

Overview

Recent economic developments in six South East Europe economies

The 2018 *Competitiveness Outlook* for South East Europe provides an economic overview of six economies in South East Europe (SEE): Albania, Bosnia and Herzegovina, the Former Yugoslav Republic of Macedonia, Kosovo,* Montenegro, and Serbia. With a combined population of nearly 18 million people, a landmass roughly the size of the United Kingdom and its strategic location at the crossroads of Central Europe, the Adriatic and Black Sea regions, this region has for centuries played an integral role in European business and commerce. Today, the six SEE economies participating in the *Competitiveness Outlook* have a joint gross domestic product (GDP) of USD 89.1 billion (current USD; World Bank, 2017), the equivalent of roughly half of Portugal's GDP. Serbia is the largest of the six economies, accounting for 43% of the region's total GDP, followed by Bosnia and Herzegovina with 19% and Albania with 13% (World Bank, 2017).

In the wake of Yugoslavia's disintegration and the SEE region's transition towards a free market economy, the SEE economies faced the dual hardship of conflict and economic stagnation (OECD, 2016). At the turn of the new millennium, the return of peace laid the foundations for regional stability and economic growth. However, the 2008 financial crisis hit the six economies hard: GDP fell by 2% in 2009 and growth remained sluggish for years afterwards. Indeed, between 2008 and 2012, average unemployment rates increased by 8 percentage points (World Bank, 2017).

Eight years after the crisis, a return to economic growth brought with it new investment opportunities. In 2016, the average GDP growth rate for the six SEE economies was 2.8%, with Kosovo (3.6%) and Albania (3.2%) showing the strongest growth (Table 0.1; World Bank/WIIW, 2017). What is more, at 5% of GDP in 2016, regional average foreign direct investment (FDI) inflows were well above the OECD average of 2.6%. FDI inflows were particularly strong in Albania (9.3%) and Serbia (6.1%), with about 60% of FDI inflows to the region originating from the European Union (EU), and other investments originating from the People's Republic of China, the Middle East, the Russian Federation and Turkey. Over the last decade, the SEE mining, manufacturing and financial sectors have attracted the most FDI (UNCTAD, 2017).

However, the six economies' overall economic development record is less positive than in neighbouring transition economies. Among the assessed economies, GDP per capita levels have reached 34.3% of the EU average, compared to 68.5% in Central Europe and the Baltic states (CEB) (World Bank, 2017). A similar picture can be drawn

* This designation is without prejudice to positions on status, and is in line with United Nations Security Council Resolution 1244/99 and the Advisory Opinion of the International Court of Justice on Kosovo's declaration of independence.

for the unemployment rate, which stood at 23.1% in the SEE economies in 2015, compared to 7.8% in CEB (World Bank/WIIW, 2017; World Bank, 2017). Average youth unemployment in the region is higher yet, resting at a staggering 48% (World Bank, 2017).¹ High levels of unemployment compounded by slow regional growth make it unlikely that the income gap with the European Union will narrow in the near future.

Table 0.1. **Key data for the six SEE economies (2016)**

Economy	Population (million inhabitants)	GDP (current USD billion)	GDP per capita, PPP (current international USD)	Unemployment (% of labour force over 15 years old) ²	FDI inflows (% of GDP)
ALB	2.87	11.9	11 540	17.1	9.3
BiH	3.51	16.9	12 172	27.7	1.7
MKD	2.08	10.9	14 942	26.1	3.6
KOS	1.81	6.7	10 064	32.7	3.6
MNE	0.62	4.4	17 633	17.5	5.5
SRB	7.05	38.3	14 515	17.7	6.1
Averages/total	17.94	89.1	13 478	23.1	5

Note: 1. Unemployment data are from 2015 (World Bank/WIIW, 2017), whilst all other data are from 2016.

Source: World Bank (2017), *World Development Indicators* (database), <http://data.worldbank.org/data-catalog/world-development-indicators> (including FDI inflows for Kosovo); for unemployment data: World Bank/WIIW (2017), *The Jobs Gateway in South Eastern Europe* (database), www.seejobsgateway.net/charts; for FDI inflows (except Kosovo): UNCTAD (2017), *World Investment Report 2017: Investment and the Digital Economy*, <http://unctad.org/en/pages/PublicationWebflyer.aspx?publicationid=1782>.

