Competitiveness and Private Sector Development

Western Balkans Competitiveness Outlook 2024: Regional Profile

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Foreword

The Western Balkan economies have demonstrated resilience in the face of the COVID-19 pandemic. Despite challenges such as surging energy and food prices, tightening financial conditions and ongoing geopolitical uncertainties, the region's economies maintained a trajectory of growth, albeit at an increasingly modest pace since Russia's invasion of Ukraine in 2022. The six Western Balkan economies grew by a remarkable 7.9% in 2021, after which the growth rate has slowed to 3.4% and 2.6% in 2022 and 2023 respectively.

Since 2021, the region's economies made important progress in digital transformation and infrastructure, with broader Internet access, enhanced electronic government services, and improvements in transport infrastructure. Further, the GDP per capita of the six Western Balkan countries rose by 80% between 2003 and 2022, according to the OECD's Economic Convergence Scoreboard for the Western Balkans published in 2023. The road ahead demands more. In 2022, GDP per capita in the Western Balkans stood at 38% of the EU and OECD averages, and over the past two decades this gap has narrowed by only 11 percentage points. If the Western Balkan economies were to maintain their current growth rates, it would take at least 50 years to achieve economic convergence with the EU and the OECD.

These figures underscore the need for strong, inclusive and sustainable growth for people across the six Western Balkan economies. To advance towards this goal, we propose three priority areas:

First, governments should address barriers – including informality, corruption, inefficient state-owned enterprises – that distort the level playing field for businesses to promote trade and investment.

Second, revamping education systems and designing policies to foster conducive environment for talent retention is necessary to address labour shortages.

Third, stepping up decarbonisation and conservation efforts, including through measures aimed at facilitating private sector access to green finance, are key to further boost sustainable economic growth.

In line with these policy priorities, the new *Growth Plan for the Western Balkans*, adopted by the European Commission in November 2023, aims to provide a structured approach to increase the pace of much-needed reforms and promote faster economic convergence with the EU.

The *Western Balkans Competitiveness Outlook 2024* serves as an indispensable resource for policymakers. Offering in-depth assessments across 15 key policy areas for bolstering economic competitiveness, the *Competitiveness Outlook* provides comprehensive guidance to navigate economic reforms, enhance regional co-operation and helps the Western Balkan economies in aligning their legal frameworks and policies with those of the EU.

Now in its fourth edition since 2016, this publication tracks the implementation of reforms based on previous policy recommendations, and measures progress towards OECD standards and the EU *acquis*.

This year, the *Competitiveness Outlook* focuses on mainstreaming the green and digital transitions horizontally across all covered policy areas, by identifying measures essential to future-proofing the region's economies. The publication's findings are accessible for the first time through a landmark

interactive digital tool: the *Western Balkans Competitiveness Outlook Data Hub*. By providing policymakers with greater ability to assess and benchmark economic reforms seamlessly, the Data Hub aims to become a catalyst for designing policies that drive competitiveness and convergence.

Co-funded by the European Union, the *Competitiveness Outlook* and the accompanying *Data Hub* are the culmination of extensive collaboration. Alongside inputs from hundreds of representatives from the Western Balkans' governments, statistical offices and other regional stakeholders, the work has benefitted from a close partnership with the European Commission's Directorate – General for Neighbourhood and Enlargement Negotiations and EU delegations across the region. Thank you to all those who have contributed to this collective effort.

We are confident that the *Western Balkans Competitiveness Outlook 2024* will offer valuable insights and direction for implementing the new *Growth Plan* through Western Balkan economies' reform agendas, helping accelerate the six Western Balkan economies' EU integration, enhance sustainable economic growth, attract foreign investments, and leverage the opportunities of the Common Regional Market as a gateway to the Single Market.

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Secretary-General

OECD

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The regional profile of the *Western Balkan Competitiveness Outlook (CO) 2024* presents the assessment results of five policy clusters that are critical for economic growth, sustaining a competitive economy and achieving convergence with the European Union (EU):

1. **Infrastructure and connectivity**: Infrastructure constitutes an essential component of physical capital, facilitating the efficient movement of goods, services and people, thereby enhancing productivity.
2. **Skills**: Skills development supports human capital growth and a productive labour force.
3. **Business environment**: A strong business environment attracts investment, promotes innovation, and fosters a fair and competitive market.
4. **Digital transformation**: A digital transformation improves efficiency and creates new business opportunities.
5. **Greening**: Greening ensures that economic growth is sustainable and not at the cost of the environment.

The CO 2024 comprises 15 policy dimensions that are assessed using nearly 400 combined qualitative and quantitative indicators. These indicators detail whether policies achieve the desired results and the extent to which they help the Western Balkans achieve socio-economic convergence with the EU and the OECD area. As detailed in Table 1, the 15 dimensions, all of which are key for economic competitiveness, are grouped into the most relevant of the five clusters, allowing for a more comprehensive overview of regional progress in pursuing economic reforms. Some policy dimensions are relevant to multiple clusters and are therefore included more than once.

Drawing from cluster analysis results, the regional profile provides a comprehensive overview of regional trends to identify notable policy advancements, challenges and areas for improvement in economic development, with a particular focus on convergence with the EU. It highlights variations between economies within specific policy clusters, noting where some are excelling and where others require further development. Each cluster then offers dedicated policy recommendations on further strengthening economic growth, paying special attention to enhanced regional collaboration and integration.

The assessment and monitoring of the policy developments took place between 1 March 2021 and 1 March 2024. Any policy changes and new developments after 1 March 2024 have not been considered in the assessment. The methodology of the individual assessment of the policy areas for the economies is further explained in the reader's guide for each economy profile. More information on the methodology of the assessment can also be found at the Western Balkans Competitiveness Data Hub.

Table 1. Clusters and constituent policy dimensions

Cluster	Dimension
Infrastructure and connectivity	Transport policy
	Energy policy
	Digital society
	Science, technology and innovation
	Transport policy
Skills	Education policy
	Employment policy
	Science, technology and innovation
Business environment	Investment policy and promotion
	Trade policy
	Tax policy
	Access to finance
	State-owned enterprises
	Anti-corruption policy
Digital transformation	Digital society
	Science, technology and innovation
	Trade policy
	Access to finance
Greening	Environment policy
	Energy policy
	Agriculture policy
	Transport policy
	Tourism policy

Abbreviations and acronyms

ACER	Agency for the Co-operation of Energy Regulators
ADR	Alternative dispute resolution
AI	Artificial intelligence
ALMP	Active labour market programmes
BAN	Business angel networks
BAT	Best available techniques
BCP	Border crossing points
CBA	Cost-benefit analyses
CBAM	Carbon Border Adjustment Mechanism
CDW	Construction and demolition waste
CEFTA	Central European Free Trade Agreement
CERT	Computer emergency response teams
CIT	Corporate income tax
CRM	Common Regional Market
CSIRT	Computer security incident response teams
EBRD	European Bank for Reconstruction and Development
ECEC	Early childhood education and care
EECC	European Electronic Communications Code
EIB	European Investment Bank
EIF	European Interoperability Framework

EIP	Economic and Investment Plan
EPR	Extended producer responsibility
ETS	Emissions Trading System
EU	European Union
EURES	European Employment Services
FAS	Financial Acess Survey
FBiH	Federation of Bosnia and Herzegovina
FDI	Foreign direct investment
GDP	Gross domestic product
GERD	Gross domestic expenditure on research and development
GIS	Geographical information system
GPP	Green public procurement
GVC	Global value chains
HEI	Higher education institutes
ICC	International Chamber of Commerce
ICT	Information and communication technology
IFCMA	Inclusive Forum on Carbon Mitigation Approaches
IoT	Internet of Things
IP	Intellectual property
IPA	Instrument for Pre-accession Assistance
IPPC	Integrated Pollution Prevention and Control
IT	Information technology
ITS	Intelligent transport systems
KAS	Kosovo Agency of Statistics
KODE	Kosovo Digital Economy
MCA	Multi-criteria analysis

MSCA	Marie Sklodowska-Curie Actions
NAP	National adaptation plans
NDC	Nationally determined contributions
NECP	National Energy and Climate Plans
NEET	Not in education, employment or training
NIS	Network and information system
NPL	Non-performing loan
NRA	National regulation authorities
NTC	Net transfer capacity
NTM	Non-tariff measures
ODR	Online Dispute Resolution
PES	Public employment services
PIAAC	Programme for the International Assessment of Adult Competencies
PIRLS	Progress in International Reading Literacy Study
PISA	Programme for International Student Assessment
PIT	Personal income tax
PRTR	Pollutant Release and Transfer Register
QDMTT	Qualified Domestic Minimum Top-Up Tax
R&D	Research and development
R&I	Research and innovation
RCC	Regional Co-operation Council
RES	Renewable energy sources
RS	Republika Srpska
SDG	Sustainable Development Goals
SEA	Strategic Environmental Assessment
SEE	South East Europe

SME	Small and medium-sized enterprises
SOE	State-owned enterprises
SSC	Social security contribution
STEM	Science, technology, engineering and mathematics
STI	Science, technology and innovation
STP	Science and technology parks
TE	Tax expenditure
TIMSS	Trends in International Mathematics and Science Study
TSO	Transmission System Operators
UNDP	United Nations Development Programme
UNFCCC	UN Framework Convention on Climate Change
VAT	Value-added tax
VET	Vocational education and training
VNR	Voluntary National Review
WBIF	Western Balkans Investment Framework
WBL	Work-based learning
WCAG	Web Content Accessibility Guidelines

Executive summary

Despite the Western Balkans experiencing a robust post-pandemic recovery, marked by a gross domestic product (GDP) growth of 7.9% in 2021, further progress was subsequently hampered by the economic fallout of the Russian aggression against Ukraine. The region has grappled with economic slowdown and inflationary pressures, primarily driven by escalating food and energy prices that have disproportionately impacted lower-income households and energy-intensive sectors. Furthermore, the energy crisis has underscored the critical need to diversify energy supply and accelerate the Western Balkans' transition towards a low-carbon and environmentally sustainable economy. Against this backdrop, a comprehensive economic reform agenda that charts a course towards sustainable, inclusive and resilient growth and improved living standards is paramount for the region. This report seeks to contribute to this endeavour.

The regional profile of the *Western Balkans Competitiveness Outlook 2024* groups and presents findings from assessments of 15 policy dimensions across five broad policy clusters that are key to the region's economic growth and convergence towards OECD and EU standards. It leverages the complementarities among different policy areas and provides a holistic and comprehensive approach to economic reform agendas. The five clusters comprising this report's main chapters are 1) infrastructure and connectivity; 2) skills; 3) business environment; 4) digital transformation; and 5) greening. The new structure also closely resembles the economy-specific reform agendas requested by the Western Balkans to submit to the European Commission as part of the new Growth Plan, thus offering continuous guidance in the design and monitoring of these agendas across the region.

Key achievements

Since the last Competitiveness Outlook assessment in 2021, the Western Balkans has made strides across the five policy clusters, with infrastructure and connectivity and digital transformation particularly standing out for their notable progress.

Efforts to address infrastructure gaps and improve regional connectivity have improved

Public investment in transport – boosted by EU financing – have accelerated, albeit mostly focusing on road infrastructure rather than other travel modes. Nevertheless, visible work is ongoing on building and rehabilitating railways, including train stations. Continuing to improve physical transport infrastructure, especially along the main connectivity corridors, remains essential, as this will be translated into important gains in connectivity for businesses and citizens. The region has continued to advance towards aligning its energy policies with the EU by transposing a significant share of the EU's Third Energy Package, which has contributed to liberalising the markets for new entrants. Substantial progress has also been made in deploying organised markets for electricity in the region, providing a key step towards further regional energy market integration and enabling potential improvements in price competitiveness and supply security. Many economies have also rolled out auctions for solar, wind and hydro energy, and increased their total renewable energy capacities – total energy consumption from renewable sources stood at 26.8% in 2022, compared to 23% in the EU.

Digitalisation is increasingly being leveraged as a primary driver of economic growth

Digitalisation remains a key priority for the Western Balkan governments and is receiving further impetus through reform agenda measures. E-government national portals are continuously being upgraded with new services, functioning as a one-stop shop for e-government services and serving as a central access point for businesses and citizens. Broadband roll-out and access to fast broadband speeds are also progressing – in 2022, one-third of all connections were fibre. Additionally, many of the region's economies have witnessed robust growth in the information and communication sector (ICT), with exports of ICT services increasing from 8.2% of total service exports in 2018 to 13.0% in 2022. The region's economies are increasingly focusing on supporting small and medium-sized enterprises (SMEs) to adopt digital technologies, develop e-commerce and e-business, and engage in digital innovation.

Key priorities

By contrast, progress has been more muted in the skills, business environment and greening clusters. The following recommendations would help the region to address challenges and further promote economic growth and convergence towards the OECD and EU.

Revamp education systems and design policies to equip the population with the necessary skills for the future

Continuous brain drain coupled with skills gaps and mismatches cause labour shortages. Businesses in the Western Balkans have increasing concerns about labour shortages and report that finding skilled labour is challenging. Despite the increasing number of tertiary education and vocational education and training (VET) graduates, education systems are unable to supply the skills needed by businesses. Results from the 2022 Programme for International Student Assessment (PISA) reveal challenges in delivering quality education, with the majority of 15-year-olds (79%) in the Western Balkans assessed as low performers in at least one of the three tested subjects, compared to an OECD average of 45%. Fostering a conducive environment for talent retention and skill development is imperative for mitigating the adverse effects of brain drain and alleviating labour shortages in the long term.

Address barriers that distort the level playing field for businesses

Addressing barriers that distort the level playing field for businesses is crucial to promote trade and investment, and thereby facilitate economic growth. Progress has been limited in tackling the region's large informal sector and combating corruption, both of which hinder the business environment and create unfair distortions to competition. Strengthening the implementation of anti-corruption and tax reform measures, as well as further advancing on digitalising public services, hold significant potential to spur economic transformation by reducing corruption and informality. Prioritising reforms of state-owned enterprises (SOEs) and improving their governance also remains essential for the region. The development of a robust corporate sector is hindered by the significant presence of inefficient SOEs in the economies. It is imperative to transform SOEs' management structures, eliminate political patronage and reduce fiscal risks.

Step up decarbonisation and conservation efforts to sustainably boost economic growth

Measures to mitigate climate change and ensure the sustainability of economic activities are scarce across the Western Balkans, leading to environmental and health concerns, most notably air pollution. The annual average concentrations of fine particulate matter ($PM_{2.5}$) is almost double EU levels (22.8 µg/m^3 vs. 13.5 µg/m^3, respectively), and is four times higher than World Health Organization recommended levels of 5 µg/m^3. Meanwhile, economic sectors such as tourism, mining and agriculture persist in posing threats to biodiversity conservation and ecosystem health. Alongside combatting pollution and environmental degradation, the Western Balkans must retain private sector competitiveness in light of the EU's Carbon Border Adjustment Mechanism, particularly as the EU is the region's largest trade partner, constituting close to 70% of its goods exports. Supporting the private sector's access to green finance and training, introducing carbon pricing, and developing supporting policies aimed at protecting vulnerable populations is essential to shift the WB6 economies towards increased sustainability.

Detailed insights into the Western Balkans' performance across all the assessed policy dimensions, trends over time, or comparisons with other economies can be found in the economy profiles of the *Western Balkans Competitiveness Outlook 2024,* and the Western Balkans Competitiveness Data Hub.

1 Context

Regional co-operation across the Western Balkans is crucial for achieving convergence with the European Union. This chapter offers an overview of the region's economic developments and progress towards aligning with European Union and OECD standards, which is further explored throughout the report. It outlines the region's economic developments, its progress towards achieving the Sustainable Development Goals and its status in accession efforts. Based on these developments, the chapter sets the stage for in-depth examination across five key policy clusters necessary for achieving convergence: 1) infrastructure and connectivity; 2) skills; 3) business environment; 4) digital transformation; and 5) greening.

Economic context

Key economic developments

The Western Balkan region consists of six transitioning economies: Albania, Bosnia and Herzegovina, Kosovo*, Montenegro, North Macedonia, and Serbia. The economies of the region have become increasingly service-oriented in recent years, with services accounting for 53.3% of gross domestic product (GDP) since 2022 (World Bank, 2024[1]). Tourism is a significant contributor to the services sector, especially in Montenegro and Albania. Tourism's direct contribution to the GDP of Albania and Montenegro is almost 9%, while its indirect contribution is estimated at over 20% (WTTC, 2022[2]; EBRD, 2022[3]).

Industry contributes, on average, 22.5% to the GDP of Western Balkan economies, with the highest contribution coming from the manufacturing and construction sectors. However, the size of the manufacturing sector ranges from 3.9% of GDP in Montenegro and 6.5% of GDP in Albania to between 13% and 14% in the remaining four economies (World Bank, 2024[1]). Agriculture represents an average 10.6% of the economies' GDP, and has slightly expanded in Albania, Kosovo and Serbia in recent years. As of 2022, Albania has the largest agricultural sector as a percentage of GDP, at 18.6%, while Bosnia and Herzegovina has the smallest, at just 4.83% (World Bank, 2024[1]). The informal sector of the Western Balkan economies remains sizeable, ranging between 20% and 35% of GDP (IMF, 2024[4]).

The Western Balkans experienced strong post-pandemic recovery, with GDP growth reaching 7.9% in 2021, after which growth slowed to 3.4% in 2022 and 2.6% in 2023 (World Bank, 2024[5]). The post-pandemic recovery was marked by a divergence of performance between the more manufacturing-oriented economies (Serbia, Bosnia and Herzegovina, and North Macedonia) and the relatively more services-oriented and tourism-dependent economies (Albania, Montenegro and Kosovo). Serbia, Bosnia and Herzegovina, and North Macedonia displayed slower recovery rates relative to the services-oriented economies as they were more affected by the economic slowdown in the European Union (EU) (World Bank, 2024[5]). Meanwhile, the strong demand for tourism and international travel buoyed the economies of Albania, Kosovo and Montenegro (World Bank, 2024[5]). As of end-2023, levels of real GDP in the Western Balkans surpassed pre-pandemic levels (World Bank, 2024[5]). However, the region has made limited progress in closing the gap with the EU, with regional GDP per capita at just 38% of the EU average in 2022 (OECD, 2023[6]).

Economic growth has generally been driven by domestic demand, helped by higher real wages, policy support, tourism and recovering investment amid improving expectations in the euro area (European Commission, 2024[7]; IMF, 2024[8]; World Bank, 2024[5]). In Albania, real wages in the private sector experienced a significant growth rate of 10.2% in 2022, while real wages grew by as much as 6.7% in Bosnia and Herzegovina over 2023, supporting the contribution of consumer spending to output growth (IMF, 2024[4]). While public and minimum wage increases to mitigate the impact of the cost-of-living crisis have supported domestic demand in Albania, Bosnia and Herzegovina, and North Macedonia, they also risk fuelling inflation (IMF, 2024[8]). On the supply side, services led growth across the Western Balkan economies. Construction became an important engine for growth in Albania and Serbia, while it contributed negatively to growth in North Macedonia and Montenegro (World Bank, 2024[5]).

After a dramatic increase in regional inflation during 2022, reaching an average of 11.8%, average inflation slowed from 14.3% in January 2023 to 5.1% in December 2023 (World Bank, 2024[5]). However, the pace of price deceleration varies across the region, with inflation in December 2023 ranging from 2.2% in Bosnia and Herzegovina to 7.6% in Serbia. To counter extraordinary inflationary pressures

* This designation is without prejudice to positions on status and is in line with UNSCR 1244/1999 and the ICJ Opinion on the Kosovo declaration of independence.

over the period, the Western Balkan economies took various measures depending on their exchange rate regimes. In North Macedonia, the central bank intervened to keep the stability of the exchange rate, decreasing foreign exchange reserves by 20%. The National Bank of Serbia used tight monetary policies to curb inflation, which has kept interest rates at 6.5% since July 2023. Interest rates in North Macedonia increased considerably, rising from the historic 1.25% end-2021 value to 6.3% in September 2023 (European Commission, 2024[7]). Likewise, interest rates in Albania increased from 0.5% in March 2020 to 3.25% in November 2023, and the Albanian lek appreciated in relation to the euro (European Commission, 2024[7]; Bank of Albania, 2023[9]). Interest rates are projected to remain low in Bosnia and Herzegovina as inflation continues to decline (IMF, 2024[10]).

Despite challenges, the regional labour market improved over the period, although structural problems persist, including disparities within economies, gender gaps, informality and high youth unemployment (European Commission, 2023[11]). The unemployment rate fell across most economies over the assessment period, reaching a regional average of 10.9% in 2023 (World Bank, 2024[5]). Youth unemployment also fell significantly, reaching 25.5%, although this remains more than double the overall unemployment rate and well above the EU average of 13.8% (World Bank, 2024[5]). Participation in the labour market increased in all economies except North Macedonia, and reached an average of 54% in 2023, 0.5 of a percentage point higher than in 2022 (World Bank, 2024[5]). Albania attained the highest labour force participation rate of the Western Balkans, marking a record high for the region of 64.1% in 2023. Real wages increased by 8.4% on average in 2023, reversing 2022 trends of inflation outpacing wages (European Commission, 2024[7]). However, the growth in real wages has not been in line with productivity growth (World Bank, 2024[5]).

Despite a weakened external sector in 2022 due to challenges of persistent supply shortages and inflation resulting from the Russian Federation's war of aggression in Ukraine (Box 1.1), as well as ongoing consequences of COVID-19, the external sector of the Western Balkan economies saw improvement in 2023. The current account deficit declined to a historic low of 4.9% of GDP in 2023, from 7.8% of GDP in 2022 (World Bank, 2024[5]). The improvement in the region's external position primarily stems from reduced imports, both in volume and value, and robust net services exports, particularly evident in tourism-dependent economies. However, weak and often shrinking goods exports have dampened trade dynamics (World Bank, 2024[5]). While Bosnia and Herzegovina experienced a marginal uptick in its external deficit in 2023, all other economies in the region showed improvements in their external balances, with the most significant improvements seen in North Macedonia and Serbia (World Bank, 2024[5]). Remittances also continued to rise in the region, albeit more slowly, reaching 6.5% of GDP in 2023 compared to 7% in 2022 (World Bank, 2024[5]). Foreign direct investment (FDI) inflows amounted to 5.4% of GDP in 2023, exceeding the external deficit by 0.5% of GDP (World Bank, 2024[5]). While Albania, Bosnia and Herzegovina, and North Macedonia experienced a slight decline in foreign exchange reserves in 2022, these continued to grow in 2023 for most regional economies (World Bank, 2024[5]). Table 1.1 further explores the macroeconomic indicators.

The financial sector in the Western Balkans has been relatively stable, despite slowing growth, inflationary pressures and tighter financing conditions (World Bank, 2024[5]). Following accelerating credit growth across most economies in the second half of 2021, higher interest rates over 2022 led to decreased demand for private credit, and although credit growth stood below 6% in the second half of 2023, higher interest rates helped increase bank lending margins and profitability (World Bank, 2024[5]). From end-2021 to end-2023, the average non-performing loan (NPL) ratio improved from 4.5% to 3.8% (World Bank, 2024[5]). Improvement in capitalisation was observed in several WB6 economies over the assessment period, and as of September 2023 the bank capital adequacy ratio averaged 19.3%, which is higher than the December 2021 average of 18.2% (World Bank, 2024[5]).

The fiscal position of the Western Balkan economies also improved following the shocks of 2019 and 2020, with most showing a steadily improving fiscal balance into 2022 and 2023. Over 2023, Albania, Kosovo and Serbia exhibited an improving but still negative fiscal balance at approximately -1.4%,

-0.2% and -2.2% of GDP, respectively (World Bank, 2024[5]). Meanwhile, the fiscal balance of Montenegro turned positive in 2023, increasing from -4.9% in 2022 to 0.5% in 2023. However, the fiscal performance of Bosnia and Herzegovina and North Macedonia decreased in 2023. In Bosnia and Herzegovina, higher government spending contributed to a fiscal deficit of 0.9% of GDP in 2023, almost double the year before. This was due to an increase in subsidies, social benefits and transfers. North Macedonia's fiscal deficit remains the highest in the Western Balkans: in 2023 its fiscal balance dropped from -4.5% to -4.9% of GDP owing to lower than expected revenues and higher expenditure for wages and transfers (World Bank, 2024[5]).

Given strong GDP growth and fiscal performance, public and publicly guaranteed debt declined in most Western Balkan economies. Over 2022 to 2023, the regional average of the public and publicly guaranteed debt-to-GDP ratio fell from 50.4% to 47.3% (World Bank, 2024[5]). Despite the high cost of external borrowing, several Western Balkan economies have received improved credit ratings. In March 2024, Standard & Poor's (S&P) Global Ratings raised its long-term foreign and local currency sovereign credit ratings for Albania to "BB-" from "B+", and affirmed its "B" short-term foreign and local currency sovereign credit ratings, with a stable outlook. At the same time, Montenegro's long-term sovereign credit ratings were upgraded from stable to positive, and S&P ratings affirmed the "B/B" on Montenegro's long- and short-term foreign and local currency sovereign credit ratings (S&P Global, 2024[12]). In June 2023, S&P raised the long-term local and foreign currency sovereign credit ratings for Bosnia and Herzegovina to "B+" from "B", which it has maintained as of February 2024 (S&P Global, 2024[12]).

Table 1.1. Main regional macroeconomic indicators in the WB6 economies (2022)

Indicator	Unit of measurement	Albania	Bosnia and Herzegovina	Kosovo	Montenegro	North Macedonia	Serbia
GDP growth	% year-on-year	2.1	3.8	5.2	6.4	2.1	2.5
National GDP	USD billion	15.4	24.4	9.4	6.2	13.5	63.6
Inflation	% average	1.4	14	11.6	13.0	14.2	12.0
Current account balance	% of GDP	-7.9	-4.3	-10.5	-13.2	-6.1	-6.8
Exports of goods and services	% of GDP	31.3	48.1	38.5	51.5	74.9	63.8
Imports of goods and services	% of GDP	45.0	61.9	71.1	74.4	95.9	74.8
Net FDI	% of GDP	7.5	3	-6.2	13.5	-5.1	7.1
Public and publicly guaranteed debt	% of GDP	67.9	31.5	19.9	71.7	59.6	55.6
External debt	% of GDP	60	52.1	38.5	157.9	83.6	69.3
Unemployment	% of total active population	12	15.4	12.6	15.1	14.5	9.4
Youth unemployment	% of total	27.2	31.9	21.4	28.1	32.4	24.3
International reserves	In months of imports of G&S	6.5	6.8	2.2	5.2	3.7	5.2
Exchange rate (if applicable local currency/euro)	Value	123	1.9	1	1	61.62	117.4
Remittance inflows	% of GDP	9.6	10.5	17.1	12.6	2.7	7.1
Lending interest rate	% annual average	6.2	3.4	6.7*	5.6	4.63	2.47
Stock markets (if applicable)	Average index	n.a.	1 009	n.a.	11 077	5 888	1 720

Note: G&S = goods and services; "n.a" refers to data unavailable; * = Data from 2018.
Sources: European Commission (2024[7]); World Bank (2021[13]; 2024[5]); EBRD (2023[14]); IMF (2024[15]); UNCTAD (2024[16]).

Box 1.1. Economic impacts of Russia's full-scale invasion of Ukraine

Russia's ongoing large-scale aggression in Ukraine has had varying negative economic implications for the Western Balkan economies, with the degree of impact dependent on pre-existing economic exposure to trade and tourism from Russia and Ukraine, and reliance on Russian energy. In response to Russa's actions, all Western Balkan economies, with the exception of Serbia and Bosnia and Herzegovina (Republika Srpska), have introduced sanctions or restrictive measures on trade in line with those imposed by the EU, even if with delay, as in the case of Montenegro (Konrad-Adenauer-Stiftung, 2023[17]; Loshaj, 2024[18]).

Tourism to the region has generally continued a positive post-pandemic recovery, with limited impact by Russian and Ukrainian tourists over 2021 and 2022 (UNDP, 2022[19]). Tourism continues to increase since COVID-19 in Bosnia and Herzegovina, Montenegro, North Macedonia, and Serbia, but is yet to exceed its 2019 levels (UN WTO, 2023[20]; Eurostat, 2024[21]; World Bank, 2024[22]; Agency for Promotion and Support of Tourism, 2024[23]), as has been the case in Albania and Kosovo (Ministry of Tourism and Environment, 2023[24]; World Bank, 2024[25]; Kosovo Agency of Statistics, 2024[26]). This is in part attributed to the war in Ukraine and other persistent challenges due to COVID-19 and the energy crisis.

Since February 2022 there has been a significant and mixed shift in **trade** relations among the Western Balkan economies and Russia. While Albania, Kosovo and Montenegro have registered a sharp decline in imports from Russia, Bosnia and Herzegovina, North Macedonia, and Serbia have registered an increase, mainly due to increased energy prices, which constitute a significant part of their imports (Kostadinov, 2023[27]). However, the trade sectors of the Western Balkan economies have generally continued to expand, contributing more to GDP, as neither Russia nor Ukraine constitute a significant share of total trade for the Western Balkan economies. With the exception of Serbia, trade with Russia typically accounts for less than 2% of the Western Balkans' total trade volumes. In 2023, Russia accounted for around 4% of Serbia's total trade exports and 5.3% of its imports (United Nations, 2024[28]). From 2021 to 2022, Russian exports to Serbia increased by 118%, from EUR 1.5 billion to EUR 2.6 billion (United Nations, 2024[28]). Serbian exports to Russia likewise increased from EUR 842 million in 2021 to EUR 1 billion in 2023 (United Nations, 2024[28]). However, trade in certain goods has been particularly affected, as Russia accounts for a significant share of wheat and fertiliser imports in several Western Balkans economies (United Nations, 2024[28]).

Trade relations with Ukraine tend to represent an even smaller percentage of total trade for the Western Balkans and have generally declined since the start of the conflict (United Nations, 2024[28]). In 2022, the value of exports from Albania and Serbia to Ukraine declined, while those from Bosnia and Herzegovina, Montenegro, and North Macedonia increased significantly (United Nations, 2024[28]). In the same year, reported imports from Ukraine decreased in Albania, North Macedonia and Serbia, while they increased in Bosnia and Herzegovina[1] and Montenegro. However, the uptick in imports from Russia to Bosnia and Herzegovina was reversed in 2023 when they dropped to below the 2021 value (United Nations, 2024[28]).

FDI into the region has generally increased, although 2023 saw varying scales of FDI decreases for Montenegro, North Macedonia and Serbia (Bank of Montenegro, 2024[29]). While Russia is not a major source of foreign investment in Albania, Kosovo and North Macedonia, it is the largest foreign investor in Montenegro and the fourth largest investor in Serbia (UNCTAD, 2023[30]). Bosnia and Herzegovina has begun receiving increased FDI from Russia due to the lack of sanctions (FIPA, 2023[31]). In Montenegro, where Russian investment is historically directed towards tourism and real estate, FDI

significantly declined from EUR 164.5 million in 2011 to EUR 27.4 million in 2022 (European Commission, 2024[7]; Bank of Montenegro, 2024[29]).

The **energy** sectors of Albania, Kosovo and Montenegro have not been significantly affected by the conflict as they consume little or no Russian gas, instead relying on domestic or imported fossil fuels, and some hydropower and solar. For Bosnia and Herzegovina, North Macedonia, and Serbia, natural gas accounts for 3.6%, 2.8% and 12.1% of total final energy consumption (IEA, 2022[32]), respectively. Given that Russia is the main source of natural gas imports for these three economies, increased focus has been placed on building infrastructure to diversify energy sources (WBIF, 2023[33]). Since the start of the conflict, energy prices have risen considerably throughout the region, with the cost of gas for household consumers increasing by as much as 60% for Bosnia and Herzegovina and 90% for North Macedonia (Eurostat, 2024[34]). The higher prices have negatively impacted households' real disposable income, with a disproportionate impact on those most vulnerable and at risk of poverty. In response to the social and economic impact of the energy crisis generated by the Russian war of aggression against Ukraine, the EU allocated EUR 1 billion to the Western Balkans under the 2023 Energy Support Package immediate measures (European Commission, 2023[35]).

1. In the case of Bosnia and Herzegovina, reported imports from Ukraine increased, while Ukraine's reported exports to Bosnia and Herzegovina decreased over 2021-2022.

Sustainable development

All Western Balkan economies have committed to implementing the 2030 Agenda for Sustainable Development; **however, its integration into national policy practices could improve in most economies** (Table 1.2). While all economies except Serbia have a designated lead unit responsible for the co-ordination and implementation of the Sustainable Development Goals (SDGs) across ministries, the convening and capacity of these units are uneven, with some holding a nominal rather than active role (such as in North Macedonia) (Sachs et al., 2023[36]). Monitoring of the SDGs is also weak across most economies. All Western Balkan economies, apart from Kosovo, have undertaken at least one Voluntary National Review (VNR) of their implementation of the SDG Agenda. As Kosovo is a non-member of the United Nations it is unable to submit a VNR; however, a review of Kosovo's implementation of the SDG Agenda was undertaken by the Institute for Development Policy in 2019 (INDEP, 2019[37]).

Amidst challenges owing to the COVID-19 pandemic and Russia's war of aggression against Ukraine, progress towards improving economic and social outcomes in the Western Balkan economies has slowed over the assessment period. Poverty in the Western Balkans returned to a declining trend during 2023, but at a slower pace than pre-pandemic levels (World Bank, 2024[5]). Significant challenges remain in the area of nutritional well-being for most economies (SDG 2), with little progress made since 2021. Health and well-being outcomes tend to be strongly affected by high rates of non-communicable diseases (cardiovascular disease, diabetes, cancer, etc.) and obesity; lack of access to high-quality healthcare; and stagnation in the area of universal health coverage (SDG 3). Above-target pollution rates also negatively affect health and well-being.

Improvement in economic outcomes continues to be undermined by weaknesses in competitiveness, infrastructure and innovation. High unemployment rates weigh on the performance of most economies in the area of decent work and economic growth (SDG 8), while low levels of expenditure on research and development tend to hinder performance in industry, innovation and infrastructure (SDG 9). Inequality also continues to pose a considerable challenge in the Western Balkan economies, although Montenegro, North Macedonia and Serbia are on track towards SDG achievement (SDG 10). Access to basic sanitation services has generally increased, although wastewater treatment

rates tend to remain low (SDG 6). Air pollution remains a major problem and continues to impede progress in sustainable urban development (SDG 11), as does the lack of access to public transport.

Table 1.2. Progress of the WB6 economies in achieving the Sustainable Development Goals

SDG	Albania	Bosnia and Herzegovina	Montenegro	North Macedonia	Serbia
1 – No poverty	SDG achieved	SDG achieved	SDG achieved	Challenges remain	SDG achieved
2 – Zero hunger	Significant challenges	Significant challenges	Major challenges	Significant challenges	Significant challenges
3 – Good health and well-being	Significant challenges	Significant challenges	Significant challenges	Significant challenges	Significant challenges
4 – Quality education	Challenges remain	Significant challenges	Challenges remain	Significant challenges	Challenges remain
5 – Gender equality	Significant challenges	Significant challenges	Significant challenges	Significant challenges	Significant challenges
6 – Clean water and sanitation	Significant challenges	Significant challenges	Significant challenges	Significant challenges	Significant challenges
7 – Affordable and clean energy	Challenges remain	Significant challenges	Challenges remain	Significant challenges	Significant challenges
8 – Decent work and economic growth	Major challenges	Significant challenges	Significant challenges	Significant challenges	Significant challenges
9 – Industry, innovation and infrastructure	Significant challenges	Significant challenges	Significant challenges	Significant challenges	Significant challenges
10 – Reduced inequalities	Challenges remain	Significant challenges	Significant challenges	Significant challenges	Significant challenges
11 – Sustainable cities and communities	Significant challenges	Major challenges	Significant challenges	Major challenges	Significant challenges
12 – Responsible consumption and production	Significant challenges	Significant challenges	Information unavailable	Significant challenges	Significant challenges
13 – Climate action	SDG achieved	Significant challenges	Challenges remain	Challenges remain	Significant challenges
14 – Life below water	Major challenges	Challenges remain	Major challenges	Information unavailable	Information unavailable
15 – Life on land	Significant challenges	Significant challenges	Major challenges	Significant challenges	Major challenges
16 – Peace, justice and strong institutions	Major challenges	Significant challenges	Significant challenges	Significant challenges	Major challenges
17 – Partnerships for the goals	Significant challenges	Challenges remain	Challenges remain	Challenges remain	Challenges remain

Note: The order of progress (from greatest to least) is as follows: SDG achieved; challenges remain; significant challenges; major challenges. Kosovo is not included in the table as it is not a member state of the UN and therefore unable to submit a VNR.
Source: Sachs et al. (2023[36]).

Progress across environment-oriented goals has been variable. In the area of clean energy (SDG 7), high CO_2 emissions from fuel combustion for electricity output is a common indicator of low performance across all economies, although some perform better in terms of renewable energy share as a percentage of final energy consumption (Albania, Bosnia and Herzegovina, and Montenegro). While Albania has achieved its target in the area of climate action (SDG 13), the other economies face challenges ranging from moderate (Montenegro and North Macedonia) to significant (Bosnia and Herzegovina and Serbia). The lack of protection for terrestrial and marine ecosystems poses a significant challenge in most economies, as does integrating circular economy principles into economic models (SDGs 12, 14 and 15).

Institutional integrity remains one of the lowest performing areas across the Western Balkan economies (SDG 16). Significant challenges remain in the case of Bosnia and Herzegovina, Montenegro, and North Macedonia, with moderate improvement in the latter two economies. Meanwhile, Albania and Serbia present major challenges and stagnating improvement within institutional integrity. Impediments to progress in SDG 16 are due to persistent corruption, continuance of unlawful expropriation practices, poor timeliness of administrative proceedings and declining performance in press freedom.

EU accession developments

All WB6 economies are committed to pursuing EU accession, and the process of convergence with the EU acquis continues to be a key anchor for reforms in the region. Albania, Bosnia and Herzegovina, Montenegro, North Macedonia, and Serbia are candidates for EU accession, and Kosovo is a potential candidate. In February 2020, the European Commission presented its revised enlargement methodology, which emphasises credible fundamental reforms, stronger political steer, increased dynamism and predictability of the process (European Commission, 2021[38]). The negotiating framework incorporates the new approach to negotiations on the chapters on judiciary and fundamental rights, and on justice, freedom and security, as well as the issue of the normalisation of relations between Serbia and Kosovo. Along with the revised methodology, the Commission adopted an Economic & Investment Plan to support and bring the Western Balkans closer to the EU.

Bosnia and Herzegovina and Kosovo have reached notable milestones in their candidacy journeys during the assessment period, and Albania and North Macedonia have started accession negotiations. Having submitted its application for membership in 2016, Bosnia and Herzegovina was granted EU candidate status in December 2022. Bosnia and Herzegovina started its EU accession talks in March 2023 after adopting some long-awaited reforms. The Commission recommended candidate status for Kosovo in October 2022, which was officially granted by the European Council following Kosovo's submission of application for EU membership in December 2022 (European Commission, 2023[39]). Since 2010, citizens of the WB6 economies except for Kosovo have been able to travel visa-free to EU Member States within the Schengen area. As of January 2024, visa liberalisation for Kosovo citizens entered into force, allowing Kosovar nationals to travel freely into the Schengen area.

Albania, Montenegro, North Macedonia and Serbia have made varying levels of progress in negotiations during the assessment period. For Montenegro, 33 of the 35 negotiating chapters have been opened, of which three have been provisionally closed as of December 2023 (European Commission, 2023[11]). So far, 22 out of 35 negotiation chapters have been opened for Serbia. The European Council's latest conclusions stated that Serbia had made overall progress, but progress on judiciary reforms, strengthening fundamental rights and the normalisation of relations with Kosovo determines the pace of negotiations (European Council, 2023[40]). The first intergovernmental conference with Albania and North Macedonia took place in July 2022, marking the formal start of accession negotiations. At the same time, the first step in the accession negotiation process was taken with the launch of the analytical examination of the EU acquis, the "screening". The next step in Albania and North Macedonia's accession process is the opening of the first negotiation cluster, which covers chapters on the judiciary, fundamental rights and justice.

The importance of advancing on the socio-economic reform agenda remains a critical priority in the journey of the WB6 to EU membership. The findings of this Competitiveness Outlook 2024 offer monitoring and assessment on a number of critical chapters for the EU acquis, while its recommendations provide the guidance needed to meet accession requirements.

On 8 November 2023 the European Commission adopted a new Growth Plan for the Western Balkans. Backed by EUR 6 billion in non-repayable loan and support, the aim of the Growth Plan is to bring the WB6 closer to the EU by offering some of the benefits of EU membership in advance of accession,

boosting the region's economic growth and accelerating socio-economic convergence (European Commission, 2023[41]). The new Growth Plan is based on four pillars that are aimed at:

1. "Enhancing economic integration with the European Union's single market, subject to the Western Balkans aligning with single market rules and opening the relevant sectors and areas to all their neighbours at the same time, in line with the Common Regional Market;
2. Boosting economic integration within the Western Balkans through the Common Regional Market;
3. Accelerating fundamental reforms, including on the fundamentals cluster[1], supporting the Western Balkans' path towards EU membership, improving sustainable economic growth including through attracting foreign investments and strengthening regional stability;
4. Increasing financial assistance to support the reforms through a Reform and Growth Facility for the Western Balkans" (European Commission, 2023[42]).

As part of the new Growth Plan, the Western Balkan economies have been asked to submit to the European Commission economy-specific Reform Agendas listing a number of structural reforms that would need to be implemented in order to access part of the Growth Plan's funding. All Reform Agendas are structured along the same four policy areas: 1) business environment and private sector development; 2) green and digital transformation; 3) human capital development; and 4) fundamentals (of the EU accession process). They replace Economic Reform Programmes' chapter IV on structural challenges, as, going forward, the Economic Reform Programmes will only cover macro fiscal aspects.

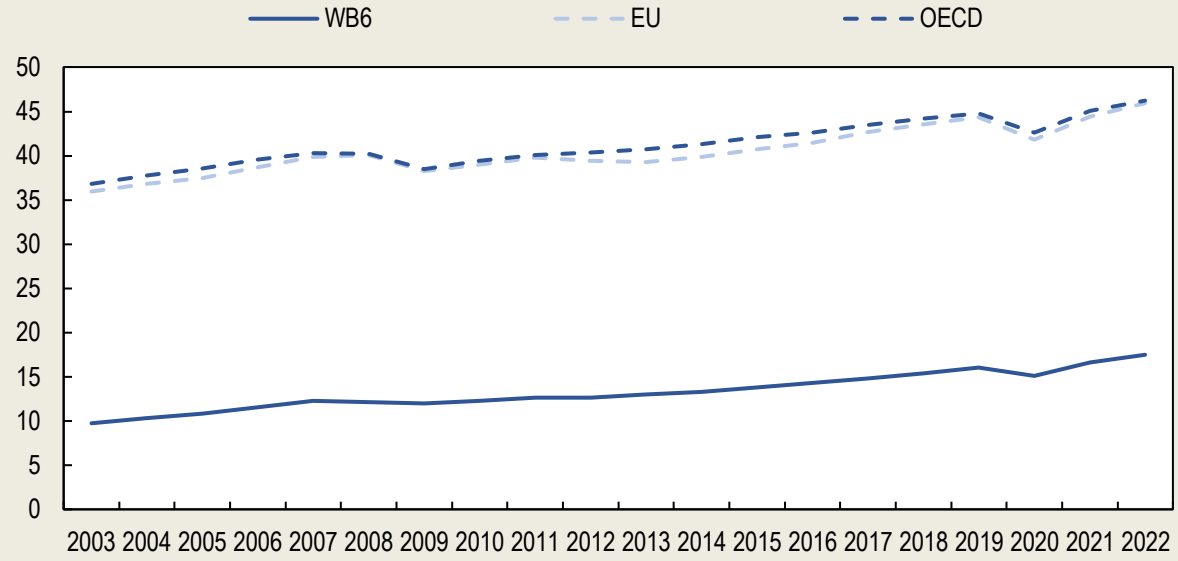
The new Growth Plan builds on the existing enlargement methodology and creates a package of mutually reinforcing measures. The aim is to speed up accession negotiations by providing incentives to economies to accelerate the adoption and implementation of the EU *acquis*, while narrowing the economic convergence between the Western Balkans and EU member states. The OECD has recently released the Economic Convergence Scoreboard for the Western Balkans 2023 to track the region's performance in achieving economic convergence with the EU and the OECD, and to highlight policy bottlenecks that hinder faster economic growth in a sustainable and inclusive way (OECD, 2023[6]) (Box 1.2).

Box 1.2. Economic Convergence Scoreboard for the Western Balkans 2023

The GDP per capita of the Western Balkans grew by 80% between 2003 and 2022, marking significant progress and contrasting with the comparatively modest increases of 27% in the EU and 25% in the OECD (Figure 1.1). This growth has helped narrow the economic gap, reducing the percentage difference in GDP per capita between the region and the EU and OECD averages by approximately 40%. However, with the region's GDP per capita in 2022 standing at USD (purchasing power parity [PPP] international $) 17 505 (EUR 16 6291) – less than half of the EU's USD 45 978 (EUR 43 679) and the OECD's USD 46 208 (EUR 43 897) – the regional economy faces persistent challenges in achieving economic convergence (Figure 1). These contrasting trends highlight the complexities of convergence across the region and the need for both collaborative and comprehensive policy development to foster a productive and competitive region.

Figure 1.1. Western Balkan GDP per capita convergence with the EU and OECD area

In purchasing power parity 2017 USD (thousands)



Note: Data unavailable for Kosovo between 2003 and 2007.
Source: World Bank (2022[43]).

StatLink https://stat.link/ahw5l6

In this context, the OECD developed the Economic Convergence Scoreboard in 2023, marking the establishment of a recurring assessment mechanism and dedicated tool designed to evaluate the extent of the Western Balkans' economic convergence with the EU and the OECD area. The scoreboard was prepared to inform discussions at the Berlin Process Western Balkans Leaders' Summit 2023 and is grounded in a decade-long series of policy assessments, the scoreboard offers a thorough analysis of the region's progress across five key policy areas, or clusters, crucial for attaining sustainable and inclusive economic growth. These clusters are *business environment*, *skills*, *infrastructure and connectivity*, *greening*, and *digitalisation*.

Since 2008, the Western Balkans has made positive progress across most of the policy clusters – albeit with some areas still requiring significant development – underscoring not only the adoption of policies in alignment with the EU acquis and OECD standards, but also the region's shared commitment to achieving convergence. The region achieved notable advances during the three observed periods (2008-12, 2013-17, 2018-22) in *business environment*, particularly in attracting FDI, trade openness and new business density, all of which exceed EU rates. The WB6 has also made positive strides in *infrastructure and connectivity*. For instance, the region is nearing convergence with EU rates in road in total freight transport and logistics performance, and has achieved convergence in average time to obtain electricity. However, the region must still improve its rail and road infrastructure, which will be crucial for fostering economic connectivity, underscoring persistent challenges within the *infrastructure and connectivity* cluster.

The *skills* and *greening* clusters require further development. In particular, the rate of young people not in employment, education or training (NEET) has stagnated since 2008, suggesting a policy gap relating to youth employment and empowerment. Furthermore, the level of research and development remains

approximately one-fifth of the EU level, highlighting another policy gap in an area critical for fostering a competitive economy. As for *greening*, the region recognises the importance of environmental policy in achieving convergence, as seen in the improved OECD Competitiveness Outlook environmental policy indicator, but upsurges in fertiliser use and waste generation, both of which started from low levels compared to the EU, reflect inconsistent policy development. Additionally, CO_2 emissions per GDP by the WB6 have consistently remained at approximately double EU levels between 2008 and 2020, which is a policy area that receives significant priority from both the EU and OECD area, emphasising the necessity for improvement in this area.

In the context of aligning with OECD good practices and standards, the Western Balkans has demonstrated overall progress, albeit with setbacks in the OECD's *Services Trade Restrictiveness Index* and *Digital Services Trade Restrictiveness Index*, and the Competitiveness Outlook anti-corruption policy. Notably, advances have been made in Competitiveness Outlook energy, environment and finance policies, with the region experiencing consistent progress since 2008 in these areas.

1. The 2022 market exchange rate has been used to convert PPP constant 2017 international dollars into EUR.
Source: OECD (2023[6]).

EU financial and development support

The EU is the largest provider of external financial assistance to the Western Balkan economies. The continued significant support from the EU helps the WB6 economies to realise their reform processes and endeavours that bring them closer to the acquis. EU financial support to the region has been provided through both temporary support, such as COVID-19 assistance packages, and long-term investment programmes and funds such as the Instrument for Pre-accession Assistance (IPA), European Investment Bank (EIB) loans and Western Balkans Investment Framework (WBIF) grants. The EU also provides important support through guarantees for public and private investment to reduce the associated risks and costs.

Since 2007, the EU has provided the Western Balkans with over EUR 12 billion in pre-accession funds aimed at strengthening democracy and the rule of law, strengthening competitiveness, boosting innovation in agriculture and rural development, reforming the public administration, improving energy and transport infrastructure and policies, and fostering climate action. A further EUR 10.2 billion of financing has been provided through the EIB since 1999, while financing of EUR 1.14 billion through the WBIF has leveraged additional investment worth an estimated EUR 16.4 billion. The EU has also provided significant grant financing to support disaster relief and reconstruction in the aftermath of the floods that have affected many regional economies, as well as the disastrous earthquake that struck Albania in 2019 (IBRD/World Bank, 2021[44]).

The EU has also been instrumental in supporting the Western Balkan economies in their response to the COVID-19 pandemic, providing the region with combined support of more than EUR 3.3 billion. This included more than EUR 500 million in repurposed IPA 2014-2020 financing to cover the urgent needs of the health sector, support economic and social recovery in the aftermath of the crisis, and help economies gain access to COVID-19 vaccines through a EUR 70 million package adopted in December 2020. In addition, in February 2021 a joint EU/World Health Organization project provided assistance of EUR 7 million to support vaccination readiness and health sector resilience in the region (European Commission, 2021[45]). The WB6 economies have also been recipients of the EU's regional economic reactivation package of EUR 385 million. A further EUR 500 million was provided in macro-financial assistance to support economic recovery in Albania, Kosovo, Montenegro and North Macedonia, while the EIB has mobilised EUR 1.7 billion.

Through the Economic and Investment Plan (EIP) for the Western Balkans 2021-2027, the EU will provide the Western Balkans with EUR 9 billion through IPA funds, with the aim of mobilising another EUR 20 billion in investments through the Western Balkan Guarantee Facility (WBIF, 2024[46]). As of 2023, the EU has approved funding of EUR 4.29 billion in grants, which is expected to mobilise EUR 15.9 billion in overall investments. The plan supports investment in the green and digital transition through projects in six priority areas: 1) sustainable transport; 2) clean energy; 3) environment and climate; 4) digital future; 5) competitiveness of the business sector; and 6) human capital development (WBIF, 2024[46]). Ten flagship projects are foreseen for the region and are currently at various stages of implementation. These projects include cross-border transport routes for the region (e.g. the construction of the Peace Highway to connect Niš, Serbia via Priština, to Tirana and Durrës in Albania) and several cross-border rail interconnections, such as Serbia to Bulgaria, Montenegro with Albania and Serbia, and North Macedonia to Bulgaria (WBIF, 2024[46]). Notably, in the area of clean energy the EIP also endorses the Trans-Balkan Electricity Corridor, which is a regional power network connecting the electricity transmission systems of Bosnia and Herzegovina, Montenegro, and Serbia with those of Croatia, Hungary, Romania and Italy (European Commission, 2024[47]).

The Reform and Growth Facility for the Western Balkans, which supports the new Growth Plan for the Western Balkans, was adopted in November 2023 and will provide a further EUR 6 billion in non-repayable support and loan support over 2024-2027, complementary to the EU assistance already provided through IPA funding. The proposed facility will provide financial support in the form of non-repayable support (up to EUR 2 billion) and loans (up to EUR 4 billion) through direct disbursements to the national budgets, or as capital investment financing through the WBIF over 2024-2027.

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Note

[1] In line with Communication on "Enhancing the accession process – A credible EU perspective for the Western Balkans" COM(2020)57, the fundamentals cluster includes: chapter 23 – Judiciary and fundamental rights; chapter 24 – Justice, Freedom and Security, the economic criteria, the functioning of democratic institutions, public administration reform; chapter 5 – Public procurement; chapter 18 – Statistics; and chapter 32 – Financial control (European Commission, 2023[42]).

2 Infrastructure and connectivity cluster

This chapter aims to assess and quantify tangible progress in the six Western Balkan (WB6) economies in policies related to infrastructure and connectivity, focusing on the development, functioning and integration of infrastructure in the transport, energy and digital sectors. It also examines progress in establishing functioning research and development infrastructure that can serve as a bedrock for regional collaboration and competitiveness. First, the chapter looks at the region's policies in planning and managing the development of its transport, energy and digital infrastructure networks, including to what extent policies are in place to ensure that infrastructure is resilient to the impacts of climate change, cyberattacks and other threats. Second, it examines the extent to which the region is benefitting from the potential of market-based reforms to improve the functioning of its transport, energy and digital infrastructure networks. Finally, the chapter assesses the degree to which reforms are using infrastructure to drive the region's integration into a common economic space, both between the WB6 economies and with the European Union.

Key findings

The WB6 economies have a significant infrastructure gap with the European Union (EU) and struggle to converge to the EU level of infrastructure development and performance. Particularly, challenges persist in developing the density of transport infrastructure, the reliability of energy infrastructure and upgrading the digital infrastructure. Nevertheless, some **key achievements** have been made in recent years:

- Substantial progress has been made in deploying organised markets for electricity in the region. With market coupling between Albania and Kosovo having taken place in early 2024, five out of six economies have organised day-ahead markets for electricity. This provides a key step towards further regional energy market integration and has the potential to improve price competitiveness and supply security.
- Policies to enhance the resilience of critical infrastructure are at an early stage in the region, and primarily focus on assessing rather than mitigating risks. Nevertheless, progress has been made, particularly in the cybersecurity field with the establishment of the Western Balkans Cyber Capacity Centre in 2023.
- The energy crisis has pushed the WB6 economies to become increasingly aware of the need to improve their resilience to external supply shocks by preparing adequate emergency response plans and working on the diversification of their energy supplies. Most economies are looking to achieve this goal through an increased focus on the deployment of renewable energy sources, although more ambitious efforts are required to achieve both goals.
- Progress is being made in most WB6 economies to lower barriers to market entry in the electronic communications sector as a means of supporting digital connectivity. This is being achieved by the introduction of EU good practices in facilitating market access through alignment with the European Electronic Communications Code (EECC), with Albania and Serbia having made the most progress and other economies following suit.

