift as possible, opening up to trade and foreign direct investment constitute pivotal steps to boost economic expansion, competitiveness and real convergence. While contributing to the reduction of external disequilibria and aid dependency, FDI and its role in enhancing know-how and creating access to international markets can be considered a 'key to success' in modernizing the economies of the region and fully 'attaching' them to the world economy. In doing this, FDI can make an important contribution to alleviating joblessness, although this seems to be an extended and not painless process. Featuring among the region's leading investors, Austrian enterprises are strongly engaged in these endeavours. However, FDI still falls well short from what it could be in most countries of the region. What would be needed to attract more foreign business into the south-east of Europe?

Shaping up banking and financial intermediation is another crucial area for harnessing South-East European economic expansion. And it is particularly the banking sector where foreign investors, among them Austrian ones, are prominently positioned in the modernization drive. They have raised the quality of services and contributed to restoring confidence in financial systems. Since the fall of the Iron Curtain, Austrian bankers have acted as pioneers not only in Central Europe, but have also been among the first to take risks and venture south-east. Today, Austrian banks together account for no less than a quarter of total banking sector assets in South-East Europe. The earlier referred to integration dynamics, the strong economic links as well as the involvement of our credit institutions in the region and its impact on the financial stability of the Austrian banking sector explain why it is essential for the Oesterreichische Nationalbank to monitor and analyse South-East Europe closely. Given multiplying cross-border links, to what degree is increased supervisory coordination on the European level necessary? Are there sizeable risks connected to the current lending booms in the region? These are just a few of the questions that are dealt with in the following pages.

Summing up, we do hope that this book will offer some fresh insights into and a better understanding of this new focus of emerging Europe which, for all its variety, possesses one overriding prospect – as Jean-Claude Trichet put it in a nutshell: progress toward EU membership.