A heavy dependence on remittances in the six SEE economies continues to pervade economic life. In Kosovo, personal remittance payments account for 14.8% of GDP. The statistics are similar, if less pronounced, in Bosnia and Herzegovina, where remittances account for 11% of GDP, and Albania, where they are 8.9% (World Bank, 2017).

What is more, investments in knowledge-intensive activities that create high value remain the exception. The region's labour market will have to contend in the near future with the middle-income trap. Rising wages in the main export sectors may reduce their competitive edge – particularly in manufactured goods and textiles – while underdeveloped skills in the labour market keep the economies from competing with more developed countries in advanced value-added services (OECD, 2017).

In view of the macroeconomic weaknesses of the assessed economies, governments are showing renewed commitment to enacting policy reforms. The reform agenda is also structured by the goal of eventual EU membership, which was invigorated by the recently adopted European Commission Strategy for the Western Balkans and is an important driver of change. In this context, the European Commission and the OECD are partnering with the assessed SEE economies to develop annual economic reform programmes. These initiatives assist in shaping economic governance by identifying and addressing key economic obstacles to growth.

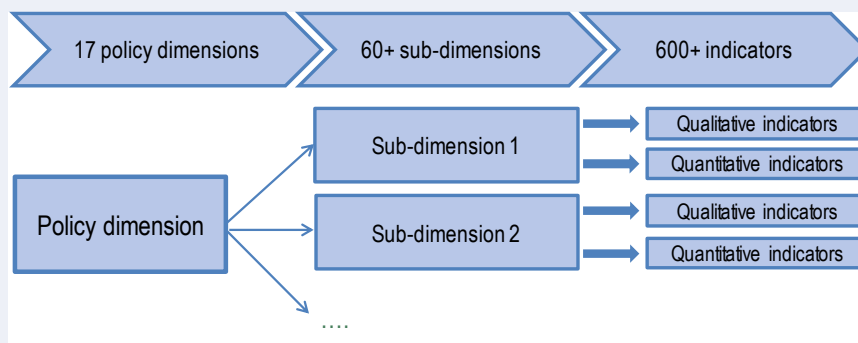
Given the small size of their economies, participating SEE governments recognise the need for deeper regional economic co-operation. Addressing macroeconomic challenges in a collaborative way can help generate stronger, more inclusive and more sustainable growth that can benefit the entire region. The idea of reinforced regional economic co-operation was endorsed during the Berlin Process Western Balkan Six Summit in Trieste in 2017.

This publication seeks to complement the existing regional initiatives by resolving competitive challenges as the basis for stronger, more inclusive and more sustainable economic growth. The report seeks to help policy makers by: 1) providing a comprehensive assessment of economic competitiveness in the region across 17 policy dimensions, assessed on a score gradient from 0 to 5 (Box 0.1); and 2) proposing actionable policy recommendations based on international and OECD good practice. Greater economic competitiveness – driven by productivity gains – is needed to unlock these economies’ potential. In view of these objectives the report offers key findings on a range of socio-economic challenges, including how current policies can be improved to support economic governance reform and how policy makers can draw on regional experience to tailor solutions that better serve local communities.

Box 0.1. The *Competitiveness Outlook* scoring methodology

In each of the six economies, the 17 policy dimensions are assessed as to whether the relevant competitiveness-enhancing policy settings, strategies, processes or institutions are in place, and if so, the extent to which they have been adopted, implemented, monitored and updated. Each policy dimension has two to five sub-dimensions that highlight the key elements of that policy area. The sub-dimensions in turn are made up of a total of more than 600 indicators, both quantitative and qualitative (Figure 0.1), which capture in detail the design, implementation and performance of policy settings, processes and institutions.

Figure 0.1. Overall assessment approach of the *Competitiveness Outlook 2018*



In 15 of the 17 dimensions,¹ the indicators are assigned a numerical score according to the level of policy development and implementation so that performance can be compared across economies. A score of 0 denotes absence or minimal policy development while a 5 indicates alignment with what is considered best practice: a score of 1 denotes a weak pilot framework, 2 means the framework has been adopted as is standard, 3 that is operational and effective, 4 that some monitoring and adjustment has been carried out, and 5 that monitoring and improvement practices are systematic.