However, despite these positive regional trends, there is still significant scope to strengthen policies and improve outcomes related to infrastructure and connectivity. As such, some of the most salient **key challenges** facing the region are as follows:

- Project appraisal and selection processes have significant room for improvement to ensure that investments are channelled into cost-effective and sustainable infrastructure projects. Albania, Montenegro and Serbia have made the most progress in improving their appraisal processes since the previous assessment, but have not yet been followed by the other WB6 economies.
- Insufficient competition in electricity markets and domination by powerful incumbents often constrain any benefits of the deployment of organised power markets. In all WB6 economies, except for Bosnia and Herzegovina, dominant market incumbents represent more than 80% of the share of electricity traded on the market.
- The region's road and rail infrastructure is underdeveloped, at only 27% and 45% of the EU's respective levels of road and rail infrastructure density in 2021. When comparing with five EU member states (EU-5) that have similar topographic characteristics,[1] the gaps remain sizeable, with the WB6 average only 60% of the average road infrastructure density and 56% of the average rail infrastructure density of the selected EU member states.
- Although participation in regional and European research collaboration platforms has increased, it is constrained by the overall low competitiveness and development of the region's research and innovation infrastructure, underpinned by low human resources and insufficient financial support.

Introduction

Well-developed and well-functioning infrastructure networks are the foundation for economic competitiveness as they are necessary for trade, communications and economic activity. Composed of small economies that neighbour both each other and the European Union, the Western Balkan region stands to gain from promoting the connectedness of its infrastructure networks, which can facilitate trade flows, the movement of people, and the efficiency of electronic communications and energy networks. The notion of infrastructure is broad and can cover a wide array of sectors and sub-sectors. The analysis in this chapter focuses on the policy dimensions relevant for infrastructure and connectivity covered under the *Western Balkans Competitiveness Outlook 2024*, namely transport, energy, digital society, and science, technology and innovation.

Closing the infrastructure gap and building quality infrastructure

To support their economic competitiveness and development, the WB6 economies will need to expand and modernise their transport, energy and electronic communications infrastructure networks. Large-scale initiatives, such as the EU's Economic and Investment Plan for the Western Balkans, initiated in 2020, are in place to help bridge the infrastructure gap and mobilise the capital investments necessary for developing the region's infrastructure.

Planning for current and future infrastructure needs

Governments need to have well-developed, comprehensive and strategic visions to ensure the proper development of their infrastructure networks. Substantial benefits can be unleashed when these visions are long term, aligned with government's horizontal policy priorities and appropriately consider the concerns of key stakeholders. Furthermore, efficient co-ordination mechanisms between the different actors involved are key to support implementation, and robust asset management practices are necessary to ensure that infrastructure is adequately maintained throughout its life cycle and provides the best value for money.[2]

> *Comprehensive infrastructure development plans are in place, but they are not always based on data-driven tools and implementation is not consistently monitored*

The infrastructure development strategies of the WB6 economies in the transport, energy and digital sectors are generally well developed, set over a long-term horizon, and aligned with overarching policy priorities such as national development strategies or economic reform programmes. However, these plans are not always supported by evidence-based quantitative models or mapping tools that aim to align infrastructure development plans with projected demand. While the situation is better in the energy and broadband infrastructure areas than in the transport sector, it could be improved across the board.

The WB6 economies are at different stages of developing or updating their strategic frameworks to enhance long-term planning and resource allocation for the **transport** sector. These policy frameworks outline planned reforms in the sector that help align and prioritise investments into transport infrastructure. The updated strategies for Albania and Serbia are currently pending adoption, while the other WB6 economies are implementing their frameworks.

While these efforts demonstrate a commitment to planning infrastructure in the long term, the effectiveness of these frameworks ultimately depends on their successful implementation, effective interinstitutional co-ordination mechanisms and long-term political commitment. Moreover, monitoring and evaluation of transport policy frameworks is not consistently applied in all economies. For instance, even in Montenegro, which can be considered a good performer in monitoring its transport policies compared to regional peers,

the last monitoring report for its Transport Development Strategy 2019-35 was published for the 2019-2020 period, showing a lack of consistency and commitment to the monitoring process.

The WB6 transport sectors are also supported by transport master plans, which guide the overall development of the transport network and allocate investments to transport infrastructure projects. Apart from Albania, Montenegro and Serbia, limited progress has been observed in the development of national transport models that can support these plans with quantitative demand forecasts, highlighting a need for enhanced data-driven decision making in transport infrastructure development. In May 2023, the WB6 economies and the European Commission signed a high-level understanding on the extension of the Trans-European Transport Network[3] (TEN-T) to the region, establishing a dedicated Western Balkans-Eastern Mediterranean transport corridor that should help facilitate the planning and alignment of transport networks and the allocation of relevant investments (Transport Community, 2023[1]).

The **energy** policy, legal and institutional frameworks in the WB6 economies contain long-term network development plans as a key tool for planning the development of electricity and natural gas infrastructure networks and identifying priority projects for investment. Most economies have also conducted adequacy assessments of their energy networks, which are essential for maintaining and planning energy infrastructure investments in line with projected supply and demand. However, Albania and Kosovo have not yet conducted such assessments, and due to concerns over the role of national policy making in determining the energy mix, the focus of adequacy assessments in the region continues to be economy-specific, which is a barrier to potential synergies through an understanding of the impacts of varying consumption patterns and supply configurations across the region.[4]

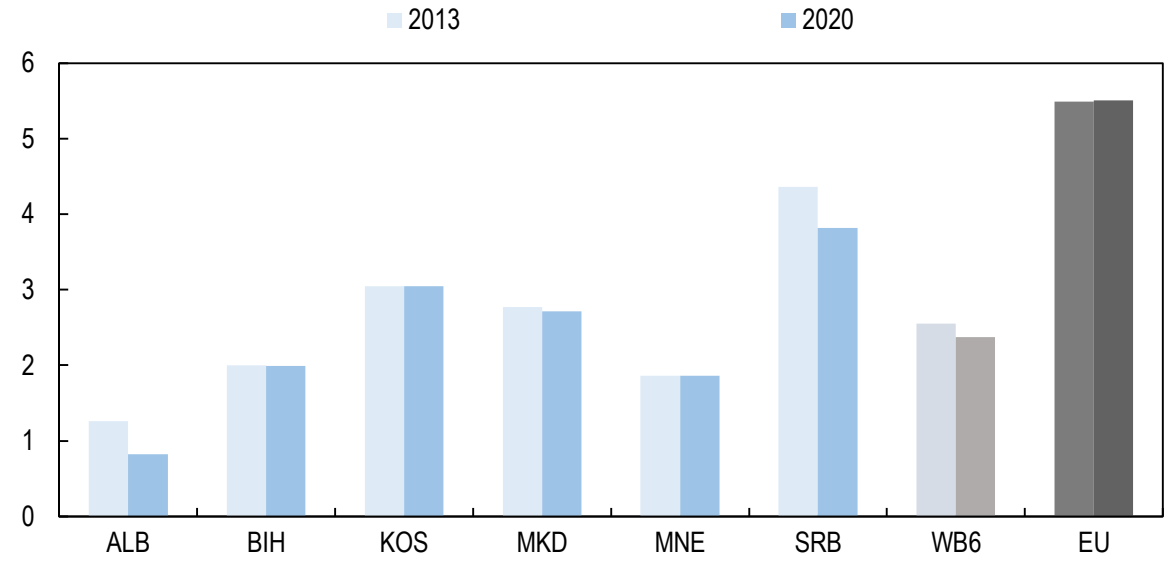
Regarding the planning of **digital infrastructure**, WB6 economies are implementing plans to improve their digital connectivity by supporting the deployment of broadband infrastructure networks, with a particular focus in recent years being put on extending coverage to rural areas. Some economies have also made progress in establishing broadband mapping to support the development of these networks and prioritise underserved areas, with Serbia, Montenegro, North Macedonia and Kosovo showing the best progress so far and Bosnia and Herzegovina lagging behind (for more information, see Chapter 4: Digital transformation).

Infrastructure investment plans are in place in all WB6 economies but do not adequately capture the region's investment needs to achieve the green transition

The **transport** infrastructure of WB6 economies is considerably less developed than in the EU. Regarding the density of rail infrastructure, WB6 economies exhibited an average density of 2.4 kilometres (km) per area of 100 km^2 in 2020, which is 45% of the EU's average value (5.5 km^2) (Figure 2.1). The development of road infrastructure follows an upward trend – the average road infrastructure density in the WB6 economies rose from 37.5 km in 2017 to 39.3 km in 2021. However, the gap with the EU is even wider, as EU average density reached 146.8 km in 2021, more than three times the density in the WB6 (Figure 2.2). When also taking topography into consideration, and comparing the WB6 to the five EU member states with geographic proximity to the region and similar topography, a sizeable gap can still be identified.

Figure 2.1. Rail infrastructure density in the WB6 economies and the EU (2013, 2020)

Rail infrastructure (km) by area of 100 km^2



Notes: Methodological details in the Annex document. EU-5 comprises Austria, Bulgaria, Croatia, Greece and Romania.
Sources: OECD (2023[2]); Kosovo Agency of Statistics (KAS).

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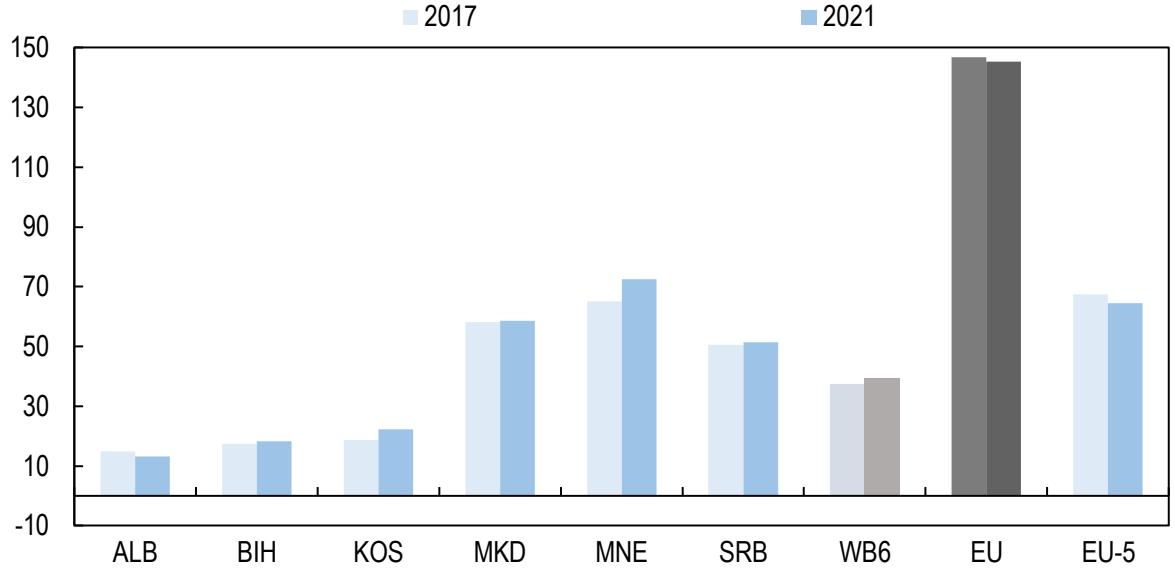
Figure 2.2. Road infrastructure density in the WB6 economies and the EU (2017, 2021)

Road infrastructure (km) by area of 100 km^2



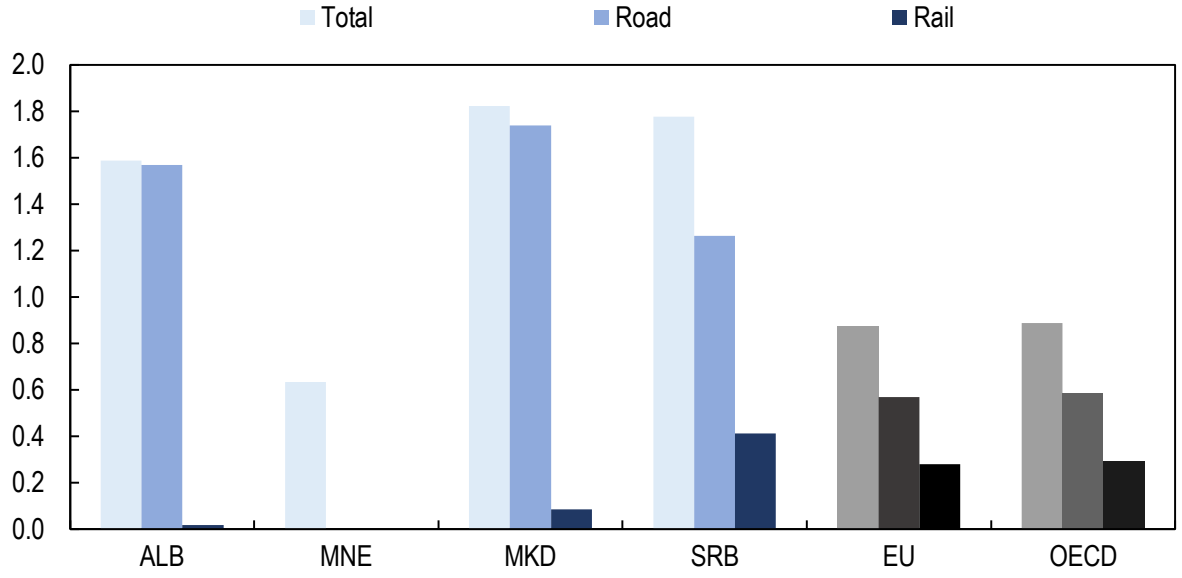
Notes: Methodological details in the Annex document. EU-5 comprises Austria, Bulgaria, Croatia, Greece and Romania. Data for Greece are not available.
Sources: OECD (2023[2]); Kosovo Agency of Statistics (KAS).

StatLink https://stat.link/n7l3wp

The WB6 economies are primarily focusing their **transport** infrastructure investments on road networks, with spending on other modes, notably rail infrastructure, significantly lower. Investments into road infrastructure dominate total inland infrastructure investments in all economies (Figure 2.3). In recent years, Albania and North Macedonia have experienced notably high levels of investment in road infrastructure compared to their overall inland infrastructure investments, even exceeding the levels seen in the EU and the OECD. This trend reflects significant road construction and rehabilitation initiatives underway in these economies, which are helping to bridge the gap with the EU in road infrastructure density. However, it also reflects the fact that the level of investment in rail infrastructure is dwarfed by the size of investments in roads and falls below the averages observed in OECD and EU countries. This is a challenge, as most of the region's modal share for both passengers and freight is concentrated in road transport, which is more polluting and costlier for businesses than rail. The region's low level of rail infrastructure density compared to the EU highlights untapped potential to develop rail infrastructure to facilitate the flow of goods and people.

Figure 2.3. Inland transport infrastructure investment, including for road and rail, in the WB6 economies, the EU and the OECD (2019-21)

In percentage of GDP



Notes: Data for Montenegro are available only for 2019, hence the figure shows the absolute value for 2019 for Montenegro and no data on road investment in Montenegro are available. Data for Kosovo and Bosnia and Herzegovina are not available.
Sources: OECD (2023[2]); ITF Investment in Transport Infrastructure questionnaire filled by respective economies.

StatLink https://stat.link/zmf071

Given the age and deteriorating conditions of railway assets in most WB6 economies, significant financial resources are needed to maintain and modernise the region's railway network (Transport Community, 2023[3]). Important efforts are underway to modernise key railway routes in the region, including with financial support from the EU, the European Investment Bank (EIB), the European Bank for Reconstruction and Development (EBRD) and other international financial institutions. Flagship projects financed under the Economic and Investment Plan for the Western Balkans include the modernisation and expansion of rail infrastructure along key corridors such as Corridor VIII and Corridor X,[5] as well as railway interconnections between WB6 economies (WBIF, 2023[4]). Table 2.1 gives an overview of the flagship

regional transport investment projects being implemented under the Economic and Investment Plan, their approximate correspondence to the pan-European corridors, and their projected completion dates.

Table 2.1. Economic and Investment Plan flagship investments and pan-European transport corridors

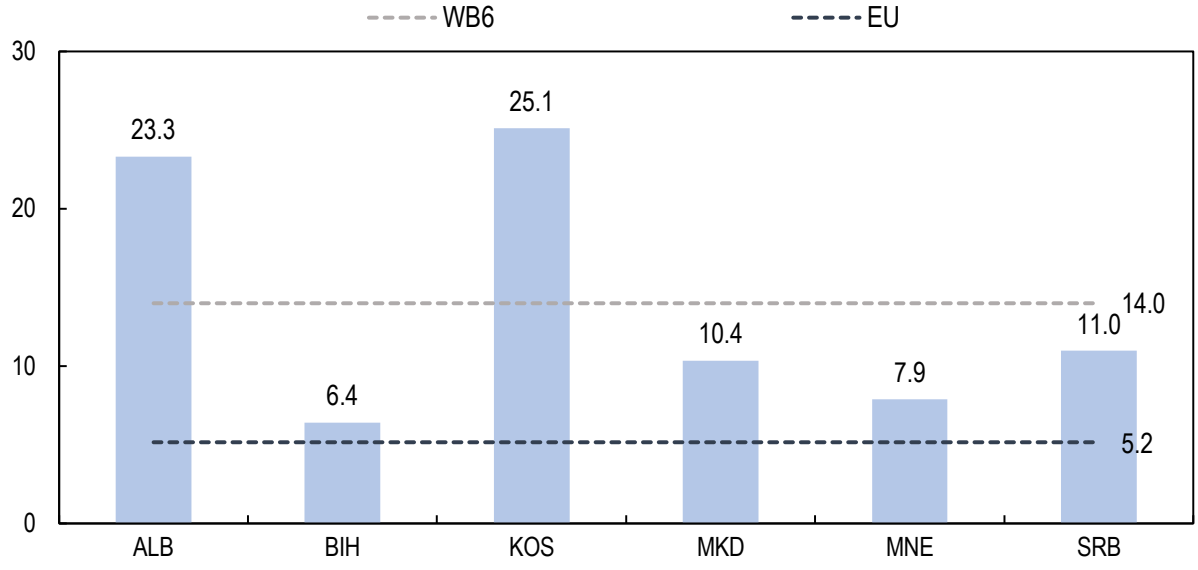
EIP flagship projects in the transport area	Corresponding pan-European corridor	Economies involved	Estimated investment amount under the EIP	Projected completion year of projects
Flagship 1: Connecting east to west	Corridors VIII and X	BIH, KOS, MKD, SRB	EUR 1.92 billion	2029
Flagship 2: Connecting north to south	Corridor Vc	BIH, MKD	EUR 1.99 billion	2028
Flagship 3: Connecting the coastal regions	N/A	ALB, MNE	EUR 0.47 billion	2029

Notes: EIP = Economic and Investment Plan. The nomenclature of the pan-European corridors, also called the "Helsinki corridors" is often used in reference to projects on the TEN-T networks. Nevertheless, these two networks are separate, with the TEN-T taking precedence in policy making at the European level. Estimated investment figures are as of 2022.
Source: WBIF (2023[5]).

The Western Balkan economies grapple with outdated **energy** infrastructure and suffer from substantial losses: on average 14% of electricity injected into the grid is lost, compared to only 5.2% in the EU (Figure 2.4). These figures indicate that significant investments are needed to modernise the energy infrastructure in the Western Balkans, especially in Albania and Kosovo, which have the highest rates of power losses. Such investments should also be targeted at developing sustainable and resilient energy networks to ensure the region's transition to low carbon energy sectors. According to the EBRD, an annual investment of approximately USD 23 billion is needed in the wider South East Europe (SEE) region (comprising the WB6 plus Bulgaria and Romania) to facilitate a sustainable, secure and affordable transition to a net-zero economy by 2030 (Mirbabaeva, Nigina, 2023[6]).

Figure 2.4. Total power losses in the WB6 economies and the EU (2018)

% of total electricity injected into the distribution and transmission grid



Sources: CEER (2020[7]); Energy Regulatory Authority of Albania (2022[8]).

The region's electricity networks are currently facing significant barriers to the deployment and integration of renewables, including capacity constraints, a lack of flexibility and demand response, and inadequate investment incentives.[6] These factors are therefore also an obstacle for the greening of the WB6 energy sectors, as well as for diversification and energy security. Significant additional investment into developing WB6 electricity grids is needed to modernise and expand transmission and distribution infrastructure, and enable increasing electrification and the integration of renewable energy sources into the power network.

Appraisal, selection and procurement processes of infrastructure projects are improving, but challenges persist in systematically assessing their financial and non-financial impacts

Since the previous Competitiveness Outlook assessment in 2021, the main efforts to improve the project selection processes for infrastructure projects in the region have been focused on the broadening of criteria assessed by project selection tools and frameworks. Albania and Montenegro updated their respective project selection processes in 2023, improving the alignment of selection criteria with strategic and sectorial priorities, and integrating environmental and social impact assessments into the process. Serbia has also updated its project selection process through the introduction of its Public Investment Management Information System (PIMIS) in 2023. However, it is not consistently applied for all projects.

Despite these advancements made in some economies, others continue to face challenges in effectively appraising infrastructure projects. Bosnia and Herzegovina, Kosovo, and North Macedonia face challenges in ensuring that their project selection tools are regularly updated, putting into question their continued use and relevance. These economies also lack legal mandates for cost-benefit analyses (CBA), and inconsistent regulatory frameworks hinder the effective and comprehensive appraisal of infrastructure projects.

Without properly developed and applied appraisal tools, the WB6 economies risk investing in projects that are not economically viable, fail to address the most recent needs of the population and underestimate the potential negative consequences – especially on the environment. The concerns of the region's stakeholders on the economic viability of projects such as the Belgrade-Budapest railway and the Bar-Boljare highway attest to this. So far, the only economy that has developed CBA guidelines tailored to its own circumstances and needs is Serbia, and these have not been updated since 2010.

Several WB6 economies have established consistent and coherent implementation and procurement processes for infrastructure projects, and to varying degrees use alternative procurement methods such as public private partnerships (PPPs) and concessions. Most notably, Montenegro and Serbia have taken steps to improve their public procurement systems and to align the governance of alternative procurement methods with EU good practices through updates to their legal frameworks. Albania, Kosovo and North Macedonia require additional amendments to their legal frameworks to ensure that alternative procurement methods are appropriately monitored and fully integrated into the frameworks for public financial management.

Given the risks associated with alternative procurement methods such as PPPs, strong institutional frameworks are imperative to ensure that they are governed and implemented in line with government priorities and that they do not represent significant fiscal risk (IMF, 2023[9]). In Bosnia and Herzegovina, the absence of coherent and up-to-date legal frameworks for PPPs and concessions hampers the adoption of alternative procurement methods throughout the economy – limiting investment in infrastructure.

The implementation of infrastructure projects is delayed by administrative constraints and challenges in co-ordination

Institutional co-ordination challenges persist in some WB6 economies, hindering the translation of **transport** visions and development plans into tangible outcomes. Bureaucratic hurdles and differing mandates among government agencies often impede seamless co-operation, as seen most prominently

in Bosnia and Herzegovina and North Macedonia. Moreover, challenges in on-the-ground implementation are leading to delays in the implementation of key projects on the core TEN-T network, with most road and railway infrastructure projects in the region suffering delays of over two years following their approval.

In the **energy** sector, most WB6 economies are facing delays in the implementation of their energy infrastructure development plans. Only Montenegro is on track, while Albania and North Macedonia, and to a greater extent Serbia, have encountered delays. The main reasons cited for delays are budget constraints, lack of human resources, and problems with land purchase and usage rights. As of 2022, the majority of flagship connectivity projects in the energy sector were facing delays of at least a year, with some facing more serious delays (WBIF, 2022[10]).

The development of **broadband** networks has steadily progressed in the region, leading to a rise in both fixed and mobile broadband connectivity and coverage throughout the WB6 economies. However, significant disparities exist between the WB6, with Albania, Kosovo and North Macedonia lagging behind the other economies in terms of fixed broadband penetration due to significant infrastructure financing needs. The regional Balkans Digital Highway initiative aims to create a wholesale broadband network leveraging the optical fibre infrastructure of participating transmission systems operators. The feasibility study, cost benefit analysis and preliminary design were completed in 2023 (for more information, see Chapter 4: Digital transformation).

The region could significantly improve the establishment of effective practices for managing and maintaining infrastructure assets

The efficiency and implementation of asset management systems for **transport** infrastructure remains limited across the region. Economies such as Albania and Serbia have secured international assistance and funding to develop comprehensive asset management systems in the rail and road sectors, laying the groundwork for proactive maintenance planning and resource allocation. However, the implementation of asset management practices for other modes of transport such as maritime and aviation remains limited across the region. The absence of fully developed asset management systems hampers the ability of the WB6 economies to prioritise maintenance activities and allocate resources effectively, leading to deteriorating infrastructure conditions and higher maintenance costs in the long run.

The picture is more positive for **energy** infrastructure. Except for Montenegro and Bosnia and Herzegovina, all WB6 economies have put in place methodologies for managing and maintaining their energy infrastructure, and use tools such as maintenance plans and software solutions, albeit with varying degrees of sophistication. All economies are also regularly collecting key indicators related to energy infrastructure, and most are regularly publishing these indicators, although Montenegro is more restrictive in this regard, citing potential security risks as a reason for the non-publication of information.

Building sustainable and resilient infrastructure

WB6 infrastructure is increasingly exposed to climate-induced risks, with floods being a common source of damage in the region. The region's digital infrastructure is also susceptible to cyberattacks, the intensity and frequency of which have been increasing in recent years, as evidenced by recent cyberattacks on the critical government information and communication technology (ICT) infrastructure of economies such as Albania and Montenegro.

Definitions of critical infrastructure exist, but policies to improve its resilience are at an early stage, and potential for regional co-operation is underdeveloped

Most WB6 economies, with the exception of Bosnia and Herzegovina[7] and North Macedonia (which developed a draft law in 2022 that is yet to be adopted), have defined critical infrastructure in their domestic legal frameworks. It is generally defined as systems, networks or assets which are essential for their social

and economic functioning, and whose disruption would cause significant damage to economic, material or human security. Broadly speaking, the definitions of critical infrastructure in WB6 economies comprise sectors such as energy, ICT and transport infrastructure, as well as other sectors such as public services, healthcare and the financial system. While such definitions are overall comprehensive and represent progress in alignment with the EU acquis,[8] definitions between the WB6 economies are not harmonised. This can create a barrier to information sharing and improved regional co-operation in the development of more resilient critical infrastructure (KCSS, 2023[11]).

The region is making progress in introducing policies to protect its infrastructure from the impacts of **climate change** such as changes in weather conditions and natural disasters. With the exception of North Macedonia, all economies have either adopted, or are in the process of adopting, national adaptation plans (for more information, see Chapter 5: Greening). However, in Bosnia and Herzegovina, the lack of a critical infrastructure definition results in the limited coverage of this aspect in its plan.

Despite these steps, policies to manage risk to critical infrastructure in the region are at an early stage and remain mostly reactive rather than proactive, focusing more on risk mapping and anticipation than adaptation measures to improve the resilience of critical infrastructure to potential threats (Popovski et al., 2023[12]). For instance, Serbia's Climate Change Adaptation Programme 2023-30 plans to conduct a risk assessment of road infrastructure's vulnerability to climate change impacts and an assessment of the impacts of changing hydrometeorology conditions on hydropower generation.

Recent **cybersecurity** incidents have increased the region's awareness of the importance of this field and have led to all WB6 economies, except Bosnia and Herzegovina,[9] adopting policy frameworks that aim to reinforce cybersecurity, including for critical ICT infrastructure. While the region's legal frameworks need to be further reinforced to align with EU good practices and ensure the resilience of critical ICT infrastructure (for more information see Chapter 4: Digital transformation), encouraging initiatives have been deployed, such as the establishment of the Western Balkans Cyber Capacity Centre in 2023. This centre, established with the support of France and Slovenia, aims to play a leading role in capacity building for the region's cybersecurity authorities,[10] constituting a good example of regional collaboration to enhance the resilience of critical infrastructure.

Project selection and procurement processes show a positive trend towards promoting low-carbon and sustainable infrastructure, but progress is uneven between economies

While some economies have made strides in integrating sustainability and resilience goals into project selection criteria and investment allocation, others lag behind. As mentioned, through updates to their project selection frameworks, Albania and Montenegro have recently incorporated environmental and social impact assessments into their project selection processes. The integration of these goals into criteria for selecting projects and allocating investments is inconsistent. Namely, the lack of strong mandates for the use of project selection tools prevents Bosnia and Herzegovina, Kosovo, and North Macedonia from comprehensively considering resilience and sustainability factors in their project appraisal processes.

Public procurement frameworks for infrastructure projects have not yet been adapted to reflect good practices in the areas of green procurement in the region, and further efforts will be needed to ensure that environmental considerations are mainstreamed in procurement processes. One notable exception is Serbia, which updated its Law on Public Procurement in 2023 to emphasise quality as the primary criterion in the tendering process, with a strong focus on criteria such as the product's lifespan, maintenance costs, water and electricity consumption, and the recyclability of materials used in construction. Bosnia and Herzegovina has recently adopted a new strategy on the development of public procurement that aims to reinforce the use of environmental criteria in public procurement, including for infrastructure projects.

Policies to enhance the resilience and sustainability of electronic communications networks are starting to emerge in the region but have yet to be embraced by all economies

Policies to build the resilience of **broadband** infrastructure in the WB6 economies are at an early stage of development. Existing electronic communications frameworks include basic rules related to network security and integrity, such as requirements for implementing security measures against unauthorised access and breaches, and ensuring network availability and quality of service. However, they lack the more detailed provisions needed to address the evolving security challenges of the telecommunications sector. Moreover, capacity building and training initiatives to enhance the skills and knowledge of key stakeholders involved in broadband infrastructure resilience, such as network operators and emergency responders in disaster preparedness, cybersecurity and resilience planning, are underdeveloped in the region.

The European Electronic Communications Code (EECC) represents a significant advancement in enhancing the reliability and availability of critical communication infrastructure across the EU. Efforts by WB6 economies to align their legal frameworks with this code could help build resilience by increasing requirements for network operators, encouraging collaboration between stakeholders and co-ordinating responses to emergencies. Currently, Serbia has made the most progress in this regard, with Albania following and the other WB6 economies making slower progress (for more information, see the section: Improving the functioning of infrastructure through market-based reforms and regulatory efforts).

Albania stands out as the only regional economy that has introduced initial provisions on supply chain diversification to address the risks associated with reliance on a limited number of suppliers for critical broadband equipment and components.[11] The Albanian Electronic and Postal Communication's Authority's (AKEP) Strategic Plan on 5G Technology recognises supply chain diversification as a key measure for strengthening the resilience of critical infrastructure, such as 5G networks, against various threats and disruptions. In this regard, it aims to establish two bodies: the Albanian Trusted Supplier Certification Company/Department, which will be responsible for identifying and closing regulatory gaps and ensuring compliance, and the National Telecoms Lab, which will be responsible for independently testing network equipment security, resilience and performance under various conditions.

Policies to ensure that digital technologies and networks are operated in a sustainable way are also at an early stage in the region, although have recently gained traction in some economies, with Albania, Kosovo and North Macedonia integrating objectives such as deploying broadband networks based on environmentally friendly and sustainable technologies, utilising alternative energy sources to power communication systems,[12] and reducing environmental pollution from electronic equipment usage into their broadband development policies. Despite this encouraging trend, the implementation of measures related to these objectives is at an early stage even in these economies.

The energy crisis has encouraged some WB6 economies to develop policies to improve the resilience of their energy systems to external shocks, but others lag behind

The rise in global energy prices, compounded by Russia's full-scale aggression against Ukraine since 2022, has impacted the energy sectors of the WB6 economies, leading to price volatility and even power outages in some economies[13] (CEE Bankwatch Network/ETX, 2022[13]). The region's economies are becoming increasingly aware of the need to improve their resilience to external supply shocks by preparing adequate emergency response plans and working on the diversification of their energy supplies.

All WB6 economies introduced immediate measures as a response to the energy crisis, ranging from price caps and tax subsidies to information campaigns and support mechanisms to reduce energy consumption and boost the uptake of energy efficiency measures. Moreover, all WB6 economies have implemented measures to improve energy security, albeit with different approaches and levels of ambition.

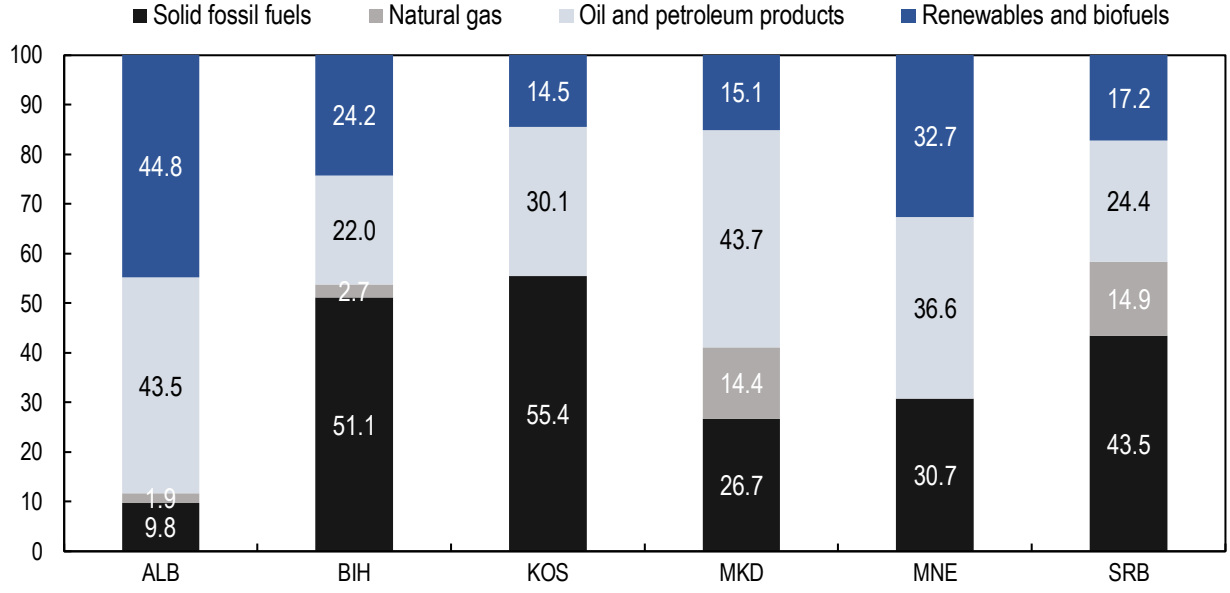
North Macedonia has introduced new processes focusing on better crisis reaction mechanisms and international co-ordination, and stands out as the only economy that has developed coherent and comprehensive demand and supply side emergency plans to cope with eventual energy supply disruptions. Bosnia and Herzegovina performed an Energy Security Stress Test that included an assessment of the risks associated with natural gas supply disruptions and security of supply. The other WB6 economies have focused their efforts on creating dedicated working groups or changing the composition and frequency of meetings of existing groups.

Regarding supply diversification, most WB6 economies have increased the focus of their policies on deploying renewable energy solutions to counter future supply challenges, aiming to enhance both sustainability and energy security. Other economies, such as Serbia, have focused on the diversification of natural gas import sources to reduce supply risks.

Differences in energy mixes between the WB6 economies lead to different sectoral vulnerabilities to supply shocks. Hydropower generation represents an overwhelming majority of the region's renewable energy mix, limiting its potential for contributing to diversification (for more information, see Chapter 5: Greening).[14] The continued reliance on fossil fuels across all economies shows significant room for improvement for the deployment of non-hydro renewable energy sources (RES) to drive forward both energy security and sustainability (Figure 2.5). More ambitious policies will be needed to ensure both effective decarbonisation and diversification through the deployment of new RES capacities.

Figure 2.5. Composition of the total energy supply by energy sources in the WB6 economies (2022)

Percentage of the total energy supply



Sources: Data provided by the International Energy Agency; IEA (2024[14]).

Recommendations for closing the infrastructure gap and building quality infrastructure

- **Improve the use and regional sharing of data for infrastructure planning and decision making**. WB6 economies should prioritise the establishment and utilisation of robust data-driven approaches for infrastructure planning to enhance the clarity and effectiveness of their strategic visions for infrastructure development. This involves investing in comprehensive data collection, analysis and modelling techniques to inform decision-making processes. By leveraging

data on economic and demographic trends, transportation patterns, and environmental factors, governments can gain valuable insights into infrastructure needs, identify priority areas for investment, and assess the potential impact of infrastructure projects on sustainability and connectivity. Introducing data-sharing practices between WB6 economies can also strengthen the basis for co-ordinated infrastructure planning and investment to maximise the region's potential.

- **Develop robust cost-benefit analysis guidelines and impact assessment frameworks that assess a wide range of criteria**. The WB6 economies should collaborate to standardise cost-benefit analysis guidelines and impact assessment frameworks for infrastructure projects, aligning them with EU and OECD standards that provide comprehensive guidelines outlining the criteria for assessing the economic, social and environmental impacts of infrastructure projects. This would facilitate the consistent evaluation of project viability and potential impacts across the region, thus enhancing transparency and the comparability of infrastructure investments. Tailored guidelines should also be developed to address the unique socio-economic and environmental contexts of each economy, ensuring that infrastructure projects contribute effectively to long-term sustainability and competitiveness. Mainstreaming resilience and sustainability considerations into project selection and prioritisation processes and increasing the importance of relevant criteria will also be important to properly assess the benefits of investing in resilient and sustainable infrastructure, and fully integrating the costs of not doing so. Box 2.1 provides an example of multi-criteria analysis (MCA) as practiced in the United Kingdom.

Box 2.1. The UK's Multi-criteria Analysis Manual: A guide for comprehensive impact assessment

In 2009, the UK's Department for Communities and Local Government introduced a manual for multi-criteria analysis (MCA) to help local authorities assess a wide range of criteria when planning, prioritising and selecting infrastructure projects.

The manual covers instructions and methodologies for monetary valuation techniques such as cost-benefit analysis (CBA) that look at the financial consequences of implementing a given project, as well as non-monetary criteria such as the environmental and social impacts of a project. It also gives guidance on how to integrate monetary and non-monetary valuation techniques into project selection processes to ensure that all relevant impacts and costs are assessed.

The WB6 economies should look to develop similar documents to provide guidance to their sub-national and local authorities, which often play an important role in selecting and implementing infrastructure projects, and to ensure that infrastructure decisions avoid adverse lock-in effects.

Sources: OECD (2009[15]); UK Government (2009[16]).

- **Integrate environmental criteria into public procurement frameworks.** The WB6 economies should introduce policies and legislation emphasising the importance of environmental criteria in awarding public procurement contracts. Green public procurement can drive innovation by providing an important incentive to businesses seeking to compete for public contracts, and can result in savings for governments and public authorities by integrating the full life-cycle costs of contracts into the bidding criteria. Serbia's recent amendments to its Law on Public Procurement can serve as an example of good practice for the other WB6 economies.
- **Strengthen asset management systems.** The WB6 economies should prioritise the development and implementation of asset management systems for all types of infrastructure, particularly transport infrastructure, where it is underdeveloped, to ensure the efficient maintenance of

infrastructure assets. This includes investing in capacity building, technical assistance and institutional strengthening to support the establishment of robust asset management frameworks, data collection mechanisms and performance monitoring systems.

- Adopt proactive policies that aim to improve the resilience of critical infrastructure and increase regional and international co-operation. The WB6 economies would benefit from aligning their legal definitions of critical infrastructure. This would allow them to improve co-operation in identifying and building resilience to transboundary threats such as natural disasters (including those induced by climate change), sabotage and economic shocks, while maintaining the national specificities of their legal frameworks where relevant and necessary. The WB6 should also look to develop proactive policies to increase the resilience of their critical infrastructure to such threats, adopting a whole-of-government approach and exploring possibilities to reduce the impacts of potential shocks to broader societal and economic functioning. In this regard, increased regional co-operation has the potential to leverage synergies by pooling resources and expertise and creating platforms to exchange good practice, such as the recently launched Cyber Capacity Centre. Box 2.2 shows how OECD and EU member states are exchanging good practice and experience with resilience-enhancing policies.

Box 2.2. Good practice sharing platforms for critical infrastructure resilience in the EU and OECD

In 2022, the European Union adopted Directive 2022/2557 on the Resilience of Critical Entities, giving member states until October 2024 to transpose it into their national legislation. The European Commission established a list of 11 sectors and sub-sectors[1] constituting essential services through a delegated regulation.

Under the directive, member states have until 2026 to adopt strategies for reinforcing the resilience of their critical infrastructure entities. These strategies must contain elements such as measures to improve the resilience of critical entities, risk assessment, definition, mapping and justification thereof of critical entities, and a governance framework for resilience building measures. To facilitate the co-ordination of efforts and exchange of good practice between member states, the directive also establishes a Critical Entities Resilience Group composed of relevant authorities and stakeholders from member states.

Since 2014, OECD members adhering to the Recommendation on the Governance of Critical Risk have been implementing policies to monitor, mitigate and prevent the impacts of threats involving risk to critical infrastructure and services. As an official OECD working party, the annual High-Level Risk Forum serves as a platform for regular exchange of good practice between OECD members and other adhering parties, involving sub-national authorities and other stakeholders such as civil society and the private sector.

The WB6 economies, due to the shared challenges they face, could look to establish similar platforms for the exchange of good practice in managing risks to their critical infrastructure, and to co-ordinate efforts. In parallel they could explore options for membership or observer status in the aforementioned bodies in order to further align their policies with both the EU acquis and international good practice.

1. Energy; transport; banking; financial market infrastructure; health; drinking water; waste water; digital infrastructure; public administration sector services; space; and food production, processing and distribution.
Sources: European Commission (2023[17]); European Union (2022[18]); OECD (2014[19]).

- **Focus on enhanced regional co-ordination in energy network management to strengthen resilience and crisis response.** A regional approach in managing energy networks allows for the sharing of resources, expertise and information among neighbouring economies. It enhances the ability to manage energy supply disruptions, natural disasters or other emergencies more effectively by pooling resources and co-ordinating responses to emergencies. Assessing supply and demand needs with a regional perspective also facilitates the integration of renewable energy sources and ensures a more stable and secure energy supply across the region, ultimately leading to a more efficient and resilient energy infrastructure network.

Improving the functioning of infrastructure through market-based reforms and regulatory efforts

Beyond planning and implementing the development of infrastructure networks, the WB6 economies also need to ensure that the operation of these networks is efficient and aligned with the EU acquis. In this regard, market-based reforms have the potential to significantly improve the competitiveness of infrastructure operation markets, as well as to prepare the region for both the regulatory requirements and competitive pressures of the EU single market.

Harnessing the potential of market-based reforms for efficient and integrated infrastructure networks

EU policy governing energy and transport networks is strongly defined by the unbundling of vertically integrated natural monopolies in network sectors such as rail, electricity and natural gas, ensuring the openness of markets to competition and promoting cross-border co-operation and integration. As prospective members of the EU and members of the Transport Community and Energy Community, WB6 economies are making efforts to align their domestic legislation and market governance structures with essential parts of the EU acquis, facilitated through the technical assistance, financial support and monitoring of these organisations.

The WB6 are gradually opening and reforming their rail and aviation markets, fostering competition, and aligning the governance of transport networks with EU good practices

Some WB6 economies have taken significant steps to liberalise their **rail** markets in recent years, allowing for the entry of new operators and fostering competition. However, challenges remain in ensuring effective competition and reducing barriers to entry across the region. These include limited interest from private operators, regulatory complexities and infrastructure bottlenecks. Serbia stands out as a leader in rail market liberalisation, having fully opened its rail market and attracted multiple private operators. Albania and Kosovo have also initiated steps to liberalise their rail sectors, with plans for market opening approved in recent years. Montenegro and North Macedonia have made initial steps in updating their rail regulations and aligning with EU standards, laying the groundwork for future market opening. However, challenges persist in implementing liberalisation measures effectively, such as bureaucratic hurdles, inadequate infrastructure capacity and limited promotion of competition.

Various **aviation** reforms have been carried out by the WB6 economies to improve the competitiveness of the aviation sector. These include aligning with the relevant EU legislation, enhancing safety standards and modernising aviation infrastructure. The region is aligning airspace management practices with the EU standards set out in the Single European Sky (SES) regulations. The most progress is being made in Montenegro and Serbia, which have fully aligned with the SES II provisions, whereas alignment efforts in the other WB6 economies are ongoing. Investments in airport infrastructure, air traffic management systems and staff training are also contributing to improved safety, efficiency and capacity in the aviation

sector. However, challenges such as institutional capacity constraints, staffing issues and delays in regulatory reforms persist in some economies, particularly Bosnia and Herzegovina and Kosovo, which impact the pace and effectiveness of these reforms. With the exception of Bosnia and Herzegovina, none of the region's economies are part of a Functional Airspace Block, which results in inefficiencies in air traffic management, restricted routing options, safety risks and limited opportunities for airspace optimisation, and impacts the region's connectivity and competitiveness in the global aviation market.

The region has significantly developed its organised electricity markets, but barriers to competition remain

Since the previous Competitiveness Outlook assessment in 2021 there have been major developments in the deployment of organised **energy** markets in the Western Balkans. In 2023 alone, three additional day-ahead markets for electricity were launched in Albania (ALPEX), North Macedonia (MEMO) and Montenegro (MEPX), and have been operating continuously since then. These power markets have the potential to improve the efficiency, stability and sustainability of the energy sector.

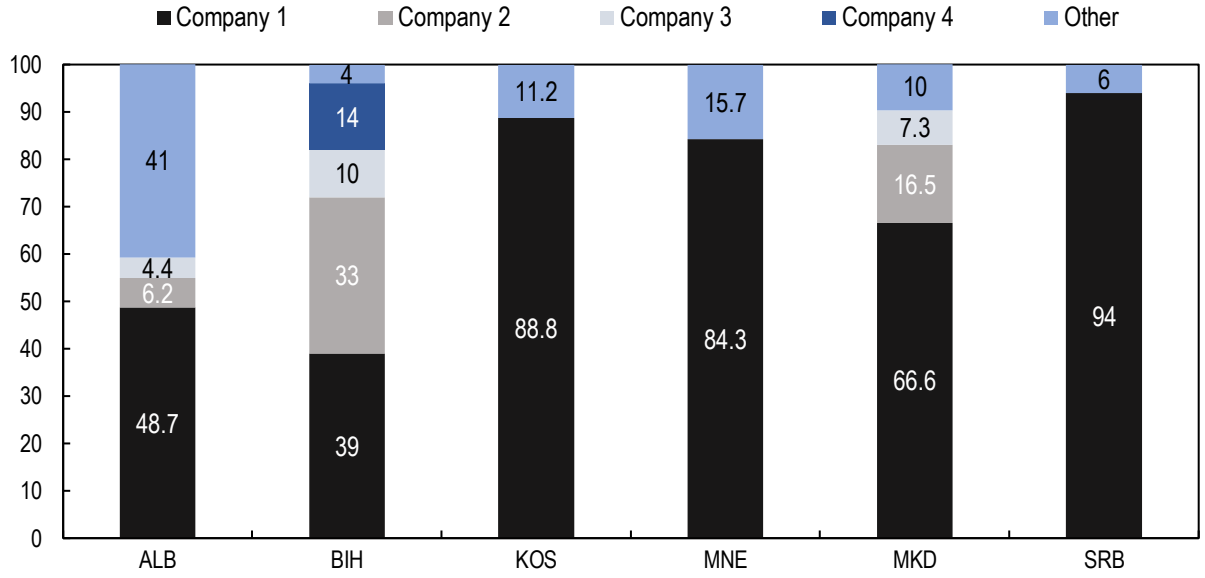
With the opening of an ALPEX branch in Kosovo in early 2024, Bosnia and Herzegovina is the only economy in the Western Balkans without an organised day-ahead market for electricity. Serbia, which has been operating a day-ahead market since 2016, has further developed its market structure by launching an intraday market in 2023, further improving the flexibility and competitiveness of its electricity sector (Spasić, Vladimir, 2023[20]). While overall liquidity at the different power exchanges remains limited, the creation of organised markets is a big achievement and will enable additional integration in the region and beyond.

Despite this progress, in some economies there is insufficient deregulation. Although legally deregulation is quite advanced in most WB6 economies, existing tariff structures prevent a full liberalisation, which hampers the creation of truly competitive markets. This is also mirrored by the high degree of market concentration present in the different economies, as shown in Figure 2.6, which illustrates the dominant position of market incumbents across the region.

Unbundling in the electricity sectors has been further advancing in recent years in line with EU and Energy Community good practices, including the appointment of compliance officers and the adoption of detailed compliance programmes in most WB6 economies. Additional efforts, however, are needed to unbundle the respective operators in the gas sectors, as shortcomings in this area persist in multiple economies. There is also room for improvement in ensuring third-party access and the mutual recognition of licenses, and discriminatory practices in some economies present market entry barriers and hamper the development of competitive markets.

Figure 2.6. Market shares of traded electricity volumes in the day ahead timeframe in the WB6 economies (2022)

Percentage of traded electricity



Note: Companies with a market share smaller than 4% are grouped under
" Others. Please note that the market shares in Bosnia and Herzegovina most likely reflect a fragmentation of the electricity market along entity and cantonal lines, rather than actual competition in the market.
Source: ACER (2023[21]).

Recent legislative efforts have the potential to improve competition in the region's electronic communications markets

While legal and policy frameworks for the governance of **electronic communications** markets include measures to ensure competition and reduce market entry barriers, persisting challenges hinder market efficiency and innovation in the telecommunications sector across the region. In all Western Balkan economies, both mobile and fixed electronic communications markets are dominated by a small number of major players, leading to limited competition. Factors contributing to this concentration include regulatory barriers, such as outdated regulations in the case of Bosnia and Herzegovina, high entry costs, exemplified by the expensive spectrum auctions across the region, and the legacy of state-owned incumbents, such as Telekom Srbija in Serbia and BH Telecom in Bosnia and Herzegovina.

Barriers to market entry are particularly challenging in terms of the deployment of high-speed networks such as 5G. WB6 economies are currently lagging behind the EU in the deployment of such technologies, which have the potential to support technological advancement and economic growth through faster data speeds, greater capacity and new applications for digital connectivity across several industries.

The region's economies are in the process of updating and aligning their legal and regulatory frameworks with the European Electronic Communications Code (EECC). This alignment with EU good practice aims to create opportunities for new market players by improving spectrum management, strengthening access regulation measures to promote competition in wholesale markets for network infrastructure and services, and facilitating access to passive and active infrastructure,[15] thereby lowering the costs of market entry for new operators. Serbia has led this alignment process by adopting a new electronic communications law in 2023, and Albania should soon complete the final adoption stages of similar legislation.

In the past three years, several economies have implemented reforms to strengthen their regulatory frameworks to ensure fairer competition, prevent anti-competitive behaviour and facilitate market entry for new players. Albania, Kosovo and North Macedonia have adopted regulations aiming to reduce administrative burdens and costs, and facilitate investment in high-speed network infrastructure, thus advancing the alignment of their policies with the EU Connectivity Toolbox.[16] Bosnia and Herzegovina, Montenegro, and Serbia are yet to implement similar reforms. Despite these modernised rules, the effective implementation and enforcement of regulatory reforms will determine the efficiency in fostering a dynamic telecommunications market in each economy.

Aligning regulatory regimes with the EU acquis and ensuring the efficient functioning of regulatory authorities

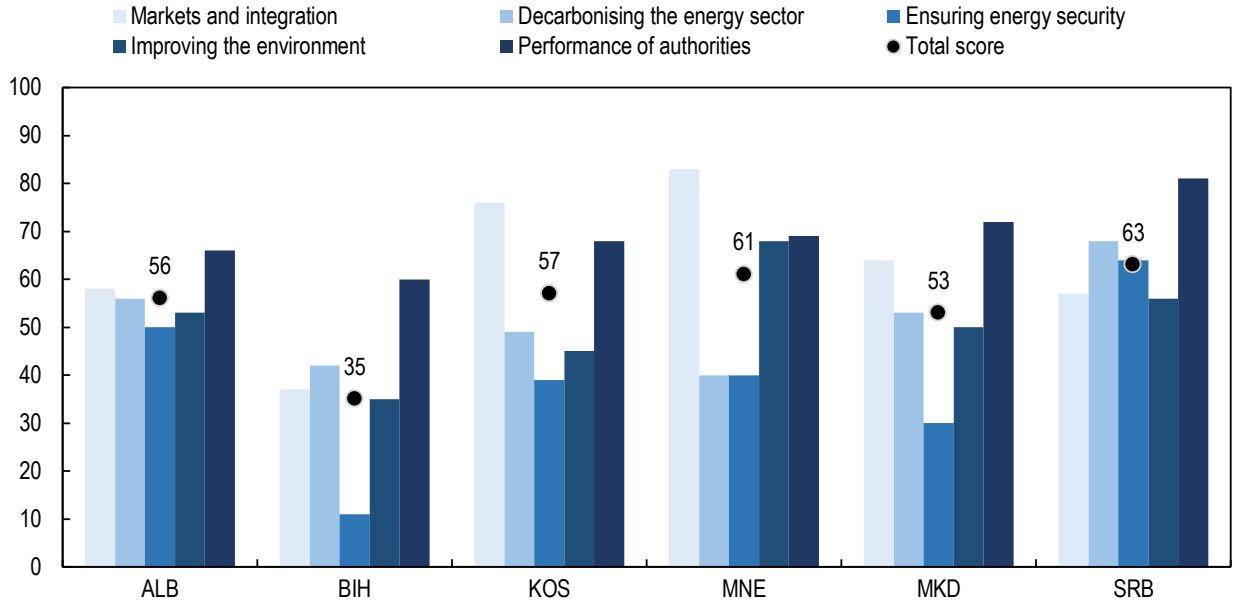
Strong, independent and proactive regulatory authorities are needed to ensure the proper functioning of the transport, energy and electronic communications markets in the WB6 economies, in line with the requirements of the EU acquis. The alignment of secondary legislation in a wide range of sub-sectors is also a key prerequisite for the implementation of the acquis and requires significant regulatory and legislative efforts, which can be hindered by a lack of administrative capacity in the WB6 economies.

WB6 economies have advanced in aligning with, and to a lesser degree implementing, important pillars of the EU energy and transport acquis

The adoption of the Clean Energy Package at the ministerial level of the Energy Community in December 2022 constitutes a strong commitment towards the alignment of the region's **energy** markets with EU good practices and market requirements, as well as with EU policy for promoting the sustainable development of the energy sector and decarbonisation. Throughout the Western Balkans, governments are working on developing their legal frameworks in line with these additional requirements. Progress has been made both in terms of alignment with and implementation of legislation, although additional efforts are needed across all economies, as shown by monitoring conducted by the Energy Community Secretariat (Figure 2.7).

When it comes to **transport**, most WB6 economies have shown greater progress for rail transport than road transport in the improvement of regulatory regimes in accordance with the Transport Community Action Plans (Figure 2.8). Albania is the only economy that has aligned its road transport sector with the Action Plan to a greater extent than rail, showing a stronger commitment to addressing road transport challenges and implementing the recommended measures outlined in the Transport Community Action Plans. Additionally, Serbia has surpassed the WB6 averages for implementing road and rail action plans, indicating significant progress in both sectors compared to other economies in the region.