Policy dimension and sub-dimension average scores are arrived at by calculating the simple average across the relevant qualitative indicator scores. Indicators are not weighted because the importance of each indicator will be different for different stakeholders. Average scores should therefore be interpreted with caution and taken only as a rough indicator of policy development.

1. The exceptions are Dimension 5 and Dimension 16, which used a slightly different assessment approach.

Source: For more information see the methodology chapter.

Key findings for each policy dimension

Dimension 1: Investment policy and promotion

Investment is central to economic growth and sustainable development. It expands an economy's productive capacity, drives job creation and secures overall competitiveness. To these ends, the investment policy and promotion dimension examines the existence of policies for market access and exceptions to national treatment, investor protection and intellectual property rights. With regard to investment promotion, the dimension assesses strategies and institutional frameworks, investment promotion activities, investment facilitation services and measures to promote linkages between foreign and domestic firms.

Across the assessed economies, flows of FDI have increased in the last decade, indicating a more favourable business environment for foreign firms. Moreover, procedures for setting up companies have been streamlined. Despite progress, more could be done to further strengthen the linkages between foreign and domestic firms.

Table 0.2. Assessment in Dimension 1: Investment policy and promotion

Dimension 1	ALB	BIH	KOS	MKD	MNE	SRB
Average	2.6	2.1	2.6	3.3	2.6	3.4

Dimension 2: Trade policy and facilitation

Fair, reciprocal and predictable cross-border trade arrangements are important pillars of a healthy regional economy. Consequently, the trade policy and facilitation dimension assesses the implementation, evaluation and co-ordination of cross-border trade, including the monitoring of domestic law to meet OECD good practice.

Throughout the region, the economies perform best on non-tariff measures and export promotion, including the removal of technical barriers to trade. However, the *ex post* monitoring of free trade agreements, as well as the transparency and effectiveness of public-private consultation mechanisms, could be improved. The region would also benefit from limiting undue regulatory restrictions on services, such as easing barriers on the free movement of people.

Table 0.3. Assessment in Dimension 2: Trade policy and facilitation

Dimension 2	ALB	BIH	KOS	MKD	MNE	SRB
Average	2.8	2.2	2.3	3.8	2.6	3.3

Dimension 3: Access to finance

Facilitating access to finance is important for small and medium-sized enterprises (SMEs) and entrepreneurship promotion, and ultimately for an economy's competitiveness, growth and employment creation. External finance, whether acquired through bank loans, grants or investments from private individuals or investment firms, enables enterprises to meet their working capital requirements. This dimension focuses on policies and instruments which facilitate access to finance for SMEs in the assessed SEE economies. Across the six economies, the role of SMEs in economic activity is greater than in the European Union, and all economies have taken steps to establish better regulatory frameworks and financing support programmes. Notwithstanding these efforts, the implementation phase of these developments remains weak and there is a shortage of alternative financing instruments and mechanisms across the region.

Table 0.4. Assessment in Dimension 3: Access to finance

Dimension 3	ALB	BIH	KOS	MKD	MNE	SRB
Average	2.5	1.9	2.4	3.1	2.4	3.2

Dimension 4: Tax policy

Tax policy refers to the design of domestic and international tax rules which allow economies to raise revenues to finance public services in ways which are the least distorting for economic growth and share the tax burden across different agents in a fair manner. Throughout the six SEE economies assessed, corporate and personal income (CIT and PIT) tax rates are low and social security contributions (SSCs) are high. The six SEE economies would benefit from broadening the tax base – particularly for value-added tax (VAT) and CIT – as well as strengthening their tax policy assessment tools. The region should also revisit its wide range of corporate tax incentives and take steps to avoid falling into the trap of a “race to the bottom” type of tax competition.

Table 0.5. Assessment in Dimension 4: Tax policy

Dimension 4	ALB	BIH	KOS	MKD	MNE	SRB
Average	2.8	1.4	2.3	2.4	2.0	2.6

Dimension 5: Competition policy

An effective competition policy allows for new firms to challenge incumbents, while also encouraging efficient ones to grow and inefficient ones to exit the market. As such, competition regimes ensure that markets operate at their optimal level by taking remedial action against anti-competitive behaviour. In general, a competitive environment drives economic growth, increases living standards and reduces inequality. While the six SEE economies have the basic legal structures in place for a functioning competition regime, efforts should be made to implement them and to allocate additional resources to the relevant authorities. This dimension was assessed using a different methodology to the other dimensions; hence it lacks an assessment table.

Dimension 6: State-owned enterprises

State-owned enterprises (SOEs) represent the most direct way for a government to intervene in the commercial economy. Historically, SOEs have been concentrated in critical sectors of the economy such as energy, infrastructure and finance. Throughout the region, financial disclosure and audit practices have improved. Nevertheless, SOEs would benefit from the further professionalisation of the ownership function, including ensuring that SOEs are free from potential conflicts of interest with other government agencies, as well as prioritising oversight mechanisms.

Table 0.6. Assessment in Dimension 6: State-owned enterprises

Dimension 6	ALB	BIH	KOS	MKD	MNE	SRB
Average	2.7	1.9	3.3	2.4	2.7	3.1

Dimension 7: Education and competencies

Ensuring inclusive and high-quality education is central to creating a competitive environment. Investing in education is necessary to increase human capital and further improve labour productivity. Across the region, the SEE economies have adopted

national strategies to improve the overall standard of education and/or address specific aspects of education, such as equity, vocational education and training, and adult education. However, the latest results from the Programme for International Student Assessment (PISA) for participating SEE economies are well below those for peers from Central and Eastern Europe and the OECD average. Encouraging participation in early childhood education and increasing spending on primary and secondary education could help to ensure that all students reach the PISA baseline level needed for full socio-economic participation.

Table 0.7. **Assessment in Dimension 7: Education and competencies**

Dimension 7	ALB	BIH	KOS	MKD	MNE	SRB
Average	2.4	1.8	2.5	2.8	2.8	2.5

Dimension 8: Employment policy

Employment policy can provide a framework of strategies, action plans, laws, measures and institutions that improves the functioning of labour markets, makes them more inclusive, and enhances their ability to address post-crisis and demographic challenges. The participating SEE economies have a number of common structural labour market challenges, including high rates of youth unemployment and long-term unemployment, as well as a significant share of the population working outside the formal sector. While most SEE economies have made efforts to design comprehensive employment frameworks through consultative processes, and have relevant institutions in place, more efforts are required to address the structural challenges in the labour market. Specifically, labour market institutions should be strengthened and broadly co-ordinated to ensure effective delivery of services to job seekers.

Table 0.8. **Assessment in Dimension 8: Employment policy**

Dimension 8	ALB	BIH	KOS	MKD	MNE	SRB
Average	2.6	2.0	1.5	2.3	2.1	2.5

Dimension 9: Science, technology and innovation

Science, technology and innovation (STI) provide the means for the transition to high value-added products and services. This dimension assesses the governance of STI policy, the performance of the public research system, the support to business innovation, as well as the linkages between the public and private sectors. Throughout the region STI outcomes remain modest. A lack of funding for research and development (R&D) limits the potential for innovation, while the wider diffusion of technology does not receive sufficient policy attention. In the future, a more structured link between business and academia would help facilitate the spread of cutting-edge research, while an emphasis on individual innovation could help foster new creative sectors.

Table 0.9. **Assessment in Dimension 9: Science, technology and innovation**

Dimension 9	ALB	BIH	KOS	MKD	MNE	SRB
Average	1.3	1.3	1.1	2.1	1.8	2.1

Dimension 10: Digital society

The digitization of society has emerged as an important driver of socio-economic benefits. A solid policy framework for digital society ensures the availability and uptake of digital technologies for a well-connected digital economy. Participation in the envisioned Digital Single Market in Europe promises to boost the SEE economies' growth. Throughout the region, positive steps have been taken to expand broadband and increase access to e-business and e-commerce. In light of certain weaknesses in the digital society framework in South East Europe, e-business uptake remains low, e-inclusion is not a priority and users' perception of trust and security in digital technologies is not yet established. Improving these frameworks has therefore become a key priority in the region's economic reform agenda.

Table 0.10. **Assessment in Dimension 10: Digital society**

Dimension 10	ALB	BIH	KOS	MKD	MNE	SRB
Average	2.9	1.6	2.2	2.3	2.4	2.4

Dimension 11: Transport policy and performance

Transportation networks are necessary to facilitate the flow of people moving between rural and urban areas. There is a positive correlation between efficient transportation logistics and overall competitiveness as it lowers access costs to regions and cities, as well as to international markets. An efficient transportation grid is also critical for securing foreign investment. Across the region, development strategies ensure the alignment of transport investment and maintenance spending with long-term goals (Table 0.11). Strides have also been made in the governance sphere, owing to wide-ranging legislative and regulatory efforts. However, progress has been slow on the operational front, including on procurement and asset management.