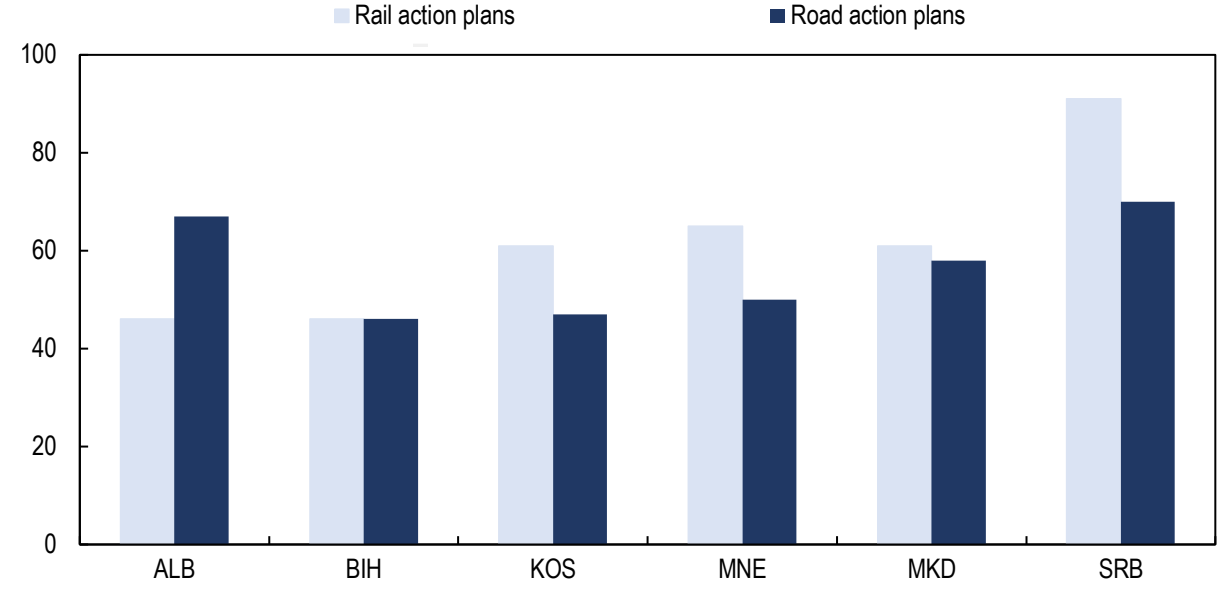
Figure 2.7. Energy Community Secretariat's implementation scores for the WB6 economies (2023)



Source: Energy Community Secretariat (2023[22]).

StatLink https://stat.link/2g0hy8

Figure 2.8. Overall progress of WB6 economies in progressing on the Rail and Road Action Plans until 2023



Source: Transport Community (2023[23]).

StatLink https://stat.link/viecd3

Regulatory authorities for key infrastructure networks are being progressively strengthened but require additional resources to effectively conduct their mandates

The regulation of **transport** modes in the region is improving through efforts to update legislation and establish regulatory bodies to enhance safety standards, promote competition and ensure compliance with EU regulations. However, inconsistencies in implementation, limited institutional capacity and infrastructure deficiencies hinder full alignment with the EU acquis across the region.

In the **rail** sector, efforts have been made to support the implementation of market opening and address safety concerns through the establishment of regulatory bodies and the adoption of legislation on safety standards, worker's rights and passenger protection across the WB6 economies. Kosovo, Montenegro and Serbia are the most advanced in this regard, with Albania and North Macedonia making progress during the assessment period, and Bosnia and Herzegovina lagging behind (Transport Community, 2023[23]). However, challenges persist in ensuring market access and oversight, and fostering competition in the rail market. In 2023, through the Transport Community, the WB6 economies established a Regional Railway Centre of Excellence to help strengthen the human capacities of the region's railway sectors by providing dedicated capacity building opportunities for the public sector, railway operators and other stakeholders (Transport Community, 2023[24]).

In the **road** sector, good progress has been made in adopting road safety strategies, establishing regulatory bodies, and implementing road safety measures such as Road Safety Inspections (RSI) and Road Safety Audits (RSA). Bosnia and Herzegovina and Serbia have established road safety agencies, allowing them to centralise expertise, resources and efforts towards implementing comprehensive road safety strategies, and as a result enhancing co-ordination, accountability and effectiveness in reducing road traffic injuries and fatalities. However, challenges persist in all economies in improving road safety data collection and analysis systems, aligning targets with EU recommendations, and enhancing institutional capacities.

As apparent from Figure 2.7 above, most WB6 economies are relatively advanced in terms of the performance of public authorities in the **energy** sector. Energy regulators in the region largely fulfil the criteria of legal, functional and financial independence; however, salaries mostly remain below industry standard, and additional financial resources will be needed to prevent further brain drain. There is also a need for additional capacity building, particularly to ensure that regulators can take on increasing responsibilities as the WB6 economies transpose additional elements of the EU and Energy Community acquis. Co-operation with European organisations such as the Agency for the Co-operation of Energy Regulators (ACER) is taking place at different levels between the WB6 economies. Currently, only the regulatory authorities of Montenegro and North Macedonia enjoy observer status in ACER, allowing them to take part in some of its meetings and facilitating the exchange of good practice with EU member states.

While the regulatory authorities responsible for **electronic communications** in the WB6 economies are adequately staffed to fulfil their responsibilities, various challenges have influenced their financial and operational independence, particularly in Bosnia and Herzegovina, Montenegro, North Macedonia, and Serbia.[17] The European Commission has raised concerns about the independence of regional regulatory authorities in its latest reports for these economies (European Commission, 2023[25]). Legal changes aiming to align with the EECC have the potential to strengthen the independence of electronic communications regulatory authorities across the region, addressing challenges they have encountered over the past three years.

Recommendations for improving the functioning of infrastructure through market-based reforms and regulatory efforts

- **Implement comprehensive regulatory rail reforms aligned with EU guidelines.** This includes streamlining licensing procedures, ensuring non-discriminatory access to railway infrastructure and fostering a competitive market environment. Investments in rail infrastructure and capacity expansion are also essential to accommodate new market entrants and promote efficient operations. Collaboration among regional stakeholders, including governments, regulatory bodies and industry players, is crucial to overcome challenges and harmonise standards between economies.
- **Enhance the role of organised energy markets and enforce their de facto deregulation.** This will positively impact the energy sector's efficiency and competitiveness. Organised markets facilitate transparent price formation through supply and demand dynamics, encourage competition among providers, and offer consumers more choice, potentially lowering prices. Deregulation also removes monopolistic barriers, fostering innovation and efficiency improvements and paving the way for making the most of enhanced regional integration. Together, these mechanisms ensure that a more dynamic market can stimulate investments in renewable energy and new technologies, leading to a more sustainable and resilient energy system.
- **Ensure the timely and full transposition of the Clean Energy Package.** Full alignment with and implementation of the Electricity Network Codes will allow the WB6 economies to better exploit the potential of regional integration. Particular focus is needed on strengthening long-term planning, institutional co-ordination and energy security.[18] In this regard, the revision of the WB6 National Energy and Climate Plans in line with the Energy Community Secretariat's comments will be crucial, as will continued diversification as a result of renewable energy sources.
- **Ensure that reforms aligning primary legislation with the EECC are followed by the necessary secondary legislation.** All Western Balkan economies will need to rigorously implement such reforms, including updating relevant product and service markets within the electronic communications sector, and aligning voice termination rates across operators' fixed/wireless networks in accordance with the Commission's Delegated Regulation[19] to ensure a more competitive, cross-border environment. Such measures have the potential to improve competition by identifying areas where it may be lacking or distorted. They can also prevent discrimination against certain types of operators and create economies of scale by promoting co-operation between operators in different economies.
- **Implement regulatory reforms to accelerate the development of high-speed networks.** Given the transformative potential of new technologies such as 5G, governments in the region should work consistently to facilitate network infrastructure investments, while fostering innovation in its applications. It is crucial for Western Balkan economies to complete reforms aligned with the EU Connectivity Toolbox to streamline high-speed network development, and to adopt regulations aligned with the EU 5G Cybersecurity Toolbox[20] to ensure secure deployments of the newest high-speed network technology. The WB6 economies should also explore options to align with and take inspiration form upcoming EU legislation such as the Gigabit Infrastructure Act (Box 2.3). Harmonising regulations across the region could eliminate barriers to the deployment of high-speed networks. This can be achieved by adopting a permit-exempt deployment regime for small-area wireless access points (small antennas), in line with relevant EU legislation.[21]

Box 2.3. EU Connectivity Toolbox and the Gigabit Infrastructure Act

In September 2020, the European Commission recommended the development of a common Union Toolbox to aid member states in rolling out very high capacity networks. In March 2021, in accordance with the Commission Recommendation (EU) 2020/1307 of 18 September 2020, the member states, in close co-operation with the Commission, collectively agreed upon a set of 39 best practices, as part of the "Connectivity Toolbox", which they identified as the most efficient in achieving a swift roll out of very high capacity networks such as fibre and 5G. These best practices include measures to help network operators reduce the cost of deploying networks and EU member states give operators access to the spectrum they need to rollout 5G and to encourage them to further invest in 5G coverage. The Connectivity Toolbox is the result of exchanges between member states, in co-operation with the Commission, following the Commission's recommendation. Member states have committed to implement a subset of the identified best practices following an assessment of their national circumstances to reduce the cost of deployment of very high capacity networks.

Building on some of the best practices of the Connectivity Toolbox, the Commission has reviewed the Broadband Cost Reduction Directive (2014/61/EU), leading to the proposed Gigabit Infrastructure Act (GIA). The need for proposing a replacement for the Broadband Cost Reduction Directive emerged because the flexibility given to member states not to implement certain measures or to apply exemptions has resulted in inconsistent implementation across the EU, and a diverse interpretation of certain provisions through national dispute resolution and guidelines. Moreover, the ambition and scope of the 2014 Directive no longer fits market and technological developments. Thus, the GIA responds to the growing needs for faster, reliable, data-intensive connectivity, driven by the advancement and use of technologies such as cloud computing, artificial intelligence (AI), data spaces and virtual reality.

In February 2024, a political agreement was reached, and the GIA will soon become law. The act updates the rules to ensure faster, cheaper and simpler rollout of gigabit networks installation, addressing the main hurdles such as expensive and complex procedures for network deployment.

In parallel, the Commission adopted the recommendation on the regulatory promotion of gigabit connectivity, which provides guidelines to national regulation authorities (NRAs) on how to design access remedy obligations for operators with significant market power, thus promoting competition.

Sources: European Commission (2024[26]; 2022[27]; 2024[28]).

Strengthening regional infrastructure connectivity

Reforms that focus on removing barriers to regional connectivity by facilitating the transportation of goods and people, integrating energy markets, and reducing roaming costs are key to leverage the region's potential as a strategic corridor, and a prerequisite for regional and European integration. In the field of research and innovation infrastructure, a regional approach is important for ensuring that all WB6 economies are using their comparative advantages to maximise their collective research potential and ensure the efficient allocation of individual resources.

Integrating regional infrastructure networks and relevant markets

Efforts to facilitate regional connectivity and promote intermodal transport are gradually gaining momentum in the Western Balkans, albeit with varying degrees of implementation. A notable aspect of this endeavour is the integration of infrastructure networks and the implementation of relevant reforms aimed at fostering

closer ties and the smoother movement of goods and people within the region. The recently proposed Growth Plan for the Western Balkans has the potential to further support the integration of regional infrastructure markets in the transport, energy and digital sectors (Box 2.4).

Box 2.4. The European Commission's new Growth Plan for the Western Balkans: Priority areas related to infrastructure market integration

To support accelerated economic convergence with the EU and incentivise further reforms, in November 2023 the European Commission introduced a proposal for a new Growth Plan for the Western Balkans. The proposal aims to increase financial support to reforms in the region by EUR 6 billion over the 2024-27 period, comprising direct disbursements to government budgets and to projects to be implemented by the Western Balkans Investment Framework (WBIF).

The second pillar of the Growth Plan proposes the gradual integration of the WB6 into different segments of the EU's single market, which has the potential to provide substantial economic benefits for WB6 economies. Both the financial support and the incentive of the single market opening will depend on progress made in establishing a Common Regional Market (CRM) between the WB6 economies, as well as on the implementation of fundamental reforms as part of the EU accession process.

The European Commission has pre-identified seven priority areas for integration into the EU's single market, contingent on strong progress by the WB6 on implementing the CRM in the relevant areas. The areas relevant to infrastructure and connectivity are:

- **Facilitation of road transport**: Reforms supported by the Growth Plan could aim to integrate the region's road transport networks and align their road transport governance with the EU acquis. This could allow the EU to introduce additional road transport facilitation measures and open the road market to the WB6.
- **Integration and decarbonisation of energy markets**: This priority area includes advancing on the integration of the region's electricity markets and introducing carbon pricing measures, which could allow electricity market coupling with EU member states and address the impacts of the introduction of the Carbon Border Adjustment Mechanism by the EU.
- **Digital single market**: This priority area would require comprehensive reforms to accelerate the digital transformation of the WB6. Benefits would include integration into the EU single market for e-commerce, reduction of roaming costs and increased interoperability with digital government services in the EU.

Note: The final priority areas will depend on the reform plans adopted by the WB6 governments in co-operation with the European Commission.
Source: European Commission (2023[29]).

Transport facilitation reforms are showing gradual progress, but additional efforts are needed to unleash the region's potential as a key transport corridor

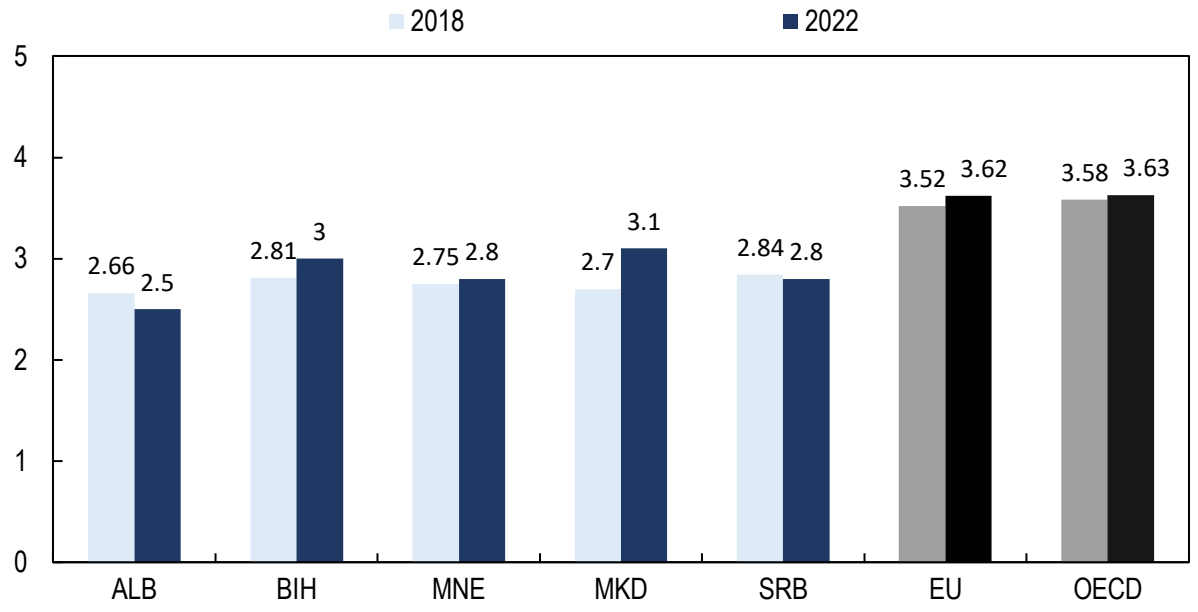
Efforts to enhance regional transport connectivity have been ongoing since the last assessment, with a strong focus on transport facilitation measures under the Transport Community's Transport Facilitation Action Plan. Notable advancements have been observed in the establishment and operationalisation of common border crossing points (BCPs), facilitating smoother trade flows and fostering closer co-operation among neighbouring economies. Concrete achievements during the assessment period include the establishment and operationalisation of BCPs such as Zatrijebacka Cijevna-Grabon between Montenegro

and Albania, and the launch of the one-stop shop system at Kjafasan-Qafë Thanë border crossing between North Macedonia and Albania.

Despite progress, challenges persist in fully implementing reforms to leverage infrastructure for regional integration. Delays and bureaucratic hurdles in finalising bilateral agreements, as observed in negotiations between Serbia and Bosnia and Herzegovina for rail border control agreements, underscore the complexities involved in aligning policies and procedures across borders. Additionally, while advancements have been made in implementing joint BCPs, further investments and improvements are needed to optimise their functionality and efficiency.

Regarding combined transport, several WB6 economies have initiated policies and strategies to support the development of multimodal transport. However, challenges in deploying the necessary infrastructure, as well as a lack of dedicated legislation and funding constraints, hinder progress in this area. While efforts in individual economies such as Serbia, for example the establishment of intermodal terminals and the development of multimodal transport nodes, show promise, more comprehensive and ambitious policy frameworks and co-ordinated investments are necessary to unlock the full potential of multimodal transport in supporting the region's role as a key transport corridor and helping them to converge with the EU's level of logistics performance (Figure 2.9).

Figure 2.9. Logistics performance Index scores in the WB6 economies, the EU and the OECD (2018, 2022)



Notes: Data for Kosovo not available. The World Bank's Logistics Performance Index is an international benchmarking tool, consisting of a composite indicator that comprises surveys of international shipping and freight forwarding companies, data on logistics and international shipping and data on supply chains. The overall score (ranked from 1 as the lowest to 5 as the highest) is calculated based on scores on performance in areas such as the quality of logistics services, shipment pricing and speed, infrastructure and efficiency of customs.
Source: World Bank (2024[30]).

The development of organised electricity markets presents an opportunity to strengthen regional integration and tackle the underutilisation of transmission capacity

The go-live of the power market coupling between Albania and Kosovo in early 2024 represents an important milestone in the integration of electricity markets in the WB6 region, demonstrating that organised marketplaces can be the basis for additional regional integration. With this achievement, five out of the six Western Balkan economies are operating day-ahead markets for electricity, with significant potential benefits in terms of supply security and price competitiveness. Nevertheless, further efforts are needed to effectively enhance regional integration and cross border trade in the energy sector.

The need for regional integration is particularly pressing given that WB6 economies are currently facing a significant underutilisation of their installed electricity transmission capacity. This underutilisation is evident in the value range for the ratio between maximum export/import net transfer capacity (NTC) and the nominal transmission capacity[22] of the interconnectors within the region, which falls between 21% and 42.5%, and is below the 70% target set by the Electricity Integration Package (Table 2.2).

Table 2.2. Electricity: Ratio between maximum export/import net transfer capacity and nominal transmission capacity (2021)

Percentage of nominal transmission capacity

ALB	BIH	KOS	MNE	MKD	SRB
29.5	28.0	24.0	37.5	21.0	42.5

Source: Energy Community (2021[31]).

This underutilisation results from several factors, such as inadequate capacity calculation processes, political barriers or a lack of co-ordination among transmission system operators. An example of political barriers hampering regional integration reaching its full potential can be seen in relation to the Coordinated Auction Office (Box 2.5).

Box 2.5. Coordinated Auction Office in South East Europe (SEE CAO) as a driver of regional integration

SEE CAO was established in 2014 to facilitate the explicit allocation of cross-border transmission capacity in both directions between the control areas of participating Transmission System Operators (TSOs) through NTC-based auction processes. It was formed following several years of intensive preparations and aims to comply with EU regulations and the principles of the Energy Community. It focuses on harmonising congestion management methods in the SEE region. The shareholders of the SEE CAO are the TSOs of Croatia, Greece, Turkey, Albania, Bosnia and Herzegovina, Kosovo, Montenegro, and North Macedonia.

One of the main advantages of SEE CAO is its ability to perform co-ordinated auctions of cross-border electricity capacity rights, which is crucial for ensuring efficient and fair access to transmission networks across borders. This co-ordination helps to optimise the allocation of transmission capacity between economies, which is beneficial for market participants by enhancing the transparency and fairness of the electricity market. SEE CAO supports the secondary market for transmission capacity, allowing participants to resell or transfer long-term capacities, which contributes to the flexibility and efficiency of the market. Moreover, it plays a significant role in reporting and transparency, being among the first

to report auction-related data to the ENTSO-E Transparency Platform and regularly reporting to the ACER REMIT Information System, thus enhancing market transparency in the SEE region.

However, the full potential of SEE CAO is not being utilised due to political barriers that are holding back the active participation of all WB6 economies as shareholders within the shareholder structure, limiting the extent to which SEE CAO can facilitate electricity market integration throughout the region.

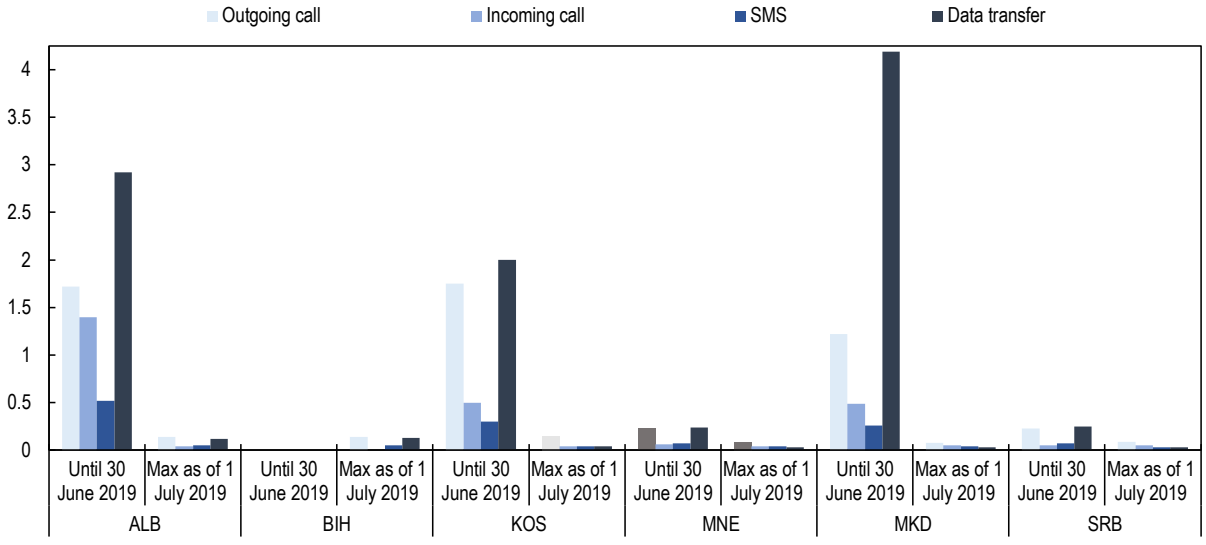
Source: SEE CAO (2024[32]).

Substantial progress has been made in reducing roaming charges between WB6 economies, as well as between the region and the EU

Mobile roaming charges have decreased significantly between the WB6 economies because of the Regional Roaming Agreement, signed in 2019 under the umbrella of the Regional Co-operation Council (RCC). Figure 2.10 shows that before this agreement entered into force, significant charges were applied when roaming in the region, particularly for calls and data transfer. In 2021, roaming charges between the region's economies were successfully abolished, representing an important milestone in facilitating the movement of people through the engagement of national regulatory authorities and telecommunications operators.

Figure 2.10. Roaming prices in the WB6 economies (2019)

In EUR



Note: Prices in Euro, VAT included. Data not available for Bosnia and Herzegovina for "Until 30 June 2019".
Source: RCC (2019[33]).

StatLink https://stat.link/78x3zk

Building on this progress, 38 telecommunications operators from the EU and the Western Balkans signed a declaration in 2022 aiming to ensure the gradual decrease of roaming charges between the region and the EU, further facilitating connectivity for citizens and businesses. The first major reduction in charges took place in October 2023, with further reductions planned for 2026 and an alignment with domestic prices for 2028 (European Commission, 2023[34]). Such reductions have the potential to improve connectivity

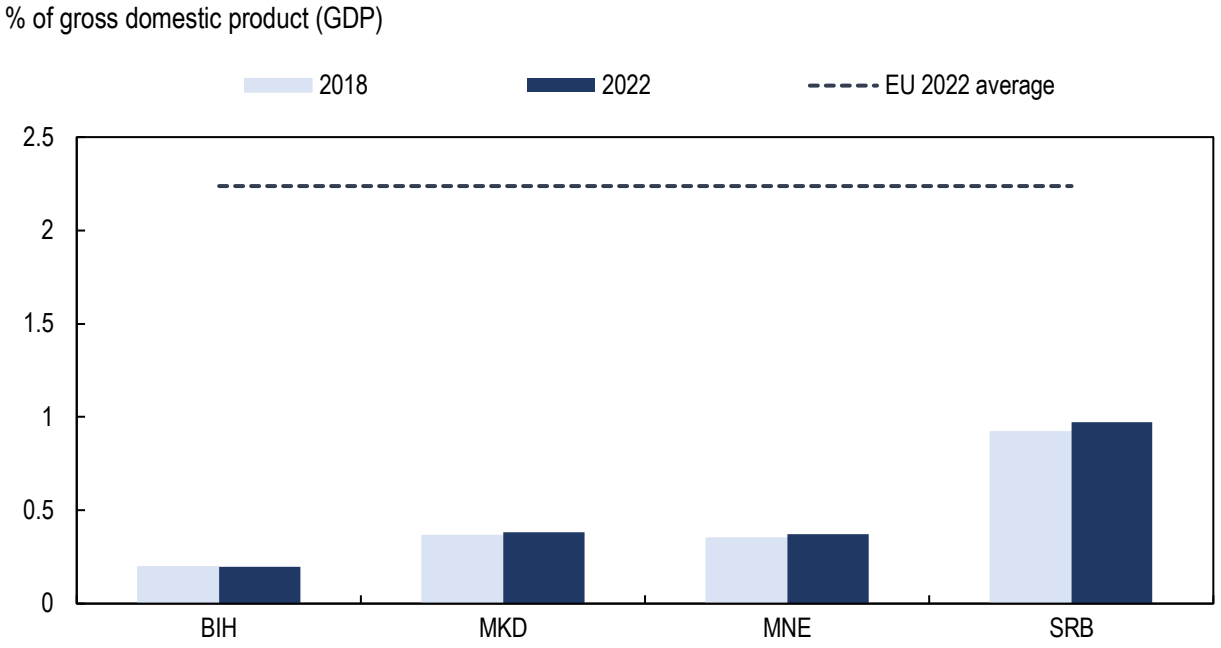
between the region and the EU by facilitating the movement of people, lowering the cost of cross-border business activities and promoting tourism.

Strengthening regional research and innovation infrastructure

Research and innovation (R&I) infrastructure consists of the resources, services and facilities available in local economies to foster research excellence and innovation. Effectively developing R&I infrastructure requires large-scale financing. For the small open economies of the Western Balkans, the regional integration of local infrastructure can leverage economies of scale and ensure that investments into R&I support structures are as effective and cost-efficient as possible, as well as support regional and European research priorities. It also supports the region's ambition to create a Regional Industrial and Innovation Area, outlined in the CRM[23] action plan, and to implement the Western Balkans Agenda on Innovation, Research, Education, Culture, Youth and Sport.[24]

Overall, R&I infrastructure in the Western Balkans remains at an early stage of development, with individual economies at different stages. A major obstacle to the creation of effective and scalable support[25] is the lack of investment in research and development (R&D). Across the region, gross domestic expenditure on research and development (GERD) remains significantly below EU and regional peer averages (Figure 2.11), although is increasing. In particular, private sector investments remain negligible, accounting for less than one-third of total investments in R&D in most economies.

Figure 2.11. Gross expenditure on research and development (GERD) in the WB6 economies and the EU (2018, 2022)



Notes: Data for Albania and Kosovo are not available, and Montenegro's 2018 data are from 2019.
Sources: UNESCO Institute for Statistics (2024[35]); Eurostat (2024[36]).

StatLink https://stat.link/ahf23k

Progress has been made in strengthening the ecosystem to be conducive to startups and innovation, but research infrastructure remains non-competitive

Most WB6 economies have progressed well in establishing a support infrastructure for innovation and startups, with incubation services, business training and networking opportunities available across economies, and some also providing scalable financial support. While dedicated agencies such as the Serbian Innovation Fund or North Macedonia's Fund for Innovation and Technological Development (FITD) offer targeted financial schemes to foster innovative business activities, most support targets early-stage companies more generally rather than specific innovation activities.

In contrast, research infrastructure often suffers from chronic underinvestment across all WB6 economies. Scientific research, including its infrastructure, is predominately publicly funded and implemented by higher education institutes (HEIs). However, public sector funds are mainly allocated for teaching purposes, often overlooking research facility investments. Identifying, assessing and mapping R&I infrastructure, including HEI research facilities and equipment, is therefore an important step in identifying shortcomings and prioritising investment. All economies have adopted an R&I infrastructure roadmap with support from the RCC in recent years. In 2022, the RCC also published a regional Western Balkan R&I infrastructure roadmap[26] to identify opportunities for the increased interconnectivity of individual structures. The report emphasises the lack of funding for scientific research and concludes that R&I infrastructure in the region is currently insufficiently competitive to integrate into pan-European networks.

Several WB6 economies are focusing on bricks and mortar investments, particularly science and technology parks (STPs), but progress remains highly uneven. For instance, in Serbia, the network of STPs is reaching full capacity and expanding with a loan and technical assistance from the EBRD,[27] and construction of the Bio4 campus commenced in late 2023, supported by the Development Bank of the Council of Europe.[28] In North Macedonia and Montenegro, plans to establish centralised STPs are yet to be fully finalised. Technology transfer facilities, which support the adoption of innovative business practices, remain limited, and are only available at scale in North Macedonia, where the Centre for Technology Transfer and Innovations (INNOFEIT) has operated since 2018, and through a Technology Transfer Facility in Serbia, established by the economy's flagship Innovation Fund.

Some economies have established centres of excellence in support of their smart specialisation strategies (S3). For instance, in 2020 Montenegro set up a centre of excellence for digitalisation in the field of food safety and authenticity, while Serbia is in the process of establishing a biotechnology centre. If backed with sufficient financial and non-financial support, these can build the region's capacity to offer competitive and state of the art scientific research in priority areas for regional development and EU integration.

Participation in pan-European R&I infrastructure is gradually increasing, but regional integration remains well below potential amid a lack of human and financial resources

All WB6 economies participate in international and regional collaboration activities, but the priority focuses on participation in the European Research Area rather than creating intra-regional linkages. Performance in EU umbrella programmes such as Horizon Europe has improved in all economies, with the region having received over EUR 111 million in EU contributions between 2021 and 2023, compared with EUR 171 million during the entire implementation period of Horizon 2020 (2014 to 2020) (European Commission, 2023[37]). However, significant disparities remain, with Serbia receiving an overwhelming share of this funding due to insufficient absorption capacities in the rest of the region (Table 2.3).

Table 2.3. Horizon Europe net contribution in the WB6 economies (2021-24)

In EUR millions

ALB	BIH	KOS	MKD	MNE	SRB
5.76	5.48	1.24	8.68	3.80	86.69

Source: European Commission (2024[38]).

There is some regional collaboration under Horizon Europe activities, particularly between Montenegro and Serbia, although there is little evidence of a strategic effort to leverage regional partnerships to participate in such EU framework programmes. Participation in projects and landmarks of the European Strategy Forum on Research Infrastructure (ESFRI) is equally driven by individual economies: according to the 2021 ESFRI roadmap, WB6 economies only participated in six activities, with just half including participation by more than one economy.[29]

There is also little focus on enhancing the intra-regional exchange and mobility of researchers, which could in the long term play an important role in increasing R&I capacities, as well as leverage existing expertise and contribute to the development of a regional R&D ecosystem.

Notwithstanding the strong international focus, some regional R&D initiatives have emerged. For instance, in 2017 the WB6 economies, alongside Bulgaria and Slovenia, established the Southeast European International Institute for Sustainable Technologies (SEEIIST)[30] with the objective of setting up a regional centre of excellence for cancer therapy and biomedical research. However, the institute is yet to become a fully operational research centre, and as of the end of 2023 activities were co-ordinated out of Switzerland. In 2020, NanoALB[31] was established to co-ordinate activities in the area of nanoscience and nanotechnology across Albania, Kosovo, North Macedonia and Montenegro.

Such initiatives constitute important milestones in the region's pathway to creating a regional R&I infrastructure; however, without strong commitment from all stakeholders, manifested in sufficient financial and human resources, these initiatives will likely not develop into competitive WB6 flagship R&I infrastructures that can integrate into global networks.

Recommendations for strengthening regional infrastructure connectivity

- **Develop credible roadmaps for further power market integration, including alignment with the Electricity Integration Package.** The implementation of all network codes will allow the region to reap the full benefits of EU and Energy Community best practices and provide the needed level playing field for further regional integration, eventually leading towards joining the European Single Day Ahead Coupling (SDAC). This initiative is a crucial step towards the integration of the WB6 and the European electricity markets and aims to create a single pan-European electricity market for day-ahead trading, ensuring the efficient, transparent and fair allocation of cross-border electricity trading capacities. This initiative is part of the broader goal of integrating national electricity markets into a single regional market, which is expected to enhance competition, increase security of supply, and ensure the optimal use of generation and transmission resources.
- **Strengthen cross-border institutional co-operation in transport facilitation**. Establishing joint committees or platforms for dialogue on transport and infrastructure issues can facilitate information exchange, policy alignment and collaborative decision making. Additionally, enhancing technical assistance and capacity-building initiatives can support economies in implementing reforms effectively and navigating challenges related to regional connectivity and combined transport. By fostering a culture of co-operation and partnership, WB6 economies can leverage synergies and maximise the benefits of regional integration efforts.

- **Increase investment and policy support for the development of intermodal infrastructure.** The WB6 economies should allocate additional resources towards the development of multimodal transport infrastructure, including the construction of intermodal logistics centres and the modernisation of railway networks. Leveraging funding opportunities from international organisations and public-private partnerships can help address financing gaps and accelerate progress towards seamless regional connectivity and efficient combined transport operations. The WB6 economies should also explore pathways for enhanced regional co-operation in these areas as there is room to mobilise the region's untapped potential by developing partnerships between governments, freight forwarding companies and infrastructure operators.
- **Promote innovation and digitalisation in transport**. Embracing innovation and digitalisation in the transport sector can further enhance the competitiveness of WB6 economies by improving efficiency, reducing costs and enhancing the quality of services. Investing in smart transport solutions, such as intelligent transport systems (ITS), digital logistics platforms and real-time data analytics, can optimise supply chain management, streamline operations and enhance the overall competitiveness of the region's transportation sector. Moreover, promoting the adoption of digital technologies and innovation in transport infrastructure planning and management can help WB6 economies stay at the forefront of technological advancements and adapt to evolving market demands. By embracing innovation and digitalisation, WB6 economies can enhance their competitiveness and attract investment. Lessons could be learned from the example of Southeast Asia: following initial constraints on the movement of goods and people during the COVID-19 pandemic, initiatives including the adoption of more efficient procedures and the digitalisation of documentation were launched in the ASEAN economies to enhance trade facilitation.[32]
- **Increase investment to strengthen existing R&I infrastructure**. Increased funding for research and development remains the prerequisite for creating competitive R&I infrastructure that supports the development of a knowledge-based economy. For investments to be cost-efficient, governments should leverage and strengthen existing infrastructure by updating equipment and ensuring that facilities are well resourced, while encouraging businesses to invest in R&D and collaborate commercially with R&I infrastructure.
- **Introduce support mechanisms to encourage targeted R&D and innovation at the regional level**. WB6 economies are largely united in their science, technology and innovation priorities, but do not sufficiently collaborate and leverage intra-regional R&I infrastructure to achieve joint objectives. Incentivising regional research, for instance by introducing joint scientific research grant programmes for selected priority sectors, could stimulate competition for research excellence, which would leverage existing R&I infrastructure and investment into strategically important sectors, while stimulating intra-regional collaboration that may increase the region's participation in global research networks as a result of economies of scale. Ireland provides an example of how cross-border innovation can be supported through institutional and financial means (Box 2.6).

Box 2.6. Cross-border innovation in Ireland

As part of the Belfast Agreement in1998 that brought peace to Ireland, a cross-border trade and business development body, IntraTradeIreland, was established to foster cross-border collaboration, innovation, entrepreneurship and trade.

IntraTradeIreland offers a suite of support instruments tailored to small and medium-sized enterprises (SMEs) to facilitate cross-border trade and business development between Northern Ireland (part of the United Kingdom) and the Republic of Ireland. These instruments encompass financial support, capability development, networking and advisory services, each designed to address specific challenges and opportunities in the cross-border market.

Financial support schemes:

- Acumen Programme: Facilitates sales personnel hiring or market research consultancy for cross-border market entry.
- Elevate Programme: Grants for micro-businesses to access consultancy services for identifying sales opportunities and developing marketing strategies.

Capability development programmes:

- Trade Accelerator Vouchers: Vouchers for accessing expert advice on taxation, employment law and certification.
- Innovation Boost Programme: Supports SME innovation through collaboration with third-level institutions, focusing on new product, process or service development.

Networking and knowledge sharing:

- Business Insight Programmes: Events and workshops for knowledge exchange and networking on cross-border trade topics.
- Sectoral Programmes: Sector-specific initiatives offering bespoke support and networking opportunities.

Advisory services:

- Brexit Advisory Service: Guidance on Brexit-related issues such as customs, supply chain management and legal considerations.

These support instruments aim to enhance SME competitiveness, innovation capacity and market expansion in the cross-border economy, reflecting IntraTradeIreland's commitment to fostering a vibrant cross-border trade environment.

Sources: InterTradeIreland (2024[39]); Queens University Belfast (2024[40]).

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WBIF (2023), *Economic and Investment Plan: Endorsed Flagship Investments 2020-2023*, Western Balkans Investment Framework, https://www.wbif.eu/storage/app/media/Library/FactSheets/Factsheets%202023/WBIF%20Endorsed%20Flagship%20Investments%20Dec%202023%20updates.pdf. [4]

WBIF (2022), *2015 and 2016 Connectivity Agenda Projects: Progress to date (January 2022)*, Western Balkans Investment Framework, https://www.wbif.eu/storage/app/media/Document%20PDFs/Progress.pdf. [10]

World Bank (2024), *Logistics Performance Index*, World Bank Data, https://data.worldbank.org/indicator/LP.LPI.OVRL.XQ?locations=AL-BA-XK-ME-MK-RS-EU-OE (accessed on 5 May 2024). [30]

Notes

[1] For the purpose of comparing the rail and road infrastructure density of the WB6 economies with a relevant benchmark, the category of "EU-5" was created. This category comprises Austria, Bulgaria, Croatia, Greece and Romania. These member states have a geographic proximity to the region and similar topographic characteristics, including significant shares of mountainous terrain – which can complicate the development and operation of infrastructure. Data for road infrastructure density for Greece were not available.

[2] For more information, please see the OECD Recommendation on the Governance of Infrastructure (2021), https://www.oecd.org/gov/infrastructure-governance/recommendation.

[3] The Trans-European Transport Network (TEN-T) maps key transport corridors identified at the EU level to prioritise development planning of transport connectivity. The TEN-T contains a core network and a comprehensive network. For more information, please see: https://transport.ec.europa.eu/transport-themes/infrastructure-and-investment/trans-european-transport-network-ten-t_en.

[4] Although such joint assessments are being reluctantly introduced even within the EU, due to its interconnection capacities the region has significant potential to benefit from such an approach, as security of supply concerns cannot be fully evaluated using an economy-specific approach.

[5] Corridor Vc, Corridor VIII and Corridor X are examples of pan-European corridors for transport flows, reflecting the importance of developing transport infrastructure along these routes. Corridor Vc connects Bosnia and Herzegovina with Croatia and the Adriatic coast, while Corridor VIII connects Albania and North Macedonia with Bulgaria, and Corridor X connects Serbia and North Macedonia with Greece and Central Europe. While these corridors are distinct from the TEN-T corridors used by the European Commission, they are often referred to when talking about infrastructure projects along the TEN-T network.

[6] There are a lack of sufficient incentives in the WB6 for transmission and distribution system operators to invest in the development of the grid to accommodate the deployment of renewables, as investors implementing RES projects do not own, operate or maintain the transmission and distribution networks.

[7] Republika Srpska (RS) has had a Law on the Protection of Critical Infrastructure since 2019, and the Federation of Bosnia and Herzegovina (FBiH) is working on adopting its own entity-level legal framework. However, there is no commonly agreed framework for the protection of critical infrastructure at the state level.

[8] Such as Directive 2022/2557 on the Resilience of Critical Entities and the accompanying Commission Delegated Regulation establishing EU-level categories and sub-categories of critical infrastructure.

[9] While a Law on Information Security has been in place since 2011 in the RS, it is outdated and non-compliant with key evolutions in the EU legal framework such as the Network and Information Security (NIS) Directive (2016) and NIS2 Directive (2022). Moreover, FBiH has not adopted any framework regulation cybersecurity, and there is no co-ordinated framework at the state level.

[10] For more information, please see: https://www.diplomatie.gouv.fr/en/press-room/latest-news/article/cyber-security-signing-of-the-treaty-on-the-western-balkans-cyber-capacity and https://me.ambafrance.org/Western-Balkans-Cyber-Capacity-Center-WB3C.

[11] Failure to address supply chain diversification can expose network infrastructure operators to various risks, including operational disruptions, increased costs, cybersecurity threats and regulatory challenges.

[12] Such as deploying solar heating systems at remote sites and stations.

[13] Other factors played a role as well, including mismanagement of state-owned enterprises and poor hydrological conditions. The consequences of these factors were aggravated by the context of the global energy crisis, as the WB6 economies were less able to rely on imported electricity from neighbouring economies to compensate for decreases in production.

[14] Primarily due to hydropower's susceptibility to variations in hydrological conditions, which will become increasingly important due to the intensifying impacts of climate change on rainfall, drought and other environmental conditions.

[15] Passive network infrastructure comprises the physical components that facilitate data transmission, while active network infrastructure includes the electronic devices and equipment that actively manage and control the flow of data within the network. Both passive and active components work together to create a functioning telecommunications network.

[16] Commission Recommendation (EU) 2020/1307 of 18 September 2020 on a common Union toolbox for reducing the cost of deploying very high capacity networks and ensuring timely and investment-friendly access to 5G radio spectrum to foster connectivity in support of economic recovery from the COVID-19 crisis in the Union. Please see: http://data.europa.eu/eli/reco/2020/1307/oj.

[17] Illustrative of these challenges, the Council of the Communications Regulatory Authority in Bosnia and Herzegovina has been operating without a renewed mandate since 2018; in Montenegro, the parliament adopted an amendment to the law in 2023 in an attempt to dismiss existing council members and the executive director of the Agency for Electronic Communications and Postal Services (EKIP) before the end of their mandate. In North Macedonia, concerns regarding the regulatory authority's independence have recently emerged around 5G spectrum auctions.

[18] For a general overview of the Clean Energy Package and the Electricity Integration Package and their overall scope and advantages, please also see https://www.energy-community.org/implementation/package/EL.html and https://energy.ec.europa.eu/topics/energy-strategy/clean-energy-all-europeans-package_en.

[19] Commission Delegated Regulation (EU) 2021/654 of 18 December 2020 supplementing Directive (EU) 2018/1972 of the European Parliament and of the Council by setting a single maximum Union-wide mobile voice termination rate and a single maximum Union-wide fixed voice termination rate (Text with EEA relevance), http://data.europa.eu/eli/reg_del/2021/654/oj.

[20] Cybersecurity of 5G networks – EU Toolbox of risk mitigating measures, 23 January 2020, https://ec.europa.eu/newsroom/dae/document.cfm?doc_id=64468.

[21] Commission Implementing Regulation (EU) 2020/1070 of 20 July 2020 on specifying the characteristics of small-area wireless access points pursuant to Article 57 paragraph 2 of Directive (EU) 2018/1972 of the European Parliament and the Council establishing the European Electronic Communications Code (Text with EEA relevance), http://data.europa.eu/eli/reg_impl/2020/1070/oj.

[22] Nominal transmission capacity refers to the maximum amount of electrical power that can be reliably transmitted over a power line, transformer or other parts of the electrical transmission network under specified conditions, without exceeding the equipment's design limitations. This capacity is usually determined by the physical and engineering characteristics of the transmission components, including their size, material and construction. It is an important figure for power system operators and planners as it defines the upper limit of power flow that the transmission infrastructure can handle under normal operating conditions. Net transfer capacity (NTC) refers to the maximum amount of electrical power that can be reliably transferred between two areas or countries under normal operating conditions, taking into account the safety standards of the transmission system. NTC is a critical parameter for cross-border electricity trading as it determines the volume of electricity that can be exchanged without compromising the stability and reliability of the power systems involved.

[23] In 2020, the EU and the Western Balkans launched a regional economic integration initiative entitled "The Western Balkans Common Regional Market" aimed at economically integrating the Western Balkans based on the EU Single Market rules by 2025. Please see https://neighbourhood-enlargement.ec.europa.eu/enlargement-policy/policy-highlights/common-regional-market_en.

[24] In 2021, the EU launched the Western Balkans Agenda on Innovation, Research, Education, Culture, Youth and Sport, a comprehensive, long-term co-operation strategy of the European Union and the Western Balkans. It will promote scientific excellence and reform of the region's education systems, create further opportunities for the youth and help prevent brain drain. Please see: https://op.europa.eu/en/publication-detail/-/publication/22b8829d-b786-11eb-8aca-01aa75ed71a1/language-en/format-PDF/source-233221374.

[25] Support which can grow and adapt in response to increased demand.

[26] Published in 2002 by the Regional Cooperation Council, the Western Balkans Research and Innovation Infrastructure Roadmap is a strategic policy document that sets out an overall vision for research and innovation infrastructure in the Western Balkans and the major steps needed to achieve it. Please see: https://www.rcc.int/pubs/149/western-balkans-research-and-innovation-infrastructure-roadmap.

[27] In 2023, the EBRD provided a loan of EUR 70 million to the Government of Serbia to be used to finance the construction, fit-out and purchase of new equipment for the expansion of existing STP facilities in the cities of Niš and Čačak, which have currently reached almost full capacity, and the development of a new STP facility in Kruševac. An additional EUR 10 million is available to be used for the expansion of existing STPs in Belgrade and Novi Sad or the development of new STP facilities within the new biotechnology park Bio4 in Belgrade. EBRD's financing is complemented by a technical assistance project to strengthen

the innovation ecosystem in Serbia and reinforce STP practices in their alignment with international best practice for the establishment, management and operation of STPs. The project will focus on the following four elements: 1) performance management; 2) strategic orientation and financial sustainability; 3) linkages between STPs and the wider Serbian innovation ecosystem; and 4) skills development and linkages with universities. Please see: https://www.ebrd.com/news/2023/serbia-to-build-science-and-technology-parks-with-80-million-ebrd-loan.html.

[28] The Bio4 campus construction commenced in late 2023 near the Torlak Institute in Belgrade and is expected to be completed by 2026. The estimated value of the new bioeconomic hub is around EUR 450 million, with EUR 200 million secured from a loan by the Development Bank of the Council of Europe. Please see: https://www.srbija.gov.rs/vest/en/217212/construction-of-bio4-campus-to-be-completed-by-end-of-2026.php.

[29] The European Strategy Forum on Research Infrastructures (ESFRI) is a strategic instrument to develop the scientific integration of Europe and to strengthen its international outreach. Please see: https://roadmap2021.esfri.eu/media/1252/rm21-part-3.pdf.

[30] SEEIIST is regional development project in South-eastern Europe initiated in 2017 to support the establishment of scientific, medical and green infrastructure in the region. Please see: https://seeiist.eu/about-us.

[31] NanoAlb is a virtual centre established under the Albania Academy of Science to co-ordinate activities in the area of nanoscience and nanotechnology in Albanian universities across Albania, Kosovo, North Macedonia and Montenegro. Please see: https://www.nanoalb.al.

[32] For more information, please see: https://www.oecd.org/southeast-asia/ERIA%20COVID19%20and%20ASEAN%20Connectivity.pdf and https://asean.org/wp-content/uploads/2021/02/asean-covid-19-guidelines.pdf.

3 Skills cluster

This chapter aims to evaluate and quantify the progress of the six Western Balkan (WB6) economies in strengthening skills through the overlapping lenses of education, employment and innovation policies. It first highlights the gradual but relatively modest convergence of the region's outcomes towards European Union levels, showing the significant variation across the six economies. The chapter then delves into how skills policies and programmes in the region have aimed to develop relevant competencies. Specifically, it examines how the economies seek to build strong foundational skills, develop skills for the green and digital transitions, and attract and utilise migrant and diaspora talent. The region's policy framework for putting these skills to effective use is then examined, emphasising efforts to improve the school-to-work transition, match skills with labour market needs, activate unused skills and leverage skills for innovation. Finally, recommendations outline how the region can more effectively build and leverage skills to increase inclusion, productivity and innovation – and consequently reinforce economic competitiveness and EU convergence efforts.

Key findings

The six Western Balkan (WB6) economies have made some progress on skills policies in recent years and are increasingly (albeit slowly) converging towards European Union (EU) levels. Some **key achievements** are:

- All WB6 economies have made considerable strides in implementing their respective Youth Guarantee schemes, which aim to improve the school-to-work transition and reduce youth inactivity and unemployment rates. Specifically, five of the six economies have adopted implementation plans, with most either planning or already rolling out pilot programmes.
- All WB6 economies have made progress towards modernising their vocational education and training (VET) systems, primarily through the enhanced promotion of work-based learning (WBL). This serves as a key step towards strengthening the labour market relevance of VET programmes and improving the employment outcomes of participants.
- The region's widespread adoption of common digital competence frameworks and the inclusion of information and communication technology (ICT) courses in primary and secondary school curricula have advanced how students' acquisition of digital skills is supported. These strengthened policy measures reflect a concerted push to give students the skills demanded by current and future labour markets.
- To expand the region's skills pool, recent measures have sought to open labour markets and increase the recruitment of regional and international talent. The 2023 memorandum of understanding for the mutual recognition of professional qualifications among the WB6 economies serves to increase intra-regional mobility, while ongoing strategies and initiatives seek to better engage and attract migrants and diaspora communities.

Despite these positive regional trends there is still significant scope to strengthen policies and improve outcomes related to education, employment and innovation. As such, some of **key challenges** facing the region are as follows:

- The WB6 economies continue to struggle with delivering quality education, which impacts the development of students' foundational skills. In the 2022 Programme for International Student Assessment (PISA), most 15-year-olds (79%) in the region were low performers in at least one of the three tested subjects (mathematics, reading, science), compared to an OECD average of 45%.
- Education spending in the region is both insufficient, standing at 20% lower than the EU average, and inefficient. Over 80% of WB6 economies' education budget is allocated to salaries for teachers, despite a relatively higher student-to-teacher ratio than the EU (nearly 16 students to 1 teacher in the WB6 vs. 13 to 1 in the EU). Despite donor funding, there is limited room for investment in essential areas such as updated technologies or infrastructure, which could constrain students' learning and academic achievement.
- Skills intelligence systems in the WB6 economies are notably underdeveloped. Irregular analyses, decentralised data collection and the overarching lack of predictive tools limit the efficacy of intelligence systems to inform policy makers and the public about current and future skills needs.
- Despite a shrinking labour force due to an ageing population and declining birth rates, WB6 economies have made limited efforts to better engage adults in the labour force. The participation of adults in lifelong learning in the region is half that of in the EU, and activation policies only marginally address the needs of older unemployed individuals. These factors

significantly limit opportunities for adults to adapt to constantly evolving skills demands, hindering them from maintaining relevant, up-to-date knowledge and competences.

- Investment in research and development (R&D) is critically low. In five out of six economies, R&D expenditure (as a percentage of gross domestic product, GDP) does not surpass 20% of EU levels, posing a serious barrier to the region's innovation capacity and the development of skilled researchers.

Introduction

Skills play a pivotal role in enhancing competitiveness. Systemic issues such as large-scale emigration, gaps in education and training infrastructure, and limited innovation capacity can constrain labour productivity growth: in 2023, the WB6 had an average labour productivity level that was only 36% of that of the EU[1]. A highly skilled population not only boosts the region's productivity, but also ensures an innovative, resilient workforce that can adapt to the constantly evolving needs of the labour market. Ensuring the development and effective use of skills is particularly important as the region advances on its EU accession journey: through harmonising their employment and training systems with EU standards and requirements, the WB6 economies will enhance their ability to integrate and compete in the European market.

This chapter discusses the issues related to skills policy in the WB6, drawing upon the policy areas of education, employment, and science, technology and innovation (STI). Specifically, it will examine how the WB6 economies are Developing relevant skills and Putting skills to effective use.

Developing relevant skills

Building strong foundational skills

Quality basic education for all students, irrespective of their personal background or schools' characteristics, is central to ensure the acquisition of strong foundational skills and competencies. This focus on ensuring strong and inclusive education is important in the Western Balkan context, particularly as the region moves to align with EU education standards.

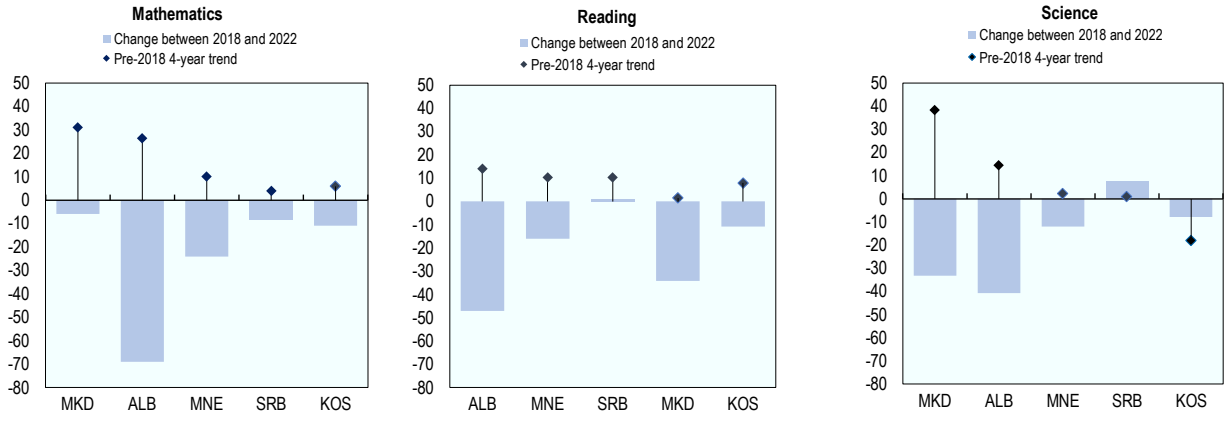
A large majority of 15-year-olds in the Western Balkans fall below baseline proficiency levels in learning outcomes

Results from the 2022 cycle of PISA reveal that learning outcomes in the five participating Western Balkan economies saw a sharp decline between 2018 and 2022, with the exception of Serbia (Figure 3.1). Of note, Bosnia and Herzegovina is the only WB6 economy that did not take part in PISA 2022, nor does it plan to join the upcoming 2025 assessment.[2]

The drop in the region's performance in PISA 2022 was shared across most PISA participants, although the decline in Albania[3] and North Macedonia was particularly acute. However, despite this drop in the last PISA cycle, the performance of the five participating Western Balkan economies improved significantly between their first participation in PISA[4] and the 2018 assessment. Learning outcomes in the Western Balkans are still considerably lower than those seen across EU member states, reflecting shortcomings in the quality of education. The Western Balkans' average in mathematics, the main domain assessed in PISA 2022, was 391 score points, compared with an EU average of 472. Achievement within the region also varies greatly, with Serbia scoring 440 in mathematics and Kosovo just 355 (OECD, 2023[1]).