Table 0.11. **Assessment in Dimension 11: Transport policy and performance**

Dimension 11	ALB	BIH	KOS	MKD	MNE	SRB
Average	2.7	1.2	1.8	2.0	1.6	2.6

Dimension 12: Energy policy

Energy policy seeks to achieve energy security and long-term sustainability based on effective governance and regulation; where possible energy should be delivered through market-based mechanisms. Although the six economies have taken steps to improve the competitiveness of their energy sectors, significant hurdles remain. Energy strategies and action plans must set out measurable objectives and outcomes, including on renewable energy and energy efficiency. Similarly, energy policy should be more closely aligned with international and EU good practice, and in particular should aim to meet each economy's commitments under the Paris Climate Accord. Taken as a whole, this new dimension reflects how the assessed economies have improved the delivery of reliable and affordable energy to consumers. Nevertheless, there exists room for improvement in several areas, notably in modernising infrastructure and meeting sustainability goals.

Table 0.12. **Assessment in Dimension 12: Energy policy**

Dimension 12	ALB	BIH	KOS	MKD	MNE	SRB
Average	1.9	1.4	2.3	1.6	2.1	2.2

Dimension 13: Environmental policy

Long-term economic competitiveness in the six SEE economies depends on fostering growth while also safeguarding natural assets. Despite progress in adopting overarching legal and policy frameworks, as well as land-use management frameworks, significant challenges remain in the assessed economies. Crucially, they should further integrate environmental considerations into their main economic and sectoral policies, emphasising the transition to a low-carbon economy. A key sector is energy, where their current energy mix and future plans to build coal-fired power plants contradict their climate change objectives and, ultimately, will exacerbate already high levels of air pollution. Furthermore, economic instruments including taxes and user fees should better reflect environmental costs.

Table 0.13. **Assessment in Dimension 13: Environmental policy**

Dimension 13	ALB	BIH	KOS	MKD	MNE	SRB
Average	1.8	1.3	1.8	1.6	1.8	2.1

Dimension 14: Agriculture

Increasing the productivity and sustainability of agriculture in the six SEE economies is critical for achieving their full economic potential. Regulations for agricultural inputs safeguard the economies' rich natural resources, while also enabling more productive agricultural activities. However, further policy measures and regulations are required to ensure greater efficiency and to protect local populations from harmful pollutants. For example, agricultural producer support schemes should be oriented towards productivity and sustainability objectives. Additionally, farmland consolidation plans should be implemented. Policy analysis, including evaluation and data collection, should be strengthened to better inform policy development.

Table 0.14. **Assessment in Dimension 14: Agriculture**

Dimension 14	ALB	BIH	KOS	MKD	MNE	SRB
Average	2.9	2.5	2.4	3.0	2.4	3.3

Dimension 15: Tourism

A robust tourism sector can support economic development and offer employment growth, particularly in seasonal labour markets. This dimension considers how tourism policy can be leveraged to meet the highest industry standards and support regional economies in destination branding and promotion. Considering the importance of tourism to regional economies, the private sector is slowly embracing strategy development. Nonetheless, the tourism workforce in the six SEE economies still lacks professionalism, and tourism is not yet seen as an attractive and profitable career choice. Hence, stronger links between the business sector, academia and tourism are needed to achieve the sector's full potential.

Table 0.15. **Assessment in Dimension 15: Tourism**

Dimension 15	ALB	BIH	KOS	MKD	MNE	SRB
Average	1.9	1.2	1.3	1.5	2.0	2.1

Dimension 16: Public services

High-quality public services – including all aspects of their design and delivery – are critical to competitiveness and growth in the six SEE economies. Legal frameworks for public procurement, merit-based recruitment and government session procedures are generally well developed, but full implementation remains a challenge. In public procurement, procedural compliance is the focus rather than good outcomes. The legislated principle of merit-based access to civil service positions is not fully reflected in practice. The assessed economies should strengthen the use of evidence-based approaches and public consultations in policy making. They should also continue their efforts to modernise and digitalise public services. This dimension was assessed using a different methodology to the other dimensions; hence an assessment score table is not applicable.

Dimension 17: Anti-corruption policy

Corruption imposes a variety of costs on society and can diminish the competitiveness of an economy. It wastes public resources, widens economic and social inequalities, breeds discontent and political polarisation, and reduces trust in institutions. Corruption perpetuates inequality and poverty, affecting well-being and the distribution of income. Moreover, it undermines opportunities to participate equally in social, economic and political life. Corruption can hamper growth, lower the productivity of capital, reduce incentives for innovation and productive labour, and discourage foreign direct investment. As such, fighting corruption is essential to foster long-term economic growth and competitiveness. This dimension assesses the state of current anti-corruption policies across the region. All of the SEE economies have begun to effectively collect detailed information on the implementation progress of their anti-corruption strategies and action plans. They have adopted new laws and established anti-corruption institutions. While public awareness has been raised across the region, there remains scope for governments to co-operate more effectively with civil society groups on anti-corruption issues.

Table 0.16. **Assessment in Dimension 17: Anti-corruption policy**

Dimension 17	ALB	BIH	KOS	MKD	MNE	SRB
Average	1.8	1.7	1.6	2.4	2.7	2.6

Overarching insights

Across these 17 policy dimensions, a series of common challenges and recommendations can be identified. Taken together, these cross-cutting challenges represent a formidable set of obstacles to economic growth in the participating SEE economies, ranging from labour market deficiencies to inadequate infrastructure and human resource challenges. In recognition of these obstacles, the *2018 Competitiveness Outlook in South East Europe* offers a set of strategic recommendations (see last section) which aims to reinvigorate regional productivity by fostering inclusive economic growth and sustainable development.

Crucially, these insights should not be treated as a series of stand-alone challenges and recommendations, but should be understood as part of a wider set of regional reforms – while also accounting for the various nuances of the six individual economies. The *2018 Competitiveness Outlook* is therefore an essential change-management tool for policy makers and citizens alike, combining an unparalleled breadth of coverage with clarity of analysis to deliver guidance on economic reform.

Cross-cutting challenges

- **Lack of co-ordination in policy design and weak implementation monitoring**

Across the policy dimensions, the SEE economies generally have a comprehensive set of policy frameworks in place; however, policies often lack coherence and are hobbled by weak institutional co-ordination. Moreover, implementation is frequently affected by insufficient funding or limited institutional capacities, as well as an absence of robust monitoring and evaluation systems.

- **Human capital and labour market deficiencies**

Education systems in the assessed economies are characterised by low rates of enrolment in early childhood education and a high percentage of students who are not developing the skills required to integrate into the job market. Similarly, labour markets in the economies generally exhibit high rates of unemployment, especially among the youth, as well as high levels of long-term unemployment, persistent gender gaps, and a substantial informal sector.

- **Inadequate transition towards a knowledge-based society**

In order to escape the middle-income trap, the SEE economies need to transition towards higher value-added products and services that include greater innovative and knowledge-based content. Insufficient financial support for R&D, weak support for technology diffusion and weak linkages between businesses and academia are further aggravated by a lack of incentives for business creators and endemic “brain drain”. Here, digitalisation can act as a driver of productivity.

- **Difficulty in business financing and misalignments in the tax system**

Enterprise growth is often challenged by frequent changes in legislation, which undermines their ability to plan for the long term. Small and medium-sized enterprises face the greatest difficulties in accessing finance. Entrepreneurship is further hampered by steep regulatory barriers related to restructuring and liquidation proceedings. Businesses are also affected by inefficiencies in tax incentives, while their employees face high tax burdens on their income, ultimately leading to further informality.

- **Uneven playing field for economic actors**

Existing policy measures and institutional settings often have unintended consequences and lead to unfair market competition. Challenges include poor enforcement of competition policy; regular government interference – including corruption – which undermine international competition rules; insufficient anti-corruption co-ordination and enforcement; sub-optimal governance of state-owned enterprises; tax avoidance and evasion; and public administrations with significant room for improvement.

- **Insufficient regional trade, transport and energy connectivity**

The SEE regional market faces a number of challenges in trade, transport and energy connectivity. Trade barriers affect business operations and the exchange of goods and services, as well as capital and FDI flows. Additional obstacles include an underdeveloped regional electricity market characterised by high vertical integration and an overall poorly developed transport infrastructure.