Figure 3.1. Short- and long-term changes to the WB6 economies' performance in PISA

Score point difference

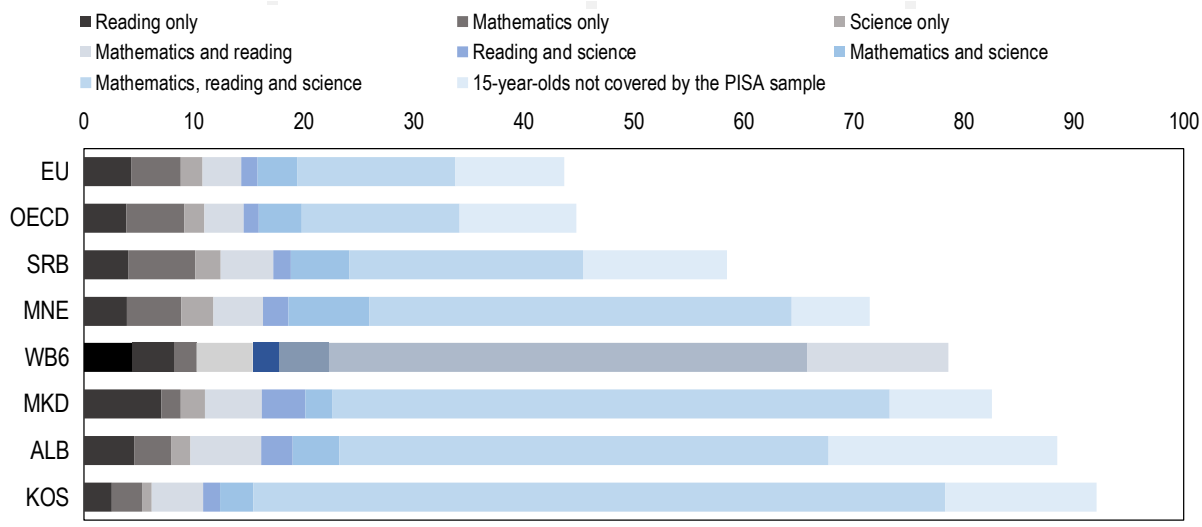


Note: Statistically significant differences are shown in a darker tone. Ranked, within each chart, in descending order of the pre-2018 trend for the corresponding subject.
Sources: OECD (2019[2]; 2022[3]).

StatLink https://stat.link/o4spq2

The large majority of 15-year-olds in the participating Western Balkan economies did not meet baseline proficiency levels, with an average of 79% of 15-year-old students across the region not attaining the baseline proficiency level (Level 2)[5] in at least one subject, compared to an EU average of 44%.[6] This percentage has grown significantly since the last PISA cycle. However, there are large differences across economies in the region. In Serbia, 59% of students did not reach Level 2 in at least one subject, compared to 92% in Kosovo (Figure 3.2). Similarly, the share of high achievers in the region (Level 5 and 6) in at least one subject was far lower than the EU average: 2% versus 14%. An important dimension of evaluating these baselines is examining the gender gap in learning outcomes. In most Western Balkan economies the gender gap in favour of girls was larger than the OECD average. For example, whereas girls outperformed boys by 3 points in mathematics in the region, this trend was reversed among OECD countries, where boys outperformed girls by 9 points on average. Moreover, girls in the Western Balkans outperformed boys by 30 points in reading (versus 24 points in OECD countries) and 12 points in science (versus 0 points in OECD countries).

Figure 3.2. Students below PISA Level 2 in the WB6 economies, the EU and the OECD (2022)



Notes: 15-year-olds not covered by the PISA sample are 15-year-olds who are not enrolled in school; or who are in school but in grade 6 or below, or who were excluded from the PISA sample due to student or school-level exclusions. Ranked in ascending order of the total percentage of students who are low performers in at least one subject.
Source: OECD (2022[3]).

StatLink https://stat.link/9jxi54

Insufficient resources affect the quality of education systems in the Western Balkans

Low baseline proficiency levels among most students can be attributed to several notable obstacles that hinder education systems in the region from meeting international learning standards. These challenges exacerbate disparities in educational outcomes and hinder students' abilities to develop strong foundational skills.

Insufficient public spending on education represents a substantial issue, and has been shown to contribute to relatively lower outcomes of students at all levels of education (OECD/UNICEF, 2022[4]; OECD, 2023[1]). The average for government spending on education (as a percentage of GDP) in the Western Balkans is approximately 3.9%[7] – more than 20% lower than the average spending seen in the OECD and the EU, both of which devote an average of 5% of GDP to education (Eurostat, 2023[5]; UIS, 2024[6]). WB6 governments remain heavily reliant on donor funding to support educational initiatives.

However, while the level of funding might be relatively modest, the money is then allocated inefficiently and inequitably, for several reasons. First, most economies in the region allocate funding based on the number of teachers or the student-to-teacher ratio rather than the number of students, which can better align expenditure with student needs (OECD, 2022[7]). The average student-to-teacher ratio in the region is 15.6:1 at the level of primary education – slightly above the EU average of 13:1.[8] Second, despite this higher ratio, WB6 economies spend a disproportionately large amount on teacher salaries: the percentage of staff compensation (compared to total expenditure in public institutions) exceeded 80% for all economies with data available,[9] reaching 90%[10] in Bosnia and Herzegovina. Given that teacher salaries in the Western Balkans are among the lowest in Europe,[11] this high expenditure indicates that there is little room for investment in areas beyond personnel compensation. As such, there is little financing available for other necessary materials such as textbooks, classroom supplies, technology or infrastructure improvements, resulting in relatively high levels of education material shortage compared to OECD countries (OECD, 2023[1]). This limited margin for investment restricts the ability of educational systems to adapt to changing needs and continuously innovate.

Learning standards and standardised assessments are used across the region, although there is still room for improvement

Ensuring a high quality of learning through well-aligned learning standards and student assessments is essential for improving overall learning outcomes – which can then translate into strong foundational skills for students. In the Western Balkans, all economies have learning standards in place that express what students should know and be able to do at different levels of education. Moreover, all have developed or are in the process of developing competency-based (as opposed to traditional content-based) curricula, which align with learning outcomes that promote the cultivation of important skills, although implementation remains sluggish due to inadequate materials and the insufficient training of teachers.

Most economies in the region conduct regular standardised examinations to certify achievement, with a formal consequence on students' progression through school. The most common examination is a state matura, or a matriculation examination that certifies the completion of secondary education. A matura is in place in Albania, Kosovo, Montenegro and North Macedonia, and Serbia plans to introduce one in the 2024/25 school year. Bosnia and Herzegovina does not have a centralised state matura, but they exist in the entities: Republika Srpska (RS) has an entity-level matura, but only two of the ten cantons[12] in the Federation of Bosnia and Herzegovina (FBiH) have implemented an external matura. Additionally, Albania, Kosovo, Montenegro and Serbia all have a national examination between grades 8 and 9.[13]

All WB6 economies participate in international assessments of student learning, although Bosnia and Herzegovina's involvement is less consistent than the other economies. The most popular examinations are PISA, the Trends in International Mathematics and Science Study (TIMSS), and the Progress in International Reading Literacy Study (PIRLS). Participation in these assessments is crucial for allowing the region's policy makers to benchmark how each economy's students are performing compared to the other WB6 economies, as well as OECD and EU counterparts. This comparable benchmarking can help evaluate the efficacy of existing learning standards, curricula and other education policies.

While there are initiatives for boosting the equity and inclusiveness of education systems in place, access – particularly for early childhood education and care – remains inequitable

Increasing equity and inclusiveness is a priority in numerous strategies and policy frameworks for education across the Western Balkans (Table 3.1). However, there is a significant gap between the policy emphasis placed on equity and inclusiveness and the outcomes achieved in practice.

Early childhood education and care (ECEC), which encompasses both early childhood educational development and pre-primary education,[14] is crucial for building strong foundational skills due to its positive effect on improved learning and employment outcomes later in life. All WB6 economies have recognised the importance of ensuring the provision of ECEC and have strategic and legal frameworks in place. However, in terms of legal obligations, there is significant variation across the region. For example, Bosnia and Herzegovina[15] and Serbia have legislation stipulating that pre-primary education is mandatory from ages 5 and 5.5 years, respectively. Kosovo recently adopted a law that makes pre-primary education mandatory starting in the 2024/25 school year. The remaining economies do not mandate participation in ECEC programmes and only require attendance for primary school (which typically begins when children are between the ages of 6 and 6.5 years).

In the region, ECEC is typically not provided free of charge. However, there are partial exceptions in Serbia and Bosnia and Herzegovina. In Serbia, the mandatory preschool preparatory programme for children aged 5.5 to 6.5 years is free (although nurseries and kindergartens are not). Similarly, in Bosnia and Herzegovina, a preschool programme for children aged 5 is free in RS and free for up to five hours a week in FBiH. To alleviate the financial burden of ECEC, all economies have put some support mechanisms in place for children from socio-economically disadvantaged families or from marginalised groups. In Albania, Kosovo, Montenegro and North Macedonia, children from such groups can enrol in public preschools for

free, and in Serbia and RS it is available at a reduced cost. Other ways of promoting equity and accessibility include adjusting opening hours (FBiH, Kosovo and Montenegro) and raising awareness about the importance of ECEC to academic success and lifelong learning (FBiH, RS, Kosovo, Montenegro and North Macedonia).

Table 3.1. Policy frameworks with objectives for increasing inclusivity in early childhood education and care (ECEC), primary and secondary education

Economy		Main policy frameworks	Objective
Albania		National Strategy on Education 2021-26	Enhance inclusion and participation in preschool and compulsory education, as well as increase access to preschool education and upper secondary education.
		Law on the Pre-University Education System	Increasing the inclusion of children aged 5-6 years in preschool education and raising awareness regarding importance of participation.
Bosnia and Herzegovina	State-level	Recommendations for action policies with a roadmap for improving inclusive education in Bosnia and Herzegovina	Improve the quality and inclusivity of education at all levels.
		Framework law on Primary and Secondary Education in Bosnia and Herzegovina	Outlines the importance of every child's right to access and equal possibility to participate in educational processes.
	FBiH	Strategic Plan for the Improvement of Early Growth and Development of Children 2020-25	Improve access to early learning opportunities for children.
		Development Strategy 2021-27	Improve the quality of preschool, primary and secondary education for the needs of development and ensure inclusive education for all.
	RS	Strategy for the development of preschool, primary and secondary education 2022-30	Increase coverage of training in preschool education.
Kosovo		Education Strategy 2022-26	Strategic objective on increasing inclusion and equal access to early childhood education. Mentions improving inclusion of students with special needs or members of marginalised communities in pre-university education.
		Law on Early Childhood Education	Defines measures to make early childhood education more accessible to marginalised groups (adjusting opening hours, inclusive language, lowering cost barriers, raising awareness).
		Administrative instruction for the inclusion of children in preschool institutions	Increase engagement of children from the Roma community and other social categories.
Montenegro		Strategy for Early and Preschool Education 2021-25	Increasing coverage of children in preschool education, improving quality of preschool education, and improving chances for early development of children from marginalised groups.
North Macedonia		National Roma Strategy 2022-30 (and Action Plans for Education)	Reduce the rate of young Roma not in education, employment or training (NEET) by at least 50%.
		Law on Primary Education	Emphasises protection against discrimination and the promotion of equality, as well as the inclusive nature of primary education.
		National Strategy on the Rights of Persons with Disabilities 2023-30	Improve educational access and representation of people with disability in education.
Serbia		Strategy for Education Development by 2030 (and Action Plan 2023-26)	Specific goals of increasing the accessibility, equity and openness of pre-university education and higher education.
		Rulebook on the Resource Centre	Outlines professional support to children, students and adults who – due to developmental disorders or disabilities, social deprivation, or those who face an elevated risk of dropout – need additional support for inclusive education with the goal of increasing the quality of inclusive education and the availability of additional support.

Source: Ministries of education of the WB6 economies.

These different approaches have likely contributed to the discrepancies observed in actual enrolment rates. When looking at just the pre-primary education component of ECEC,[16] enrolment rates range from 28.5% in Bosnia and Herzegovina to 82.9% in Albania (Table 3.2). The regional average of 50.9% was far below the EU average of 91.8% in 2021 (Eurostat, 2023[8]). Moreover, in terms of early childhood educational development programmes (those that target children aged 0 to 2 years), the region's average enrolment rate falls to 34.6%, with only Serbia and Montenegro reporting rates above 50%.

Table 3.2. Enrolment in pre-primary education, WB6 economies vs. EU (2022)

Percentage of students from age 3 to the starting age of compulsory education enrolled in pre-primary education

Economy	Enrollment rate
ALB	82.9
BIH	28.5
KOS	37.8
MNE	57.2
MKD	33.8
SRB	65.5
WB6	50.9
EU	91.8

Notes: Data from ALB, BIH and MKD are from 2022, while data from KOS, MNE and SRB are from 2021.
Sources: Data provided by the National Statistical Offices (WB6); Eurostat (2023[9]).

This disparity in access partly reflects the existing inequity and limited inclusiveness among disadvantaged groups. For example, while participation rates are low in Kosovo across the board – with only 15% of children aged 3-4 years attending ECEC – these rates are even lower among the most vulnerable groups, dropping to 8% for children from Roma and Egyptian communities (UNICEF, 2024[10]). In Albania, the enrolment rate of Roma children aged 3-5 years is 33%, which is nearly 50 percentage points lower than the economy's average pre-primary enrolment rate (Qejvanaj, 2021[11]). Even Serbia, which offers free and compulsory ECEC for children aged 5.5 and above, sees stark disparities in access: more than 80% of children from advantaged socio-economic backgrounds participate in ECEC programmes, compared to less than 10% of those from disadvantaged backgrounds (World Bank, 2017[12]). Thus, access to ECEC is far from universal, revealing an important area in which equity and inclusiveness could be improved. Table 3.1 demonstrates that most WB6 economies have strategies that aim to address inequities in participation among diverse groups; while these policies generally look at all levels of education, the largest emphasis tends to be on ECEC.

Accessibility issues are less evident at the level of primary education, which is compulsory and free in all WB6 economies. The region's average net enrolment rate in primary education in 2022 was 91.1% – 6.5 percentage points lower than the EU average (UIS, 2024[13]). However, dropout rates notably rise during the transition from lower to upper secondary education. In most economies, compulsory education only includes primary and lower secondary education.[17] The regional average for net enrolment rates in upper secondary education is 83.2% – 10 percentage points lower than the EU average.[18]

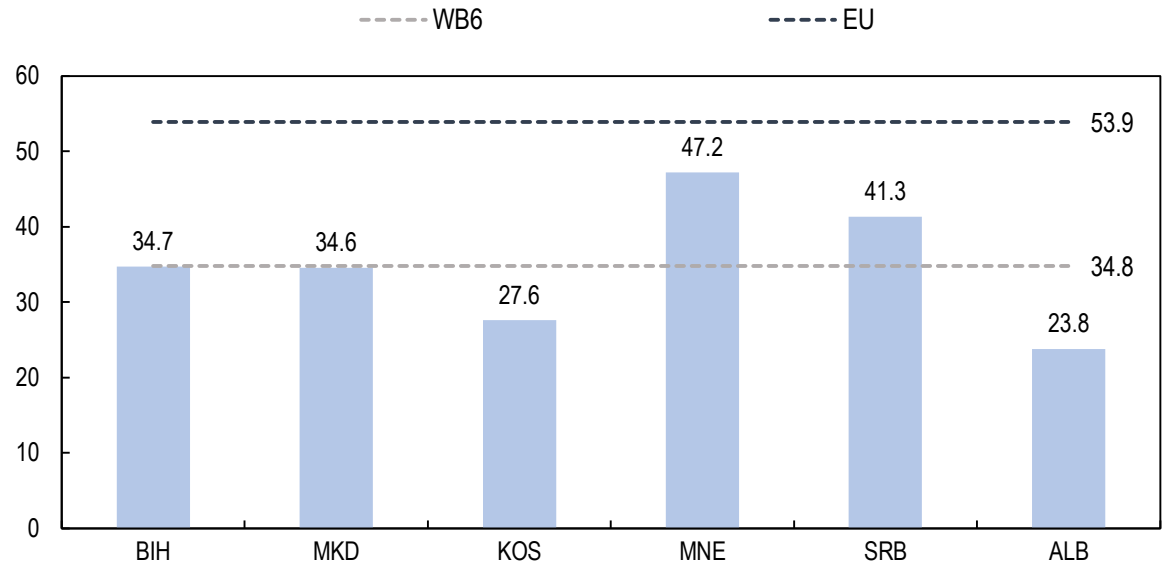
Developing skills for the future

As the WB6 economies embark on the green and digital transitions, their skills systems must anticipate future skills needs. This includes establishing proper education and training infrastructure for developing and adapting skills that enable and sustain these transitions.

Digital skills are uneven across the region, but universally below EU levels

Currently, the development of digital skills in the region shows limited convergence towards EU levels, with the proportion of individuals in WB6 economies possessing at least basic digital skills nearly 20 percentage points lower than in the EU (see Chapter 5). However, while all economies fall below the EU average, there is significant variation: Montenegro is the region's best performer, within 7 percentage points of EU levels, whereas Albania and Kosovo reported rates of less than 30% – essentially half of EU levels (Figure 3.3). This reveals the universal need to continue improving and developing these skills among students and the labour force in the region, while taking into account each economy's unique standing.

Figure 3.3. Individuals with basic or above basic digital skills in the WB6 economies and the EU (2021)



Note: Data for Kosovo are from the latest available year (2019).
Sources: Eurostat (2020[14]; 2024[15]).

Policies and initiatives increasingly prioritise the promotion of skills in schools, but there is a "policy-practice" gap

The current state of digital skills development in schools across the Western Balkans reveals notable regional trends. There is a general and growing emphasis on digital skills within the education sector across the region, although approaches and frameworks differ. Several economies have established relatively comprehensive frameworks or strategies prioritising digital skills development. Serbia is the only economy to have a dedicated Digital Skills Development Strategy (see Serbia economy profile),[19] with Montenegro and North Macedonia currently working to elaborate such a strategy. The other economies do not have a dedicated framework, but instead have incorporated explicit objectives or sections of strategies related to digital skills and competence acquisition within broader frameworks, particularly education or digitalisation strategies. However, almost all WB6 economies have adopted a common digital competence framework for students covering several key areas – including data literacy, communication and collaboration, digital content creation, and safety skills – which align with the competence areas outlined in the EU Digital Competence Framework (DigComp). The sole exception is Kosovo, which is in the process of adapting DigComp to better suit its own context.

ICT and digital skills development courses are largely incorporated into the curricula in both primary and secondary education across the region. Most economies have made it compulsory for students to complete relevant ICT classes, ranging from computer science in Serbia and coding in Albania to informatics in both Montenegro and North Macedonia. Beyond these dedicated subjects, Albania, Montenegro and Serbia have all integrated the development of digital skills across various subjects in their curricula. This approach not only increases students' exposure to these skills, facilitating their acquisition, but also underscores the transversal nature and application of digital competencies. Conversely, in economies such as Kosovo and Bosnia and Herzegovina, the inclusion of ICT into other school subjects is encouraged but not formalised.

To translate this policy priority to concrete outcomes (i.e. improved digital skills among students) there must be adequate and up-to-date ICT infrastructure in educational institutions, which continues to be a challenge across the region. For example, 30% of primary and secondary schools in Bosnia and Herzegovina do not have Internet connection. Furthermore, although some economies boast a relatively low computer-to-student ratio, such as 1:2 in Serbia and Montenegro, this ratio surpasses 1:20 in Bosnia and Herzegovina and Kosovo.[20] Even in the economies where Internet connectivity and computer availability are sufficient, issues persist due to slow Internet speeds and outdated computer equipment.

Beyond infrastructure, teachers with strong digital skills, as well as access to continuous professional support, are necessary to educate their students. There are some burgeoning efforts to strengthen digital competencies among teachers in several WB6 economies. For example, Albania has introduced new professional teacher standards that describes the use of digital skills, and North Macedonia offers training to teachers on new technologies under the framework of its education strategy. However, teacher capacities remain overall underdeveloped and serve as another limiting factor for increasing the use of digital technologies – which in turn limits the development of students' skills.

The development of skills in schools for the green transition remains very limited due to a lack of supporting policies and programmes

The development of students' skills for the green transition in the Western Balkans is even more limited than for digital skills, and represents a significant gap in education policies across the region. This restricts the ability of WB6 economies to educate a skilled workforce for the green transition. Currently, no WB6 economy has a national framework that outlines skills for the green transition for students, although one is being developed in both Kosovo and Montenegro. Most economies have made efforts to include competences related to the green transition in school curricula, such as environmental protection and sustainability, adaptability, climate change, and biodiversity. However, WB6 economies have not yet aligned their curricula for skills for the green transition with internationally recognised frameworks, namely the European Competence Framework on Sustainability (GreenComp) or the European Entrepreneurship Competence Framework (EntreComp). The exceptions are Albania (which has already aligned its curricula with GreenComp) and Kosovo (which has planned but not yet released the aim of such alignment). Moreover, while green skills are integrated into broader curriculum assessments, they are not separately assessed. This restricts the ability of governments and schools to gauge whether students are effectively acquiring these competencies, especially considering the relatively recent introduction of many educational initiatives.

Strategies and adult learning programmes for workforce adaptation to sustain the green and digital transitions are still largely in the early stages

Upskilling and reskilling the workforce through adult learning programmes is crucial for ensuring that workers have relevant, up-to-date knowledge and skills. However, participation in adult learning is generally low in the WB6 economies, with the regional average significantly below that of the EU (Table 3.3). The exceptions are Albania and Kosovo, both of which have nearly converged to EU levels.

Table 3.3. Participation in lifelong learning in the WB6 economies (2018-22)

Economy	Participation in lifelong learning (% 25-64 years population)
ALB	9.8
BIH	2.1
KOS	9.6
MNE	2.8
MKD	2.6
SRB	4.4
WB6	6.0
EU	10.6

Sources: European Commission (2023[16]); Eurostat (2024[17]).

Although participation in education and training activities is generally low, it further decreases when focusing on programmes aimed at skills for the digital and green transitions. This limited engagement is partly due to the lack of relevant opportunities given the early stage of development of such programmes in the region. The importance of cultivating digital skills among workers was highlighted by the Western Balkan Digital Skills Multistakeholder Working Group, which sought to kick off regional dialogue on digital skills development and catalyse efforts to develop strategies explicitly governing these skills. However, despite this recognised need almost all WB6 economies lack a dedicated policy framework guiding the development of adults' digital competencies (apart from Serbia, as previously mentioned), although certain economies, such as Montenegro and Albania, have policy documents that emphasise their commitment to ensuring that their workforces acquire in-demand digital skills.

In the absence of well-defined policy frameworks, most WB6 economies have opted to promote the digital skills of adults through ad hoc programmes or donor-funded initiatives supporting adult learning. For example, some training activities for the development of digital skills for employed individuals and jobseekers have been implemented by economies' public employment services (PES), such as programmes in Albania and Kosovo that seek to equip jobseekers with programming and/or coding skills by financing their participation in training. The aim of these programmes is to increase individuals' employability by helping them acquire digital skills that are in demand in the labour market. Other economies, such as FBiH and North Macedonia, offer less targeted services but still provide programmes to equip unemployed individuals with digital skills training. However, most of these programmes primarily focus on upskilling jobseekers rather than the current workforce; only Albania, North Macedonia and Serbia have programmes that encourage employers to upgrade their employees' digital skills. This reveals a significant gap in approaches for developing digital competences among adults.

Additionally, some WB6 economies have advanced in identifying the digital skills needs of employers. This is generally performed either through consultations with key stakeholders, such as in Albania and RS, or through sector studies on the current and future development of employment in the IT sector, such as in North Macedonia and RS. However, these consultations and studies are only useful if their results are used to revise or shape training policies and programmes, but there is no available evidence that these economies have used their findings in this way.

There is significant scope to strengthen adult learning programmes in relation to the region's green transition, which is expected to significantly impact the labour market across numerous sectors and occupations. One expected change is the generation of new opportunities in sectors such as renewable energy and the concurrent reduction of roles in fossil fuel industries. Specifically, as the WB6 economies move to reduce or phase out their coal use (see Chapter 6), such efforts will directly impact the estimated 138 000 jobs tied to coal production in the region (Ruiz Castello et al., 2021[18]). Consequently, as the labour market evolves in response to these changes there will likely be shifts in skill requirements and job transitions – creating demand for new and expanded education and training opportunities for workers.

Programmes and initiatives related to green jobs in the Western Balkans are still in their infancy, with economies progressing at different rates. Most WB6 economies lack an overarching policy framework to equip their workforces for the green transition. Additionally, their existing employment and environmental strategies do not adequately address employability or skills development for the evolving landscape of green jobs. The exceptions are Albania, FBiH and Montenegro – but even in these cases, where the significance of skills for the green transition is acknowledged, these references are not accompanied by concrete measures. Tailored adult learning programmes, VET training courses, employment incentives and entrepreneurship programmes that promote employment in the green economy are largely non-existent or are in the early phases of implementation.

A crucial aspect of supporting the greening of the labour market involves conducting studies that identify the skills and jobs most relevant for the green transition. Such assessments can not only identify new occupational profiles as new jobs appear, but can also determine which types of skills might be transferable from one sector or occupation to another. However, only Albania and Montenegro have embarked on such studies: Albania's employment agencies[21] are developing a study on green jobs, while Montenegro's Chamber of Commerce has begun forecasting the impact of the green transition on employment and identifying and categorising related occupations. No WB6 economy currently has programmes for training and adapting skills among either employed or unemployed individuals to meet the demands of the green transition.

Insufficient financial incentives limits workers' participation in training on skills for the digital and green transitions

Beyond the nascent status of policies and programmes on skills for the digital and green transitions, the region's low rates of participation in adult learning is partly due to the lack of financial incentives (including tax breaks, grants or vouchers) to encourage individuals to participate in continuous training. By reducing cost barriers to participation, and thus facilitating movement between education, training and employment, such incentives have proved effective in supporting flexible adult learning pathways (OECD, 2023[19]). However, while little has been done to address this lack of financial resources, most economies have strategies or initiatives that aim to promote adult participation in learning, and thus expand available employment opportunities. The notable exception is North Macedonia, which currently lacks a framework but is in the process of adopting its new Adult Education Act. However, only Albania, Montenegro and Serbia implement policies that specifically aim to address skills mismatches in adult learning. This reveals a gap between the presence of broad, overarching frameworks guiding adult learning and the presence and utility of specific, well-targeted policies.

Expanding the skills pool

Over the past decade, the emigration rate from WB6 economies has accelerated, resulting in approximately one-fifth of the population residing abroad (OECD, 2022[20]). Such significant outflows, compounded by contracting birth rates, have led to a shrinking labour force, underscoring the importance of retaining and attracting talent. These trends have had a significant impact on the region, with the availability of labour and the impacts of emigration jointly identified as the second most significant concern for businesses (surpassed only by concerns of macroeconomic instability) (ACIT Centre, 2023[21]). Thus, given the pace and intensity of brain drain, as well as chronic labour shortages, making the most of foreign and diaspora skills is an important consideration in supplying relevant skills to the labour market.

Migration policies in the region are well developed but fail to address the systemic issues that initially contribute to labour shortages

All Western Balkan economies have begun adapting policies with the aim of attracting migrants with relevant skills to meet the demands of the labour market. Specifically, they have all developed dedicated migration strategies that are broadly overseen by ministries or other government agencies responsible for implementation. The economies have also established dedicated inter-ministerial bodies to co-ordinate migration policies, as well as implemented legal frameworks addressing migration that include specific laws on foreigners. Efforts are underway to harmonise national legislation with EU standards in this regard. However, there are significant differences in terms of progress: while laws in Serbia and Montenegro largely align with the EU *acquis*, Bosnia and Herzegovina and North Macedonia have yet to adopt relevant legislation that complies with EU guidance on the mutual recognition of professional qualifications.[22]

The effectiveness of migration policies in attracting skilled migrants to the domestic labour market in WB6 economies hinges on the alignment of these policies with each economy's specific needs and conditions, as well as the broader regional context. A key opportunity for the region lies in attracting highly skilled migrants to the rapidly growing ICT sector, which wields significant potential for economic growth and skilled employment (Mara and Landesmann, 2022[22]). Indeed, most WB6 economies have not fully utilised their migration frameworks to attract and retain ICT jobs, which could help reduce high-skilled emigration from the region (see Chapter 4).

The WB6 economies have shown a commitment to enhancing regional economic integration through initiatives such as the Common Regional Market (CRM) 2021-24 Action Plan,[23] endorsed at the Berlin Process Summit in November 2020. This plan aims to facilitate intra-regional mobility by adopting frameworks for the recognition of professional qualifications, implementing freedom of movement for students and professionals, and enhancing the recognition of academic qualifications.

In this regard, WB6 foreign ministers approved three regional agreements at the WB-EU ministerial meeting organised within the Berlin Process in 2022: 1) Freedom of Movement with Identity Cards; 2) Recognition of Higher Education Qualifications; and 3) Recognition of Professional Qualifications for Doctors of Medicine, Dentists and Architects (RCC, 2022[23]). Building on these agreements the WB6 economies signed a memorandum of understanding in October 2023 for the mutual recognition of professional qualifications with the aim of improving professional mobility and aligning skills with labour market needs.[24] Moreover, in March 2024 Albania, North Macedonia and Serbia fully opened their labour markets to one another as part of the Open Balkan initiative.

Given the proximity and cultural ties between the WB6 economies, regional co-operation on migration policies can help address common challenges and maximise the benefits of skilled migration for the entire region. However, despite these initiatives migration intentions within the WB6 remain limited, with only a small percentage of citizens interested in intra-regional migration, according to the 2023 Balkan Public Opinion Barometer (ACIT Centre, 2024[24]).

Beyond regional efforts, Albania, Montenegro and Serbia are actively engaging in bilateral agreements and ongoing negotiations to co-ordinate qualifications, education and social security systems. In contrast, Bosnia and Herzegovina, Kosovo and North Macedonia have made limited progress in these areas. Albania, North Macedonia and Serbia are also making strides in preparing to join the European Employment Services (EURES), while the remaining WB6 economies have shown limited progress in this regard.

Between 2018 and 2022, five of the WB6 economies saw a rise in the number of temporary foreign work permits issued (Table 3.4). While improvements to the design and implementation of migration policies might explain some of this increase, other factors – namely the Russian war of aggression against Ukraine – have played a more central role. For instance, in Serbia the war has contributed to the three-fold increase observed in temporary foreign workers, with the economy hosting an estimated 150 000 Russian

migrants as of February 2024 (Euronews, 2024[25]). This influx can be attributed to a combination of logistical, economic and cultural factors.[25] Similarly, Montenegro's increase in foreign workers can be partially explained by the increase in Russian migrants who are attracted to the economy's tourism sector and the ease of starting a business (the economy facilitates the acquisition of temporary residence permits that allows foreign workers to stay) (Ivanovic, 2023[26]).

Table 3.4. Temporary foreign workers in the WB6 economies (2018-22)

Economy	Number of temporary foreign workers (2018)	Number of temporary foreign workers (2022)	Percentage change (%)
ALB	6 974	7 930	+ 13.7
BIH	2 822	3 780	+ 33.9
KOS	2 899	2 976	+ 2.7
MNE	26 327	29 319	+ 11.4
MKD	852	800	- 6.1
SRB	8 990	35 173	+ 291.2

Note: The data for North Macedonia in the first column are from 2019.
Sources: European Commission (2023[27]; 2023[28]; 2023[29]; 2023[30]; 2023[31]); Government of Kosovo (2018[32]; 2023[33]); International Organization for Migration (2022[34]); INSTAT (2019[35]); Kovačević (2020[36]); Ministry of the Interior (2021[37]); Ministry of Security (2020[38]).

While the increase in foreign workers in 2022 was primarily driven by the external shock of the Ukraine conflict, more recent efforts by the Western Balkan economies indicate a growing focus on addressing labour shortages by expanding the quota for foreign employment permits. For instance, North Macedonia raised its quota from 3 250 permits in 2022 to 5 000 in 2023. Bosnia and Herzegovina increased its quota by almost 50%, from 3 500 permits in 2023 to 6 073 in 2024. Additionally, in March 2024 Montenegro proposed raising its quota to 30 000.[26] However, these increases may still fall short of meeting demand, with economies such as North Macedonia and FBiH advocating for doubling the new quotas.[27]

Although raising the quota of foreign employment permits can offer a short-term solution to expanding the region's skills pool, the focus needs to shift towards addressing the underlying issues driving high levels of emigration, such as uncompetitive salaries and a lack of employment opportunities. A more systematic approach will help engage and strengthen ties with migrant workers effectively. One strategy to achieve this is by enhancing mechanisms for the inclusion and integration of migrants.

The scope and depth of initiatives to promote the inclusion and integration of skilled migrants vary substantially across the region

The migration policy strategies of most WB6 economies contain objectives and measures to address irregular migration and to support the socio-economic integration of immigrants, while also making the most of foreign talent. These strategies also envisage the facilitation of labour mobility for return migrants and other migrant workers through adapted services, promotion programmes, language courses and the recognition of prior learning. Albania, Bosnia and Herzegovina and North Macedonia have ongoing active action plans to implement domestic strategies, while plans in Montenegro, Kosovo and Serbia expired in 2023 (with no indication of whether new initiatives are envisaged).

Several actions have been taken across the region to more tangibly promote the inclusion and integration of skilled migrants into domestic labour markets and society. As shown in Table 3.5, Albania and North Macedonia offer the broadest array of measures, whereas Bosnia and Herzegovina and Kosovo do not have any of these elements included in their policy frameworks – which may prove particularly problematic for Bosnia and Herzegovina given the significant increase in foreign workers in recent years

and plans to nearly double this quota in 2024.[28] Most economies ensure that migrants have the right to emergency healthcare, public education and equal pay for equal work.

Table 3.5. Inclusion and integration measures for skilled migrants in the WB6 economies

	ALB	BIH	KOS	MNE	MKD	SRB
Free and fair ethical recruitment of migrant workers	✓	×	×	✓	×	×
Portability of social security benefits	✓	×	×	×	✓	✓
Aligning labour migration policies with actual or projected market needs	✓	×	×	✓	✓	×
Facilitating the recognition of skills and qualifications acquired abroad	✓	×	×	×	✓	×
Facilitating access to language training	✓	×	×	×	×	×

Source: Ministries of labour/employment or ministries of foreign affairs of the WB6 economies.

Governments in the region are actively liaising with diaspora communities through diverse initiatives to expand the transfer of skills and knowledge

With an estimated diaspora population of 10 million, the Western Balkans could benefit from closer engagement with those living abroad to attract their skills, particularly those who are well educated and highly skilled. This would help to support the region's socio-economic development. All WB6 governments have established institutional and policy frameworks to engage with their diaspora communities. These frameworks vary in extension and focus: Kosovo, Montenegro, North Macedonia and Serbia have a longer history of institutionalised co-operation with the diaspora, while Albania and Bosnia and Herzegovina have only recently prioritised strategic development. However, all economies seek to encourage and facilitate diaspora engagement to maximise their contributions to national development and strengthen trust between the state and diaspora communities. Diaspora policies in the region are elaborated through targeted strategies and usually fall under the competence of ministries of foreign affairs. The exception is Serbia, where related efforts are part of its strategic framework on migration, with multiple ministries and governmental bodies involved in diaspora policy.

While some WB6 economies have ongoing diaspora strategies, others have outdated frameworks: Montenegro and North Macedonia's strategies expired in 2023 and there is no information available regarding plans for new ones. Kosovo is preparing to launch public consultations for a new diaspora strategy and law after the National Diaspora Strategy 2019-23 failed to gain approval due to political turmoil.

Governments in the Western Balkans have launched diverse initiatives to attract diaspora skills, focusing on skills and knowledge transfer programmes, networking and summits, and collaboration platforms. Each economy has developed some version of an online platform to map and engage with diaspora (Table 3.6). Fellowships, which can contribute to the transfer of important knowledge and skills, are also common and include the Albanian-American Development Foundation's Research Expertise from the Academic Diaspora Fellowship Programme, the Citizen Diplomacy Fellowship (Kosovo), Engaging Diaspora Professionals Programme (Kosovo), and Macedonia2025's internship programme (North Macedonia). Linking scientific diaspora with relevant institutions in the economies is also a popular initiative, such as through Montenegro's Scientific Network portal or Serbia's Science and Diaspora Collaboration Programme. These efforts all represent different avenues for further strengthening collaboration between domestic institutions and diaspora – particularly those who are highly skilled – to maximise skills and knowledge transfer from the diaspora population.

Table 3.6. Online platforms for diaspora engagement in the WB6 economies

Economy		Online platform	Purpose
ALB		Albanian Diaspora Professionals Network	Collect information, leverage the expertise of Albanian diaspora, and make them aware of the requirements of Albanian or foreign business members.
BIH	State-level	Interactive portal (developed by the Ministry of Human Rights and Refugees)	Facilitate knowledge transfer and skills-sharing opportunities.
	RS	Diaspora registry and online portal	Connect RS with its diaspora.
	FBiH		
KOS		KosovoDiaspora.org	Connects Kosovo with its diaspora using social and online media to showcase achievements.
		KosovaDiplo365	Strengthen relationship between citizens living in Kosovo and diaspora populations to transmit culture, identity, heritage, history and shared values.
		eDiaspora	Support the 2024 population census by registering the resident and non-resident (diaspora) populations.
MNE		"Upiši se" web application	Register diaspora members.
MKD		Connect2MK	Connects Macedonian businesses and professional expatriates.
SRB		“Tačka povratka” (Returning Point)	Assist diaspora members interested in returning to Serbia by offering support with the return and reintegration processes.

Sources: Ministries of labour/employment or ministries of foreign affairs of the WB6 economies; OECD (2022[20]).

It is vital for the WB6 economies to target engagement efforts at competitive or economically important sectors. For example, the ICT sector is one of the fastest growing in the region and offers substantial potential for economic growth and skilled employment opportunities (Mara and Landesmann, 2022[22]). Serbia has distinguished itself by offering incentives such as more competitive wages or tax relief for employers who hire highly skilled diaspora. However, other economies have yet to capitalise on this potential to attract and retain jobs in the ICT sector, and thus may struggle to curb high-skilled emigration and encourage the return of highly skilled individuals (see Chapter 4).

Recommendations for developing relevant skills

- **Increase access to high-quality, affordable childcare across the region.** First, WB6 governments should ensure that there is an adequate number of institutions that can properly meet demand. Second, improving equity in access involves ensuring that ECEC is either provided for free (supported by the government) or has fees determined by household income. Together, these two reforms would likely benefit children from disadvantaged backgrounds or those living in rural areas – the groups who tend to enrol in ECEC at much lower rates – as well as encourage increased labour force participation among women.
- **Scale up initiatives for ensuring inclusivity in educational opportunities for disadvantaged groups.** Given the relatively low enrolment rates of children and students from vulnerable and disadvantaged groups at all levels of education, the WB6 governments should consider alternative or reinforcing avenues for further strengthening existing programmes. Such measures could include scholarships for upper secondary education, additional teacher training, or more comprehensive data collection on the enrolment and completion rates for these groups.
- **Develop incentives to enhance the attractiveness of flexible adult learning opportunities, particularly those focused on developing skills for the digital and green transitions**. Given the current absence of education and training programmes focused on developing workers’ skills, WB6 economies should prioritise creating and implementing initiatives to enable individuals to upskill or reskill accordingly. It will also be crucial to ensure the affordability of these programmes. This can be achieved by encouraging employers to offer financial incentives such as tax breaks,

vouchers or other subsidies that can offset the cost of participating in training (OECD, 2023[19]). Such tools would be more impactful if they were coupled with increased government support to business initiatives in the green economy (for more information, see Chapter 6).

- **Collect comprehensive and comparable data on adult learning and skills.** Given the variation in the data collected on education and employment policy, it is crucial that WB6 economies effectively benchmark their outcomes both within the region and with international peers. While most economies (except for Bosnia and Herzegovina) participate in international assessments that measure student outcomes, such as PISA, none have a standardised way of assessing and comparing adult skills. As such, participation in the OECD's Programme for the International Assessment of Adult Competencies (PIAAC) could offer a promising avenue (Box 3.1).

Box 3.1. Measuring adult skills: OECD's Survey of Adult Skills

The Survey of Adult Skills, which is part of PIAAC, is an initiative that allows participating governments to evaluate and monitor an array of skills among their adult populations. It is the most comprehensive international survey of adult skills in the world.

By measuring the level and distribution of literacy, numeracy and problem-solving competencies it provides data on several relevant aspects of skills, including (but not limited to):

- information processing skills across different sub-groups of adults in participating economies
- factors that impact the acquisition and development of these skills
- performance of national education and training systems
- equity in educational and labour market outcomes
- lifelong learning.

A new round of data collection for the second cycle of the Survey of Adult Skills is being implemented in 2024-29. Starting to participate in the survey – and continuing on a regular basis – allows economies to benchmark progress over the time, which is particularly important for the WB6 economies given the persistent challenges facing their education systems and labour markets.

Source: OECD (2024[39]).

- **Augment efforts to support skilled migrants successfully integrate into their new communities.** To achieve this, closer collaboration with the local government, civil society organisations, businesses and educational institutions is necessary to identify and agree on effective context-based integration programmes. By leveraging their resources and expertise, stakeholders can develop more impactful programmes that address the specific needs of skilled migrants and facilitate their inclusion and integration.

Putting skills to effective use

Easing the school-to-work transition

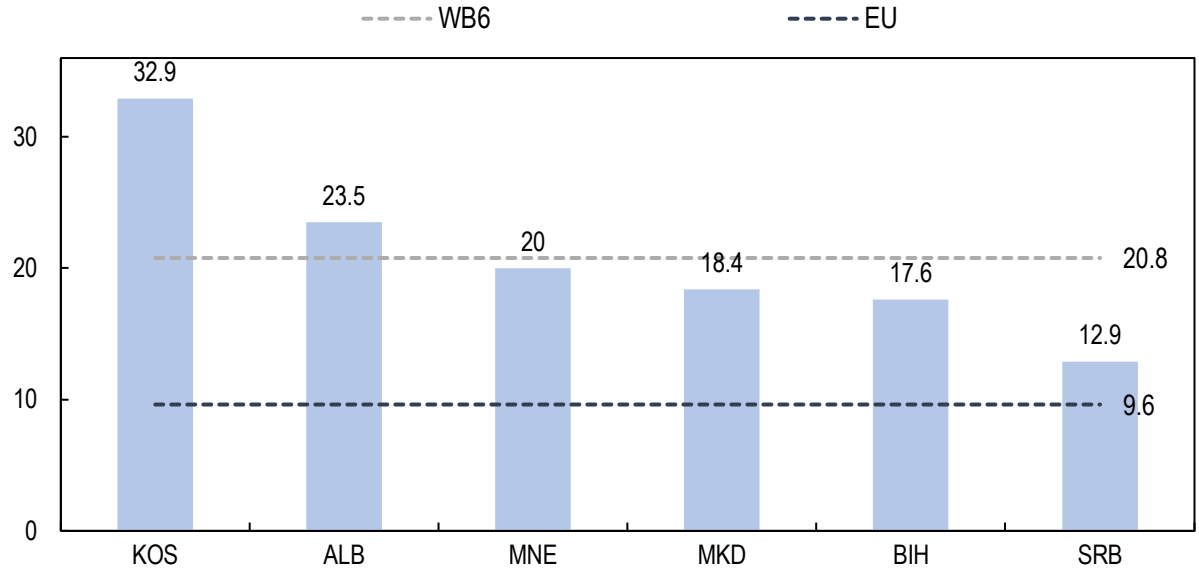
The WB6 economies surpass the EU with respect to the percentage of the labour force with advanced (tertiary) education, with the WB6 average nearly double that of the EU (76% versus 42%). However, despite this impressive tertiary education achievement, most of the region faces difficulties with education and training systems adapting to changes within the labour market. This has contributed to high youth inactivity and unemployment, as well as high levels of emigration of young skilled adults from the region.

High youth NEET and unemployment rates underscore persistent challenges with the school-to-work transition

The region is underperforming with respect to the school-to-work transition. While the average youth unemployment rate in the Western Balkans fell from 40.3% in 2017 to 25.5% in 2023, this is far above the EU average of 13.8% (World Bank, 2024[40]). Moreover, this decrease is partially a product of the sustained high levels of youth emigration, rather than well-developed employment policies or activation programmes.

As with unemployment rates, the region's NEET rates are significantly above EU levels (Figure 3.4), exhibiting a sluggish pace of convergence. Notably, while all six Western Balkan economies report rates higher than the EU average, there is significant variation across the region, with rates ranging from 12.9% (Serbia) to 32.9% (Kosovo). A high NEET rate can indicate that young people are not acquiring the skills most sought after by employers through education or training – which can result in an increased and sustained risk of becoming disconnected from the labour market.

Figure 3.4. Youth NEET rates in the WB6 economies and the EU (2022)

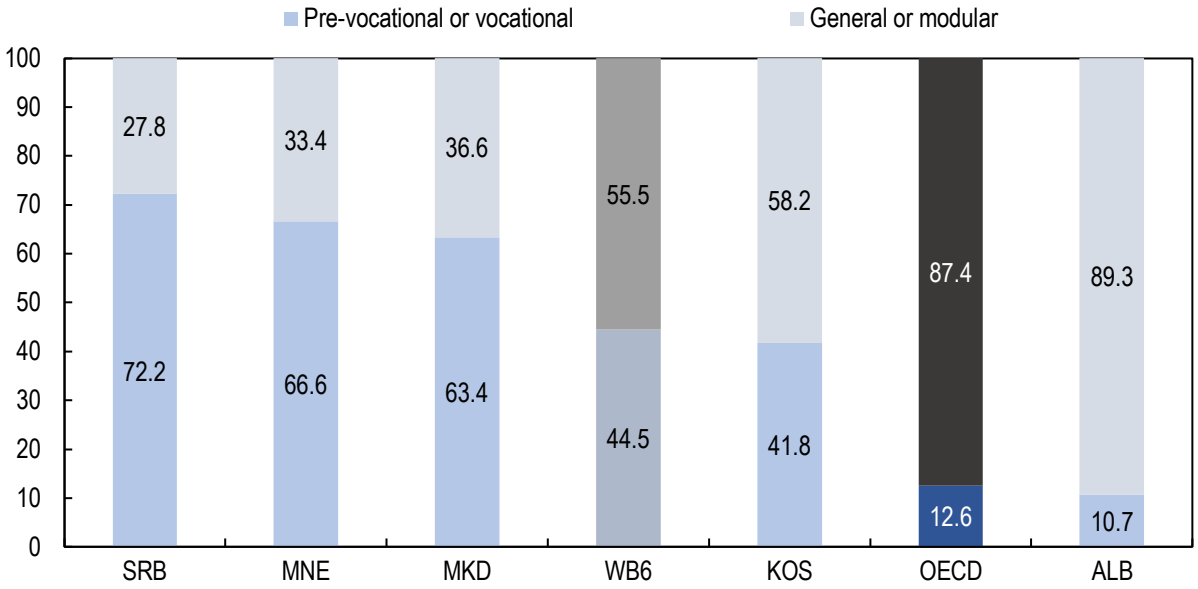


Sources: World Bank (2024[41]); Vienna Institute for International Economic Studies (2024[42]); Eurostat (2023[43]).

Vocational education and training (VET) programmes are widely used, but their quality and relevance must be improved

Strengthening VET governance is particularly important in the Western Balkans given the high levels of enrolment and the ability of these systems to provide in-demand, occupation-specific skills in quickly expanding fields. It also can counter high NEET rates by encouraging young people to remain in education or training while cultivating valuable skills. The vocational path is a common option among Western Balkan students, with the region reporting a much higher rate of enrolment in VET programmes than the OECD average: more than 50% of students in the WB6 economies are enrolled in pre-vocational or vocational programmes at age 15, compared to an OECD average of 13% (Figure 3.5). While these high enrolment rates suggest that VET programmes are considered attractive, for most WB6 economies VET is unlikely to be the preferred choice for education or training, but is rather viewed as a fallback option.[29]

Figure 3.5. ET enrolment in the WB6 economies and the OECD (2022)



Notes: Caution is advised when interpreting estimates because one or more PISA sampling standards were not met (see PISA 2022 Reader's Guide, Annexes A2 and A4). Countries and economies are ranked in descending order of the percentage of students enrolled in pre-vocational or vocational programmes. Bosnia and Herzegovina is not included due to its lack of participation in PISA 2022.
Source: OECD (2022[3]).

Most economies track VET outcomes such as completion rates, employment rates of graduates and earnings. However, only Albania, Montenegro, North Macedonia and Serbia consistently and systematically monitor and adjust their VET policies based on these data, even though such efforts can improve the labour market relevance of VET programmes.

The relevance of VET can be bolstered through strong engagement with **social partners**.[30] Almost every WB6 economy has some mechanism or structure in place to engage social partners in the decision-making process for VET policy. By consulting these partners and leveraging their "on the ground" knowledge, governments in the region can better understand skills gaps in the labour market and tailor VET curricula and policies accordingly. Surveying social partners to better understand skills demands is particularly useful, and almost all economies conduct such surveys on at least a yearly basis (and even on a quarterly basis in North Macedonia).[31] However, none of the WB6 economies has established a Centre for Vocational Excellence,[32] reflecting the relatively limited nature of formalised, systematic public-private partnerships in support of VET. Furthermore, while structures exist to engage social partners in the provision of VET, there is significant scope to improve the efficiency of these mechanisms.

Increasing the importance attached to **work-based learning** (WBL) is another way of better aligning VET programmes with the needs of the labour market. As an important component of VET systems, WBL can ease school-to-work transitions and facilitate meeting labour market demands (OECD, 2021[44]). Many VET graduates cite the lack of opportunities to develop practical, workplace-relevant skills as one of the primary reasons for problems finding suitable employment.[33] The development of dual education systems is an area of WBL that has gained traction as it aims to prepare students for the workforce by equipping them with both theoretical knowledge and practical skills demanded by employers, thereby bypassing the typical delay of the education system in responding to evolving needs. In recent years, all WB6 economies have made strides in piloting, implementing or strengthening frameworks for dual education models. Montenegro and Serbia are the most advanced: Montenegro was the first to introduce a national roll out of dual VET,

and Serbia established a dedicated Law on Dual Education in 2017. Conversely, economies such as Albania and Bosnia and Herzegovina are still in the process of piloting dual education programmes.

These ongoing developments of WBL are still relatively nascent and have not yet been matched with concrete mechanisms for expanding WBL opportunities for students. For example, very few economies offer incentives to employers to encourage WBL and apprenticeships. Only in FBiH, North Macedonia and Serbia do these incentives exist, and little information is available beyond their presence. Montenegro plans to create a "Fund for Dual Education", which will be used to pay employers to host students during their study programmes. One structural issue with increasing the availability of WBL opportunities is the prevalence of small and medium-sized enterprises (SMEs), which constitute 99% of all firms operating in the WB6 (OECD, 2022[45]). Given the small-scale operations and more limited resources of SMEs, they might be less capable of providing WBL options to students.

Despite various efforts to improve VET governance, systems across the WB6 continue to encounter significant challenges that affect their quality and relevance, although the nature and severity of these issues vary by economy. In PISA 2022, VET students across the WB6 reported weaker learning outcomes compared to those participating in general education, highlighting a disparity in educational quality between the two types of programmes (OECD, 2023[1]). These difficulties in instilling strong foundational skills not only impede a smooth work-to-school transition, but also hinder students' ability to adapt to changing labour market needs (OECD, 2020[46]).

Even in economies with high-quality systems, VET programmes still struggle with alignment with the demands of the labour market. This is partly due to outdated curricula, which leads to a gap between the skills taught to students and those required by employers (OECD, 2022[7]). This is evident from the perspective of employers across the Western Balkans, with a majority of firms reporting that they faced problems hiring workers for "routine jobs" (i.e. those usually covered by VET) due to applicants lacking skills or experience.[34] Obsolete technologies and inadequate equipment further hinder students' skills development, particularly as a growing proportion of sectors and positions require digital competences (Regional Challenge Fund, 2023[47]). Kosovo stands out due to its recent efforts to equip 10% of its VET schools with augmented reality and virtual reality tools, significantly increasing the perceived appeal among students (University for Business and Technology, 2023[48]).

All economies have taken steps to improve the labour market relevance of their higher education programmes

All WB6 economies have objectives of enhancing the labour market relevance and outcomes of higher education within their education strategies. To support these strategic goals, several mechanisms are employed, the most common of which is the use of communications or awareness campaigns to provide prospective students with relevant information when selecting their programme. These campaigns can highlight the skills and qualifications most in demand, thus encouraging students to pursue programmes in areas currently experiencing shortages or that have more employment opportunities. Other common avenues for boosting labour market relevance include the use of block grants or scholarships to finance participation in in-demand programmes, and using labour market information to inform curricula design. However, despite these efforts there is still a problem across the region with the most popular fields of study not being those where the most vacancies exist, resulting in a gap between the oversupply of humanities and social science graduates and the demand for those with science, technology, engineering and mathematics (STEM) degrees.

All economies collect some statistics to monitor progress and assess the outcomes of higher education, although the variety and comprehensiveness of these collection efforts vary. Nearly every economy collects data through employer surveys and surveys of workers/graduates. However, only North Macedonia, Serbia, FBiH and RS collect data on employment rates by field of study – an important data point for discerning which fields of study are most in demand or most "employable."

Youth Guarantee schemes across the region represent a commitment to reducing youth inactivity and unemployment, but are at different stages of development

To address the high prevalence of young people who are NEET and not actively searching for employment – and given the difficulties with the school-to-work transition in both VET and higher education – most PES in the region have started the process of adopting and implementing Youth Guarantees, a flagship project under the Economic and Investment Plan for the Western Balkans that aims to reduce youth unemployment. In July 2021 the WB6 economies pledged to implement the Youth Guarantee programme in the Western Balkans Declaration on the Sustainable Integration of Youth into the Labour Market.[35] These schemes seek to expand knowledge and access to counselling, education, training and employment opportunities for young people aged 15 to 29 years. This policy instrument was first implemented across the EU in 2014 due to persistently high levels of youth unemployment: the EU reported an average youth unemployment rate of 24.1% in 2014 – less than two percentage points below the current WB6 average of 25.6% (ranging from 21.3% in Kosovo to 29.8% in Bosnia and Herzegovina) (World Bank, 2024[49]; Eurostat, 2024[50]).

However, the WB6 economies are at very different points in the implementation process. North Macedonia was the first economy in the region to implement a Youth Guarantee scheme (2020-22) that focused on early intervention, outreach and improved quality of employment service provision, and has continued these efforts through its Youth Guarantee Plan 2023-26 (see North Macedonia economy profile). Albania and Serbia have both adopted their own Youth Guarantee plans and launched their pilot phases in October 2023 and January 2024, respectively. Montenegro and Kosovo have adopted implementation plans; however, while piloting is expected to start in 2025 in Montenegro, Kosovo has yet to achieve the conditions for launching its pilot – namely restructuring the Employment Agency. In Bosnia and Herzegovina, only RS has adopted an implementation plan, although FBiH has two ongoing “micro-pilots” in the Zenica Doboj and West Herzegovina cantons.

Matching skills with labour market needs

All WB6 economies are currently struggling with pervasive vertical and horizontal skills mismatches. Vertically, many workers find themselves over-qualified for their position. Horizontally, some sectors are oversaturated, while others face significant shortages despite high demand from the labour market.

According to recent surveys, on average 23.6% of firms in the Western Balkans identified an inadequately educated workforce as a major obstacle restricting their competitiveness (Table 3.7). The percentage by economy significantly varied, ranging from 2.3% in Bosnia and Herzegovina to 44.2% in Kosovo. This does not necessarily indicate that the region’s workers are poorly educated, but rather they lack the proper skills that align with employers’ needs. Moreover, a 2023 survey showed that 26% of employees and 31% of businesses in the region disagreed that the skills taught in their economy’s education system met the needs of their work.[36]

Table 3.7. Inadequately educated workforce as a major constraint in the WB6 economies (2019, 2023)

Percentage of firms

Economy	Percentage of firms
ALB	24.8
BIH	2.3
KOS	44.2
MNE	13.7
MKD	36.3
SRB	20.3

Notes: Data for BIH, MNE, and MKD are from 2023; data for ALB, KOS, and SRB are from 2019.
Source: World Bank (2024[51]).

Skills intelligence systems are under development across the region, although few economies are utilising advanced predictive tools to anticipate skills imbalances

The WB6 economies have begun to analyse and establish mechanisms to address the prevalent skills imbalances in their economies. Skills intelligence systems are tools and frameworks used to collect, evaluate and disseminate information about the skills and competences needed in the labour market, and enable policy makers, employers and the public to promptly identify shifts in skills and occupation profiles.

The most common skills intelligence system used in the region are **employer skills needs surveys**, which are conducted by all WB6 economies apart from Kosovo. These surveys assess the challenges that employers face in recruiting and retaining a qualified workforce by looking at the perceived skillsets of new workers, as well as inadequacies among existing employees.

Albania and Serbia have also established **sector skills councils** to analyse sectoral needs, a substantial step toward complementing national skills intelligence with sector-specific intelligence. These councils utilise their assessments to update existing or propose new qualifications to better align with market needs. Notably, Serbia has councils in 15 sectors, while Albania has councils in tourism (one of the economy's most important sectors) and ICT (the fastest growing sector that attracts substantial foreign direct investment [FDI]). However, a gap emerges in the Albanian case as there is no council for other sectors, namely energy, that are also major recipients of FDI. This underscores a broader challenge: apart from Serbia, skills intelligence in the region does not sufficiently prioritise the demands of investors in key priority sectors, which means that opportunities to bolster the competitiveness of WB6 economies may be missed.

Tracer studies, which evaluate graduates' employability and determine the skills most in demand in the labour market, are also widely used to identify skills gaps. All WB6 economies have at least piloted a tracer study, although the level of advancements of these efforts significantly varies. For example, whereas studies in Albania and Kosovo focus exclusively on graduates from VET programmes, those in Bosnia and Herzegovina and North Macedonia include both VET and higher education graduates. The frequency of these studies also varies, with Albania the sole WB6 economy that conducts an annual tracer study that requires all VET institutions to share relevant data. Thus, for most of the region the absence of regular tracer studies limits the ability of governments to systematically track progress and monitor education and employment outcomes, particularly among VET graduates.

While these tools are useful in assessing current skills imbalances, some economies have undertaken efforts to anticipate future in-demand skills and occupations with more predictive tools. One prominent avenue has been through the establishment of **skills observatories** in Albania and North Macedonia that aim to identify both current and future skills needs. These observatories compile a variety of administrative, economic and labour market data across various government sources to support evidence-based policy

making. Another method is the use of **skills intelligence barometers**. Kosovo offers a strong example as it has developed three such barometers: the Skills Barometer, the Labour Market Barometer and the VET Barometer. Specifically, the Skills Barometer, published in December 2021, aimed to forecast the supply of and demand for different occupations and sectors over a five-year period (OECD, 2022[45]). Economies such as Bosnia and Herzegovina and Montenegro seemingly lag behind their peers in terms of their use of smart skills mechanisms.

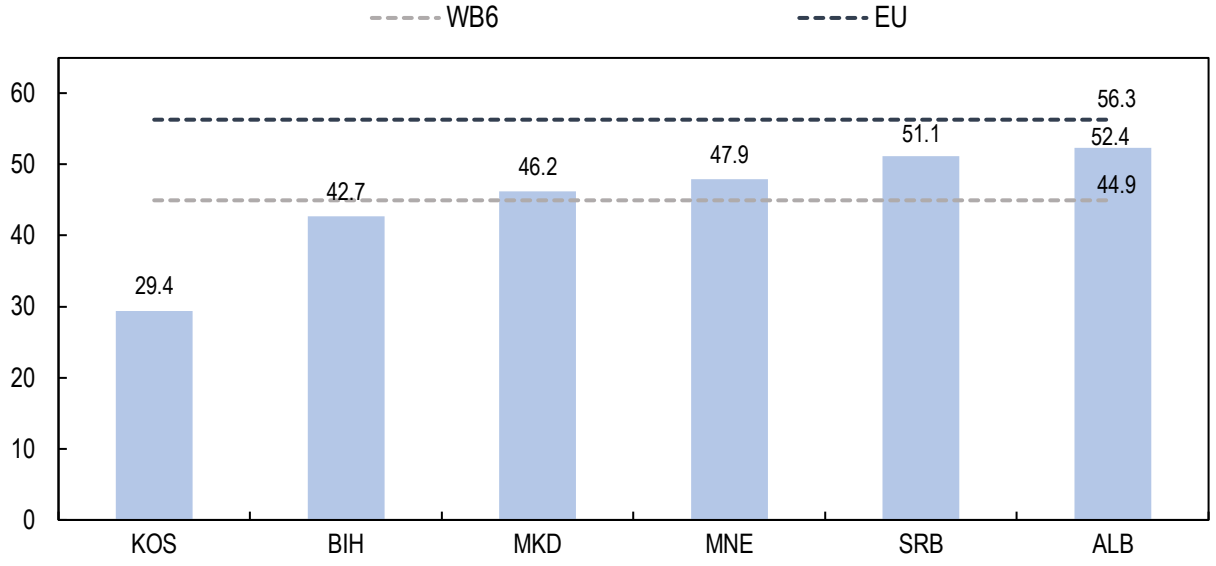
Although these various advances demonstrate ongoing efforts to develop systematic skills intelligence, and consequently address skills mismatches, these systems are still relatively new, meaning that their efficacy has yet to be observed. Moreover, there are still several shortcomings facing these tools. First, in economies with several mechanisms the results of skills analysis are rarely centralised, which limits their utility for evidence-based policy making and means that students and the workforce do not have a centralised location to access data on skills shortages and growing areas of employment or get tailored information. Second, most existing skills intelligence tools (with the exception of skills intelligence barometers) in the Western Balkans primarily use occupations or sectors as the unit of analysis, rather than specific sets of competences or skills. Such a traditional approach is likely to become less relevant in the future as occupations evolve and require a more diverse and flexible set of skills (European Commission, 2021[52]).

Activating unused skills

Providing people with better opportunities to participate in the labour market is crucial to help economies mobilise unused skills, particularly in the Western Balkans where the regional employment rate is more than 10 percentage points lower than in the EU (Figure 3.6).

Figure 3.6. Employment rates in the WB6 economies and the EU (2022)

Percentage of the total labour force



Notes: For all WB6 economies except for Kosovo, modelled ILO estimates for unemployment (as a percentage of total labour force) were available, which allows for increased comparability across economies. To populate the graph with data for Kosovo, the latest available data (national estimate from 2022) was used.
Source: International Labour Organization (2024[53]).

Government policies for improving job readiness and helping people find suitable employment remain limited due to insufficient financial and human resources

PES seek to assist jobseekers with locating suitable employment opportunities and ensuring that they have the necessary skills to demonstrate employability and subsequently enter (or re-enter) the labour market. In the Western Balkans these entities face chronic structural challenges, such as large shares of long-term unemployment, youth unemployment, and the prevalence of vertical and horizontal skills mismatches. PES are generally responsible for the implementation of active labour market programmes (ALMPs), which seek to increase jobseekers' employability and employment opportunities.

However, the efficacy of ALMPs in the Western Balkans is limited by several obstacles, one of the most prominent being insufficient funding. The budget spent on these programmes across the Western Balkans is far below the EU average, with significant differences across the region. In 2022, the budget spent on ALMPs, measured as a percentage of GDP, ranged from 0.03% in Kosovo to 0.25% in Albania – all substantially below the EU average of 0.39%.

This lack of funding negatively impacts other aspects of PES, particularly insufficient staff numbers as due to limited budgets they cannot hire additional personnel. As such, although there is a big range – 159 registered unemployed individuals per one counsellor in Montenegro to 1 160 registered unemployed individuals per one counsellor in FBiH – all economies fall above the recommended ratio of 100 registered unemployed individuals to one counsellor, which is particularly important when dealing with groups that face greater barriers to employment. Little or no improvements have been made to increase staff capacity; however, some advances have been achieved in organising PES processes more effectively, such as through digitalisation processes, reorganising work or deploying additional counsellors to municipalities most in need. As PES advance on implementing Youth Guarantee schemes the burden on these entities will only increase, highlighting the challenges involved in fulfilling their mandate and helping people find suitable employment.

Initiatives targeting vulnerable and disadvantaged jobseekers exist across the region, but some groups remain underserved

There are several employment services and ALMPs provided by PES in the region that target vulnerable groups. These include mainly jobseekers from ethnic minorities, specific groups of women (e.g. those in rural areas), people with disability and those who are long-term unemployed. One of the most common types of initiative targets Roma men and women, such as mentoring (North Macedonia), job subsidies (FBiH) or part-time employment and training opportunities (Albania). There are also programmes for those who are long-term unemployed in several economies (FBiH, Albania and Serbia).

However, several challenges are related to the current design of ALMPs. First, vulnerable groups often have not previously been employed and the resulting lack of experience and skills, compounded by lower rates of educational attainment, means that they are in particular need of intensified support. Additionally, while the aforementioned groups tend to be the priority targets of existing ALMPs, other disadvantaged groups are less well-served, including older workers, low-skilled individuals, victims of violence and migrants. As such there is a stark divide regarding which groups receive specific attention, as well as regarding the resources dedicated to supporting such programmes.

The limited focus on older unemployed individuals is particularly problematic in the WB6, as most economies (apart from Kosovo) are grappling with an ageing population and declining birth rates. As such, the region must not simply focus its efforts on engaging its youth, but instead should prioritise engaging workers aged 50+ who will constitute an increasing proportion of the workforce. While there are dedicated ALMPs for youth across all WB6 economies, only four of the six economies have ALMPs targeting older unemployed individuals. Programmes that exclusively target this population are even rarer, as the remaining economies tend to simply bundle this population with other hard-to-employ target groups.

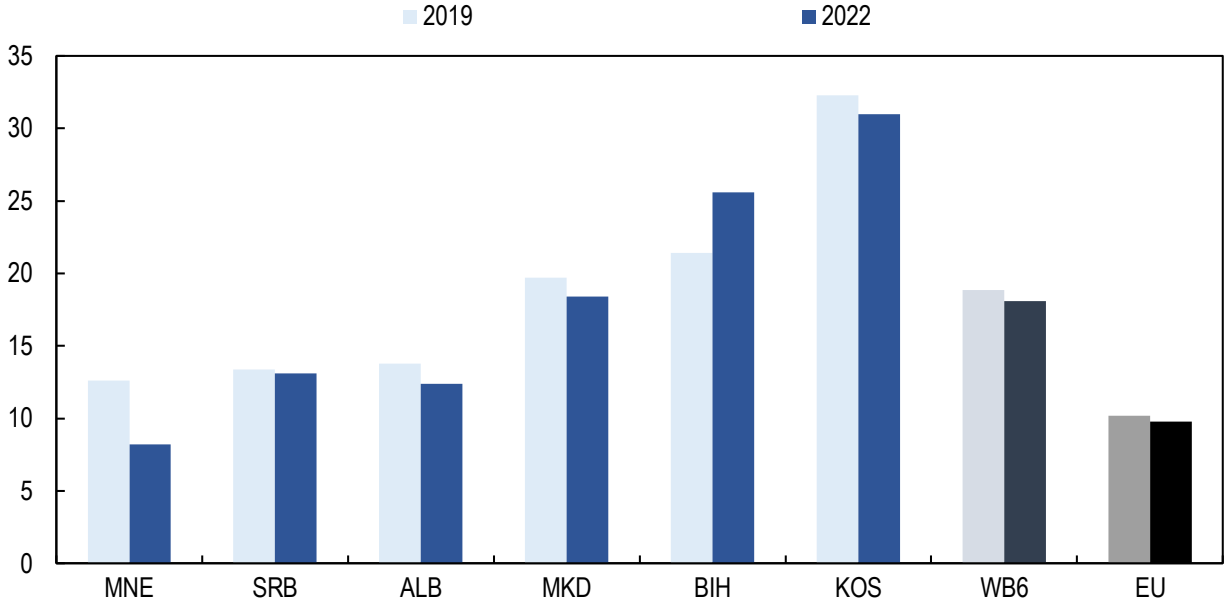
Another mechanism that benefits disadvantaged jobseekers – albeit more indirectly – is the use of profiling by PES to segment individuals by employability and consequently offer customised services. Most economies have a two- or three-tier system, with the upper tiers encompassing jobseekers with multiple barriers to employment. These individuals have access to special services such as additional training or intensive interactions with PES advisors. This profiling tool often recognises the overlapping or reinforcing challenges faced by certain groups within society and slots them into the tier that grants them access to additional support services.

Despite numerous initiatives aimed at improving the employment rates of women, low rates and a large gender employment gap persist due to multiple barriers

Gender inequalities are pronounced in the region. Women are less often employed than men, and this gap is larger in the region than the EU average (with the exception of Montenegro) (Figure 3.7). Between 2019 and 2022, Albania, Kosovo, Montenegro, North Macedonia and Serbia all reduced the employment gender gap, while it increased in Bosnia and Herzegovina. The gender employment gap was highest and the employment rates of women lowest in Bosnia and Herzegovina and Kosovo.

Figure 3.7. Gender employment gap in the WB6 economies and the EU (2019, 2022)

Percentage point difference of employment rate of men and the employment rate of women aged 15-64 years



Note: The "gender employment gap" is calculated by finding the difference between the employment rate of men and the employment rate of women aged 15-64 years.
Sources: Data provided by National Statistical Offices (ALB, BIH, KOS, MNE, MKD); Eurostat (2024[54]) (SRB, EU average).

StatLink https://stat.link/7e2xib

Gender employment gaps are noticeable in **STEM** fields across the Western Balkan economies, with women accounting for only 14% of STEM jobs in the region.[37] Part of the reason for this gap is the lower rates of enrolment by women in STEM fields in higher education in some economies. However, another important contributor is the "leaky pipeline phenomenon", which argues that women have the interest and ability to pursue STEM careers but elect not to due to systemic barriers such as gender stereotypes or significant gender pay gaps (Calhoun, Jayaram and Madorsky, 2022[55]). Nearly every WB6 economy

reports a gender pay gap between male and female employees working in STEM, particularly within the ICT sector (Drezin, 2021[56]).

One notable regional advance has been the establishment of the Regional Network of Women in STEM, led by the Regional Cooperation Council and the United Nations Development Programme as part of the Common Regional Market Action Plan 2021-24. However, at the economy level there is limited vocational guidance in place to encourage young women to take up vocational or university education in STEM study fields; instead, most initiatives are either funded by donors (Kosovo, North Macedonia, Serbia) or think tanks (Albania).

Multiple initiatives aimed at increasing women's employment rates have been instituted by every economy in the region. All are supported by key strategies and action plans (either in place or in the process of adoption) to address low labour market participation rates, although there is only a specific budget accompanying these policies in Albania, Montenegro and Serbia.

However, only some economies have policy frameworks for improving conditions for **work-life balance** – and the existing frameworks are far from comprehensive, with concrete measures and initiatives beyond paid maternity leave not well-defined in most WB6 economies. The exceptions include Albania, which offers childcare for school children through its new "Family Hub" services, as well as services for elderly support. In addition, Serbia has increased its annual vacation time for single parents and instituted flexible working hours. However, no economy has a framework or initiatives that cover all ages of children, childcare and old-age care support – despite the fact that women are more likely than men to take on childcare and elderly care roles. The lack of affordable and available childcare services in the region (particularly in rural areas) has been found to disproportionately impact the labour market engagement of women (World Bank, 2018[57]). Reconciling these obligations and ensuring a better work-life balance is vital, as women with families do not necessarily seek to work less, but instead desire adaptable arrangements such as part-time positions or those with flexible schedules to manage their responsibilities (UNDP, 2024[58]).

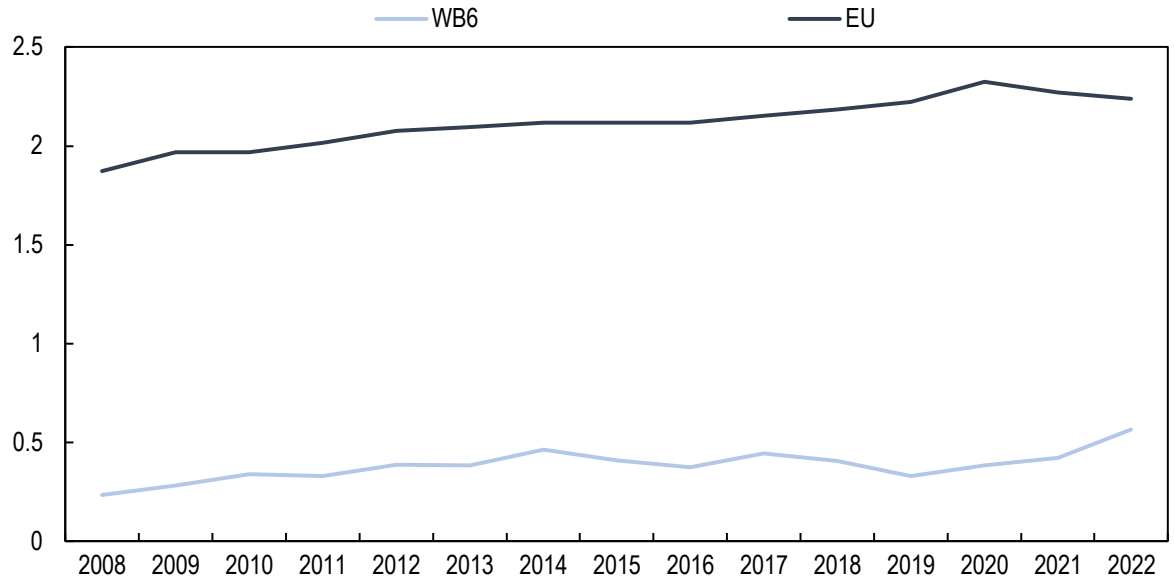
Approaches to promoting **women's entrepreneurship** significantly vary: FBiH, RS and Kosovo either entirely lack policy frameworks or have frameworks that have recently expired; Albania has a sub-measure aimed at stimulating and supporting the entrepreneurship of women, young women and girls within its National Strategy for Gender Equality 2021-30; and Montenegro and North Macedonia have specific, separate strategies that explicitly focus on promoting women's entrepreneurship. This uneven proliferation of strategies has not engendered much success, with women remaining significantly underrepresented among entrepreneurs and business owners (UNDP, 2024[58]). A likely reason for this stems from gender stereotypes that dictate entrepreneurship as being more "masculine" – a belief that can then contribute or reinforce other difficulties such as gaining sufficient and reliable access to finance. It is notable that only Montenegro, North Macedonia and Serbia have developed frameworks or programmes that seek to reduce gender stereotypes in schools starting at an early age.

Leveraging skills for innovation

Skilled people play a fundamental role in innovation through their ability to generate new knowledge and ideas. In the Western Balkan context, innovation is seen as key to strengthening regional and European integration (OECD, 2021[44]). However, while several economies have significantly increased spending on scientific research in recent years, overall investments in the sector remain negligible and show little evidence of converging towards EU levels (Figure 3.8). This lack of funding severely impacts the research and innovation capacity of the Western Balkans.

Figure 3.8. Gross expenditure on research and development (GERD) in the WB6 economies and the EU (2008-22)

Gross domestic expenditure on research and development as a share of GDP



Note: Note: This indicator measures the gross domestic expenditures on research and development measured as the share of gross domestic product.
Sources: World Bank (2024[49]) (WB6); Eurostat (2024[59]) (EU).

StatLink https://stat.link/hvynq0

The productivity and innovation capacity of scientific researchers remains low, with the sector failing to attract new talent

The number of researchers in the Western Balkans has remained largely unchanged in recent years, despite significant efforts to boost STI performance across the region. This is in stark contrast to some regional peers, although intra-regional discrepancies are evident. Proportionally, the number of researchers is the highest in Serbia (at more than 2 218 researchers per million inhabitants), falling to a low in Bosnia and Herzegovina of 447 researchers per million.[38] Even given this variation, all WB6 economies are far below the EU average of 4 450 researchers per million inhabitants (World Bank, 2024[49]). In addition, human resource capacity for research in some economies is dramatically affected by brain drain, particularly in important fields such as medical, health and ICT.

All economies provide some assistance to researchers to boost the attractiveness of the profession. Grant funding is available in most economies to support doctoral and postdoctoral research, scholarships, participation in conferences, and international tender support, although these remain largely ad hoc and small in scale. Specific programmes targeting young researchers are also in place in some economies. All economies participate in the Marie Sklodowska-Curie Actions (MSCA), the EU flagship programme that seeks to enhance researchers' training and career development through providing new knowledge and skills.[39] Between 2014 and 2023, researchers from the WB6 region participated in MSCA projects nearly 260 times,[40] although over two-thirds of these came from Serbia alone, thereby suggesting continuing capacity constraints.

All economies except Kosovo also participate in EURAXESS, a pan-European network initiative providing support services to researchers to help their mobility. Most major higher education institutions have endorsed the network's Charter and Code of Conduct for Researchers, which constitutes the principal rights and obligations for researchers and research institutions. However, few local institutions have received the EURAXESS HR Excellence in Research award, which calls into question the long-term commitment of the WB6 region to aligning their human resource policies with European best practices.

An increased focus on stimulating linkages between academia and the private sector could lead to more skills transfer and the commercialisation of research

Co-creation between R&D institutes and industry remains the weakest link across the region's STI systems, with incentives for business-academia collaboration either non-existent or applied inconsistently. The scale and scope of financial incentives range from large-scale innovation vouchers and competitive grants for joint research projects, proof of concept and technology transfer in Serbia, to the ongoing preparation of a competitive collaboration grant scheme in North Macedonia and a number of smaller scale support incentives in Montenegro and Albania. In contrast, financial support in Bosnia and Herzegovina and Kosovo is nascent or via donor-funded support to innovative SMEs, without a clear link to scientific research. Non-financial incentives specifically supporting collaboration between public scientific research and businesses are largely absent. Royalty splits between the inventor and the organisation holding the patent are not sufficiently nuanced in local intellectual property (IP) protection legislation, while the overall weak enforcement of IP continues to de-incentivise R&D activities. Tax incentives for businesses engaging in R&D are very limited.

As a result, the commercialisation of research remains limited. Except for Serbia, where monetary returns of IP have increased by nearly 300% since 2016, receipts for the foreign use of domestic IP remain negligible and largely stagnant at less than 0.1% of GDP (World Bank, 2024[49]).

The potential of smart specialisation to leverage and boost local skills for innovation is yet to be unleashed

Scientific research is a vehicle for fostering innovation and development. It is a key element of smart specialisation, which is a concept that has been at the forefront of European regional and industrial policy design in the last decade. More recently, smart specialisation has also gained momentum across the Western Balkans. All WB6 economies have embarked on the process of developing smart specialisation strategies (S3), with technical support from the European Commission's Joint Research Centre. The state of play differs significantly between economies: in Montenegro and Serbia, S3 have been in place since 2019 and 2020, respectively, and implementation is well underway; North Macedonia adopted its S3 in late 2023; and in Albania, Bosnia and Herzegovina and Kosovo the development of an S3 is still in progress. Across all existing or draft strategies, ICT and energy efficiency have been identified as priority areas, thereby addressing key aspects of the region's green and digital transitions.

Although the development of skills is recognised as an integral part of smart specialisation, incorporating human capital development, and working with education providers to upskill or reskill local workforces in support of S3 priority objectives, remains somewhat overlooked. Creating entrepreneurial and innovation skills, as well as local capacity to support the green and digital transformations, are reflected in all existing S3, with some implementation activities focused on updating curricular and study programmes. However, there is no evidence of a systematic approach to reforming vocational or higher education systems to fully align with S3 objectives.

Recommendations for putting skills to effective use

- **Continue to bolster skills intelligence systems**. While all WB6 economies have made efforts to address skills mismatches, there is a need to further enhance skills intelligence to ensure the accurate assessment and planning of current and future skills needs. When transitioning from reactive to proactive mechanisms, WB6 governments should prioritise the development and/or regular implementation of predictive skills studies and skills forecasting tools. Additionally, it is crucial for WB6 economies to centralise relevant data and analysis, thus creating a robust and accessible evidence base for policy makers and the public. The European Centre for the Development of Vocational Training (CEDEFOP) Skills Intelligence tool can serve as an illustrative example of a centralised platform (Box 3.2).

Box 3.2. CEDEFOP's Skills Intelligence platform

In 2015, CEDEFOP introduced the Skills Panorama, an interactive web platform designed to offer insights into skills needs across Europe. In 2021, the content of the Skills Panorama was integrated into the innovative Skills Intelligence tool, maintaining the original platform's commitment to providing insights across various occupations, sectors and countries. The primary goal of this transition was to facilitate evidence-based decision making for the public by aiding education and training choices, and for policy makers by supporting the revision or implementation of skills policies.

The Skills Intelligence platform employs 56 indicators and 26 skills dashboards, utilising both qualitative and quantitative data to highlight the skills most relevant and in demand by the labour market, based on current and future trends. It also offers an overview of skills anticipation approaches in EU member states, showcasing various assessments, forecasts and foresight mechanisms that can serve as inspiration or best practices.

Sources: CEDEFOP (2024[60]); European Institute of Public Administration (2024[61]).

- **Strengthen structured co-operation between VET and businesses.** These partnerships, which should span from planning to provision, are integral for updating VET curricula and increasing their labour market relevance, thereby reducing the gap between skills taught in educational systems and those demanded by employers. Moreover, ongoing, systematic co-operation between VET programme providers and businesses in the private sector could help to expand the number of WBL opportunities available to students, which would help young workers accrue practical experience and develop "real world" skills and competences. The WB6 economies could potentially establish Centres of Vocational Excellence to further formalise these public-private partnerships.
- **Continue to develop and implement Youth Guarantee schemes.** Although the WB6 economies are at different stages of finalising their Youth Guarantee schemes, all should continue towards achieving complete implementation. Specifically, while Albania and Serbia continue to the final phase and eventual roll out of their full schemes, Bosnia and Herzegovina and Montenegro should prioritise the timely adoption of their respective action plans. In parallel, WB6 governments should assess the capacities of their employment agencies to ensure that they possess the necessary resources and institutional structure to accommodate the demand of these schemes.
- **Develop targeted ALMPs to better activate older unemployed individuals**. Although most WB6 economies have employment policies or training programmes that specify older people as a target group, they receive disproportionately little attention given the changing demographic composition of the region. As such, WB6 economies should devote augmented resources towards

strengthening counselling, training and/or job matching support for this population through either existing ALMPs or through developing new programmes.

- **Further boost the capacities of PES by allocating sufficient human and financial resources**. Reducing the ratio of jobseekers to PES counsellors might be particularly beneficial in the Western Balkans given the high rates of unemployment, as lower ratios have been associated with more job offers and faster job entry (Böheim and Eppel, 2023[62]).
- **Use the new Western Balkans Research and Innovation Information Hub to enhance regional co-operation on fostering innovation**. This platform represents a valuable opportunity for the WB6 economies to individually strengthen their own innovation capacities, and for regional co-operation and information sharing in the R&D sphere to be improved (Box 3.3).

Box 3.3. The Western Balkans Research and Innovation Information Hub

Launched in 2022, the Western Balkans Research and Innovation Information Hub is a platform that seeks to stimulate and sustain regional co-operation in the fields of research and innovation. The overarching objective of the hub is to facilitate the enhanced integration of the WB6 economies into the European Research Area. The creation and implementation of the Information Hub is overseen by the EU's Horizon Europe funding programme.

The project makes available an array of tools and mechanisms to the WB6 economies. Through identifying common priorities, organising policy dialogue, establishing regional information hubs, and designing and carrying out regional pilot activities the region can boost the attractiveness of its research sector and thus attract (and retain) new talent.

One of the central objectives of the Information Hub is to strengthen linkages between governments, academia and the private sector in the WB6 economies through the application of the "triple helix model of innovation". Additionally, significant emphasis is placed on forging strong relationships between the region and participating EU member states (Austria, Croatia, Germany and Italy) and organisations such as the Regional Cooperation Council and the European Commission. As such, the exchange of ideas, good practices and lessons learned could potentially lead to substantial improvements in the region's innovation policy frameworks and outcomes.

Source: Western Balkans Information Hub (2024[63]).

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Notes

[1] Unless otherwise indicated, any reference to the EU refers to the 27 member states.

[2] This lack of participation hinders the economy's ability to gauge its own progress towards improving educational outcomes, and limits the availability of comprehensive regional comparisons with the other WB6 economies.

[3] The drop in the results of the students in Albania observed in PISA 2022 appears to be related to different factors. At the end of 2019, a strong earthquake hit Albania, causing significant damage to infrastructure, including schools and houses, across 12 main cities. About half of the students participating in PISA 2022 (50.5%) are originally from the cities most hit by the earthquake. Until April 2022, when PISA was conducted, these students were studying outside of their regular schools, with shifts and reduced teaching hours in place. The COVID-19 pandemic added to the challenges faced by the education system in Albania in 2020 and 2021, with the state of digital infrastructure posing great difficulties to the effective use of online and distance learning. The disruptions caused by the earthquake and by COVID-19 on the psycho-social life of students may have had a negative impact on the engagement of students in PISA 2022.

[4] It is worth noting that not all WB6 economies started their participation in PISA at the same time. Albania and North Macedonia were the first from the region to participate in 2000; Serbia joined in 2003 followed by Montenegro in 2006, Kosovo in 2015 and Bosnia and Herzegovina in 2018.

[5] To help understand differences in student knowledge and skills, PISA categorises student performance into different proficiency levels. They range from highest (Level 6) to lowest (Level 1). Level 2 is considered the baseline level of proficiency students need to participate fully in society.

[6] This EU average excludes both Luxembourg and Cyprus.

[7] Data on WB6 economies' expenditure on education is relatively limited. As such, this calculation was made using the latest figures available across several sources. Data for both Albania (3.1% of GDP) and Serbia (3.3%) came from the UNESCO Institute for Statistics. Data for Bosnia and Herzegovina (4.4%) and North Macedonia (3.7%) came from previous OECD reports (Guthrie et al., 2022[67]; OECD, 2019[66]). Data for Montenegro (4.1%) came from Eurydice (Eurydice, 2024[64]). Data for Kosovo (4.7%) came from a report by the Kosovo Education Centre (Kosovo Education Centre, 2021[65]).

[8] To calculate the regional average, data for Albania, Bosnia and Herzegovina, North Macedonia, Serbia, and the EU came from the World Bank (https://data.worldbank.org/indicator/SE.PRM.ENRL.TC.ZS?locations=AL-BA-XK-ME-MK-RS-EU). Data for Kosovo (https://masht.rks-gov.net/wp-content/uploads/2022/09/education-statistics-2018-2019.pdf) and Montenegro (https://www.monstat.org/userfiles/file/Obrazovanje/2016%2017/osnovne/primary%20school%20beginning%202016-2017%20-.pdf) came from their respective statistical offices.

[9] There is no information available for Montenegro or North Macedonia.

[10] See: https://documents1.worldbank.org/curated/en/719981571233699712/pdf/Bosnia-and-Herzegovina-Review-of-Efficiency-of-Services-in-Pre-University-Education-Phase-I-Stocktaking.pdf.

[11] For more on the distribution of teachers' salaries throughout Europe, including the Western Balkan economies, please see: https://op.europa.eu/en/publication-detail/-/publication/4b900c13-6977-11ee-9220-01aa75ed71a1/language-en.

[12] These two cantons are Sarajevo and Tuzla.

[13] This level of education generally corresponds to 14-15-year-olds.

[14] These two levels correspond with ISECD 01 and ISCED 02. For more on these levels see: https://uis.unesco.org/sites/default/files/documents/international-standard-classification-of-education-isced-2011-en.pdf.

[15] This requirement is outlined in the state-level Framework Law on Preschool Upbringing and Education in Bosnia and Herzegovina. To access this law, please see: https://planipolis.iiep.unesco.org/sites/default/files/ressources/bosnia-and-herzegovina-framework-law-preschool-upbringing.pdf.

[16] This corresponds with ISCED 02, which targets children aged 3 years until the start of ISCED 1.

[17] The exception is North Macedonia, which makes all secondary education compulsory.

[18] Data for Albania, Bosnia and Herzegovina, Montenegro and Serbia came from the UNESCO Institute for Statistics (UIS) database. Data on North Macedonia can be accessed here: https://makstat.stat.gov.mk/PXWeb/pxweb/en/MakStat/MakStat__ObrazovanieNauka__SrednoObrazovanie__PocetokUcebna/250_sreducil_rsm_poc_t4_ml.px/table/tableViewLayout2/?rxid=46ee0f64-2992-4b45-a2d9-cb4e5f7ec5ef. The regional average excludes Kosovo as no data are available on net enrolment rates in upper secondary education.

[19] Serbia has a Strategy for Digital Skills Development 2020-24, although digital competences are also addressed in its Law on Foundations of the Education System.

[20] The ratios for Serbia and Montenegro come from PISA 2022. The ratio for Bosnia and Herzegovina was given in the government's Economic Reform Programme 2024-26. The ratio for Kosovo was provided in the Competitiveness Outlook 2024 qualitative questionnaire.

[21] The National Agency for Vocational Education Training and Qualifications and the National Agency for Employment and Skills.

[22] This information comes from the European Commission's 2023 reports on each WB6 economy.

[23] To learn more about the CRM 2021-24 Action Plan please see: https://www.rcc.int/pages/143/common-regional-market.

[24] A notable exception is the visa regime that exists between Kosovo and Bosnia and Herzegovina.

[25] Specific reasons for this significant influx include the free-visa policy between the Russian Federation and Serbia, Serbia's abstention in aligning with Western sanctions imposed on Russia, direct air travel connection between Belgrade and Moscow, and cultural and linguistic links between Russians and Serbians.

[26] For information on North Macedonia's increase to its quota, see: https://china-cee.eu/2023/03/29/north-macedonia-social-briefing-the-government-proposes-to-import-foreign-workers-to-address-labor-

shortages. For information on Bosnia and Herzegovina's increase to its quota, see: https://www.slobodenpecat.mk/en/zgolemena-godishna-kvota-na-rabotni-dozvoli-vo-bosna-i-hercegovina/#:~:text=With%20the%20decision%20to%20determine,of%20foreigners%20amounts%20to%206.073. For information on Montenegro's proposed increase, see: https://en.vijesti.me/news/society/699122/Nisic-Ministry-has-prepared-a-proposal-for-determining-the-annual-quota-of-permits-for-temporary-residence.

[27] Government officials from North Macedonia have indicated that the economy needs at least 10 000 foreign workers annually (see: https://ecfr.eu/article/depopulation-blues-how-immigration-can-counter-emigration-in-the-balkans). In FBiH, 4 295 foreign employment permits were set in the 2024 quota, although the FBiH Employer Association asked for the quota to be raised to 10 000 (see: https://sarajevotimes.com/the-need-for-foreign-workers-is-increasing-in-bih).

[28] For more on these plans, see: https://www.slobodenpecat.mk/en/bosna-i-hercegovina-ja-zgolemuva-kvotata-za-stranski-rabotnici-na-6-000.

[29] This lack of attractiveness is further detailed in the Torino Process System Monitoring Reports (2023) for the WB6 economies, see: https://www.etf.europa.eu/en/what-we-do/torino-process-policy-analysis-and-progress-monitoring.

[30] Social partners generally encompass entities representing employers, workers and governments when meeting for the purpose of consultations and negotiations on labour, social and economic practices, policies and legislation. For more on social partners, please see: https://home-affairs.ec.europa.eu/networks/european-migration-network-emn/emn-asylum-and-migration-glossary/glossary/social-partners_en.

[31] The one exception is in FBiH, where there are information days organised in the Zenica-Doboj Canton for businesses to inform them about their rights and obligations for hiring students from vocational or technical schools.

[32] For more on Centres of Vocational Excellence (CoVEs), please see: https://ec.europa.eu/social/main.jsp?catId=1501.

[33] This conclusion has been repeated in the Serbian context (https://www.etf.europa.eu/sites/default/files/2019-07/Skills%20mismatch%20measurement_Serbia_0.pdf), the Albanian context (https://www.undp.org/sites/g/files/zskgke326/files/2022-05/Review%20of%20the%20Regulatory%20Framework%20and%20Provision%20of%20Post-Secondary%20and%20Higher%20VET%20in%20Albania.pdf) and the Montenegrin context (https://www.etf.europa.eu/sites/default/files/2019-07/Skills%20mismatch%20measurement_Montenegro.pdf).

[34] These findings were from the Skills Measurement Programme (STEP) survey.

[35] The declaration can be found here: https://www.esap.online/docs/141/western-balkans-declaration-on-ensuring-sustainable-labour-market-integration-of-young-people.

[36] These data come from the 2023 iterations of the Balkan Business Barometer and Balkan Public Barometer.

[37] For more on the gender employment gap in STEM fields in the Western Balkans, please see: https://www.balkaninnovation.com/news/15/network-of-women-in-stem-in-the-western-balkans-launched.

[38] Data were provided in Competitiveness Outlook 2024 quantitative questionnaires.

[39] For more on MSCA, please see: https://research-and-innovation.ec.europa.eu/funding/funding-opportunities/funding-programmes-and-open-calls/horizon-europe/marie-sklodowska-curie-actions_en.

[40] For data on the current HorizonData programme, see: https://dashboard.tech.ec.europa.eu/qs_digit_dashboard_mt/public/sense/app/1213b8cd-3ebe-4730-b0f5-fa4e326df2e2/sheet/d23bba31-e385-4cc0-975e-a67059972142/state/analysis. For data on the old Horizon2020 programme, see: https://dashboard.tech.ec.europa.eu/qs_digit_dashboard_mt/public/sense/app/1213b8cd-3ebe-4730-b0f5-fa4e326df2e2/sheet/0c8af38b-b73c-4da2-ba41-73ea34ab7ac4/state/analysis.

4 Business environment cluster

This chapter focuses on evaluating the progress made by the six Western Balkan (WB6) economies in fostering a competitive environment for business operations and expansion. It involves a thorough examination of key policy areas essential for developing domestic enterprises, creating a level playing field, attracting investment and promoting regional integration through trade. It also assesses the main challenges within the regional business environment and the efficacy of government measures in addressing them. The first section presents the regulatory facilities and obstacles encountered by businesses operating in the WB6 economies, focusing on access to finance and taxation. The chapter then delves into how the WB6 economies can foster levelling the playing field for businesses, looking at the prevailing anti-corruption landscape and labour market informality. The chapter also considers how the treatment of state-owned enterprises (SOEs) may potentially impede a level playing field in the region. Finally, policies supporting business expansion are explored, highlighting to what extent WB6 governments implement regional policies that help businesses improve their competitiveness, reach new markets and deepen regional co-operation.

Key findings

The Western Balkan (WB6) economies have made some progress on policies to foster an enabling business environment in recent years, and are increasingly (albeit slowly) converging towards EU levels. Some **key achievements** are:

- On the back of improved legal and regulatory frameworks, the six Western Balkan economies have bolstered banks' liquidity and solvency. This has resulted in substantial liquidity buffers, offering the potential for further expansion of financing activities to support investment and growth.
- Tax administrations across the region have significantly eased the administrative burden on businesses by enhancing key services and streamlining procedures. The expansion of tax services has increased information accessibility, while the growing use of electronic filing and payment has streamlined compliance, making it easier and more efficient.
- Supported by the continued reduction or removal of statutory restrictions on foreign direct investment, as well as continued overall improvements in the business environment, the WB6 economies have attracted substantial inflows of foreign direct investment, receiving on average 3.5 times more than the European Union (EU) over the last five years.
- The region has taken substantial steps towards regional economic integration, showcasing its commitment to align with the EU. This includes harmonising trade policies, reducing trade barriers and enhancing intra-regional customs infrastructure.

Despite these positive regional trends, there is still scope to strengthen policies and improve outcomes related to access to finance, business taxation, level playing field, trade and foreign investment. As such, some of the **key challenges** facing the region are as follows:

- Facing liquidity challenges, capital markets remain marginal in the financial landscape of the WB6 economies. At the same time, alternative finance avenues such as private equity or crowdfunding have not been developed, resulting in businesses disproportionately relying on banks for funding investments.
- High, flat social security contribution (SSC) rates increase the cost of low-skilled labour, contributing to the region's high levels of informality. However, few economies have enacted reforms to reduce the burden of SSCs, despite the looming additional strain posed on tax revenues by demographic shifts such as an ageing population and high levels of emigration.
- Persistent corruption undermines the competitiveness of the WB6 economies, as evidenced by businesses perceiving corruption as a significant obstacle to their operations and growth. The lack of sustained, long-term strategic frameworks for combating corruption makes it difficult to address high corruption levels.
- Region-wide, state-owned enterprises lack centralised ownership institutions and clearly defined ownership policies, hindering fair competition. The level playing field is further distorted as SOEs across the region are frequently loss-making, yet benefit from continued state support.
- Further progress in contract enforcement and dispute resolution is needed. An average civil or commercial court case takes 572 days to resolve, more than double the EU average of 234 days, while alternative dispute resolution mechanisms remain underutilised.

Introduction

A favourable business environment with transparent regulations, efficient administrative procedures and effective contract enforcement is essential for attracting investment, fostering entrepreneurship and driving economic growth. By implementing reforms to streamline processes and reduce red tape, promote transparency, and strengthen the rule of law, the Western Balkans can unlock its full potential, attract more investment and position itself as an attractive destination for businesses seeking growth opportunities in South East Europe.

The analysis that follows does not aim to encompass all aspects relevant to a well-functioning business environment, but instead focuses on a subset of issues covered under the *Western Balkans Competitiveness Outlook 2024*, namely access to finance, tax, anti-corruption, state-owned enterprises, employment, trade and investment.

Strengthening financial regulation and taxation policies

Easing access to finance

Access to finance is crucial for businesses as it enables them to invest in growth opportunities such as expanding operations and developing new products or services. In the Western Balkans, banks dominate the financial landscape, holding approximately 90% of total financial assets in most WB6 economies as of 2022,[1] compared to 50% held by banks in the euro area. The relative absence of alternative financial institutions in the Western Balkans underscores the importance of ensuring easy access to banking finance, with the credit gap for the region's businesses estimated at EUR 2.5 billion in 2019 (Akbas, Beltz and Gattini, 2023[1]). This gap hampers corporate investment, which reached 18.5% of GDP in 2021. With the notable exception of Kosovo (26.0%), this figure falls below the EU average of 19.2% in the WB6 economies, posing challenges to the region's economic convergence with the EU (Table 4.1)

Table 4.1. Private domestic gross fixed capital formation in the WB6 economies and the EU (2021)

In percentage of GDP

	ALB	BIH	KOS	MKD	MNE	SRB	WB6	EU
Private domestic gross fixed capital formation	19.0	15.9	26.0	17.8	16.4	15.8	18.5	19.2

Sources: World Bank (2023[2]); Eurostat (2024[3]); Competitiveness Outlook 2024 questionnaires for Albanian data.

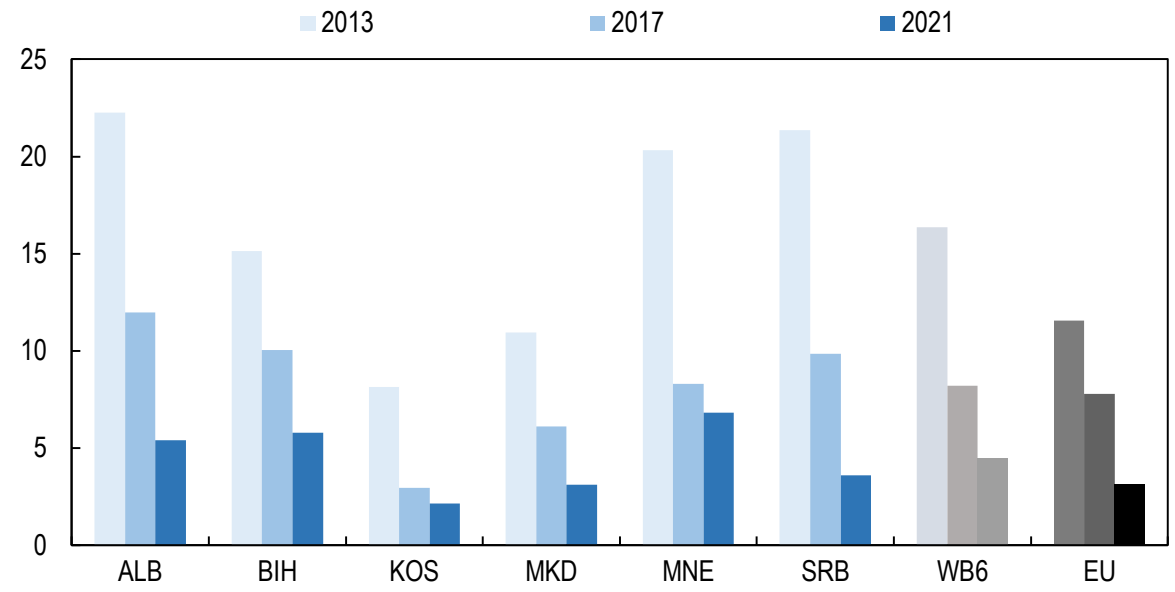
Bank financing for enterprises remains limited in the Western Balkans despite liquidity buffers

The WB6 economies' banking sector is well-capitalised and liquid, and non-performing loans have fallen to low levels. The share of non-performing loans decreased from 16.4% of total gross loans in 2013 to 4.5% in 2021, substantially converging towards the EU average (3.1%) (Figure 4.1). The financial stability of the banking sector indicates the presence of liquidity buffers and the potential to expand financing activities further.

Despite the potential to further expand financing activities, banks in the WB6 economies are much less inclined to provide credit than their European counterparts. The outstanding loans delivered by commercial banks stood at 45.4% of GDP in 2022, substantially below the EU average of 63.4% (Figure 4.2).

Figure 4.1. Non-performing loans in the WB6 economies and the EU (2013, 2017, 2021)

Percentage share of non-performing loans in total gross loans



Sources: IMF (2024[4]); National Bank of Serbia (2023[5]).

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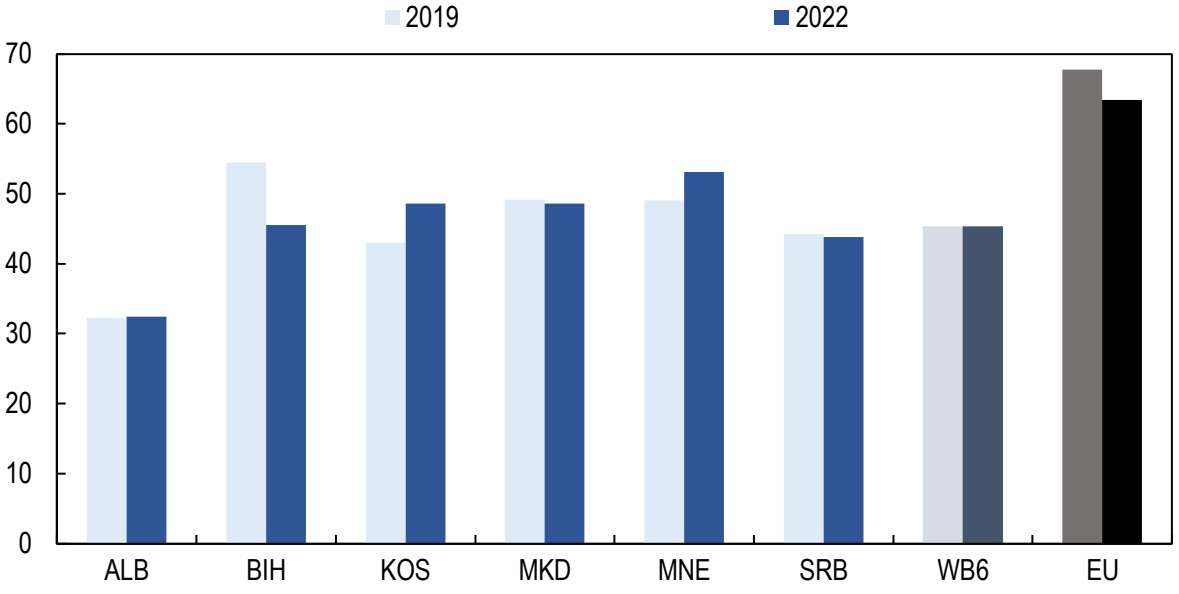
Figure 4.2. Outstanding loans from commercial banks in the WB6 economies and the EU (2019, 2022)

Value of outstanding loans from commercial banks in percentage of GDP



Source: IMF (2023[6]).

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However, the gap between the EU and the WB6 economies narrowed by 4 percentage points between 2019 and 2022, indicating that the WB6 economies suffered less from the post-pandemic monetary tightening that led to substantial rises in nominal interest rates in both the EU and the Western Balkan region. Notably, outstanding loans delivered by commercial banks recovered their pre-pandemic level in 2022 (45.4% of GDP), while remaining 3.5 percentage points below (67.8%) in the EU.

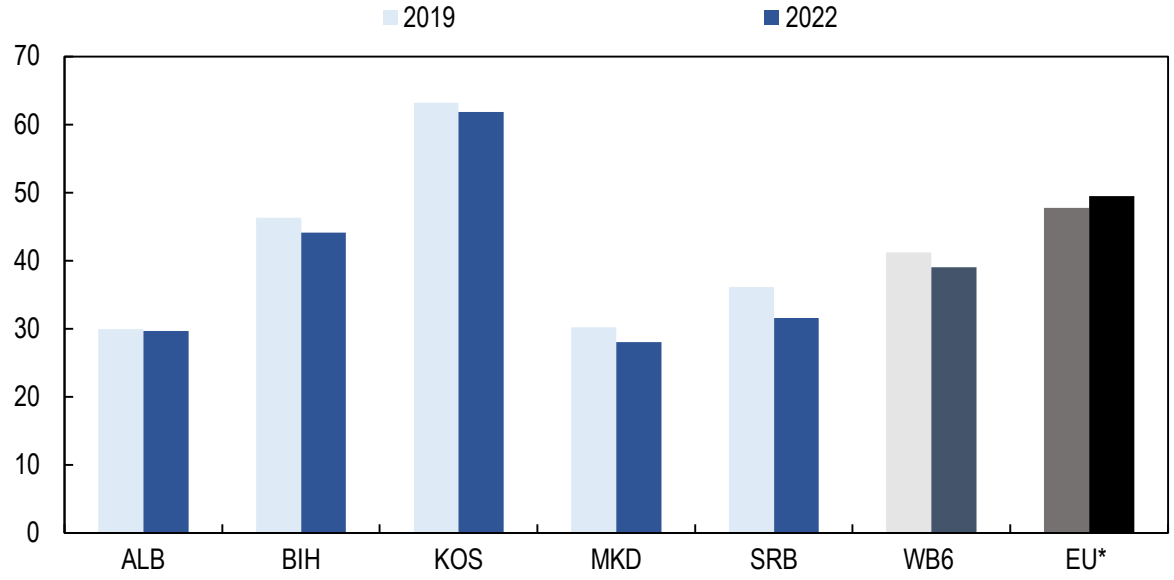
Across the region, legal frameworks could be further enhanced to facilitate access to bank finance, especially regarding collateral requirements and asset registration. Stringent collateral requirements impact businesses, especially small and medium-sized enterprises (SMEs), because they limit the availability of assets to pledge (Becchetti, Castelli and Hasan, 2010[7]). Albania, Montenegro and Serbia have implemented regulations that ease provisioning requirements for SME lending through decreased risk-weight coefficients to incentivise commercial banks to develop corporate credit for SMEs, which could offset the negative impact of high collateral requirements on access to finance in the WB6 economies (European Central Bank, 2017[8]).[2] In addition, the incomplete coverage of assets in registration systems limits the range of assets banks can use as collateral. While cadastre information systems typically cover all territories and are regularly updated, registries of security pledges are incomplete in the WB6. Except for Albania and Serbia, local banks have limited access to comprehensive information on all assets and their attributes, with documentation often incomplete. This constraint makes it challenging to assess assets for collateral purposes, particularly non-fixed assets.

Difficulty accessing bank credit is especially pronounced for SMEs across the WB6 economies. The region's SMEs accounted for only 39.0% of outstanding loans from commercial banks in 2022 – a decrease from 41.6% in 2019. By contrast, for EU SMEs, the share of corporate credit has grown from 47.7% in 2019 to 49.5% in 2022, indicating a divergence from the Western Balkan region. Kosovo is the only Western Balkan economy surpassing the EU average, with more than 60% of corporate bank credit directed towards SMEs (Figure 4.3).

In advanced economies, COVID-19 policy support and associated eased financing conditions have increased the number of zombie firms (Albuquerque and Iyer, 2023[9]). In economies where the development of corporate credit is less advanced, such as the WB6 economies, the negative risks of such support programmes are more limited, making credit guarantee schemes and public credit lines valuable instruments to promote access to bank finance. Following the continuous implementation of large-scale liquidity measures, subsidised credit lines and scaled-up state-backed credit guarantee schemes, Kosovo and Montenegro have experienced substantial corporate credit growth in the aftermath of the COVID-19 pandemic (Table 4.2). In 2022, the total financial support to enhance SME access to finance stood at 3.7% of GDP in Kosovo and 3.1% in Montenegro, compared to lower than 1% in Serbia and North Macedonia. Albania stopped implementing such financial support after the COVID-19 pandemic, despite the substantially low level of corporate credit in the economy (Figure 4.2). Moreover, with a robust legal framework, Kosovo stands out as having the most developed microfinance sector in the Western Balkans. In 2022, outstanding loans accounted for 3.2% of GDP (IMF, 2023[6]), surpassing the Western Balkan average of 1.8% and indicating microcredit's role in facilitating SME access to bank finance.