- **Lack of environmental sustainability in key policy fields**

In the six SEE economies, the energy mix is highly dependent on fossil fuels that generate high carbon dioxide emissions and pollution, directly contributing to climate change and poor air quality. The economies lack economic instruments such as taxes and user fees to encourage efficient use of resources in key sectors such as agriculture. Framework conditions for green investment and innovation have not yet been developed.

Key recommendations

- **Develop and reorient strategies to ensure policy coherence and improve policy implementation, evaluation and monitoring**

Greater inter-ministerial co-ordination is critical when designing policy frameworks that address a variety of policy areas. Frameworks should also build on international and OECD good practice. Moreover, policy frameworks could benefit from enhanced monitoring and impact assessment mechanisms to improve policy design and increase government accountability to businesses and citizens. In order to facilitate implementation, the SEE economies need to enhance the capacities and resources allocated to institutions in charge of implementation and enforcement, while ensuring that legal provisions are respected.

- **Invest in human capital formation and enhance labour market effectiveness**

The six economies should increase participation in early childhood education by improving infrastructure and affordability. Moreover, efforts should be made to reduce skills mismatches, particularly in fast-growing sectors such as tourism. The SEE economies should continue to tackle labour market challenges through creating incentives to enter the formal economy, ensuring effective enforcement of labour regulations and raising awareness of the benefits of social protection and public services. Likewise, it is important to provide effective support to jobseekers while ensuring that they respect their obligations to actively search for work.

- **Support the transition to a knowledge-based, digitalised society**

Governments should step up support to innovation and R&D and create incentives for businesses and individuals to unleash their creative potential. In particular, public procurement practices can be used to support innovation without additional budget outlays. Targeted low-budget instruments such as technology extension or innovation vouchers may generate more impact than high-ticket science and technology parks. Investment in digital skills development and awareness-raising campaigns for e-business adoption would significantly enhance the positive impact of digitalisation.

- **Facilitate business financing, broaden the tax base and address incentive problems**

The assessed SEE economies should make it easier for businesses to access finance. This can include developing alternative financing instruments, such as venture capital and business angel networks, which could particularly benefit SMEs. Furthermore, improvements in the implementation of frameworks for insolvency restructuring and liquidation are needed to reduce the risk of bankruptcy for cash-constrained companies facing late payments by clients.

- **Create fair conditions for all market participants**

While investment policy frameworks are fairly coherent, international competition rules need to be better implemented. Moreover, the economies should further strengthen FDI-SME linkages. They should also enhance the effectiveness of anti-corruption co-ordination and enforcement institutions, as well as whistleblower protection. Regional and international co-operation is vital to reduce tax evasion, while transparency for state-owned enterprises is needed to allow for fair competition. Similarly, a more open, transparent and effective public administration is required in order to ensure fair conditions for all market participants.

- **Improve regional trade, transport and energy connectivity**

While the six SEE economies should continue investing in regional infrastructure, they should also focus on implementing technical standards and reform measures in the transport and energy sectors. Railway reforms and improvements in information systems, road safety and maintenance are also needed. Furthermore, the economies should improve both internal and external border agency co-operation to re-engineer and extend the use of innovative automation tools. In the energy sector, stronger institutional capacity will be required to realise current energy market reforms, ensure unbundling of vertically integrated enterprises and facilitate third-party access.

- **Strengthen environmental and sustainability policy practice**

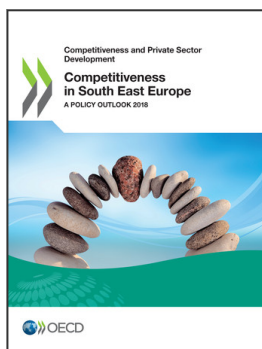
To secure long-term competitiveness, the assessed SEE economies should fully align their energy policy frameworks with climate change objectives. They should enhance policy implementation by defining roles and responsibilities for vertical and sectoral actors for water and land management. The use of economic instruments such as taxes and user fees should be adapted to encourage the efficient use of natural resources and eliminate environmentally harmful energy subsidies. Finally, the economies should strengthen policy frameworks to promote green investment and innovation.

Note

1. There are no youth unemployment data for Kosovo from 2015-16.

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