Figure 4.3. SME loans in total outstanding loans from commercial banks in the WB6 economies and the EU (2019, 2022)

Percentage share of SME loans in total outstanding loans from commercial banks



Notes: No data available for Montenegro. EU* denotes Czechia, Estonia, France, Hungary, Ireland, Italy, Latvia, Lithuania, the Netherlands, Poland, Portugal, the Slovak Republic, Slovenia and Spain.
Sources: IMF (2023[6]); OECD (2022[10]; 2024[11]).

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Table 4.2. Credit lines and credit guarantee schemes exceeding EUR 20 million annually in the WB6 economies, active in 2020 and/or 2022

Economy	Type of scheme	Name of scheme	2020 (million EUR)	2022 (million EUR)
Albania	Credit guarantee	First Guarantee Scheme (2020)	91.6 (0.6% GDP)	0
Kosovo	Credit guarantee	Kosovo Credit Guarantee Fund (KCGF)	56.0 (0.83% GDP)	116.7 (1.31% GDP)
	Credit lines		115.0 (1.70% GDP)	211.4 (2.37% GDP)
Montenegro	Credit guarantee	Investment and Development Fund of Montenegro (IDF)	284.7 (6.8% GDP)	185.0 (3.1% GDP)
	Credit lines			
North Macedonia	Credit guarantee	Development Bank of North Macedonia (DBNM)	91.0 (0.83% GDP)	102.0 (0.79% GDP)
	Credit lines			
Serbia	Credit guarantee	EU COSME "Loans for working capital and refinancing of working capital and investment loans" programme (2020-2022)	500.0 (1.07% GDP)	350* (0.58% GDP)

Notes: The overlap of entity and state-level programmes in Bosnia and Herzegovina complicates the identification of credit guarantees and credit lines for each institutional level. * denotes an estimated amount by the OECD.
Source: Information provided by national authorities for the Competitiveness Outlook 2024 assessment.

Businesses rely heavily on bank finance to fund investment

Other financing sources, especially capital markets, serve as avenues for funding riskier projects that typically do not qualify for traditional bank loans (Fiorella Carvajal and Bebczuk, 2019[12]).[3] While the size of the WB6 economies poses a challenge to the development of capital markets, the operational stock markets of the region, i.e. Bosnia and Herzegovina, Montenegro, North Macedonia and Serbia, still exhibit considerably low levels of liquidity when compared to similar economies in the EU (Figure 4.4). Low liquidity poses challenges for businesses raising funds through the stock market as it indicates a scarcity of investors willing to buy shares, making it harder and more expensive for companies to secure capital. The most liquid stock market of the WB6, the Belgrade Stock Exchange (BELEX), experienced a turnover ratio of 2.8% in 2022 (compared to 4.0% in 2013), a figure more than ten times lower than the average value of comparable EU economies, i.e. Bulgaria, Croatia, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovenia and the Slovak Republic, which stood at 31.5% (World Bank, 2022[13]).

In addition to a stable macroeconomic environment and a robust rule of law, regulations promoting financial openness can foster the development of capital markets (World Bank, 2019[14]). In the EU context, the adjustment of the domestic regulatory framework to the EU *acquis* reduces the barriers faced by investors from the EU, alleviating the constraints related to the small economic size of the WB6 economies for the development of their domestic capital market (IMF, 2018[15]).

The EU *acquis* covers crucial aspects relevant to the development of capital markets, from the management rules of institutional investors to the legal protection of investors. The Western Balkans region still has significant ground to cover in aligning domestic financial regulations. Apart from North Macedonia, no WB6 economy has implemented the EU's Undertakings for Collective Investment in Transferable Securities (UCITS) directive, which harmonises rules on the management of investment funds.[4] Moreover, apart from the partial alignment of Serbia, no WB6 jurisdiction has harmonised investor protection and transparency requirements with the EU by implementing the EU *acquis* stemming from the Markets in Financial Instruments Directive (MiFID) II and the Markets in Financial Instruments Regulation (MIFIR).[5] The absence of entities providing credit scores in all WB6 economies impedes investors from carrying out a standardised credit risk assessment on bond issuers. This makes it difficult for investors to assess risk in Western Balkan corporate bond markets.

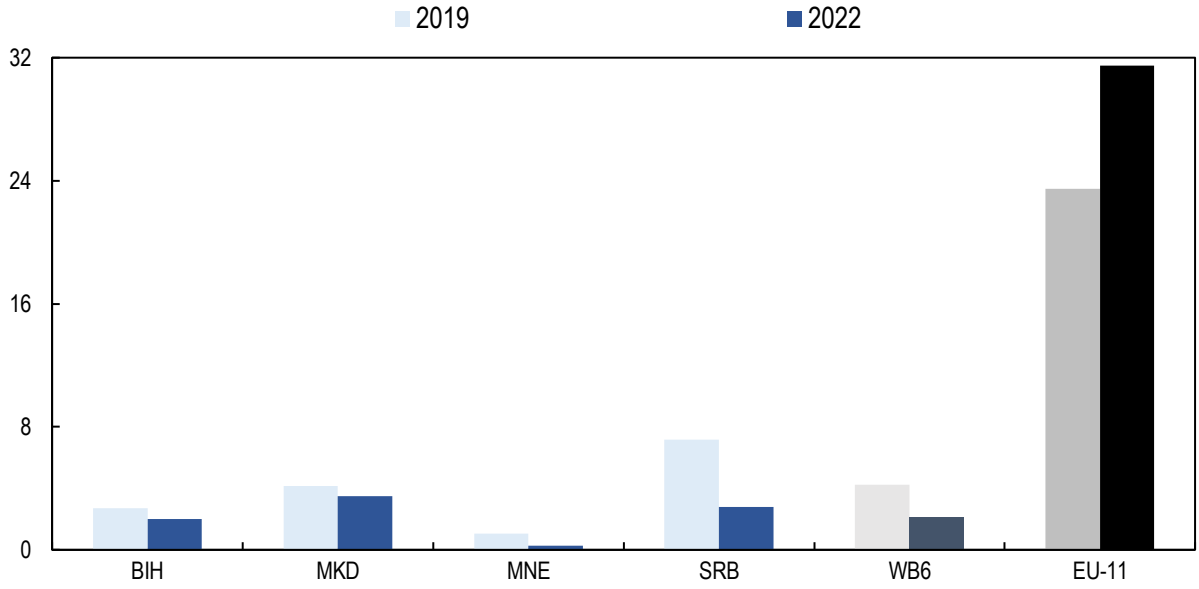
Few businesses in the Western Balkans are willing and able to list their shares in public markets because of the high costs of registration, underwriting and trading, which further limits the development of capital markets (World Bank, 2019[14]). Facilitating access for SMEs, which might currently find regulatory requirements too costly, could leverage the development of capital markets in the Western Balkans, including the emergence of new actors such as insurance companies and pension and investment funds. Among the economies with active stock and bond markets, only North Macedonia and Serbia have introduced less stringent regulatory criteria for SMEs seeking to issue stocks and bonds.

For small economies with limited capacity for full-fledged capital and debt markets, such as the WB6 economies, alternative financing sources such as business angel networks (BANs) and private equity could ease access to finance for businesses, as SMEs continue to face greater challenges than larger corporations in accessing finance. However, Western Balkan businesses operate with barely any active equity funds, restricting their options to fund early-stage investments. The lack of operating alternative investment funds (AIF) is partly due to the absence of dedicated legal frameworks that allow the establishment of private equity activities. The exception is Serbia, which has also standardised regulations regarding the operations of AIFs with the EU *acquis* by implementing the Alternative Investment Fund Managers Directive.[6] The development of BANs faces challenges due to the lack of specific legal frameworks and financial incentives. They are non-existent in Albania and Bosnia and Herzegovina, and their impact is limited in other WB6 economies. In 2022, BANs collectively generated EUR 1.8 million in

investments, a figure similar to 2020 (EUR 2.0 million) but notably lower than 2016-18, when annual investments ranged between EUR 3 million and EUR 4 million (EBAN, 2019[16]; 2021[17]; 2023[18]).

Figure 4.4. Turnover ratio in the WB6 economies and EU-11 economies (2013, 2022)

Percentage of market capitalisation value



Notes: No stock market operates in Albania and Kosovo. EU-11 economies denote Bulgaria, Croatia, Czechia, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovak Republic and Slovenia.
Source: World Bank (2022[13]).

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Advancing digital technologies such as crowdfunding could open new avenues of finance for businesses, particularly by facilitating and reducing the transaction costs of their significant remittance flows (World Bank, 2013[19]), estimated at 10.1% of GDP in 2021 (World Bank, 2022[13]). However, the current situation indicates limited potential for crowdfunding growth in the region as recorded activity is minimal, and no economy has established a dedicated legal framework.

Factoring and leasing remain underutilised across the region

The financing and further growth of business operations in the Western Balkans are compromised by the relative underdevelopment of non-bank financial intermediaries, such as factoring and leasing companies.

Factoring allows businesses to obtain immediate cash by selling their unpaid invoices, also known as accounts receivable, to a third-party company at a discount, thereby providing a solution for businesses facing liquidity constraints. Factoring is especially useful for businesses considered risky or hard to evaluate, as financing is based on the risk of the accounts receivable themselves rather than the risk of the seller (Klapper, 2006[20]). Except for Kosovo and, to a lesser extent, the Federation of Bosnia and Herzegovina (FBiH), the WB6 have established robust legal frameworks for factoring, the most advanced economy in this regard being Montenegro.[7] However, the growth of factoring across the region has been limited due to ongoing challenges in financial education and the lack of initiatives encouraging businesses to use factoring. Except for the FBiH, where interest costs on factoring are deductible and value-added tax (VAT) is only applied to service fees, no Western Balkan economy has implemented active policies

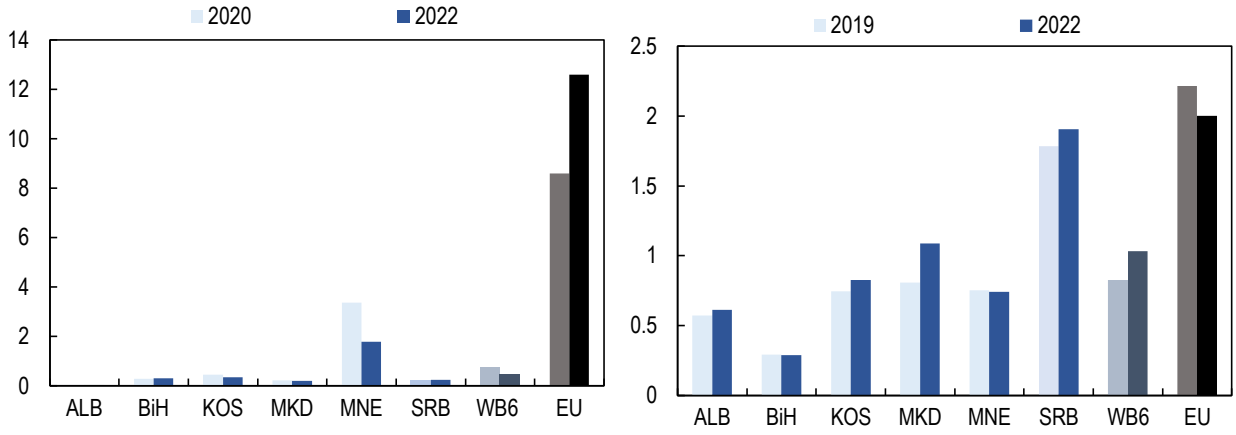
encouraging the development of the factoring market. In 2022, the value of factoring and invoice discounting reached an average of only 0.48% of GDP in the WB6, which is below the 2020 level of 0.76% and very marginal compared to the EU average of 12.6% (Figure 4.5). Montenegro is the top performer in the Western Balkans, with factoring activities accounting for 1.78% of GDP in 2022. This growth stems from significant developments following the 2013-17 reforms of factoring contracts, with activities increasing to 1.50% in 2017 (0.84% in 2013).

Leasing is a way for businesses to use an asset without owning it by making regular payments to the asset owner for the right to use it for a specified period. Leasing enables borrowers with limited track records or collateral to access the use of capital equipment, often even in cases where they would not qualify for traditional commercial bank lending (Berger and Udell, 2005[21]). Most WB6 economies have established a robust legal framework for leasing activities, except for the entities of Bosnia and Herzegovina and Kosovo, where the regulatory landscape lacks provisions for leasing mediators and leaseback conditions. No WB6 economy has implemented active policies encouraging market development, such as excluding interest from the VAT calculation base to reduce the cost of leasing contracts.[8] In 2022, the average value of leasing and hire purchases amounted to 1.04% of GDP in the Western Balkans, slightly higher than in 2019 (0.83%), but still less developed than the EU average of 2% (Figure 4.5). Figures are relatively consistent across the WB6, except for Bosnia and Herzegovina, which lacks a comprehensive legal framework and lags behind with leasing and hire purchases, which accounted for 0.29% of GDP in 2022.

Overall, despite relatively advanced legal frameworks, factoring and leasing in the WB6 economies are hindered by the fact that entrepreneurs are often not aware of the existence and functioning of these options (OECD, 2022[22]), highlighting the need for additional training opportunities for entrepreneurs and awareness-raising campaigns.[9]

Figure 4.5. Value of factoring and invoice discounting (left) and leasing and hire purchases (right) in the WB6 economies and the EU (2020, 2022)

Value in percentage of GDP



Sources: World Bank (2022[13]); EUF (2023[23]); FCI (2023[24]).

Business taxation

Governments must raise more tax revenue to finance public policies and prepare for future challenges. However, they must do this without compromising growth and investment or continuously increasing the public debt. Economies can navigate this challenge by capitalising on international tax developments and designing a tax system that supports a competitive labour market while at the same time addressing key

structural challenges. This approach can help economies raise more tax revenue and drive inclusive and sustainable growth and well-being.

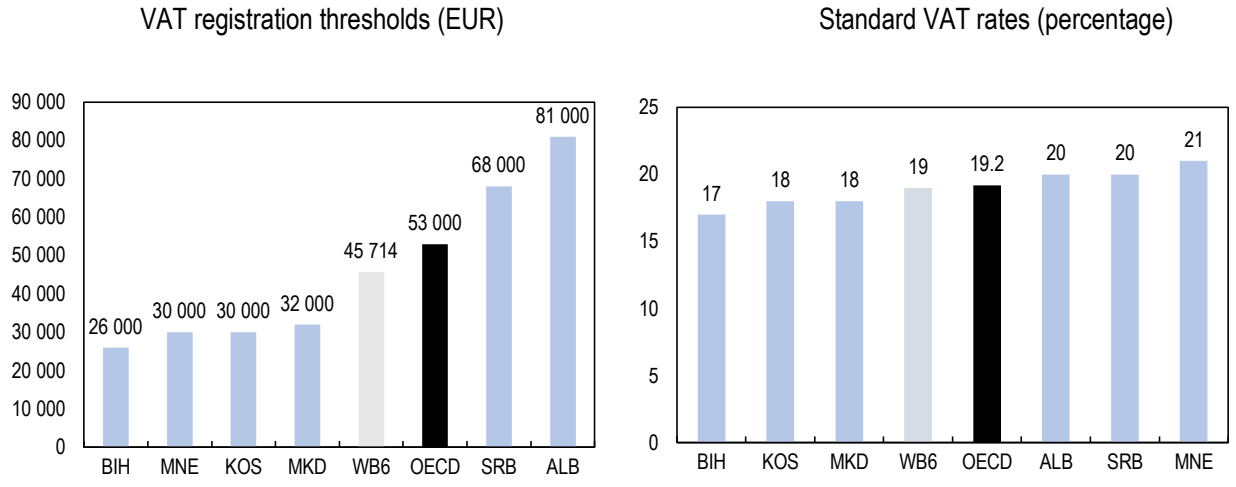
Clear and transparent tax policies are pivotal for cultivating a favourable business environment. Generally, the WB6 economies boast low corporate income tax rates and generous investment incentives. Nevertheless, complex tax systems, misaligned incentives and the absence of presumptive tax regimes can escalate businesses' requirements and burdens, particularly those characterised as very small or vulnerable.

Businesses enjoy relatively low corporate income tax (CIT) and VAT rates

In the WB6, the average statutory CIT rate is relatively low: Bosnia and Herzegovina, Kosovo and North Macedonia levy a 10% statutory CIT rate, while the top CIT rate in Albania, Montenegro and Serbia is 15% (compared to the OECD average of 21.5%). All WB6 economies currently also operate worldwide tax systems that tax resident companies on income earned domestically and abroad. In the context of the low CIT rates, these systems will likely not yield substantial additional revenue and may impose unnecessary administrative burdens.

In terms of standard VAT rates and registration thresholds, WB6 economies are overall well within the range of OECD countries (Figure 4.6). The exceptions are Albania and Serbia, which boast a relatively large VAT registration threshold. Setting the threshold requires the careful balancing of policy priorities. On the one hand, higher thresholds lower compliance costs for small businesses and decrease the burden on the tax administration. Conversely, high registration thresholds narrow the VAT base, which can have efficiency implications and can come at a significant revenue cost (Ebrill, Keen and Perry, 2001[25]).

Figure 4.6. Value-added tax registration thresholds (left) and value-added tax rates (right) in the OECD and the WB6 economies (2022)



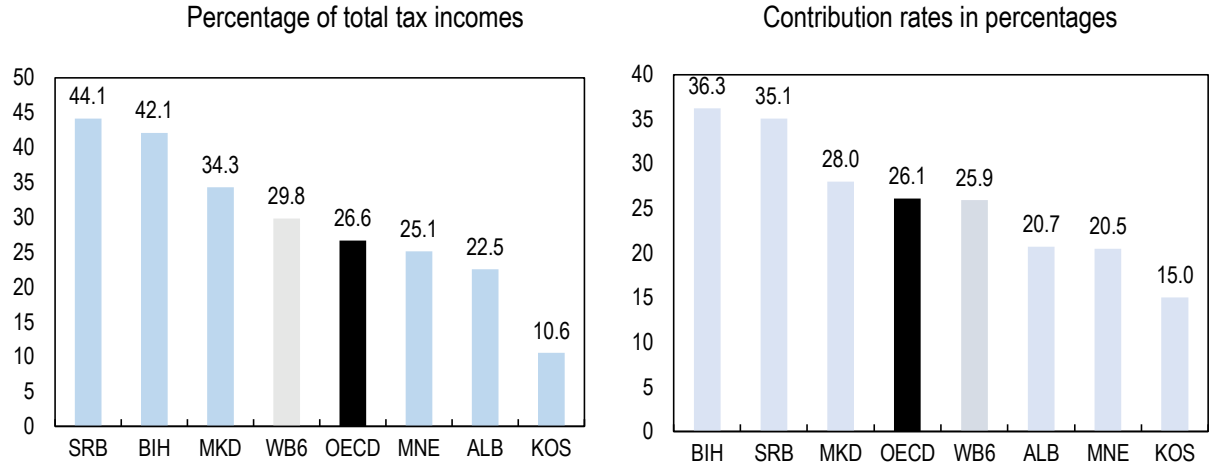
Sources: OECD (2024[26]); data provided by national authorities for the Competitiveness Outlook assessment.

High social security contribution rates increase the cost of labour to businesses and represent a significant present (and future) obstacle for WB6 economies

The lack of progressivity of personal income tax (PIT) in WB6 economies, combined with high and flat social security contribution (SSC) rates, imposes a disproportionately high tax burden on low-income employees, which may induce businesses to hire them informally. The total contribution rate (share of aggregated employee and employer contributions as a proportion of gross income) is over 20% for all

economies except Kosovo and reaches over 35% in Serbia and Bosnia and Herzegovina (Figure 4.7). These high SSC rates and the comparatively low CIT and VAT rates mean that SSCs constitute a significant part of the region's total tax revenue. Indeed, while SSC total contribution rates are similar in the WB6 and the OECD (26.1% and 25.9%, respectively), they stand for a larger share of total tax revenue in the WB6 (29.8% vs. 26.6% in the OECD). The reliance on SSCs is even higher in North Macedonia (34.3%), Bosnia and Herzegovina (42.1%) and Serbia (44%).

Figure 4.7. Social security contributions rates (left) and share of social security contributions in tax revenues (right) in the WB6 economies and the OECD (2022)



Sources: OECD (2024[26]); data provided by national authorities for the Competitiveness Outlook assessment.

High SSC rates can impose a financial strain on firms by raising the cost of low-skilled labour and increasing the overall cost of employment, encouraging businesses to operate in the informal economy to avoid the financial burden of formal employment (Asik et al., 2022[27]). Several economies have implemented reforms targeting SSC rates. For example, in 2021, Montenegro reduced its SSC rate from 32.3% to 20.5%, while Serbia and Republika Srpska (RS) have modestly lowered their SSC rate in recent years (albeit by less than 1 percentage point).

Reforming SSC rates is particularly important given the trends of ageing and emigration in the Western Balkans, as well as population ageing and labour demand in Western Europe, which is the main destination for Western Balkan emigrants. Population ageing, compounded by high emigration rates, risks shrinking the labour force and therefore tax revenue while simultaneously putting more pressure on the SSC system (Coline and Bert, 2019[28]). However, as labour demand in Western Europe increases, WB6 economies with a competitive business climate and a well-designed tax system could capitalise by attracting jobs and companies. This is particularly relevant for sectors in which remote work is common, such as software development or other information technology (IT) fields, and would also be key to reducing high-skilled emigration.

Despite the importance of demographic trends, few economies have analysed how they impact their tax systems. Montenegro stands out as it has implemented a comprehensive reform package aimed at addressing issues related to informality, ageing and emigration. Albania and Bosnia and Herzegovina have initiated some analysis, but this has yet to result in policy reforms.

Capital income in some WB6 economies is taxed more favourably than wage income

In Bosnia and Herzegovina and Kosovo, domestic dividends are untaxed; in Albania, realised capital gains are taxed at a reduced rate. Moreover, capital income is generally excluded from the SSC base in the WB6 economies. As in many OECD countries, this leads to a gap in the effective tax rates of labour and capital income in most WB6 economies, which may affect the tax system's efficiency. Further aligning PIT and CIT can mitigate problems caused by tax-induced incentives and encourage entrepreneurs to incorporate their businesses. This kind of income-shifting behaviour can negatively impact tax revenue and lead to market distortions. Balancing these implications with other policy objectives, such as promoting investment, is a key challenge for policy makers. Additionally, as capital is more mobile than labour, implementing the Automatic Exchange of Information (AEOI) standards increases transparency regarding the income earned abroad by tax residents, allowing for better compliance and creating an opportunity for capital income tax reform.[10] In this regard, Albania and Montenegro have implemented the AEOI standards, and Montenegro aims to start sharing information in 2024. North Macedonia plans to implement the standards for AEOI in 2025, and they have yet to be implemented in Bosnia and Herzegovina, Kosovo and Serbia.

Efforts to improve taxpayer services and filing procedures have reduced the compliance burden for firms in the Western Balkans

Improvements to taxpayer services have been central to increasing the ease of compliance for businesses. Readily available and comprehensible taxpayer services help to maximise compliance by providing firms with the information and assistance necessary to meet any tax obligations. The tax administrations of all WB6 economies have made a comprehensive range of tax information easily accessible to taxpayers, making it easier for businesses to find and employ information that might aid compliance. Moreover, most of the tax administrations respond quickly to any information requests; for example, Kosovo's tax administration reports that it responds to most requests within two to three days (with a maximum of 15 days), while Serbia responds to all standard requests within three working days and all written questions within seven working days. North Macedonia solved 99.7% of its written requests within 15 working days in 2022. Conversely, the tax administrations of Montenegro, RS and FBiH report that it can take up to 30 days to respond to written requests.

Keeping tax filing and payment procedures streamlined and simple limits compliance costs imposed on businesses. This is particularly true for SMEs, which may have less funding or resources to devote to compliance. All WB6 economies self-assessed the complexity and length of these procedures as being either relatively or reasonably simple.

One major stride to improve efficiency has been progress on the electronic filing of taxes. Catalysed by the COVID-19 pandemic, many economies fast-tracked the advancement of their e-filing systems, with it becoming mandatory in Albania, Kosovo and Serbia since the last Competitiveness Outlook assessment in 2021. In general, the digitalisation of tax administration facilitates a host of benefits: it enhances the audit function, reduces compliance and enforcement costs, optimises staff utilisation, minimises errors, and curtails the potential for corruption. Moreover, these systems enable the cross-checking of data across various taxes and the effective use of third-party information, further aiding compliance. E-filing has been progressively implemented and increasingly widely used, even in economies where it is not required. For example, both entities in Bosnia and Herzegovina observed a significant increase in the proportion of taxes electronically filed between 2019 and 2022: in RS, the figure rose from 43% in 2019 to 90% in 2022, and in FBiH, there was a 9 percentage point increase, from 55% in 2019 to 64% in 2022.

Recommendations for financial regulation and taxation policies

To improve bank financing for businesses and provide alternative funding options, policy makers should also focus on tax reform and policy enhancements to boost competitiveness. In this regard, they should:

- **Leverage a regional approach in establishing a common capital market aligned with the EU *acquis*, including environmental and social standards.** Establishing a common market helps address constraints that small economies face in developing capital markets, and is crucial for funding the significant investment needs in the WB6. The Baltic countries' experience in establishing a common capital market can offer useful insights for the Western Balkans (Box 4.1).

Box 4.1. The pan-Baltic capital market and the rise of private equity

Between 2012 and 2022, annual private fundraising in the Baltics grew from EUR 40 million to EUR 300 million, allowing the region to exhibit the highest penetration rates of the EU (S&P Global, 2023[29]).

The Baltics are small, with a total of 6 million inhabitants, which is approximately three times less than the WB6. One key element explaining the rise of private equity has been alleviating the burden of developing a domestic capital base by establishing an integrated pan-Baltic capital market.

Recognising the need to combine national markets to attract investors and enhance liquidity, the Baltics signed a memorandum of understanding in November 2017 to harmonise capital market regulations and eliminate investment barriers across the region, aligning with the EU's capital markets union initiative.

Substantial progress has been made, particularly in enhancing financial integration, as evidenced by significant growth in cross-border portfolio investment holdings. Key legislative milestones include progress in establishing covered bond frameworks. Estonia, Latvia and Lithuania have made strides in this regard, with Estonia and Lithuania enacting new frameworks in 2019 and Latvia advancing draft legislation. These frameworks facilitated covered bond issuance backed by pan-Baltic assets, appealing to major financial institutions operating in the region. In 2020, Luminor Bank AS and LHV Bank issued the first two covered bonds in the Baltic states, raising substantial amounts. The Baltic states benefit from a well-integrated market infrastructure, exemplified by the merger of their national central securities depositories in 2017, creating Nasdaq Central Securities Depository (CSD) Societas Europaea. Iceland's integration into this unified CSD in 2020 further enhanced market integration.

Note: The penetration rate is the share of private equity and venture capital-backed private companies in total private companies.
Sources: EBRD (2022[30]); S&P Global (2023[29]).

- **Address SMEs' credit constraints to ensure the accessibility of bank finance.** As long as SME access to finance remains substantially challenging, the Western Balkan governments should explore establishing permanent credit guarantee schemes and public credit lines to alleviate SMEs' specific credit constraints. However, the ordinary support of government should be clearly distinguished from temporarily extraordinary measures and be designed to ensure additionality and avoid excessive transfer of risk from the private to the public sector (OECD, 2018[31]).
- **Promote environmental and social standards to benefit the financial market.** By promoting environmental and social standards, the region can **leapfrog to a sustainable financial market**, **increase the capacity to attract and absorb international climate finance, and ultimately integrate into the European financial market**. The region has struggled to capture and channel

international climate finance flows, partly due to the weakness of environmental and social safeguards in investments. Many actions can be undertaken to improve this situation, such as developing sustainable finance taxonomies, sustainability disclosure regulations, green bonds standards, and environmental and social standards.

- **Introduce training opportunities for entrepreneurs and awareness-raising campaigns to cultivate the leasing market**. While most WB6 economies have instituted robust legal frameworks, leasing remains underdeveloped in the WB6 economies, indicating that measures to address entrepreneurs' financial literacy are needed.
- **Consider adopting territorial tax systems**. Given the financial and administrative challenges a worldwide tax system engenders, the WB6 economies could consider transitioning to a territorial tax system. This would mean resident companies would be taxed on their income generated domestically (rather than on their global income), which could alleviate administrative complexities without sacrificing tax revenue (Box4.2).

Box 4.2. Territoriality of tax systems in the EU

Of the 27 EU economies, 19 employ a fully territorial tax system that exempts all foreign-sourced dividend and capital gains income from domestic taxation. Such income is partially exempted from domestic taxation in the remaining eight countries.

Of the eight countries with a partially territorial tax system, only Ireland fully taxes foreign-sourced dividend income (reduced rate for a business that is tax resident in the EU or a country with which Ireland has a double taxation agreement); it also fully exempts foreign-sourced capital gains income. The opposite is the case in Poland, which fully taxes foreign-sourced capital gains income and fully exempts foreign-sourced dividends. The remaining six countries have partial exemptions for both foreign-sourced dividends and capital gains income. However, Slovenia allows for a 95% exemption on dividend income but only a 47.5% exemption on capital gains.

Many countries treat foreign-sourced income differently depending on the country in which it was earned. For example, many countries restrict their territorial systems based on a “blacklist” of countries that do not follow certain requirements. Among the EU member countries, it is common to restrict the participation exemption to EU member states or the European Economic Area.

Sources: Deloitte (2024[32]); Locher (2021[33]).

- **Assess the impact of the Global Anti-Base Erosion Rules on domestic tax systems**. Depending on the outcome of such an assessment, WB6 economies may use this opportunity to revise some of their tax incentives or reform their CIT rates more broadly, both of which could significantly impact the business environment. In the short term, WB6 economies should consider introducing a Qualified Domestic Minimum Top-Up Tax (QDMTT) to avoid forgoing revenue.
- **Use microdata to simulate the tax and business environment implications of domestic demographic shifts such as population ageing and emigration**. Unilaterally lowering SSC rates might be too costly for the region’s economies. Instead, they should assess whether there is room to improve the design of the SSC system to strengthen employment and reduce informality.
- **Foster regional co-operation and tax information sharing.** Most WB6 economies are dealing with similar challenges and undertaking reforms in similar areas. Fostering regional co-operation and information sharing is crucial for a robust and unified approach to addressing cross-border tax evasion and avoidance.

Fostering a level playing field

Corruption and informality pose significant challenges to businesses in the Western Balkans, affecting their competitiveness and hindering a level playing field. Furthermore, ensuring that state-owned enterprises (SOEs) operate efficiently and on a level playing field with private companies is crucial for well-functioning markets in the WB6.

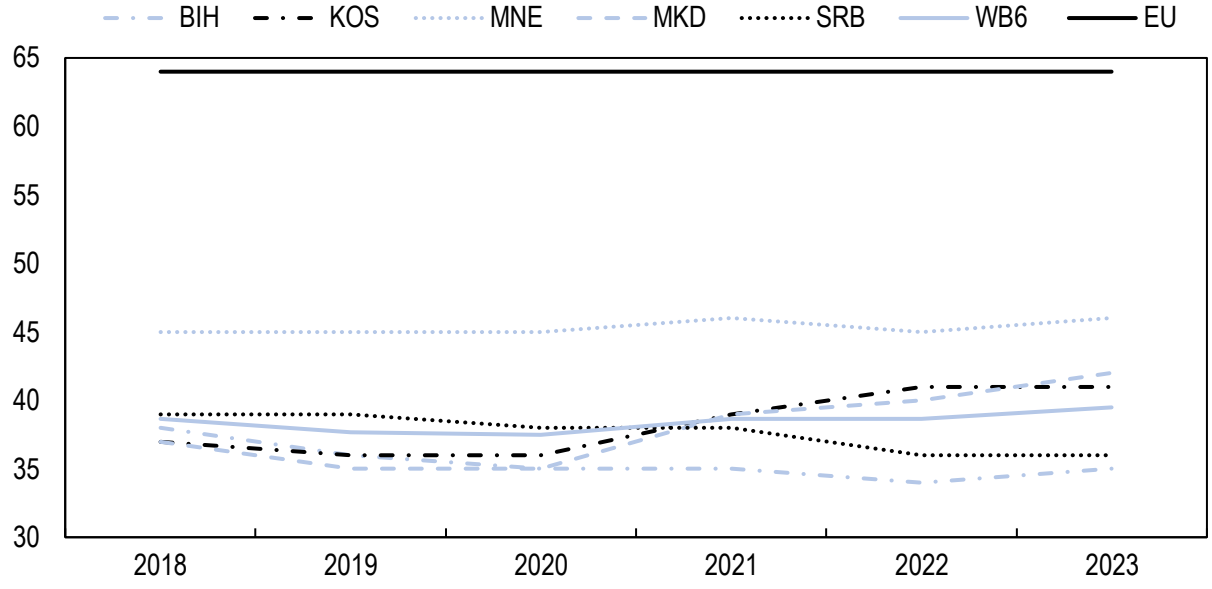
Anti-corruption

Anti-corruption policies are crucial for ensuring fair competition as they help create a level playing field where companies compete based on the quality and price of their products, services and innovation, rather than on bribes and unfair access to public resources.

Corruption persistently hampers competitiveness in the Western Balkans, and is mirrored in the lack of sustained anti-corruption strategic frameworks

Corruption remains a persistent challenge to the competitiveness of the Western Balkans, and is mirrored in the performance of the WB6 economies against international anti-corruption indicators such as Transparency International's Corruption Perceptions Index. This index reflects a limited change in the WB6 economies between 2018 and 2023: on a scale from 0 (highly corrupt) to 100 (very clean), the region scored an average of 38.7 in 2018 and 39.5 in 2023 – significantly below the EU average of 64, indicating limited convergence. Bosnia and Herzegovina has consistently recorded a lower score than the other WB6 economies, whereas Montenegro's scores have consistently remained above the WB6 average (Figure 4.8). Businesses in the region also view corruption as a significant obstacle to their growth (RCC, 2023[34]).

Figure 4.8. Corruption perception in the WB6 economies and the EU (2018-23)



Note: 1 – highly corrupt; 100 – very clean.
Sources: Transparency International (2024[35]); Eurostat (2024[36]).

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The region's performance in this regard could be partly attributed to the absence of sustained, long-term strategic frameworks for combating corruption. At the time of writing, only North Macedonia had such a framework in place: the National Strategy for Prevention of Corruption and Conflict of Interest 2021-25. In contrast, anti-corruption documents have expired in Albania (in 2023), Bosnia and Herzegovina (in 2019 at the state level, in 2022 in RS, with a provisional action plan still in place in FBiH), Kosovo (in 2017), Montenegro (in 2018-19) and Serbia (in 2023). These five economies have all prepared to develop new strategies, but various factors such as lack of political will or controversies over specific goals and actions have hindered their swift finalisation and adoption. As such, the anti-corruption policy framework in most of the region is incomplete and fails to fully implement the advice of the OECD Recommendation on Public Integrity to "develop a strategic approach for the public sector that is based on evidence and aimed at mitigating public integrity risks" (OECD, 2024[37]).

Prevention, investigation and prosecution of anti-corruption in the region remains challenging, despite improvements

All WB6 economies have **corruption prevention bodies** that mostly have safeguards for their independence and observe due public accountability, although some, as in Kosovo and Serbia, struggle to fully implement their mandate due to limited resources – possibly indicating a lack of political commitment to combat corruption more effectively. Encouragingly, prevention bodies in Albania, Montenegro and North Macedonia witnessed increased resource allocation in budgetary allocations and/or staff augmentation between 2021 and 2023. Furthermore, several prevention bodies have either launched (Albania, Kosovo) or are in the process of developing (Montenegro, North Macedonia) new digital systems for managing asset and interest disclosure. This development can enhance the effectiveness of monitoring conflicts of interest and help prevent public officials from favouring specific companies unfairly. Prevention bodies across almost all WB6 economies have also demonstrated a track record in enforcing conflict of interest regulations. The exception is Bosnia and Herzegovina, where implementation is weak and both FBiH and RS lack adequate legal frameworks for preventing conflicts of interest.

Obstacles to the sustainability and long-term efficacy of efforts to fight **high-level corruption** in the region include vulnerabilities in the independence of investigative, prosecutorial and judicial bodies, as well as resource constraints. This can lead to businesses facing increased risks and barriers to operating fairly and efficiently. The track record of the investigation and prosecution of high-level corruption has slightly improved in Albania, North Macedonia and Serbia, where increasing numbers of convictions for high-level corruption have been recorded (Table 4.3).

Table 4.3. Number of convictions and/or imprisonments for high-level corruption in the WB6 economies (2018-22)

	2018		2019		2020		2021		2022	
	Con.	Imp.	Con.	Imp.	Con.	Imp.	Con.	Imp.	Con.	Imp.
ALB	2	2	0	2	2	0	0	2	4	4
KOS	/	/	9	0	15	0	21	0	15	0
MNE	0	0	3	2	3	3	2	1	1	1
MKD	4	0	7	2	4	0	6	1	18	3
SRB	41	/	30	/	22	/	10	/	26	/

Notes: Con. = convictions; Imp. = imprisonments. Number of convictions for high-level corruption (subject to appeal and final); number of imprisonments for high-level corruption without conditional or other type of release. The data of the economies may not be mutually comparable because of differences in methodologies used by different authorities.
Sources: Based on data provided by authorities in the context of the Competitiveness Outlook 2024 assessment. For Serbia also European Commission (2020[38]).

However, across the region the confiscation of proceeds from high-level corruption cases remains weak, especially regarding assets located abroad. Moreover, the potential for recovering pecuniary benefits acquired through corruption continues to be underutilised. The absence of continuous anti-corruption strategies likely impedes corruption prevention, investigation and prosecution bodies from realising their full potential.

WB6 economies do not sufficiently encourage companies to adopt stronger internal controls and anti-corruption compliance measures for greater integrity

Business integrity policies are generally weak in the WB6, and laws do not explicitly cover corruption risk management in companies. However, there are general obligations for all or certain types of company to have risk management policies in Kosovo, Montenegro, North Macedonia and Serbia. Publicly traded companies in North Macedonia and RS are subject to codes of corporate governance or conduct and must report on compliance to the stock exchange (North Macedonia) or the meeting of shareholders (RS). A good practice example can be seen regarding the Stock Exchange of North Macedonia in 2022, which published a report on company compliance with the corporate governance code (Macedonian Stock Exchange, 2023[39]). Several economies have legally non-binding corporate governance or ethics codes, but there are no data regarding their implementation or impact.

While most WB6 economies have introduced the disclosure of **beneficial owners**, the reliability of recorded information remains uncertain as it is difficult to determine to what extent the economies verify the accuracy and completeness of the data. In recent years, Albania, Montenegro, North Macedonia and Serbia have established registers, with all except Montenegro making some or all of the data accessible to the general public. RS has the legal requirement to submit data on beneficial owners to the register of business entities, but its implementation is unclear; FBiH lacks legislation concerning the registration and disclosure of beneficial owners. In February 2024, Kosovo approved the draft Law on the Register of Beneficial Owners. Legal definitions of beneficial owners in the WB6 largely align with those outlined in EU directives, which have served as benchmarks for WB6 economies.

There is no evidence of any WB6 government making active efforts to incentivise companies to introduce corporate anti-corruption policies to mitigate potential liability. Additionally, in Bosnia and Herzegovina, Kosovo and North Macedonia, existing laws do not allow mitigating sanctions for legal persons that have adopted due diligence, compliance, internal control or other internal anti-corruption policies. In contrast, Albania, Montenegro and Serbia recognise such measures as grounds for mitigating sanctions. Overall, legal frameworks for corporate liability in the WB6 would benefit from guidance on anti-corruption compliance that managerial and supervisory bodies of legal persons should ensure.

State-owned enterprises

The importance of the efficient operations of SOEs for broader economic and societal outcomes in the Western Balkans cannot be overstated. First, SOEs in the Western Balkans are often prevalent in systemically important sectors on which other businesses depend for their efficient operations, such as electricity and gas, telecommunications, and transport. Second, as they often compete with private companies, for example in the manufacturing, agricultural and services sectors, a level playing field is crucial for building efficient markets in which the most productive firms thrive. Finally, the extent to which commercially operating SOEs deliver financial returns – or depend on state support – is critical for public finances and more broadly maintains the framework conditions for economic competitiveness.

The central governments of the Western Balkans together own approximately 470 enterprises, with the largest number of SOEs in Serbia (225) and the smallest number in Kosovo (18) (Table 4.4). SOEs accounted for an estimated 3.4% of total regional employment in 2022, ranging from 1.4% in North Macedonia to 8.4% in Bosnia and Herzegovina[11] (Table 4.5). This makes the size of the region's

overall SOE portfolio (as measured by employment share) broadly comparable with the 15 largest SOE portfolios in the OECD area, where SOEs accounted for 3.8% of non-agricultural employment on average in 2017, ranging from 1.9% in New Zealand to 9.6% in Norway (OECD, 2017[40]).[12]

Table 4.4. Number of central SOEs in the WB6 economies (2022)

	SRB	ALB	BIH	MNE	MKD	KOS
Number of central SOEs by economy	225	76	72	50	30	18

Sources: Information provided by the national and entity authorities in the context of this assessment and IMF (2019[41]) for Bosnia and Herzegovina.

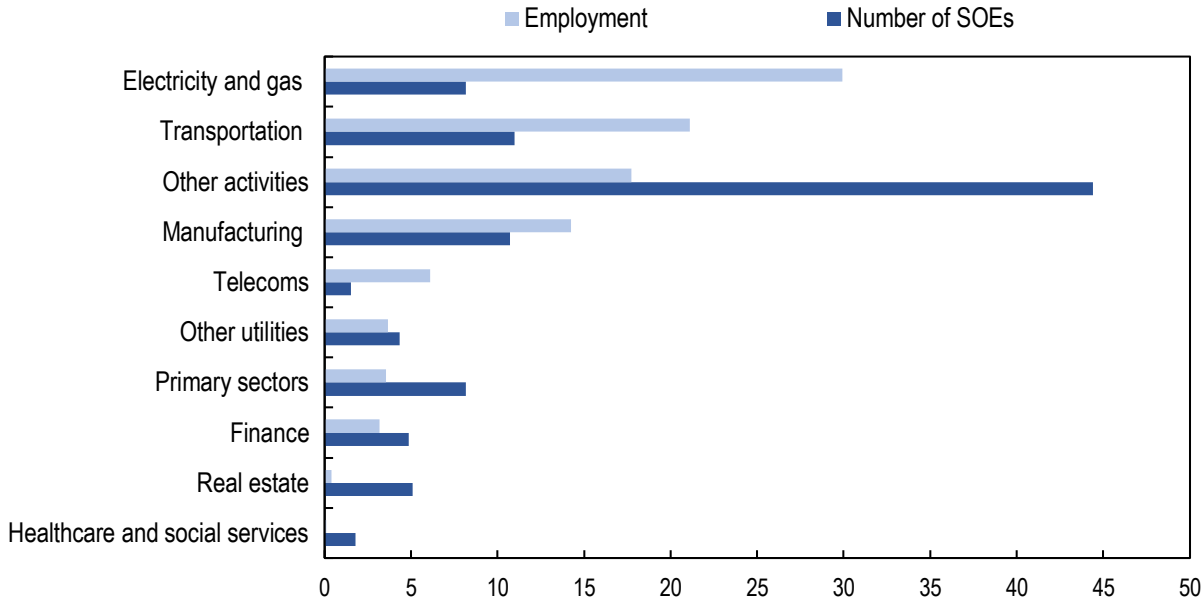
Table 4.5. SOEs' share of employment in the WB6 economies and the OECD (2022 or the latest available year)

	MKD	ALB	KOS	SRB	MNE	BIH	WB6	OECD top 15 average*
Share of employment (%)	1.4	1.5	2.8	4.8	4.9	8.4	3.4	3.8

Notes: *OECD data relate to SOEs' share of non-agricultural (rather than total) employment, making the comparison with WB6 economies imperfect. The OECD figure is a simple average of SOEs' employment shares in the top 15 countries.
Sources: OECD calculations are based primarily on information provided by the national and entity authorities in the context of this assessment. Figures for North Macedonia are based on OECD (2021[42]) and figures for Bosnia and Herzegovina are based IMF (2019[41]).

Figure 4.9. Sectoral distribution of SOEs in the WB6 economies (2022 or latest available year)

In percentages



Notes: Figures on SOEs' sectoral distribution exclude Bosnia and Herzegovina, 7 SOEs in North Macedonia and 23 SOEs in Albania for which recent employment data were not available. Figures are from 2022 or latest available.
Sources: OECD calculations based primarily on information provided by the national and entity authorities in the context of this assessment.

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When measured by employment share, SOEs in the region are highly concentrated in sectors with elements of natural monopoly such as electricity and gas, and transportation, which represent 30% and 21%, respectively, of all regional SOEs by employment (Figure 4.9).[13] SOEs also operate in other, less traditional, activities, including construction companies, hotels, tourism companies and football clubs. SOEs are also present, although less concentrated, in the primary sectors[14] (4% of all SOEs by employment), which notably include a number of enterprises engaged in mining, forestry and other agricultural activities.

Efforts to strengthen state ownership institutions and policies are nascent or underway in several economies

Strong state ownership entities and clear ownership policies can support a more level playing field by ensuring that state owners are well equipped to monitor and oversee SOEs' implementation of international standards, performance and contributions to market efficiency (OECD, 2024[43]). Across the region there is an absence of centralised ownership entities that are driven by clear ownership rationales and supported by clearly defined ownership policies, as can be found in OECD countries. This has historically allowed the region's SOEs and their ownership ministries to operate in an accountability vacuum, where SOE objectives, if they exist at all, are set in an ad hoc manner and often subject to the changing priorities of responsible ministers.

Most of the region's ownership portfolios are managed in a decentralised manner by sectoral line ministries (exceptions are Kosovo and, since 2023 legislative amendments, Serbia). This is problematic because sectoral ministries are often tasked with other functions such as market regulation, and thus objectives may conflict with shareholding objectives. The OECD SOE Guidelines recommend that the ownership function be either fully centralised and undertaken by a dedicated state ownership entity without policy or regulatory functions or, if this is not possible, subject to central co-ordination by a co-ordinating entity with a clear mandate to act on a whole-of-government basis (Box 3.4).

Currently, efforts to **professionalise state ownership** by building central state ownership institutions and/or to **clarify ownership policies** are nascent or ongoing in Kosovo, Montenegro, RS and Serbia.[15] The authorities in these economies have notably taken some steps (or, in the case of Montenegro, announced plans) to professionalise state ownership institutions, including by centralising SOE monitoring or ownership co-ordination functions under dedicated units or ministries. The authorities of Kosovo and Serbia have also elaborated ownership policies outlining the overarching objectives of state enterprise ownership and establishing some basic principles to be followed by shareholding ministries to ensure the more professional management of SOEs. In some cases, efforts to strengthen state ownership institutions have come with enhanced public accountability, such as the online disclosure (either foreseen or already implemented) of data on SOEs' financial performance.

Despite these initial steps towards improved ownership practices, the institutional strength and responsibilities of SOE monitoring and/or co-ordination units vary considerably across the region, and in most cases the units in place play primarily a performance monitoring role, with very limited formal involvement in ownership decisions such as objective setting that, among other things, could impact SOEs' financial performance and accountability. There is also scope across the region to improve the centralised collection of performance data on individual SOEs to better inform shareholding decisions for improved efficiency. Only Kosovo produces annual aggregate reports on SOEs' performance and activities. Strengthened data collection on SOEs can support a level playing field by informing the development of heightened performance expectations, thus mitigating the need for state support that distorts the competitive landscape with private companies.

Concerning the characteristics of SOE portfolios, many SOEs in the region operate in sectors where there is no obvious or compelling rationale for continued state ownership. This points to scope for a more thorough review of why the state owns these companies and whether any would be strong candidates for privatisation. Although **SOE privatisation** activity has continued to some extent over the past decade (with Serbia undertaking the largest number, at 71 SOEs since 2015), most privatisation across the region has been small in scale, with much privatisation activity involving relinquishing real-estate assets rather than selling fully operational companies. This general trend can be expected to continue as no regional authority has announced definitive plans to privatise any large or systemically important SOE in the near term.[16]

A dedicated ownership policy that outlines the agreed rationales for state ownership would help identify candidates for privatisation, with enterprises for which the agreed rationales are no longer present potentially proposed for privatisation. This would ensure that maintaining companies in state ownership results from an informed policy decision. There is also scope for the region's authorities to accelerate bankruptcy or liquidation proceedings that have already been initiated or announced, for example in economically inactive SOEs.

SOEs' underperformance distorts the level playing field and hinders market efficiency

Most SOEs in the region are incorporated as limited liability or joint stock companies, and thus subject to the same laws applicable to private companies, in line with OECD good practice. Bosnia and Herzegovina, North Macedonia, Montenegro and Serbia maintain some small portfolios of SOEs that operate under the legal form of "public enterprise" and are subject to special legislation (Table 4.6). This is not considered good practice as it can create differences in legal treatment that distort the level playing field with private companies. In some cases, the laws applicable to these public enterprises (collectively or through individual laws of incorporation) may effectively shield SOEs from bankruptcy or insolvency, perhaps creating a disincentive for their management to address structural performance issues. In other cases, such laws introduce problematic governance provisions, for example by allowing the state shareholder to directly nominate the chief executive, effectively stripping boards of directors of their fundamental role of independently supervising management and therefore shielding SOEs from political interference. Although most economies of the region perform relatively well in this regard, with a high degree of SOE corporatisation, eliminating the special legal form of public enterprise would support an even more equal playing field for all SOEs.

Table 4.6. SOEs with special legal form in the WB6 economies (2024)

	MKD	BIH (RS only)	SRB	MNE	ALB	KOS
Share of SOEs with special legal form (%)	48.3	22.2	8.9	6.0	0.0	0.0

Sources: OECD calculations based on information provided by the national and entity authorities in the context of the CO assessment.

Available data suggest that SOEs across the region are frequently loss-making, which amounts to a cost of equity capital that is not market consistent and that distorts the level playing field with private companies. Although SOE performance monitoring is limited in the region – only Kosovo, RS and, most recently, Serbia, have established centralised SOE monitoring units – external assessments and data collected for this review show that a non-trivial proportion of the region's SOEs underperform or are outright loss-making. A 2019 IMF study examining the performance of SOEs and private firms in Central, Eastern and South East Europe (including four WB6 economies) found that SOEs in every economy and sector posted lower revenues per employee, paid a wage premium comparable with private competitors and were less profitable than private competitors (IMF, 2019[44]). The same study found limited evidence that SOEs were achieving any specific non-financial objectives, such as improved infrastructure that could potentially justify their underperformance, and pointed to high staff costs as a significant source of inefficiency.

Although it remains possible that some SOEs in the region have low profitability because they cross-subsidise from profit-making to loss-making non-commercial objectives, none of the region's authorities have attempted to quantify the costs of SOEs' non-commercial objectives systematically, or indeed to establish key performance indicators to track their achievement.

Labour market informality

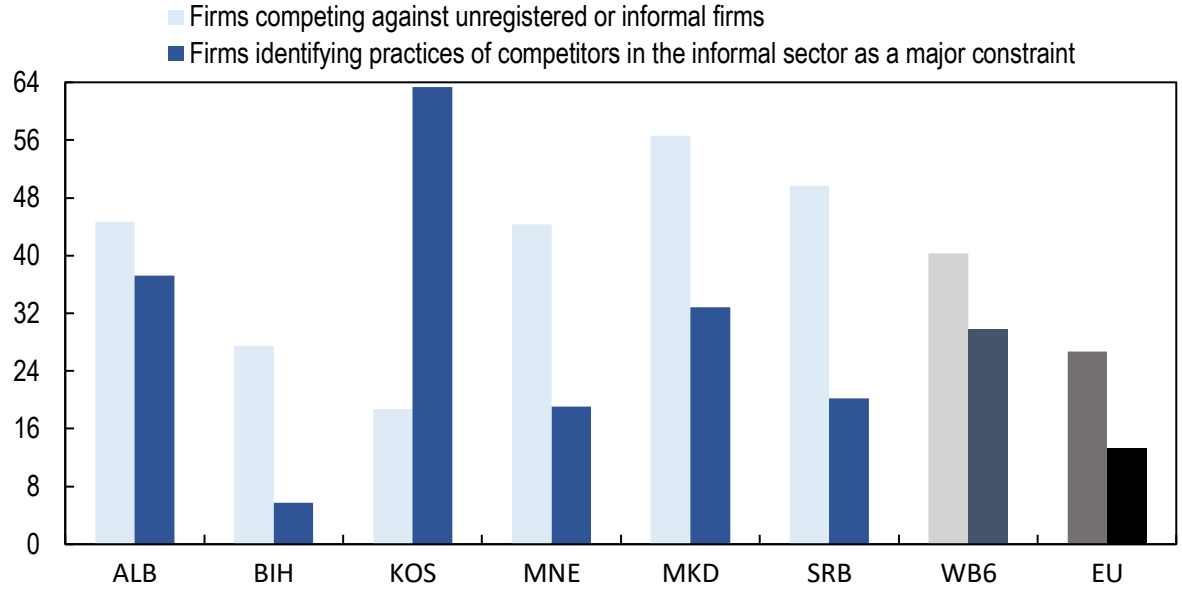
Informality poses a significant challenge to businesses in the Western Balkans, affecting their competitiveness and hindering a level playing field. Common practices such as tax evasion and unregistered employment undermine the rule of law and create unfair competition. This limits formal businesses' ability to invest, innovate and access finance and markets.

Informality remains a challenge in all WB6 economies, with moderate progress achieved

Addressing informality requires comprehensive reforms to improve governance and enforcement mechanisms, and thus foster a more conducive environment for formal business growth. In all WB6 economies (except Kosovo), the proportion of firms competing against informal businesses surpasses the EU average. The percentage of companies citing informal business practices as a hindrance to their operations is also notably higher than the EU average (excluding Bosnia and Herzegovina) (Figure 4.10).

Figure 4.10. Competition of firms with the informal sector in the WB6 economies and the EU

Percentage of firms



Notes: For Albania, Kosovo, Serbia data refer to 2019, for Bosnia and Herzegovina, Montenegro and North Macedonia data refer to 2023. EU-27: without Malta (no data available). Data for EU countries contain the most recent available data between 2019 and 2023. Unweighted average.
Source: World Bank (2023[45]).

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Identifying informality and undeclared work is primarily the responsibility of labour inspectorates. Enhanced co-operation among various ministries and relevant stakeholders is likely to facilitate the detection of informal employment, with notable progress observed in Albania and Serbia. However, most economies

have yet to advance on intensifying inter-institutional co-operation, potentially limiting opportunities to detect and combat labour market informality.

Some economies have incorporated combating informal employment into their employment and economic strategies, have established specific strategies, or are in the process of formulating such objectives to ensure good employment opportunities universally, although monitoring activities to combat informal employment remains inconsistent across the region. There are indications that awareness-raising campaigns advocating for the reduction of informal employment are conducted in most economies, including Albania, RS, Kosovo and Montenegro. Some economies have also introduced incentives to combat informal employment, such as lowering the taxation of lower-tier incomes (Albania, RS and Serbia).

Recommendations for fostering a level playing field

The following recommendations consist of the policy options most directly relevant to levelling the playing field in WB6 economies, focusing on tackling corruption and informality and improving SOE governance and performance.

- **Ensure the continuity of anti-corruption policy frameworks by avoiding gaps between the validity of old and new policy documents**. A long-term strategy in the fight against corruption is crucial for enhancing the effectiveness of corruption prevention, investigation and prosecution bodies. Moreover, by facilitating dialogue and knowledge exchange on developing anti-corruption strategies, economies can synergise their efforts and enhance agility in combating cross-border corruption cases. As such, existing regional anti-corruption initiatives, such as RAI,[17] should be further promoted. Another good example of regional co-operation is the adoption of a Regional Roadmap on Anti-Corruption and Illicit Finance Flows to fast-track the implementation of the United Nations Convention against Corruption (UNCAC) (UNODC, 2023[46]).
- **Strengthen corporate liability.** This can be achieved by ensuring that the applicable fines for all corruption offences conform with the standard of effective, proportionate and dissuasive sanctions; and by introducing incentives for compliance in the law, such as considering companies' due diligence efforts and anti-corruption policies as mitigating circumstances. Monetary sanctions should be sufficiently severe to affect large corporations that may engage in corrupt acts, which, if carried out undetected, could yield them millions of euros in profits. It is imperative to compile and publish detailed statistics to enable an assessment of the effectiveness of the corporate liability framework. Moreover, private sector best practices regarding corporate liability should also apply to SOEs (OECD, 2019[47]).
- **Consider ways of encouraging and incentivising companies to fight bribery in international business transactions**, as outlined by the *OECD Recommendation for Further Combating Bribery of Foreign Public Officials in International Business Transactions* (Box 4.3). The tools in this recommendation may be equally effective in preventing domestic bribery.
- **Develop state ownership policies and establish, or strengthen, central ownership or co-ordination entities**. Authorities in the WB6 should adopt state ownership policies that clearly outline why the state owns enterprises, what it expects them to achieve and which institution(s) are responsible for implementing the ownership policy (Box 4.4). To develop and implement these policies, the authorities should establish, or strengthen, central ownership monitoring or co-ordination bodies. Such ownership institutions could eventually play a role in developing publicly available annual aggregate reports on SOE activity and performance to enhance accountability and incentivise performance improvements. They could also usefully contribute to developing and implementing new SOE board nomination procedures that effectively establish independent and qualified boards of directors to meet SOE performance expectations.

Box 4.3. Encouraging and incentivising company compliance: The OECD Recommendation for Further Combating Bribery of Foreign Public Officials in International Business Transactions

Member countries should encourage:

- Companies, including state-owned enterprises, to develop and adopt adequate internal controls, ethics and compliance programmes or measures to prevent and detect foreign bribery [...].
- Business organisations and professional associations, where appropriate, in their efforts to encourage and assist companies […] in developing internal controls, ethics, and compliance programmes or measures to prevent and detect foreign bribery [...].
- Company management to make statements in their annual reports or otherwise publicly disclose their internal controls, ethics and compliance programmes or measures, including those which contribute to preventing and detecting bribery;
- The creation of monitoring bodies independent of management, such as audit committees of boards of directors or supervisory boards.
- Companies to implement frameworks for protecting persons reporting potential violations of law and channels for reporting [...].

Member countries should:

- Encourage their government agencies to consider […] internal controls, ethics and compliance programmes or measures for the purpose of preventing and detecting foreign bribery in their decisions to grant public advantages, including public subsidies, licences, public procurement contracts, contracts funded by official development assistance, and officially supported export credits.
- […] provide training and guidance to their relevant government agencies on how internal controls, ethics, and compliance programmes or measures are considered in their decision-making processes and ensure such guidance is publicised and easily accessible for companies.
- Encourage law enforcement authorities […] to consider implementing measures to incentivise companies to develop effective internal controls, ethics and compliance programmes or measures, including as a potential mitigating factor. […].
- […] ensure that competent authorities consider providing training and guidance on assessing the adequacy and effectiveness of internal controls, ethics and compliance programmes or measures for the purpose of preventing and detecting foreign bribery, as well as on how such programmes or measures are taken into consideration in the context of foreign bribery enforcement, and ensure such information or guidance is publicised and easily accessible for companies, where appropriate.

Source: OECD (2021[48]).

- **Elaborate market-consistent performance expectations for SOEs and separate accounting and clear cost structures for non-commercial objectives.** In many of the region's economies, a non-trivial proportion of SOEs are loss-making. Authorities could investigate the structural sources of SOEs' losses – for instance whether losses are indicative of weak performance or inadequate support for pursuing public service obligations – to inform an appropriate approach, for

instance including the development of clear financial and non-financial objectives that can be subsequently monitored. Where SOEs are subject to public service obligations they should be separately accounted and funded for, with funding proportionate and disclosed.

- **Fully corporatise SOEs engaged in commercial activities**. SOEs should be subject to the same laws and regulations as private companies when undertaking commercial activities. Several economies maintain small portfolios of incorporated SOEs subject to a separate legal form. SOEs operating commercially should be incorporated as joint stock or limited liability companies subject to company law.

Box 4.4. OECD Guidelines on Corporate Governance of State-Owned Enterprises

The OECD *Guidelines on Corporate Governance of State-Owned Enterprises* (SOE Guidelines) provide a blueprint for establishing sound ownership, corporate governance and transparency arrangements for SOEs to ensure that they operate transparently, efficiently and on a level playing field with private companies. Recommendations can be summarised as follows:

- **Rationale for state ownership**: The state should define and disclose the rationale for state ownership in a clear ownership policy. State enterprise ownership should be undertaken to create value for the general public, who are the ultimate shareholders of SOEs.
- **The state's role as an owner**: The state should act as an informed, active and accountable owner and should not intervene in the day-to-day management of SOEs. The exercise of state ownership rights should be centralised in a single ownership entity or carried out by a co-ordinating body not responsible for market regulation or other functions that could conflict with the shareholding function.
- **SOEs in the marketplace**: When SOEs undertake economic activities in the marketplace their financing conditions and legal framework should ensure a level playing field with private companies.
- **Equitable treatment of shareholders**: Non-state shareholders should have the same rights and equitable treatment as state shareholders, including equal access to corporate information.
- **Disclosure, transparency and accountability**: SOEs and the state shareholder should observe high standards of transparency and accountability. The state should publish regular aggregate reports on the activities and performance of the SOE portfolio.
- **Composition and responsibilities of SOE boards**: SOE boards should have adequate responsibilities, competencies and independence to carry out their strategic guidance and monitoring management role, without political interference.
- **SOEs and sustainability**: The state as a shareholder should integrate sustainability considerations into ownership policies and ensure that SOEs conduct business responsibly and with integrity.

Source: Adapted from OECD (2024[43]).

- **Implement comprehensive strategic frameworks to combat informal employment**. Addressing informality requires whole-of-government approaches across various policy domains. These include enhancing the capabilities of labour inspectorates to detect undeclared work and enforce penalties, fostering inter-institutional collaboration to identify informal employment, conducting awareness campaigns targeting both employers and employees, implementing lower

taxation on low incomes, enhancing safety net schemes, and simultaneously bolstering efforts to deliver integrated employment and social services.

Supporting business growth

Fostering competitiveness through business expansion drives innovation, efficiency and sustained growth. It can attract investment and encourage market expansion and overall economic development. Facilitating trade can strengthen regional businesses, promoting a dynamic environment for growth.

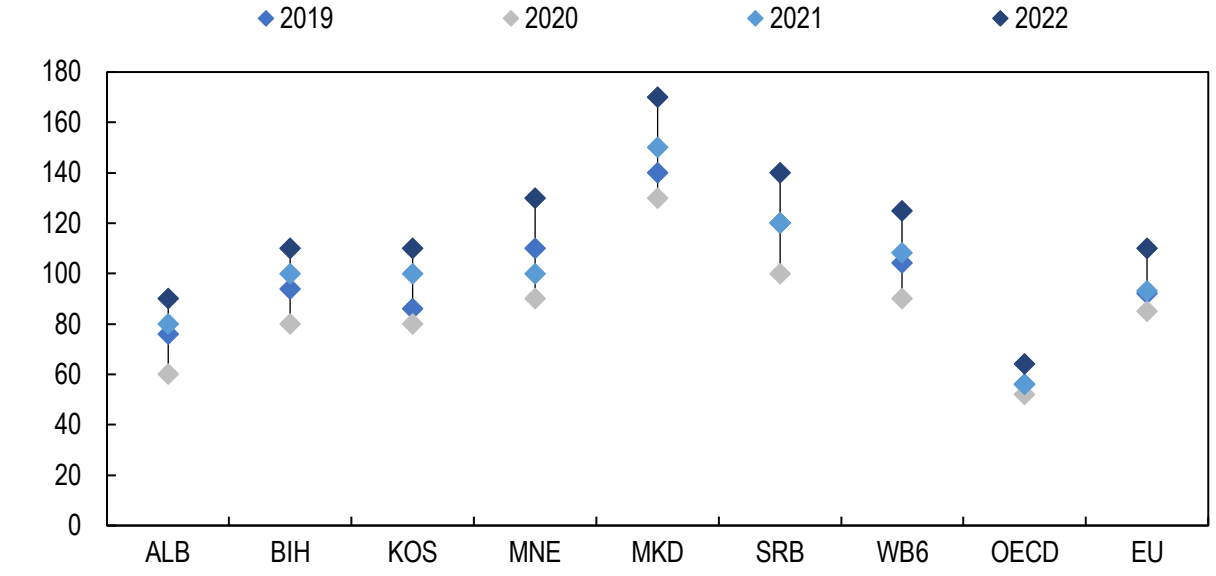
Promoting trade

Moving from local to global markets is a natural next step for companies looking to expand their operations and grow. This is particularly important for companies in the Western Balkan economies, which, as small, open economies, rely on international trade as the driver for economic growth. Companies need a conducive business environment to be able to expand their operations internationally and reap the benefits of integrating into global value chains (GVCs). However, ongoing obstacles such as trade barriers, administrative bottlenecks, limited export capacity and restricted access to finance collectively impede the internationalisation efforts of businesses.

Trade openness has increased in the region, fuelled by strengthened regional co-operation

Trade openness can fuel growth through increased imports and exports (Vujanović, 2023[49]). Regional progress in the business environment cluster underpins the region's significant level of openness and integration in trade and investment. Notably, the regional average for trade expressed as a percentage of GDP consistently exceeds that of the EU (Figure 4.11).

Figure 4.11. Trade openness in the WB6 economies, the OECD and the EU (2019-22)



Source: World Bank (2022[50]).

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Regional integration is vital for the business environment in the Western Balkans as it enables market expansion, infrastructure development, harmonisation of regulations and stimulation of investment, while fostering political stability and co-operation. Apart from trade with the EU, intra-regional trade between Central European Free Trade Agreement (CEFTA) members is growing in importance, with intra-CEFTA goods exports consistently rising since 2013 (albeit with a slight decrease in 2020 during the pandemic) to reach EUR 8.4 billion in 2022 (CEFTA, 2023[51]). This co-operation will play a crucial role in further enhancing trade openness and building stronger regional trade ties.

The region has made significant strides in advancing regional integration through several horizontal initiatives, which underscore the commitment to converge with the EU. The economies have advanced in harmonising trade policies and regulations, and in enhancing intra-regional infrastructure (RCC, 2024[52]), primarily through the adoption of CEFTA in 2006, the implementation of the Regional Economic Area (2017-20), followed by the enactment of the Common Regional Market Action Plan (CRM) (2021-24) (Box 4.5). The Additional Protocol 6 to CEFTA was ratified in December 2019 by all Western Balkan economies, and notable strides have been achieved in facilitating trade in services. Also relevant are the mobility agreements signed at the Berlin Process summits in November 2022 and October 2023 regarding the recognition of professional qualifications in various fields within the CEFTA context. The agreements have expanded opportunities for professional mobility across the region. In addition, the Western Balkans 6 Chamber Investment Forum – in co-ordination with the six Western Balkans chambers of commerce and industry – represents businesses in the region, supporting the establishment of the CRM, and facilitating and promoting the region as an investment destination.

In November 2023, the European Commission adopted the new Growth Plan for the Western Balkans to address the region's socio-economic convergence with the EU. This plan aims to stimulate growth and grant the Western Balkans access to specific areas of the EU single market before formal accession, while simultaneously accelerating preparations for EU membership (see Box 1.2 in Chapter 1).

Box 4.5. Common Regional Market 2021-24 as a tool for deepening regional integration

The Leaders' Declaration on the Common Regional Market and its Action Plan, ratified during the Berlin Process Summit in November 2020, introduced a framework for regional co-operation in the Western Balkans, emphasising regional collaboration and convergence with EU standards. Recognised as a pivotal regional initiative, CRM established the primary framework for regional socio-economic recovery and the twin green and digital transitions.

The key elements to create the CRM are the following:

1. Free movement of goods
2. Free movement of services
3. Free movement of capital
4. Connecting economies
5. Digital market
6. Regional innovation space
7. Regional investment space.

There have been several achievements under the regional trade area based on four freedoms (movement of goods, services, capital and people), such as the extension of the Green Lanes for essential goods to all CEFTA border crossing points (BCP), including rail, and the provision of pre-arrival notifications for goods subject to veterinary and phytosanitary controls (Box 3.6). Moreover, to further reduce trade costs parties have compiled and shared lists of trade-related fees and charges

with the CEFTA Secretariat to embark on the related technical work for streamlining these. Negotiations for the CEFTA Additional Protocol on Dispute Settlement have progressed positively at the expert level. Discussions on Intellectual Property Rights and trade in services under Additional Protocol 6 have advanced, with finalised guidelines expected later in 2024. Regional efforts to reduce the cost of regional payments have begun with the endorsement of a framework for modern payment systems by the Working Group on Financial Markets. Collaborating with the World Bank Group, consultations addressed all framework aspects, including interoperability and safety. WB6 economies endorsed the European Central Bank's Target Instant Payment Settlements (TIPS) for its efficiency and low implementation time. This decision supports SEPA readiness and reduces transaction costs for citizens in cross-border transactions.

The CRM offers numerous benefits to companies operating within the region. One significant advantage is the harmonisation and simplification of export-related documents, professional qualifications and licences throughout the WB6 economies, facilitating smoother business operations and trade in goods and services. Additionally, implementing one-stop shops is poised to drastically reduce waiting times at crossing points by up to 70%, providing efficient 24/7 services and establishing Green Lanes and corridors within the WB6 and with the EU. This streamlined process saves time and reduces costs in regional payments, fostering the growth of a robust regional e-commerce market. The abolition of work permit requirements for intercompany transfers and service providers encourages fluidity in the labour market, stimulating foreign direct investment (FDI) in promising sustainable regional value chains. The region also benefits from a roaming-free zone with reduced charges between the Western Balkans and the EU, enhancing connectivity and business communication.

The aim of the second phase of the CRM (2025-2028) – currently under development – is to put forward a set of activities to contribute further to economic integration within the region and with the EU single market as the main driver of economic growth, in line with the Growth Plan for the Western Balkans. The focus is also shifting to boosting human capital in education, enabling business environment and competitiveness, innovation and digitalisation, as well as labour migration and women's economic empowerment. The Action Plan for the new phase of the CRM is due to be endorsed at the next Berlin Process summit in October 2024

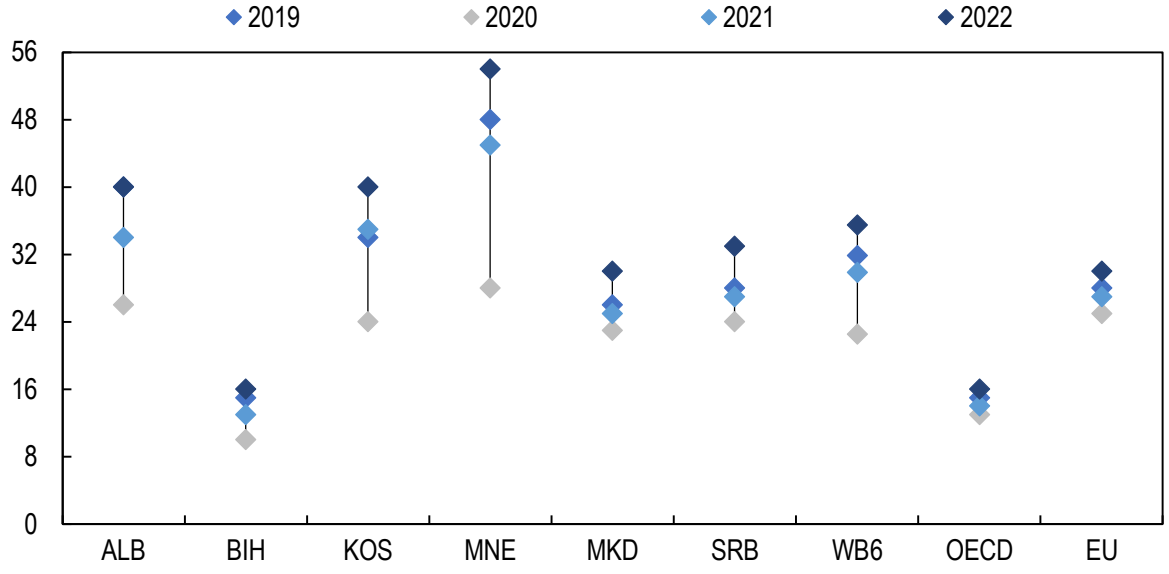
Notes: While the implementation of the CRM lies within the purview of each of the WB6 governments, the Regional Cooperation Council (RCC), CEFTA, the Energy Community and the Western Balkans Transport Community are pivotal in co-ordinating and assisting the Western Balkans in their efforts. The European Commission, specifically the Directorate-General for Neighbourhood and Enlargement Negotiations (DG NEAR), collaborates closely with these entities, providing them with political backing and financial and technical assistance.
Sources: WB6CIF (2021[53]); RCC (2023[54]); RCC (2024[55]).

CEFTA membership has had a significant effect on regional integration and the internationalisation of businesses in the Western Balkans. The liberalisation of trade within the region has enhanced intra-regional trade flows, further benefitting local businesses by facilitating access to new markets and thus diversifying their export destinations. CEFTA's entry into force contributed to a 37.7% increase in intra-regional exports (Grieveson, Holzner and Vukšić, 2020[56]). CEFTA's achievements in promoting intra-regional trade in the Western Balkans stand in contrast to the free trade agreements it superseded (Vujanović, 2023[49]). Moreover, studies show that before joining CEFTA, Western Balkan economies had a revealed comparative advantage in primary sectors such as agriculture, forestry and mining, whereas now most WB6 economies have started to gain a revealed competitive advantage in more knowledge intensive services, albeit at a moderate pace (Vujanović, 2023[49]).

Trade in services has been steadily rising since 2019 (Figure 4.12), with the exception of a decrease due to the COVID-19 pandemic. However, it is worth noting that, mirroring the global trend, the digital services sector in the Western Balkans showed greater resilience to pandemic-related shocks, demonstrating a smaller decline than overall services (IMF et al., 2023[57]). CEFTA's adoption of the Additional Protocol 6 on Trade in Services[18] lay the legal framework for trade in services and co-operation among CEFTA parties. This protocol encompasses comprehensive commitments aimed at promoting trade liberalisation, notably ensuring market access and national treatment for services suppliers across various sectors. Moreover, it set the stage for enhanced co-operation to address remaining barriers, including those related to domestic regulation and e-commerce. Additional Protocol 6 is also a tool for convergence with EU standards and encompasses provisions relevant to competition within the EU.

Figure 4.12. Trade in services in the WB6 economies, the OECD and the EU (2019-22)

Percentage of GDP



Source: World Bank (2022[58]).

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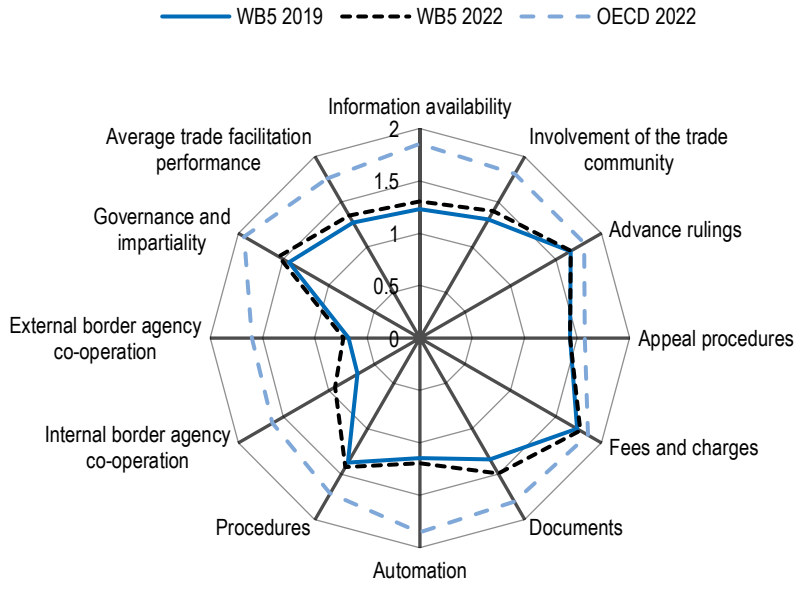
Trade facilitation performance in the region has improved, but non-tariff measures can hinder trade flows

Since 2019, the Western Balkans region has improved its trade facilitation performance, which is reflected in the 2022 OECD Trade Facilitation Indicators (Figure 4.13). This modest improvement stems from advances in internal and external border co-operation and streamlined documents submission, mainly through the digitalisation of customs procedures and streamlined import/export procedures within the context of the Green Lanes. Further improving the trade facilitation policy environment of the Western Balkan economies will be of particular importance to the region and its overall economic growth. Some studies show that reducing the border waiting times by three hours, for example by implementing national single window solutions, can result in a 1.5-3% increase in real income across the Western Balkans. If these efforts were co-ordinated, the gains would increase to 8%[19] (Gómez, Zárate and Taglioni, 2023[59]).

While the Western Balkans has made strides towards establishing a tariff-free trade environment and facilitating trade, some non-tariff measures (NTMs)[20] continue to hinder trade flows between the economies. Traders identify the most common NTMs as price control measures, additional formalities related to export and import, release and clearance of goods, and sanitary and phytosanitary measures (SPS)[21] (GIZ, 2022[60]). The percentage of companies perceiving cross-border costs as too high for exporting rose from 34% in 2022 to 43% in 2023 (RCC, 2023[61]). The challenge posed by NTMs is that they may inadvertently lead to increased costs of trade through burdensome procedures (GIZ, 2022[60]). As such, the reduction of the negative impact of NTMs is emphasised in the new Growth Plan for the Western Balkans[22] as a means to increase convergence with EU standards and strengthen trade ties between WB6 and the EU.

Figure 4.13. OECD Trade Facilitation Indicators (2022)



Note: The assessment covers Albania, Bosnia and Herzegovina, Montenegro, North Macedonia and Serbia.
Source: OECD (2022[62]).

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Within the context of the Common Regional Market, one of the flagship trade facilitation initiatives in the region is the establishment of Green Lanes. Initially, Green Lanes facilitated trade between only the Western Balkan economies; however, due to their success in streamlining border procedures they now extend to the EU, further contributing to the region's integration into the EU single market (Box 4.6)

Although some progress has been achieved, challenges remain in harmonising regulations, minimising trade barriers and bolstering infrastructure to foster competitiveness and access to markets. Further improvements are needed in terms of electronic data exchange and electronic payments to establish a robust paperless trade environment. Additionally, effective pre-arrival processing and the swift clearance of shipments are crucial components of a paperless trade environment, which is needed to support the rising uptake of e-commerce in the region (see Chapter 5). These practices facilitate faster trade flows and reduce bottlenecks at borders; however, they are not uniformly adopted across the WB6 economies. Efforts to address these obstacles require collaborative initiatives among CEFTA members to streamline

processes and enhance cross-border efficiency, ultimately paving the way for smoother trade operations and economic growth in the region.

Box 4.6. Green Lanes/Corridors as a tool to reduce border waiting times

Green Lanes are a regional co-operation initiative that aims to reduce waiting time in border passages between Western Balkan economies. Launched in 2020 as a response to the COVID-19 pandemic, Green Lanes/Green Corridors are the result of a joint proposal between CEFTA, the Regional Cooperation Council and the Transport Community to facilitate the cross-border transport of necessary[1] goods in the Western Balkans.

During the COVID-19 pandemic, Green Lanes helped preserve trade flows and provided a well-functioning transit system through the improved exchange of information and co-operation between customs administrations. In 2021 a "one-stop-go" model was introduced that further facilitates the two-way transit of goods. The prioritisation of essential goods in transit and the system's simplified procedure lower the time of transit and reduce the transport and trade cost for all businesses. Three months into its launch, Green Lanes accounted for more than 70% of all truck transit in the border crossing points where they were established. The total transit of trucks went from 18 000 trucks in March 2020 to 134 000 trucks in June 2020. This increase in trade volume was also facilitated by the electronic exchange of customs data before the arrival of the transported goods, which helped to significantly reduce waiting times by 30%, or three hours on average, representing the equivalent of a 2% reduction on tariffs (European Commission, 2023[63]).

Green Lanes use the System Exchange of Electronic Data (SEED) infrastructure, a CEFTA initiative in place since 2010 that was subsequently amended with Additional Protocol 5 to become SEED+. A main characteristic of SEED+ is CEFTA TRACES NT, which facilitates the issuance of veterinary and pharmaceutical certificates and entry documents for animals and goods, as well as provides assistance in risk management by notifying authorities of non-compliant consignments for animals and goods. The adoption of the SEED+ system has facilitated the exchange of customs information within the region and between Western Balkan economies and neighbouring EU countries.

The first functional Green Lanes border between North Macedonia and Greece became operational in July 2022, marking a milestone in the region's co-operation with the EU's common single market.

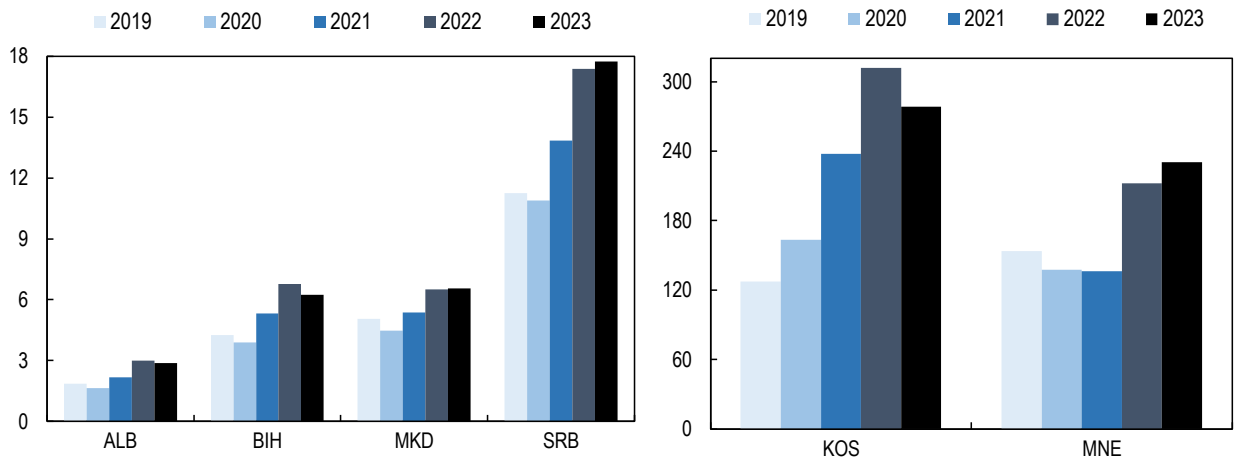
Note: Some of the essential goods included food supplies, livestock, animal feed, chemicals, and medical supplies and equipment.
Sources: European Commission (2023[63]); Transport Community (2023[64]); CEFTA (2024[65]); Berlin Process (2023[66]).

Lack of export capacity among Western Balkan SMEs hinders integration into global value chains

The EU is the region's predominant trade partner, constituting 67.2% of its merchandise exports and 51.9% of imports in 2022. The Western Balkans also directed 35.6% of its total service exports and 36.9% of its imports towards the EU in the same year (CEFTA, 2022[67]). With the use of implemented trade facilitation and regional initiatives, the governments in the region have continued to ensure that they can trade with minimum obstacles. However, the trade trajectory of the Western Balkans is tied to the economic outlook of the EU. Partially affected by the EU's lower growth, some exports of goods from WB6 economies to the EU have decreased (Figure 4.14).

Figure 4.14. Exports of goods from the WB6 economies to the EU (2019-23)

Millions of EUR



Source: Eurostat (2024[68]).

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Increasing efforts to support existing exporters, particularly SMEs, has not translated into the improved participation of SMEs in economies' exports, with the proportion of exports contributed by SMEs remaining stable since 2018, reaching 49.7% in 2021 compared to 49.1% in 2018 (Figure 4.15). While the share has increased in Albania, North Macedonia and Serbia, it has experienced a gradual decline in Bosnia and Herzegovina and Kosovo. However, the WB6 average remains higher than the EU average, which reached 45.5% in 2021 (OECD, 2022[22]).

SMEs can export either directly or through indirect forward participation, which entails supplying inputs to another exporter (WTO, 2019[69]). In the Western Balkans, one of the main obstacles hindering SMEs from exporting is their limited access to information on foreign markets. The scope of capacity-building programmes varies across the region, with many economies lacking a strong emphasis on SME internationalisation. In 2023, 23% of surveyed companies identified lack of export capacity and information as their main obstacle to exporting, marking an increase from 17% in 2022 (RCC, 2023[61]).

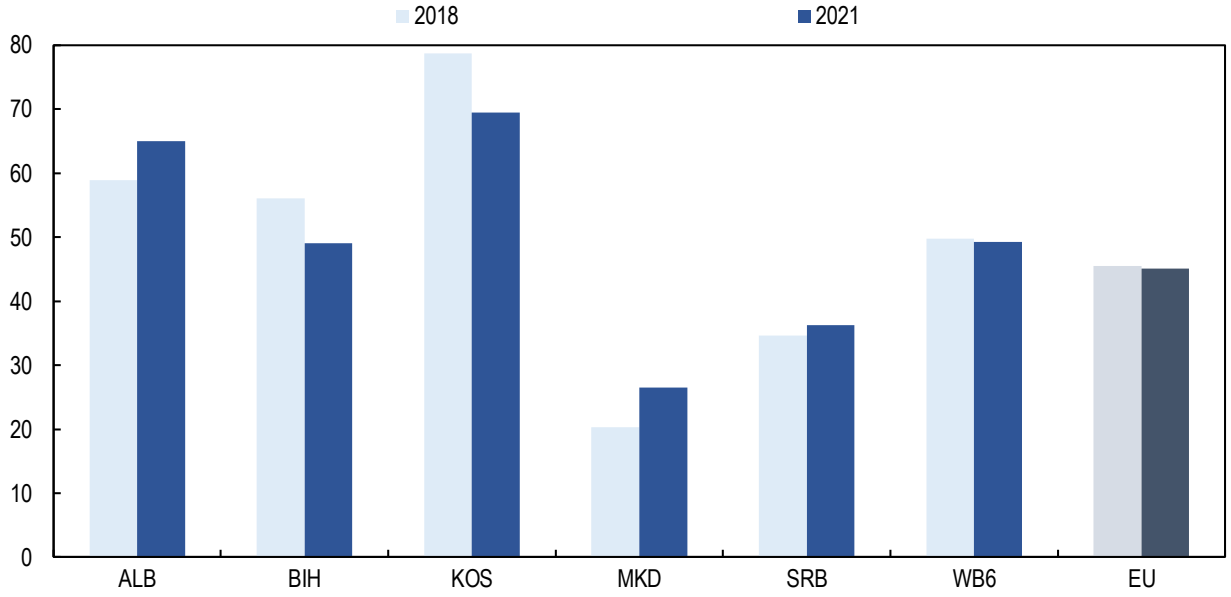
By participating indirectly in exports, Western Balkan SMEs can overcome some of the barriers associated with direct exporting, such as navigating complex international markets, securing financing for expansion and meeting stringent export regulations, thereby improving their export capacity. This approach allows SMEs to leverage the expertise and resources of larger exporters while still benefitting from access to global markets and potential growth opportunities.

Export promotion programmes can help build export capacity among SMEs. Since the last Competitiveness Outlook assessment in 2021, the region has seen progress, with an increasing number of economies implementing more targeted programmes, especially regarding SME integration into GVCs. These programmes have a broader reach and adequate monitoring and evaluation. However, their impact is continuously hampered by the limited human and financial resources of the region's export promotion agencies. The administrative capacity of these agencies is of particular importance in the Western Balkans, where in some economies the agencies have a broad mandate encompassing SME development (Albania, Kosovo, North Macedonia, Serbia) and investment facilitation (Albania, Kosovo, Montenegro, North Macedonia, Serbia). While this is common practice, with 56% of agencies in OECD countries sharing

an export promotion and investment facilitation remit (OECD, 2018[70]), the broader mandate requires enhanced resources.

Figure 4.15. SME contribution to total exports in the WB6 economies and the EU (2018, 2021)

In percentage of total exports



Notes: The last available year for Albania is 2022 and Bosnia and Herzegovina is 2020. No data are available for Montenegro in 2018, 2020 and 2021.
Source: OECD (2022[22]).

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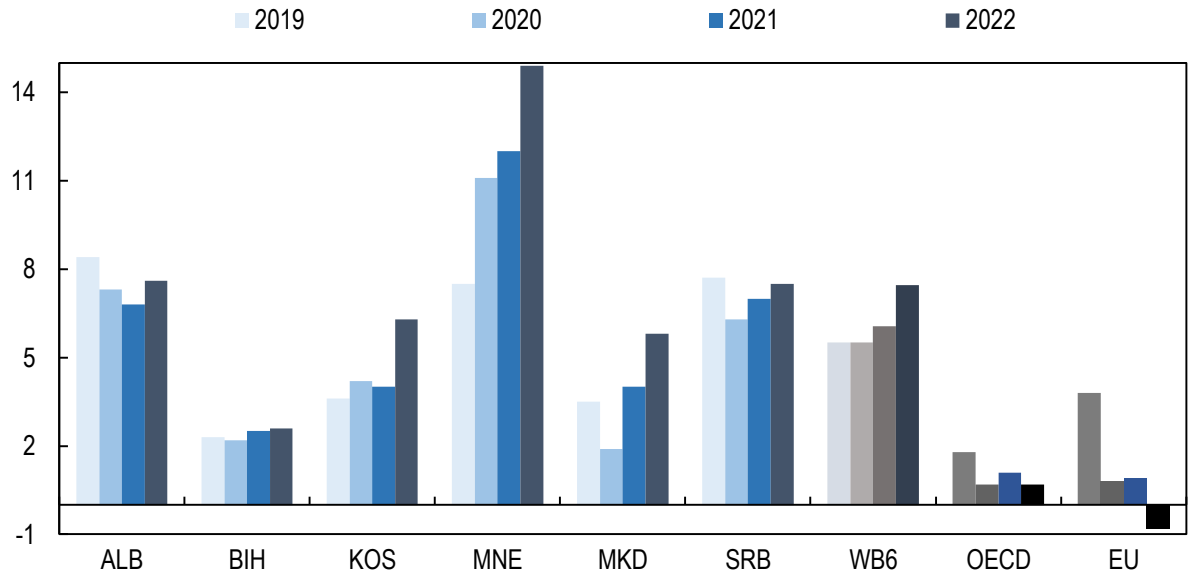
Facilitating foreign direct investment

Providing investors with a stable regulatory environment, transparent and fair policies, and effective implementing institutions can significantly enhance both the quantity and quality of foreign investment. FDI can play a crucial role in enhancing the business environment and competitiveness of local enterprises by fostering technological advancements and expanding market and employment opportunities (OECD, 2015[71]).

Since 2019, net inflows of FDI to the Western Balkans have been uneven, with Montenegro standing out as the largest recipient of FDI in terms of percentage of GDP, followed by Albania and Serbia, with Bosnia and Herzegovina recording the lowest ratio in the region (2.6% of GDP) (Figure 4.16). In terms of net FDI inflows in nominal value, Serbia outperforms the region, attracting a record EUR 4.2 billion in 2023 (National Bank of Serbia, 2024[72]). The highest increases since 2019 were observed in Kosovo and Montenegro, both of which almost doubled their ratios, reflecting a notable surge in foreign investment confidence. The EU remains the main source of FDI in the region, accounting for 70% of FDI inflows (RCC, 2024[52]).

Figure 4.16. Net FDI inflows in the WB6 economies, the OECD and the EU (2019-22)

Percentage of GDP



Sources: UNCTAD (2023[73]); World Bank (2023[74]).

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The WB6 economies consistently outperform EU and OECD countries, partly due to the steady reduction and elimination of statutory restrictions on FDI, as well as a favourable business environment. The WB6 is notably open to FDI, as indicated by the *OECD FDI Regulatory Restrictiveness Index*, and compares favourably to the EU average included in the index[23] (OECD, 2021[42]).

Continued high FDI inflows could also be partially explained by Western Balkan economies becoming an increasingly preferred investment destination for EU companies, especially following the COVID-19 pandemic. This is mostly due to tax incentives, strategic connectivity and the low cost of labour (Vienna Institute for International Economic Studies, 2021[75]). However, to maintain investment attraction and mobilise sustainable investment, the Western Balkans must prioritise skilled labour, modernise education, and improve infrastructure and governance, as well as strengthen the participation of SMEs in global value chains. These are also pre-requisites for the Western Balkans to benefit from the emerging trend of nearshoring. By fostering workforce upskilling and integrating local firms into global supply chains, the region can position itself as a competitive and attractive destination for nearshoring investments (RCC, 2024[52]).

The region's stable investment framework continues to draw investment inflows

Fostering an enabling business environment that attracts investors and fosters sustainable growth relies on establishing a solid legal investment framework. This framework encompasses laws, regulations and policies to streamline investor entry and safeguard their assets. Almost all WB6 economies have implemented comprehensive legal frameworks to support investment. Continuous revisions and updates to investment regimes are underway as economies aim to enhance market access for foreign investors. Across the region there have been improvements in the quality of investment frameworks as governments continuously align their legislation with EU standards.

Moreover, each of the six economies has signed an extensive investment agreement network that provides extra safeguards for foreign investors. Notably, in July 2021 Montenegro introduced a new bilateral investment treaty (BIT) model, while in August 2023, Bosnia and Herzegovina established new foundational principles for a new BIT model. Some economies in the region, such as Albania, are presently revising their current network of BITs to establish a new model that strikes a balance between investor protection and national strategic interests. This entails incorporating protection provisions, balanced with domestic ones to achieve sustainable development objectives.

Since 2019 there has been an increase in the number and size of greenfield investment deals, with Serbia emerging as a prominent recipient of such investment (Table 4.7 and Figure 4.17). The post-pandemic rise of greenfield investment projects in the region and a recent decrease in the inflow of greenfield investment projects to the EU[24] suggest an increasing confidence among investors towards the Western Balkan investment environment. The inflow of greenfield investment projects offers domestic companies an opportunity to become partners or suppliers to incoming multinational investors and create new export opportunities. FDI inflows in the Western Balkans have historically focused on less knowledge-intensive sectors[25]; however, there is growing evidence of higher technology and capital-intensive sectors attracting more greenfield investment projects in the Western Balkans. The largest increases in both the number of announced greenfield investment projects and their pledged value occurred in the electricity, business services, and sales and marketing sectors (Vienna Institute for International Economic Studies, 2022[76]). As the WB6 continue to attract FDI inflows and gradually increase greenfield investment projects, it will be crucial to direct investment to strategic sectors with the highest potential for technology and knowledge transfer.

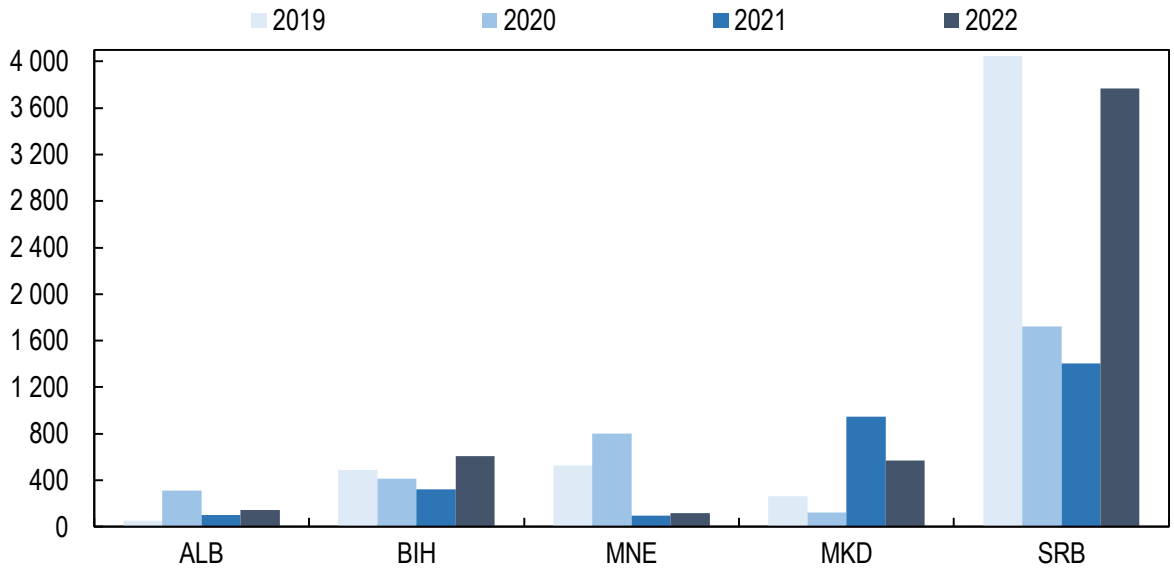
Table 4.7. Number of greenfield investment deals in the WB6 economies (2019-22)

	2019	2020	2021	2022
ALB	3	5	3	7
BIH	30	13	11	19
MNE	10	5	3	9
MKD	13	3	19	29
SRB	117	42	44	99

Note: Data for Kosovo are unavailable.
Source: UNCTAD (2023[77]).

Figure 4.17. Greenfield investment volumes by destination in the WB6 economies (2019-22)

Millions of EUR



Notes: Data for Kosovo are unavailable. Data have been converted from USD using the European Central Bank average exchange rate for 2024 of 1 USD = 0.9222 EUR.
Source: UNCTAD (2023[77]).

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The region relies on generous tax incentives to foster business activity and create an investment-friendly environment

All WB6 economies offer an array of **investor incentives**. These incentives have been a cornerstone strategy for WB6 economies and include tax reductions, social contribution exemptions, customs duty relief, tax holidays, salary subsidies and investment grants. Special economic zones and strategic investment laws also play significant roles, receiving preferential treatment in administrative processes and enhancing the WB6's investment attraction strategies.

The WB6 economies offer generous **tax** incentives to businesses operating within their borders. Most economies offer several types of incentive, with the most common being for intellectual property (in Kosovo, Montenegro, North Macedonia, Serbia and FBiH). Other common incentives include those for SMEs, research and development (R&D), and staff training. The scope of these investments varies: for instance, while Kosovo's R&D incentives are only available for firms working with minerals or natural resources, Albania offers R&D incentives for any scientific research and development area.

Regardless of the target of these incentives, most economies rely on a mix of cost- and profit-based tax incentives, with little evidence showing any shift towards the increased use of cost-based incentives. Exceptions to this trend include Serbia, where the 2018 tax reform mainly introduced cost-based incentives, and the two entities of Bosnia and Herzegovina. Profit-based tax incentives may reduce effective corporate tax rates below 15% and are less efficient in stimulating investment than cost-based incentives. In the past, profit-based tax incentives in WB6 economies were used to compensate for non-tax constraints to productivity, such as a lack of infrastructure.

Developments in the international tax system are thus an opportunity for WB6 economies to increase tax revenue through growth-oriented policies that aim to improve available infrastructure and attract additional jobs and investment. The economies will need to maintain an attractive business climate to attract additional investment; however, this will not necessarily require tax incentives, but rather investment in infrastructure, skills and other measures to enhance productivity. Policy makers may wish to reassess tax incentives in the context of the GloBE Rules and introduce a Qualifying Domestic Minimum Top-Up Tax (QDMTT) not to forgo revenue (OECD, 2021[78]). Jurisdictions that adopt the GloBE rules (which are not mandatory) will apply an effective tax rate test using a common tax base and a common definition of covered taxes to determine whether a multinational enterprise is subject to an effective tax rate below the agreed minimum rate of 15% in any jurisdiction where it operates. This means that in-scope ultimate parent entities of multinational enterprise groups that have their headquarters in a jurisdiction that has implemented the GloBE Rules and that operates a subsidiary (or constituent entity) in WB6 economies may be subject to a top-up-tax in the residence jurisdiction if the profits earned in the subsidiary are taxed at an effective rate below 15%. The top-up-tax is levied on the parent entity to bring the multinational enterprise's effective tax rate on income from low-taxed constituent entities up to the minimum rate. Consequently, WB6 economies that levy an effective tax rate below 15% on profits of in-scope businesses will forego tax revenue, as these profits will be taxed in the residence jurisdiction instead. The rules apply to constituent entities that are members of a multinational enterprise group with an annual revenue of EUR 750 million or more (OECD, 2021[78]). Montenegro is the only WB6 economy that plans to implement a QDMTT.

Regional governments must exercise caution when using fiscal incentives to attract investment. International evidence indicates that incentives can be costly for governments and may not adequately address fundamental shortcomings in investment conditions, such as the rule of law or public governance. (EBRD, 2024[79]; OECD, 2023[80]). Between 2021 and 2024, the Western Balkan economies generally improved in evaluating tax incentives for businesses. Regular tax expenditure (TE) reporting can improve the efficiency of tax incentives by facilitating independent and transparent evaluations. In economies that have adopted TE reporting, the resulting data can also aid in conducting cost-benefit and distributional analysis and show how tax relief is allocated across various taxpayer groups, thereby promoting a fairer tax system. Albania continues leading TE reporting, and RS completed its first TE report in 2023. North Macedonia plans to report TE more regularly in the budget from 2025. Kosovo, while calculating some TE, has yet to publish a publicly available report regularly. Montenegro and Serbia currently do not regularly and systematically report TE.

Inefficient judicial systems in the Western Balkans could deter foreign investors

Investors attempting to enter the Western Balkan market can overall rely on sound investor regulations, with improved transparency since the last Competitiveness Outlook in 2021. However, the Western Balkan economies fall short when it comes to contract enforcement, dispute settlements and efficient alternative dispute resolution, which potentially reduces attractiveness for foreign investors.

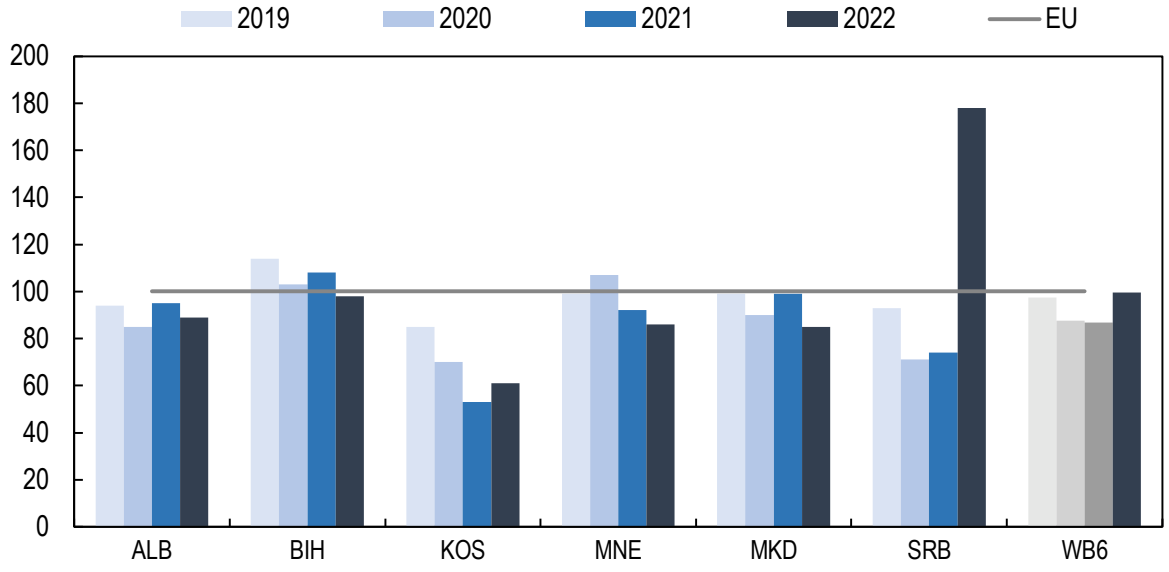
A robust judiciary is essential for ensuring fair business conditions, protecting property rights and enforcing contracts (RCC, 2024[52]); however, there are shortcomings in the efficiency of the judicial system in all WB6 economies. Despite reforms undertaken since the last assessment cycle in Albania, Kosovo, North Macedonia and Serbia, there have been no significant improvements in clearance rates,[26] which decreased in all economies (except Serbia) from 2021 to 2022. Nevertheless, clearance rates overall remain below the EU median of 100% (Figure 4.18). The disposition time[27] for cases has increased in all economies except Serbia, which stands out in the region and is the closest to converge with the EU median of 234 days to process a first instance court case, followed by North Macedonia (Despite the well-developed legal frameworks for alternative dispute resolution (ADR) in the region, the adoption rate remains low. The minimal utilisation of ADR mechanisms in Western Balkan economies hinders their

effectiveness in alleviating the burden on the courts. Only 6% of judges in the Western Balkans regularly suggest mediation in commercial court proceedings, which underscores the limited integration of ADR methods within the region's legal systems . The Western Balkans struggles with enforceability and awareness-raising capacity. Given that case backlog is perceived as the main obstacle to achieving judicial efficiency in the region , efforts to improve the take-up of mediation mechanisms should be intensified.

Figure 4.19). Kosovo is an outlier in the time to process civil and commercial court cases, although the recent establishment of a dedicated commercial court is poised to significantly improve the disposition and clearance rate for commercial cases (see Economy profiles).

Figure 4.18. Clearance rate for first instance court cases in the WB6 economies and the EU (2019-2022)

Percentage of cases



Notes: The data cover civil and commercial litigious cases. The data for the EU refer to the 2021 benchmark.
Source: CEPEJ (2022[81]).

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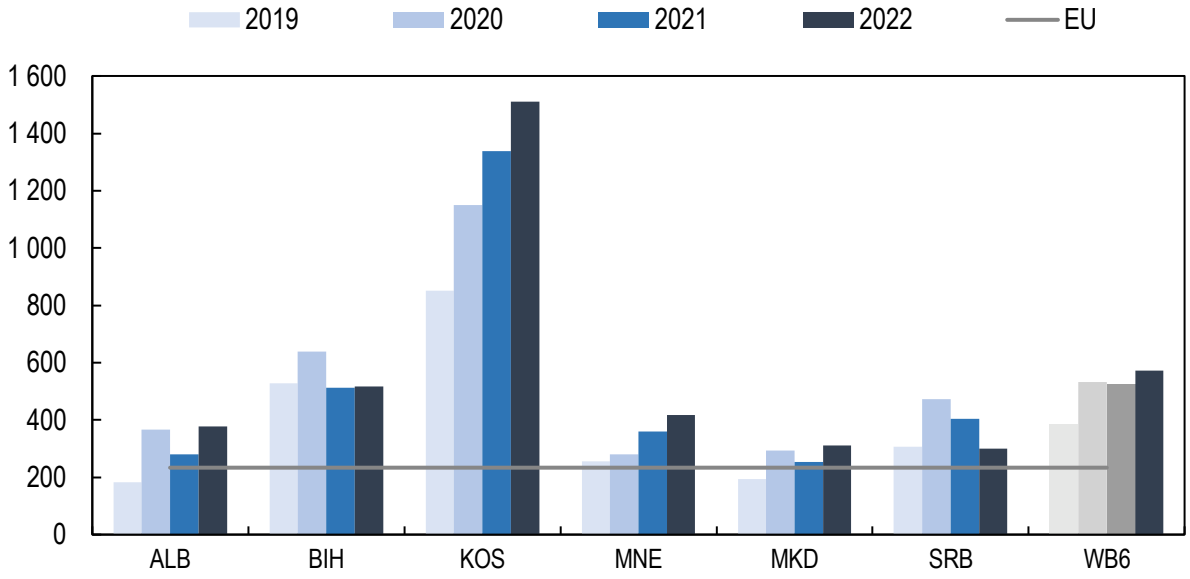
Despite the well-developed legal frameworks for alternative dispute resolution (ADR) in the region, the adoption rate remains low. The minimal utilisation of ADR mechanisms in Western Balkan economies hinders their effectiveness in alleviating the burden on the courts. Only 6% of judges in the Western Balkans regularly suggest mediation in commercial court proceedings, which underscores the limited integration of ADR methods within the region's legal systems (RCC, 2021[82]). The Western Balkans struggles with enforceability and awareness-raising capacity. Given that case backlog is perceived as the main obstacle to achieving judicial efficiency in the region (RCC, 2024[83]), efforts to improve the take-up of mediation mechanisms should be intensified.

Figure 4.19. Clearance rate for first instance court cases in the WB6 economies and the EU (2019-2022)

Days



Notes: The data cover civil and commercial litigious cases. The data for the EU refer to the 2021 benchmark.
Source: CEPEJ (2022[81]).

StatLink https://stat.link/2fp8ku

Recommendations for business growth

By providing a conducive environment with clear guidelines, economies can enhance their appeal to foreign investors, thus fostering economic growth and development. Moreover, by placing emphasis on policies that facilitate business expansion through boosting exports and further fostering cross-border trade, governments can help companies tap into new markets, access a wider array of resources and bolster their competitiveness on the global stage. Policy makers in the Western Balkans should:

- **Accelerate the implementation of trade facilitation measures and eliminate prohibitive non-tariff measures.** While progress has been observed since the last assessment cycle, especially in terms of streamlining the submission of trade documentation and reducing trade costs, mainly through the Green Lanes initiative, more targeted efforts are needed to automate border procedures. This entails further simplifying customs procedures, upgrading trade infrastructure, adopting electronic documentation systems, providing capacity-building programmes, enhancing regulatory co-operation, facilitating trade finance, and engaging in regional and international collaboration. By expediting the implementation of these measures, economies in the Western Balkans can significantly reduce trade barriers, boost cross-border trade flows and enhance competitiveness.
- **Prioritise the transition to a paperless trade environment.** Adopting digital trade solutions could streamline customs and border control processes, cutting down on bureaucratic obstacles. Electronic documentation would enhance efficiency, decrease errors and shorten processing times. Accelerating the implementation of national single window solutions for customs would further facilitate trade operations and promote harmonisation across borders.

- **Encourage a shift toward cost-based incentives**. The low CIT rates across the region undermine the need to offer substantial profit-based incentives. As such, economies should review their use of profit-based CIT incentives and special development zones and consider a more sustainable and effective approach, such as raising revenue to invest in non-tax factors such as education and infrastructure that will attract investment and foster a sustainable and competitive business climate.
- **Start estimating additional investment created by tax incentives**. Regular tax expenditure reporting and cost-benefit analysis of tax incentives could help governments better understand which investment incentives achieve their purpose and which are inefficient.
- **Identify and support sectors strategic for nearshoring.** The WB6 economies stand to gain from the nearshoring trends in the post-pandemic era. However, governments must adopt a proactive approach and use available policy tools to benefit from these opportunities fully. Furthermore, investment promotion agencies should refine their strategic focus on key sectors, emphasising those with the greatest potential for growth and development. They should tailor their marketing efforts to attract investors to these strategic sectors while collaborating with governments to create supportive policies and streamline regulatory processes (see example from Mexico in Box 4.7).

Box 4.7. Investment promotion efforts to boost nearshoring: Evidence from Mexico

The global trend of company relocation is reshaping global value chains across strategic sectors. Nearshoring, which involves businesses streamlining their value chains by locating closer to their core markets, has been increasing since the 2008 economic crisis, and has been further triggered by the COVID-19 pandemic and geopolitical tensions.

In October 2023, Mexico started offering fiscal incentives to companies in key export industries, which were identified in a sectoral analysis conducted by the government. The key strategic sectors identified were semiconductors, the automotive industry, electrical and electronic equipment, medical devices and pharmaceuticals, agribusiness, and food products. The financial incentives offered include additional tax deductions for workforce training and retraining, and accelerated depreciation for investment in new assets.[1] These measures aim to promote nearshoring by encouraging companies to move part of their production to Mexico. Moreover, the Mexican government has intensified efforts to attract nearshoring investment and enhance the inclusion of SMEs as suppliers or partners for investors and companies relocating to the country. Through the Mano a Mano programme, a comprehensive policy package, the government supports SME integration into global value chains and boosts their absorption capacity, which is necessary for successful knowledge and technology transfers.

According to a recent study by the Mexican Institute of Competitiveness, FDI related to supply chain relocation in Mexico rose by 47% in the first three quarters of 2023 (Mexican Institute of Competitiveness, 2024[84]). This shift favours European, Canadian or Asian companies seeking to export to the United States while benefitting from Mexico's tariff-free regime. In 2023, the proportion of Mexican businesses perceiving an impact from business relocations surged to 21.5%, marking a notable increase from the 10.1% observed between 2020 and 2022. This figure is projected to rise further to 40.6% by 2024-25 (Banco de México, 2023[85]).

Note: Accelerated depreciation allows companies to write off new assets more quickly, providing immediate tax benefits and encouraging investment by improving short-term cash flow.
Sources: González Pandiella and Maravalle (2024[86]); Banco de México (2023[85]); OECD et al. (2023[87]); UNCTAD (2023[88]).

- **Increase the uptake of alternative dispute resolutions.** Despite the prevalence of legal frameworks for mediation and alternative dispute resolutions, uptake remains low. Running awareness workshops, capacity building and information campaigns could contribute to increasing demand for mediation solutions. Creating a centralised portal containing all necessary legislation and a step-by-step guide to ADR could also streamline and facilitate the procedure for companies.

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Notes

[1] In 2022, banks accounted for 91% of total financial system assets in Albania (Bank of Albania, 2022[89]), 88% in Bosnia and Herzegovina (Central Bank of Bosnia and Herzegovina, 2022[93]), 94.2% in Montenegro (Central Bank of Montenegro, 2024[94]) and 91.1% in Serbia (National Bank of Serbia, 2022[97]). The dominance of bank finance is slightly lower in North Macedonia and Kosovo, where banks respectively control 79.2% (National Bank of the Republic of North Macedonia, 2023[90]) and 68.3% (Central Bank of the Republic of Kosovo, 2023[91]) of total financial assets.

[2] For positions lower than EUR 1 million, exposures to non-defaulted SMEs can have their risk weights reduced to 0.7619 from 0.85. For positions exceeding EUR 1 million, the risk weight remains at 0.85.

[3] This figure does not consider Albania and Kosovo, which do not have any publicly listed companies.

[4] Harmonisation is planned in Montenegro by the end of 2024, and harmonisation projects are in the drafting phase in Albania and RS without a specific timeline communicated. The UCITS directive aims to provide a single European market for investment funds and allows for selling these funds to retail investors throughout the EU (https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:02009L0065-20140917).

[5] MiFID II is a comprehensive set of regulations enhancing investor protection, increasing transparency and standardising regulatory disclosures across financial markets (https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0065). Serbia has aligned its capital market regulations with MiFID II but not with MiFIR, a set of regulations that complements MiFID II within the EU. It directly addresses issues such as transaction reporting, pre-and post-trade transparency, access to clearing and trading venues, and regulating commodity derivatives (https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014R0600).

[6] The AIFMD directive regulates the activities of alternative investment fund managers (AIFMs) within the EU (https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32011L0061). Legislation for alignment with AIFMD is in the drafting phase in Montenegro and North Macedonia, without a specific deadline communicated for future adoption and implementation

[7] The registration of assignments is not covered in Serbia.

[8] FBiH is preparing legislation to exclude interests calculated under financial leasing contracts from the VAT calculation base and extend fiscal incentives similar to those for factoring activities. No specific timeline has been communicated.

[9] As shown in OECD (2020[95]), adults in South East Europe scored on average about 57% of the maximum possible, lower than comparable scores obtained through the same methodology from surveys of European Union and OECD member countries, at 64% and 65%, respectively.

[10] On 21 July 2014, the OECD released the full version of the Standard for Automatic Exchange of Financial Account Information (AEOI) in Tax Matters. The Standard calls on governments to obtain detailed account information from their financial institutions and automatically exchange it with other jurisdictions annually. The Standard provides annual automatic exchange between governments of financial account information, including balances, interest, dividends and sales proceeds from financial assets reported to governments by financial institutions and covering accounts held by individuals and entities, including trusts and foundations. It sets out the financial account information to be exchanged, the financial institutions that need to report, the different types of accounts and taxpayers covered, as well as common due diligence procedures to be followed by financial institutions.

[11] SOEs held only by the central entity governments (notably excluding a large number of municipal utilities companies) employ 58 000 people, accounting for 8.4% of total employment in Bosnia and Herzegovina.

[12] This comparison is imperfect as OECD-area data relate to SOEs' share of non-agricultural, rather than total, employment. If the OECD figures used total employment, then the employment contributions of SOEs in the Western Balkans economies would appear larger in comparison.

[13] Data on the characteristics of SOEs in the region relate to end-2022, or latest available, and are based primarily on reporting by the national authorities in the context of this assessment, with some exceptions. For Bosnia and Herzegovina, only the number of SOEs is presented in this assessment and is based on IMF (2019[41]), while sectoral distribution data were not available and therefore not included in regional figures. For North Macedonia, figures on SOEs' sectoral distribution are based on earlier reporting by the national authorities published in OECD (2021[42]) concerning the year 2018 and only cover 23 entities (rather than the 30 SOEs reported by the Ministry of Finance to be held by the central government). For Albania, employment figures on 23 enterprises were not available and are therefore not included.

[14] The primary sector includes agriculture, fishing, forestry and mining.

[15] Kosovo already has predominantly centralised ownership arrangements, wherein the vast majority of SOEs are overseen by the Ministry of Economy and monitored by a dedicated unit. In Serbia, new legislation foresees a greater centralisation of SOEs under the Ministry of Economy. In RS, the 2024-2026 Economic Reform Programme of the RS establishes the ambition to improve SOE management and supervision practices and to restructure SOEs in the energy and rail sectors to improve their efficiency. RS has also established a new SOE performance monitoring unit with ambitious SOE data collection plans that have the potential to inform improvements in state shareholding practices and SOE performance. Kosovo and Montenegro have announced but not yet implemented plans to introduce legislative reforms to improve central SOE monitoring and co-ordination arrangements.

[16] The near-term privatisations of several small SOEs have nonetheless been announced in three economies (Montenegro, RS and Serbia). In 2022, the authorities of North Macedonia announced an

ambition to privatise, or partially privatise, the national postal services operator, but no definitive plans have yet been undertaken.

[17] Regional Anti-Corruption Initiative (RAI) is an intergovernmental regional organisation that deals with anti-corruption issues in nine member states: Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Moldova, Montenegro, North Macedonia, Romania and Serbia, see https://rai-see.org/.

[18] The Additional Protocol 6 on Trade in Services entered into force on 11 January 2021.

[19] 8% more relative to the scenario in which each economy implements the trade facilitation measures independently.

[20] Non-tariff measures refer to all policy measures aside from tariffs and tariff-rate quotas that have some degree of influence on international trade. These measures can be categorised into two main groups: 1) "technical" measures, which encompass regulations, standards, testing and certification, with a focus on sanitary and phytosanitary (SPS) and Technical Barriers to Trade (TBT) measures; and 2) “non-technical” measures, which include quantitative restrictions (quotas, non-automatic import licensing), price measures, and enforced logistics or distribution channels (OECD, 2024[96]).

[21] GIZ surveyed 238 companies for the study of NTMs and their impact on traders.

[22] The European Commission has introduced the new Growth Plan for the Western Balkans, designed to draw the Western Balkan partners nearer to EU standards by providing them with certain EU membership benefits ahead of accession, thereby stimulating economic growth.

[23] Bulgaria, Cyprus and Malta were not included in the assessment.

[24] From 2019 to 2020 there was a considerable decrease in the number of greenfield investment projects coming to the EU. Having fallen from 6 337 in 2019 to 4 847 in 2020, they experienced a temporary increase due to the COVID-19 pandemic to reach 5 854 in 2021. In 2022, they amounted to 5 710 (UNCTAD, 2023[77]).

[25] In 2019, 83% of incoming FDI was in real estate, while 12% was in construction (World Bank, 2019[92]).

[26] Clearance rate is calculated by dividing the number of resolved cases by the number of incoming cases in a given year.

[27] The Calculated Disposition Time sheds light on the efficiency of the judicial system by comparing resolved with unresolved cases over a reporting period, indicating how quickly cases are processed and providing insight into overall proceedings length.

5 Digital transformation cluster

This cluster investigates the role of digital transformation in enhancing connectivity, fostering innovation, and creating inclusive and sustainable societies in the Western Balkans. Structured around three key sections, it evaluates the breadth and effectiveness of policy frameworks and implementation. First, it focuses on how to strengthen the foundations of the digital ecosystem by exploring existing efforts to enhance digital infrastructure and access, and to establish a trustworthy and secure digital environment. Second, it analyses the uptake of digital technologies in both public and private sectors, and delves into initiatives to foster technological innovations to unleash the region's digital potential. Finally, it assesses societal and environmental impact, probing efforts to bridge the digital divide and design inclusive and sustainable digital policies.

Key findings

The six Western Balkan (WB6) economies have made some progress in digitalisation in recent years and are slowly converging towards European Union (EU) levels. Some of the region's key achievements are:

- Broadband coverage and quality have improved, with an annual increase of 3.8 percentage points in available fibre connections, rising from 29.2% in 2021 to 33.0% in 2022. Four economies have joined the Balkans Digital Highway initiative to improve high-speed broadband access at local and regional levels. Furthermore, the region is increasingly implementing initiatives to address connectivity disparities between urban and rural areas.
- Spurred by concerns over digital threats and data breaches, WB6 economies are increasingly focusing on improving public perception and capacity regarding privacy and data protection. Notable advancements have been made in updating policy and legal frameworks regarding cybersecurity, and privacy and data protection,
- Progress has been made in digitalising government services, including investment in digital infrastructure and user-centric e-service portals. Economies have also made headway in developing key enablers for digital government, such as improving relevant legislation, implementing electronic identification and payment systems, and integrating these systems with national e-service portals. All WB6 economies have joined the Digital Europe Programme, which provides opportunities for businesses and public administration to participate in projects that deploy innovative digital technologies across the EU.
- WB6 economies are increasingly focusing on supporting small and medium-sized enterprises (SMEs) to adopt digital technologies, develop e-commerce and e-business, and engage in digital innovation. Efforts have been intensified to promote information and communication technology (ICT) investment through programmes that offer monetary support for purchasing ICT equipment and services, as well as consulting and mentoring services.

Despite these positive regional trends, a fundamental reimagining of business models and operations, government decision-making processes, and co-ordination mechanisms across the entire economy is still needed. As such, some of the key challenges to the digital transformation facing the region are:

- The lack of electronic accessibility of digital government services, public websites and applications in the WB6 exacerbates the marginalisation of people with disability. The non-binding nature of accessibility rules in some Western Balkan economies, and co ordination deficiency in enforcing them in others, perpetuates inequality and exclusion, as these individuals face barriers to accessing critical government information, services and benefits.
- Insufficient funding limits the number of businesses benefiting from ICT adoption, with only 63.7% of WB6 enterprises having a website, compared with 78.1% in the EU. This creates challenges for the digitalisation efforts of businesses, particularly given the shortage of digitally skilled workers. This gap often creates a heavy reliance on EU and donor support across most regional economies.
- Limited cross-border interoperability hampers WB6 economies' aspirations to facilitate the free movement of workers and citizens across the region and join the European Digital Single Market.
- Lack of important reforms for protecting critical infrastructure and tangible initiatives to enhance cybersecurity capacities in public administration leave the region particularly sensitive to data

breaches and misuse. Inadequate resources and capacities of the relevant institutions persist, with understaffing a common issue across most regional economies.

- The region has yet to develop policies to ensure the integration of green digital technologies and environmentally sustainable practices into digitalisation processes. The WB6 economies have not formally assessed the environmental footprint of the digital sector in the public and private sphere, and have yet to evaluate the environmental impact of government and business digitalisation. Programmes and initiatives specifically designed to foster a green digital sector are absent.

Introduction

Digital transformation affects all sectors and permeates many facets of society, cutting across traditional boundaries and impacting governance, economy, education and beyond. Embracing digital transformation at a national level requires collaborative efforts across government, industry, academia and civil society to drive innovation, enhance efficiency and ensure inclusive development in an increasingly interconnected world. Fostering digital transformation at the regional level demands the synchronised efforts of all WB6 economies.

Strengthening the foundations of the digital ecosystem

Enhancing infrastructure and access for digital transformation

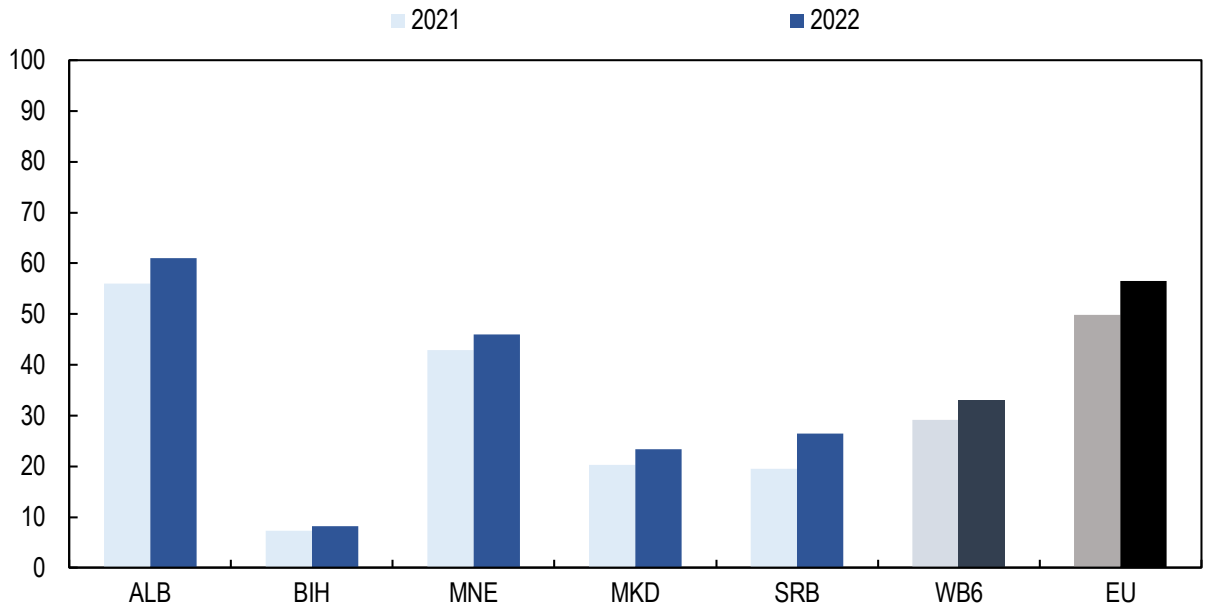
Most WB6 economies have taken steps to enhance digital infrastructure and access by adopting dedicated national broadband development strategies or integrating broadband infrastructure development targets into their sectoral or horizontal development policies. Four economies (Albania, Kosovo, North Macedonia and Serbia) have recently updated their broadband development policies to encompass Gigabit Society targets to ensure that very high capacity connectivity (above 100 megabits per second [Mbps]) reaches citizens and businesses. Meanwhile, Montenegro has outlined targets for very high-speed Internet access, without specifying gigabit connectivity objectives at this stage.

High-speed network infrastructure and broadband penetration in the Western Balkans are advancing, but still lag behind EU and OECD standards

Broadband infrastructure in the WB6 has seen significant advancements in coverage and service quality since 2021. Although the scale of investments in high-speed network infrastructure varies across regional economies, there has been a consistent annual increase in available **fibre connections** (FTTx) throughout the region (Figure 5.1).

Figure 5.1. Fibre connection penetration in the WB6 economies and the EU (2021-22)

% of broadband connections



Note: No data available for Kosovo.
Sources: Eurostat (2024[11]); data received from ALB (AKEP), BIH (BHAS), MNE (EKIP), MKD (AEC), SRB (RATEL).

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However, despite increasing network infrastructure, high-speed Internet connectivity is not yet universally available in the WB6, with both mobile and fixed broadband penetration rates lagging behind the EU and OECD averages (Figure 5.2).

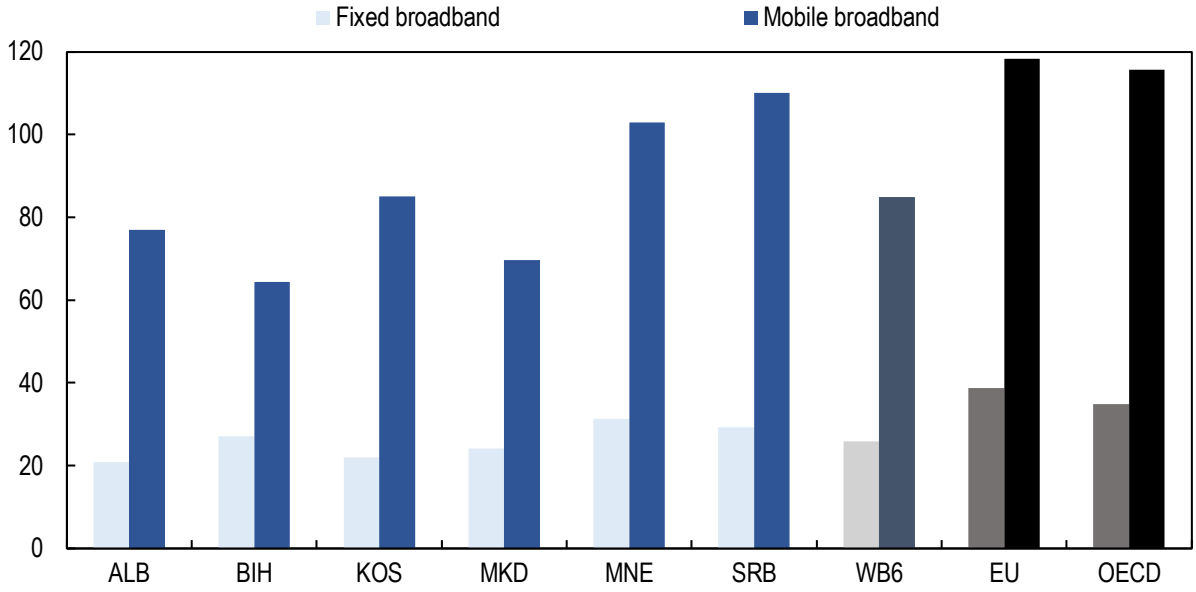
In terms of **mobile broadband penetration**, Montenegro and Serbia[1] have nearly reached EU and OECD average levels; however, Kosovo, Albania, North Macedonia, and Bosnia and Herzegovina significantly trail behind (Figure 5.2). The slow uptake of mobile broadband in Bosnia and Herzegovina, which is the lowest in the region, can be attributed to the delayed introduction of 4G technologies, which only occurred in 2019. North Macedonia, Albania and Kosovo face particular challenges due to relatively lower levels of private sector investments.

Granting 5G licences to telecommunications companies incentivises investments in 5G infrastructure, which can improve network capabilities and expand access to high-speed mobile broadband services. Nevertheless, as of early 2024, only Kosovo, Montenegro and North Macedonia have awarded commercial 5G licences. Delaying 5G deployments hinders access to faster data speeds and an increasing range of connected devices and transformative technologies and applications such as the Internet of Things (IoT), autonomous vehicles and augmented reality.

Fixed broadband penetration rates reflect a similar trend, with Montenegro and Serbia taking the lead, closely followed by Bosnia and Herzegovina. However, in Albania, Kosovo and North Macedonia, fixed broadband uptake falls below the regional average due to lower quality infrastructure, unavailability of networks in some regions, affordability and low demand.

Figure 5.2. Fixed and mobile broadband penetration in the WB6 economies, the EU and the OECD (2022)

Connections per 100 inhabitants



Sources: Eurostat (2024[2]); data received from BIH (CRA), KOS (ARKEP); OECD (2024[3]); ITU (2024[4]).

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Regional economies are developing comprehensive plans to effectively address the rural-urban broadband divide

The Western Balkan Digital Agenda has underscored the importance of investing in regional broadband connectivity. However, the challenge of increasing broadband penetration rates remains particularly pronounced in WB6 economies due to their significant rural populations.[2] Recognising the disparities between urban and rural broadband connectivity, the majority of WB6 economies have prepared dedicated policy initiatives focused on rural broadband infrastructure development and private sector investment stimulation in underserved areas. Boosted by EU and donor funding that strategically supports digital infrastructure projects under the Western Balkan Investment Framework (WBIF), most economies in the region are either implementing (Kosovo and Serbia) or preparing (Albania is well advanced, and Montenegro and North Macedonia are in the initial stages) high-speed network development projects with a focus on rural areas (WBIF, 2024[5]). However, Bosnia and Herzegovina has yet to launch a similar initiative in underserved areas.

Economy-specific endeavours are augmented by the regional Balkans Digital Highway initiative,[3] which pledges to improve access to high-speed broadband services both at economy and regional levels among the four participating economies (Albania, Kosovo, North Macedonia and Montenegro). This donor-funded initiative seeks to establish a regional wholesale broadband network leveraging the optical fibre infrastructure of participating transmission system operators (primarily electricity power utility companies).

Most Western Balkan economies have made strides in developing tools and regulatory measures to facilitate the deployment of broadband networks

Western Balkan economies have made progress since the last Competitiveness Outlook assessment in 2021 (CO 2021) in developing broadband infrastructure mapping systems similar to those available in EU member states. These systems offer valuable insights into the availability, technology and speed of broadband infrastructure, as well as the quality of broadband Internet services at the local level. They serve as an impartial market and provider overview, mitigating investor uncertainty and helping to identify coverage gaps and more efficient resource allocation in bridging the digital divide.

Albania, Kosovo, Montenegro, North Macedonia and Serbia have already implemented mapping systems. By contrast, although geoportals in the two entities of Bosnia and Herzegovina – Federation of Bosnia and Herzegovina (FBiH) and Republika Srpska (RS) – provide some information on broadband infrastructure, the economy has yet to plan the development of a nationwide broadband mapping system. This delay is primarily attributed to factors such as an underdeveloped digital cadastre and the complexity of permit regimes for construction works at the various administrative levels, which complicates the associated data collection process.

Despite the progress made by most WB6 economies in streamlining network deployment processes to attract investments in high-speed communication infrastructure, several significant issues remain. Most notably, WB6 economies have yet to fully streamline the criteria for subsidising infrastructure development and demand creation, and are yet to fully address persisting hurdles related to infrastructure sharing, co-ordinating civil works, and reducing the timeframe and cost of issuing permits for infrastructure development, which are essential for making investments more cost effective.

The region is still facing relatively high costs and administrative burdens for the development of broadband networks. While Albania, Kosovo, Montenegro and North Macedonia have updated relevant legislation in 2022 and 2023, in accordance with EU legislation,[4] the alignment process is not yet complete, mostly due to legacy legislation harmonisation issues, particularly at the local administration level where the lack of co-ordination, cost-sharing and time-efficiency for civil works for infrastructure projects among relevant stakeholders remains a significant investment barrier. Serbia has yet to update relevant legislation, while Bosnia and Herzegovina has not yet adopted relevant regulations, which negatively affects network investments.

The modernisation of state aid rules for broadband infrastructure development would streamline the criteria for new investments in very high-speed networks and mobile networks, including 5G, while avoiding market distortion (see Chapter 2). Regional economies would benefit from alignment with the revised European Commission state aid guidelines,[5] enforced in 2023, which effectively address these issues in line with Gigabit Society targets. Updating relevant legislation in the WB6 economies would streamline processes and stimulate the private sector investments necessary for completing ongoing or planned rural high-speed network development initiatives.

Regulations aimed at simplifying and accelerating the installation of 5G networks, including alignment with the EU 5G Toolbox and Connectivity Toolbox,[6] and outlining specifications for small-area wireless access points (small antennas) are still pending in WB6 economies. These regulations are crucial for fostering the deployment of advanced telecommunications infrastructure and promoting technological innovation in the region.

Creating a trustworthy and safe digital environment

The rise of connectivity and the data-driven economy presents new challenges in digital security and privacy, emphasising the need for updated policies and practices to cultivate and uphold trust in the digital realm.

Policy initiatives on cybersecurity have accelerated, but capacity constraints and limited international co-operation hinders progress

WB6 economies have experienced a notable increase in cyberattacks in the past three years, which have primarily targeted critical online infrastructure, public services and ICT systems. Insufficient public awareness and **cybersecurity** capacities, combined with limited regional collaboration, have compounded the challenges faced by the region's economies in combating cybercrime. Recognising deficiencies in managing cybersecurity risks, all regional economies except Bosnia and Herzegovina have adopted cybersecurity strategies and focused on implementing legal reforms aligned with the EU cybersecurity framework, and in line with the Digital Agenda for the Western Balkans and the Multiannual Action Plan for a Regional Economic Area.

As of early 2024, Albania was the only Western Balkan economy with an established National Cybersecurity Authority[7] operating as a national focal point for cybersecurity, similar to network and information system (NIS) authorities in EU member states that are part of the NIS Co-operation Group. Kosovo and Serbia have articulated plans to establish their own national cybersecurity authorities in 2024, and North Macedonia is awaiting the adoption of a new information security law in 2024 that outlines the establishment of its own agency.

Efforts have also been made to strengthen structures for information security risk management, such as computer emergency response teams (CERTs) that aim to safeguard both public and private sector infrastructure, while fostering collaboration and information exchange across teams. However, a significant gap remains between the acknowledged importance of cybersecurity and the resources allocated to address it. While national CERTs are operational in all WB6 economies except Bosnia and Herzegovina, where there is only an entity CERT in the RS, they face substantial challenges, primarily due to limited staffing and funding. This constraint hampers their ability to conduct crucial awareness-raising and capacity-building activities, as well as to invest in international information exchange with counterpart organisations abroad. Additionally, although there is a growing presence of computer security incident response teams (CSIRTs) within both public entities and large private sector firms, progress in this area has been sluggish, lacking a systematic level of collaboration among these teams and the national CERT.

Public and private sectors across the Western Balkans face a shortage of skilled cybersecurity personnel, mainly due to outdated educational systems and teaching methodologies in this field, alongside non-standardised cybersecurity job descriptions and qualifications (PwC, 2022[6]). A notable brain drain, particularly among young professionals, exacerbates the issue. Even when cybersecurity talent is available, salary disparities between the private and public sectors further hinder the ability of public administration bodies to retain highly skilled professionals.

The region also lacks systematic mechanisms and resources to invest in international co-operation and information exchange with relevant stakeholders abroad to reinforce its response to cybercrime. Initial steps have been made with a regional cyber capacity-building initiative that emerged during the Berlin Process Summit in Tirana, Albania in October 2023. The establishment of the Western Balkans Cyber Capacity Centre (WB3C),[8] with support from the governments of France and Slovenia, aims to address the existing gap in capacity building and foster enhanced regional collaboration. However, the centre is in its early stages, and building sufficient regional capacities will take time. Currently, Serbia stands out as the only regional economy that has undertaken significant cybersecurity capacity-building initiatives since 2021. In 2022 alone, 6 638 individuals were trained through educational activities conducted by the National Academy for Public Administration, 340 individuals were trained in ICT systems of special importance and 44 individuals were trained on the operation of CERTs (MIT, 2022[7]).

Western Balkan economies are making progress in establishing higher standards of privacy and personal data protection, but allocated resources remain inadequate

Since the Competitiveness Outlook assessment in 2021, **privacy and data protection** issues have attracted increased attention in the Western Balkans, as they have globally, due to heightened awareness of digital threats, data breaches and concerns over personal information misuse. The region's personal data protection authorities have systematically invested in enhancing public perceptions and capacities in privacy and data protection, despite inadequate resources to conduct effective awareness campaigns and capacity-building training. However, these efforts have not always translated into increased trust in their work.

Since 2021, the respective authorities in North Macedonia and Serbia have adopted individual personal data protection strategies outlining goals and objectives until 2030, in line with EU and OECD standards. However, only Serbia and Kosovo have updated their personal data protection legislation to uphold the higher standards on personal data protection introduced by the EU GDPR[9] and the EU Police Directive.[10] Despite EU accession commitments, the other WB6 economies are still preparing or planning relevant reforms. Albania is expected to be the next to align with the EU *acquis* on personal data protection, with new legislation pending adoption in 2024.

Despite being in the early implementation phase of their new legislative frameworks, Kosovo and Serbia have seen evidence of heightened public perception and stakeholder trust in the work performed by relevant authorities. For example, in Serbia, 78.4% of public survey respondents expressed confidence in the level of protection provided by the Personal Data Protection Commissioner's Office (Kantar, 2023[8]). Increased trust in the work of the Information and Privacy Agency in Kosovo was also reported by international media freedom organisations and journalists (CPJ, 2022[9]).

However, the implementation of relevant frameworks in Western Balkan economies is hampered by the inadequate allocation of human and financial resources. Privacy and data protection authorities in the region are understaffed[11] in all regional economies except Albania and Serbia, where authorities have increased their human resources. Moreover, authorities face challenges in conducting effective awareness campaigns and staff capacity-building activities in public bodies and companies to enhance privacy perceptions and highlight the importance of compliance with personal data protection obligations. There are persisting issues with the non-compliance of data handlers in both the private and public sectors, and limited respect for the decisions and opinions of relevant protection authorities.

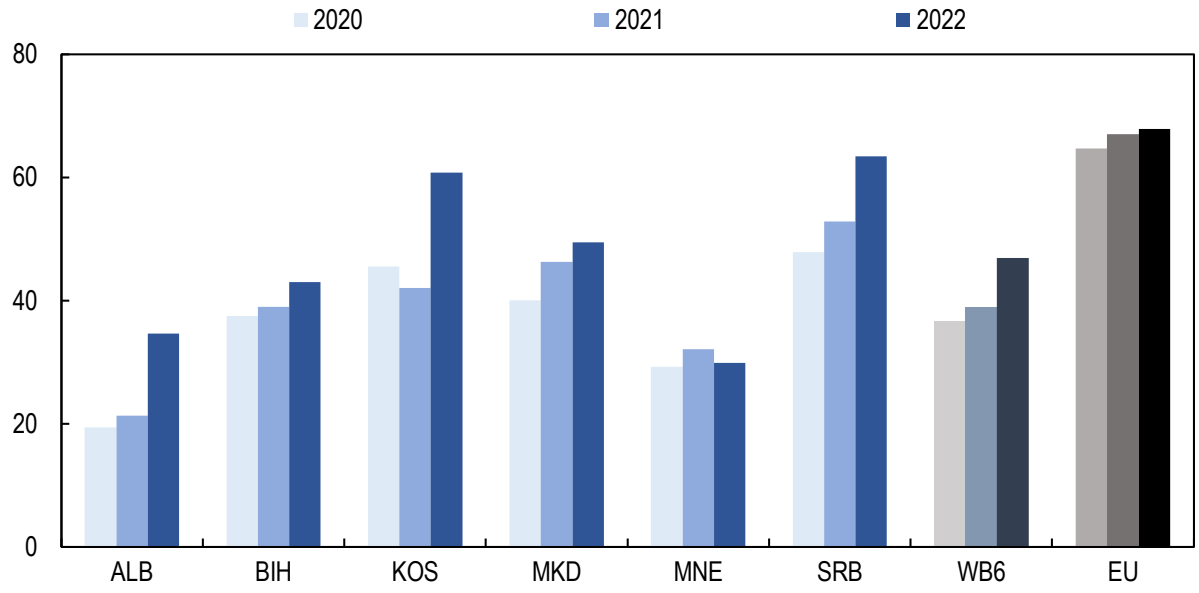
Serbia stands out as the only economy in the Western Balkans that has put significant effort into providing training for diverse groups from the private and public sectors, supporting data handlers in implementing the law and assisting citizens in exercising their rights. Kosovo, Montenegro and North Macedonia rely on donor-funded support to raise awareness on personal data protection, while such efforts are very limited in Albania and Bosnia and Herzegovina.

Online consumers in the region have limited opportunities to receive support and education on how to exercise their rights in e-commerce

WB6 economies have faced a rising trend in **e-commerce** uptake, similar to the global trend and raising environmental concerns, boosted by the COVID-19 pandemic and growing Internet penetration (Figure 5.3). Although some economies have recently modernised consumer protection rules to introduce considerations of trade in the digital realm, inspections and law enforcement in businesses conducting e-commerce remain weak. Moreover, WB6 economies are lacking resources for public awareness campaigns on consumer rights in e-commerce, as well as robust mechanisms to support them in exercising these rights effectively.

Figure 5.3. Internet purchases by individuals (in the last 12 months) in the WB6 economies, the EU and the OECD (2020-22)

Percentage of the population aged 16-74



Note: Data for individuals aged 16-74.
Sources: Eurostat (2024[10]); data received from ALB (INSTAT for 2022), BiH (BHAS for 2021), KOS (KAS for 2021-23), MKD (MAKSTAT for 2021-22), SRB (SORS).

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Recognising the challenges in consumer protection, Montenegro, North Macedonia and Serbia are implementing consumer protection policies that underscore consumer empowerment, effective out-of-court dispute resolution mechanisms and heightened consumer education, particularly in e-commerce transactions. These economies have advanced in modernising their relevant legal frameworks to align with the EU *acquis* in consumer protection, a process that is still ongoing through the adoption of new rules and the harmonisation of legacy legislation. Notably, Serbia is better positioned than other WB6 economies to provide an effective mechanism for submitting complaints and accessing alternative dispute resolution (ADR) through its National Consumer Protection Portal, which facilitates the submission of complaints and requests for ADR. The alignment of consumer protection rules in e-commerce has yet to be prioritised in Albania, Bosnia and Herzegovina, and Kosovo.

Mechanisms to inspect e-commerce businesses across the region are weak, with Albania and Montenegro standing out as the only WB6 economies to have implemented monitoring initiatives that scan online trader websites on legal compliance (“e-sweeps”), such as those conducted by EU member states.

Most WB6 economies allocate inadequate resources to consumer education, particularly in e-commerce, leaving consumers largely unprotected. Online consumers in some WB6 economies have access to online educational materials on e-commerce, but this has questionable impact on consumers’ understanding of their rights in online transactions and digital contracts. Consumer protection non-governmental organisations have an active role in raising public awareness in Montenegro, North Macedonia and Serbia, although relevant activities rarely target online consumers.

Recommendations for strengthening the foundations of the digital ecosystem

- **Facilitate investments in high-speed network infrastructure by further streamlining processes and reducing costs for broadband development**. WB6 governments must implement policy and regulatory measures aimed at alleviating persisting broadband investment barriers. This includes facilitating cost-sharing arrangements and reducing timelines of broadband infrastructure projects, while enhancing capacities in local authorities to co-ordinate the implementation of construction works planned by multiple service providers for the same locations. Additionally, efforts should focus on streamlining administrative processes for permit issuance and harmonising procedures across sub-national or local jurisdictions to reduce related costs and expedite the implementation of construction projects related to broadband networks. WB6 economies are encouraged to leverage the regulatory tools provided by the EU Broadband Cost Reduction Directive and the proposed EU Gigabit Infrastructure Act[12] to propel the regional broadband development agenda.
- **Accelerate implementing programmes to bridge the urban-rural broadband access divide**. All WB6 economies are urged to enhance collaboration on extending network coverage through initiatives such as the Balkans Digital Highway. Furthermore, leveraging the resources available through the new Reform and Growth Facility for the Western Balkans, including capital investment financing provided by the WBIF, presents a unique opportunity to accelerate the development of very high-speed networks in underserved areas, where market interest is low and private investments are economically unviable. In these efforts it will be essential for WB6 economies to streamline the criteria for public support (state aid) aimed at subsidising high-speed network connectivity in remote locations. The revised European Commission guidelines on state aid for broadband networks offer a comprehensive framework for public support. These guidelines align with Gigabit Society targets, incorporate considerations for market failures in mobile networks, including 5G, and provide streamlined rules and criteria for balancing the positive impact of state aid against its negative effect on market competition.
- **Complete the 5G spectrum allocation process, raise awareness of 5G benefits and support market innovation for 5G applications**. Albania, Bosnia and Herzegovina, and Serbia should prioritise the swift completion of the spectrum allocation process for 5G networks, ensuring sufficient spectrum availability for operators and establishing transparent and fair auction mechanisms. All governments should launch comprehensive awareness campaigns to promote the171enefitts of 5G services and applications among businesses, consumers and public institutions, highlighting how 5G technology can revolutionise various sectors such as healthcare, education, transportation and manufacturing by enabling ultra-fast connectivity, low latency and massive device connectivity. Moreover, WB6 governments should create an environment that supports market innovation for 5G applications. This can be achieved through targeted funding schemes, research and development grants, and collaboration with industry stakeholders, academia and research institutions. Encouraging the development of innovative 5G applications tailored to local needs and challenges will not only drive demand for 5G services, but will also spur investment in cost-efficient infrastructure deployment.
- **Prioritise the establishment of ADR mechanisms, investing in capacity building and awareness raising to enhance confidence in digital commerce** (Box .1). WB6 economies should ensure that legal frameworks are in place to foster effective implementation of ADR mechanisms for digital commerce and create dedicated online platforms or portals where consumers and businesses can efficiently resolve disputes. These platforms should be user-friendly, accessible and equipped with tools to facilitate effective communication and resolution. Additionally, it is essential to invest in capacity-building programmes to train mediators and arbitrators in digital dispute resolution techniques and technologies. Training should cover

areas such as online mediation, virtual hearings and the use of technology-enabled dispute resolution tools. In this endeavour, WB6 economies should foster collaboration with international organisations and jurisdictions that have successfully implemented ADR systems for digital commerce to get valuable insights and technical assistance in aligning with global standards. Furthermore, governments should launch awareness campaigns to promote the benefits of ADR mechanisms for digital commerce and encourage their adoption among businesses and consumers to help build confidence in these mechanisms and drive uptake.

Box 5.1. Increasing confidence in e-commerce through effective ADR tools

Alternative dispute resolution (ADR) offers a quicker, more cost effective and less adversarial means of resolving disputes, and can reassure consumers and businesses that any issues encountered during transactions can be efficiently addressed, ultimately fostering trust and facilitating smoother transactions in the digital marketplace. The following examples of effective implementation of ADR mechanisms can provide valuable insights for Western Balkan economies when designing their own approaches to ADR:

- The EU has established the Online Dispute Resolution (ODR) platform, which provides a single point of entry for consumers and traders to resolve disputes related to online purchases across borders. The platform facilitates the resolution of disputes through mediation or arbitration, making it easier for consumers and businesses to resolve conflicts without resorting to traditional legal processes.
- Singapore has developed a robust framework for online dispute resolution, including the Singapore Mediation Centre (SMC) and the Singapore International Arbitration Centre (SIAC). These institutions provide specialised mediation and arbitration services for resolving digital commerce disputes, catering to both domestic and international parties.
- The International Chamber of Commerce (ICC) offers various dispute resolution services, including the ICC Digital Library and the ICC Online Dispute Resolution platform, which provide resources and tools for resolving digital commerce disputes. The ICC also administers arbitration proceedings for e-commerce disputes through its International Court of Arbitration.

Sources: European Commission (2024[11]); SMC (2024[12]); SIAC (2024[13]); ICC (2024[14]).

- **Strengthen cyber resilience by enhancing co-operation in combating cybercrime, ensuring adequate resources and investing in a skilled workforce to address cyber threats effectively**. WB6 economies should advance regional co-operation efforts to develop a robust and co-ordinated response to cybercrime. It is essential to increase human cybersecurity resources and reinforce mechanisms for information sharing, joint exercises and collaborative initiatives to address cyber threats collectively. The region should support initiatives such as the Western Balkans Cyber Capacity Centre (WB3C) by allocating resources and expanding training. Moreover, WB6 economies should accelerate the establishment of national focal points for international cybersecurity collaboration, including participation in networking events organised by the EU Agency for Cybersecurity (ENISA), which provide valuable opportunities for capacity building, knowledge exchange and collaboration with EU counterparts. Furthermore, governments should promote cross-sector collaboration between public authorities, law enforcement agencies, academia and the private sector to tackle cybercrime comprehensively.

Encouraging the uptake of digital technologies

Enhancing the digital transformation of the public sector

Western Balkan economies have recognised the importance of digitalisation policies not only to digitise analogue government processes and services, but also to adopt a digital-by-design approach to transform government. However, despite formal recognition and certain open government initiatives, the region is in the initial phases of integrating digital technologies into all government functions, such as the decision-making process and the policy, legal and regulatory reform process.

WB6 governments are only just starting to address each of the six dimensions of the OECD Digital Government Policy Framework (DGPF) to transition to fully digital governments. These dimensions are: 1) digital by design; 2) data-driven public sector; 3) government as a platform; 4) open by default; 5) user-driven; and 6) proactiveness (OECD, 2020[15]). The economies have adopted digital transformation or e-government strategies alongside their public administration reform strategies. These comprehensive strategic frameworks constitute initial efforts towards a paradigm shift from traditional e-government to digital government, gradually integrating emerging technologies, data-driven decision making, citizen engagement and agile governance practices to deliver more efficient, inclusive and responsive public services, in line with the 2014 OECD Recommendation of the Council on Digital Government Strategies (OECD, 2014[16]). However, they are yet to effectively design and implement strategic approaches for the transition towards the digital maturity of the public sector.

Western Balkan economies lag behind EU member states in digital government maturity

Accelerated by the COVID-19 pandemic, most WB6 economies have invested heavily in digitalising public services for citizens and businesses. The region aims to come closer to the EU Digital Single Market by accelerating digital transformation, as affirmed by WB6 leaders at the 6th Digital Summit held in Sarajevo in October 2023.

Serbia and Albania have both accelerated government digitalisation since the CO 2021 assessment, surpassing the other WB6 economies. Serbia has invested in digital government infrastructure development including data centres, cloud infrastructure and digital identity user-friendliness, thus building a strong foundation for its digital transformation and a robust basis for the future integration of technological innovation into government functions. Albania has prioritised the digitalisation of nearly all existing services and the switching of service delivery to online channels only, with at least 95% of all services offered online by May 2022.

Despite progress, WB6 economies are lagging behind the EU average in digital government maturity. According to the EU eGovernment Benchmark 2023 report, Serbia ranks 30th, followed by Albania (33rd), Montenegro (34th) and North Macedonia (35th), among 35 European economies assessed on the maturity of their digital governments (Capgemini, Sogeti, IDC and Politecnico di Milano, 2023[17]). While Bosnia and Herzegovina and Kosovo are not participating in this study, evidence indicates that their digital government maturity lags behind the other four economies, with Bosnia and Herzegovina coming last in the region having demonstrated limited progress in government digitalisation since the CO 2021 assessment.

WB6 economies have made progress in developing government e-services, although interactions over the counter are often still required

All WB6 economies except Bosnia and Herzegovina have developed national **e-service portals**, and are increasingly converging to the one-stop shop model of service delivery for all online public services. In Bosnia and Herzegovina, RS has developed its own e-services portal, while isolated services are provided by individual national institutions, FbiH and the Brčko District. Albania is the region's frontrunner in the

number of available digital services, with 1 237 services offered online for citizens, businesses and public administration, and 68% of e-forms pre-filled. All of these services are at the fourth level of sophistication, meaning that they are fully transactional (e.g. supporting e-signature and e-payments). Montenegro, North Macedonia and Serbia each offer fewer than 400 services online, at various levels of sophistication. Transactional e-services in Serbia amount to 80% of 340 e-services in total, compared to around 24% of 392 e-services in North Macedonia; in Montenegro, only 19% of 382 e-services are more than simply informative. In Kosovo, only 10% of all public services are offered online, and most are informative.[13]

WB6 economies have actively focused on **user-centricity** by increasing e-service (or information about services) availability, mobile friendliness and availability of user support. This is confirmed by the EU e-Government Benchmark 2023 report, where Albania, Montenegro, North Macedonia and Serbia have reached the EU average level of maturity in terms of user-centricity (Capgemini, Sogeti, IDC and Politecnico di Milano, 2023[17]). These economies have also transformed their e-services according to the life-event approach, which involves developing services aimed at key life events such as the birth of a child and enrolment in educational institutions. Albania and Serbia have made particular progress in transforming how some of their key e-services are provided to citizens and businesses, and North Macedonia, one of the first economies to adopt the life-event approach, is following at a slower pace. Montenegro has outlined a shift towards the life-event approach in strategic digital transformation documents, but has been sluggish in terms of implementation. Kosovo and Bosnia and Herzegovina are lagging behind in this respect, with only RS having developed a life-event e-service (e-baby).

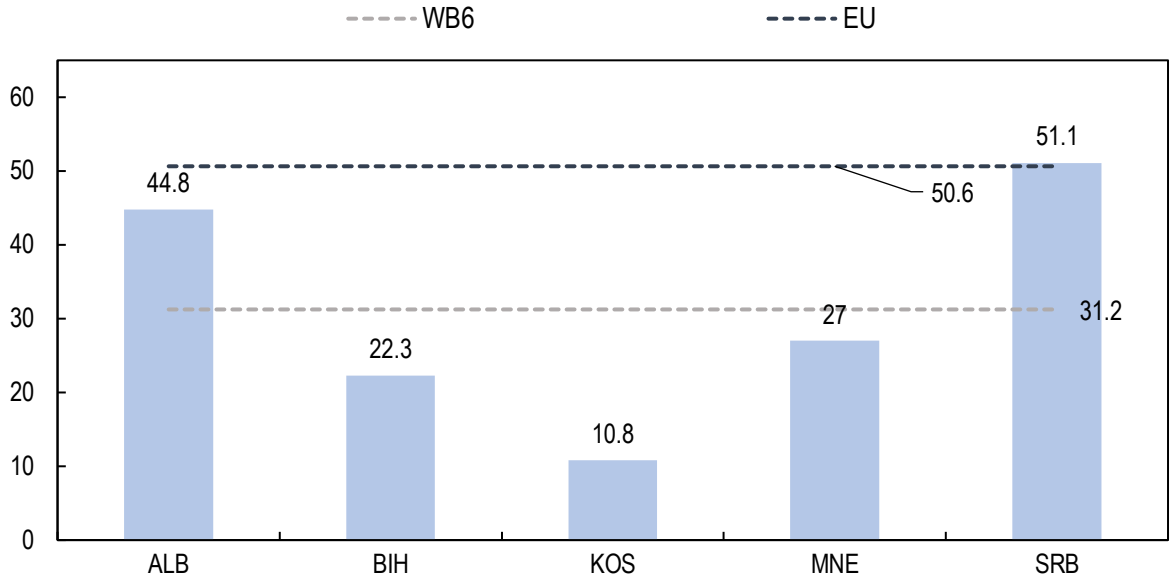
User engagement with e-government services varies significantly in the Western Balkans. Lower levels of citizen interaction with e-government services are primarily attributed to a lack of awareness about e-services or an unavailability of high-quality, fully transactional services hindering service completion online. One-third of the region's population remains unaware of available e-services (CEP, 2023[18]). Serbia has slightly surpassed the EU average in the percentage of individuals using the Internet to interact with public authorities in 2022 (Figure 5.4), while Albania is approaching this level. The remaining WB6 economies are falling behind, with Kosovo coming last in the region. According to OECD SIGMA (Support for Improvement in Governance and Management) monitoring reports for the WB6 economies in 2021,[14] user satisfaction regarding e-services was low or even declining, except in Albania. While some WB economies have since taken steps to address issues limiting user satisfaction and engagement, the adoption of a data-driven approach to effectively address issues is being hindered by the lack of systematic monitoring of user satisfaction.

Most Western Balkan economies have made strides in developing key enablers for digital government, including e-payments and e-identification

WB6 economies have made progress in developing key enablers for digital government, including the improvement of digitalisation legislation, the implementation of electronic identification and payment systems, and their integration with national e-service portals. However, the implementation of these enablers varies significantly across the region, and their maturity is below the EU average (Capgemini, Sogeti, IDC and Politecnico di Milano, 2023[17]). Most WB6 economies have enhanced their legal frameworks on digital government and are implementing adequate legal reforms to establish comprehensive legal frameworks for digital government that encompass legislation on electronic documents, electronic public registers and e-identification. However, some remaining misalignments with legacy legislation on administrative procedures create challenges, slowing down the digitalisation of public registers or limiting the enforceability of e-document and e-signature legislation, such as in North Macedonia (Metamorphosis, 2022[19]).

Figure 5.4. Individuals using the Internet to interact with public authorities (in the last 12 months) in the WB6 economies and the EU (2022)

Percentage of the population aged 16-74



Note: No data available for North Macedonia.
Sources: Eurostat (2024[20]); data received from BiH (BHAS), KOS (KAS).

The new Growth Plan for the Western Balkans proposed by the European Commission in November 2023 emphasises the importance of the region's alignment with the EU *acquis* in electronic identification,[15] authentication and trust services to enable its integration into the Digital Single Market (European Commission, 2023[21]). While legal frameworks in Albania, Kosovo, Montenegro, North Macedonia and Serbia have aligned with the EU eIDAS Regulation, practical implementations of electronic identification (eID) solutions and their uptake are still in the early development phases in most WB6 economies. Albania and Serbia have developed the most advanced, user-friendly public eID systems in the region through the integration of mobile phone identification, which has facilitated increased user uptake of e-signatures and e-government services as a whole. Albania and Montenegro have implemented their own eID systems, but uptake is still relatively low. Kosovo and North Macedonia are still preparing their public eID implementation, while Bosnia and Herzegovina has no nationwide eID system in use yet, although eIDAS compliant e-signatures have been issued by the Agency for Identification Documents, Registers and Data Exchange of Bosnia and Herzegovina (IDDEA) since 2023 at the state level, and RS issues e-signatures for its territory.

The implementation of eIDAS compliant public (free) digital identification systems is particularly important not only for the increase of digitalisation and e-government uptake in WB6 economies, but also for enabling the development of cross-border services. WB6 governments recognise the importance of cross-border collaboration in this field, and signed a memorandum of understanding on Regional Interoperability and Trust Services in the Western Balkans in November 2020, and the subsequent Joint Statement on Interoperable Western Balkans in October 2021 to improve regional interoperability, including the recognition of eIDs and trust services. Despite high-level political alignment, limited progress has been made in achieving some level of interoperability and mutual recognition of eID systems in the region. As of early 2024, WB6 economies significantly lag behind the EU average in terms of cross-border services, meaning that the region's citizens have limited opportunities to use online government services when travelling in the region or in EU member states.

Interoperability challenges with information systems and the low utilisation of interoperability platforms for data exchange among public bodies hamper the coherent use of data

Sectoral and horizontal strategies recently adopted in WB6 economies emphasise the importance of using and applying new technologies in the work and provision of services. In practice, however, the coherent use of data and digital technologies in all government functions is still constrained by challenges related to the digitisation of public registers and the integration of information systems, the availability of appropriate technical equipment and communication technologies in public administration, the development of pro-digitalisation mindsets, and the efficiency of in-service training for civil servants on the use and application of new technologies in their everyday work. These challenges are further pronounced at the local administration level. Data and digital technologies are not yet consistently used in the entire range of government functions, such as policy making and monitoring, financial management, and civic engagement.

Despite advancements in developing government interoperability platforms since 2021, data-driven decision making and transparency remain limited. Common challenges include the underutilisation of these platforms for data exchange among public bodies, and a slow pace in connecting public administration information systems and digitalising public registers. Albania and Serbia stand out among WB6 economies in terms of interconnecting public information systems with their government platforms. At the end of 2023, Albania had connected around 60 information systems and 230 public institutions (mainly from the central government) to its government platform, Serbia had connected the majority of its public sector databases, Montenegro had connected 37 out of approximately 300 public registers, while North Macedonia had interconnected only 52 public institutions. This assessment indicates that Kosovo, Montenegro and North Macedonia acknowledge that their government interoperability platforms are currently underutilised. In Bosnia and Herzegovina, technical interoperability infrastructure suffers from a lack of enforceability and support (OECD, 2022[22]).

Western Balkan economies have not yet invested in cross-border interoperability and their future integration into the European Digital Single Market

WB6 economies have not yet started to prepare for their alignment with the new Interoperable Europe Act,[16] which aims to establish a co-operation framework for EU public administrations to ensure the seamless delivery of public services across borders, and to provide support measures that will promote innovation and enhance skills and knowledge exchange. Aligning with this new EU regulation will be critical for Western Balkan economies in joining the European Digital Single Market as it will enable the cross-border interoperability of network and information systems and thus the cross-border exchange of data. The importance of strengthening cross-border interoperability through national interoperability frameworks is stressed in the new Growth Plan for the Western Balkans (European Commission, 2023[21]).

While all WB6 economies except Bosnia and Herzegovina have adopted national interoperability frameworks, Albania and Serbia are aligned with the revised European Interoperability Framework (EIF) (European Commission, 2023[23]). Alignment is still pending in Montenegro (European Commission, 2023[24]), North Macedonia (European Commission, 2023[25]) and Kosovo (European Commission, 2023[26]). Bosnia and Herzegovina has yet to develop a nationwide interoperability framework and to align with the EIF (European Commission, 2023[27]).

Since 2023, all WB6 economies have joined the Digital Europe Programme, which provides opportunities for businesses and public administrations to take part in projects that deploy innovative digital technologies across the EU. The programme will be the primary funding instrument for implementing the Interoperable Europe Act, stimulating public sector innovation and public-private “GovTech” projects. The Interoperable Europe Community that supports the programme brings together a broad set of interested practitioners and experts from GovTech companies, the open source community, regions and cities across the EU to

help implement new solutions. By actively joining this programme, WB6 economies will be making a push towards interoperability, eventually connecting with European digital governments.

Supporting private sector digitalisation

Unleashing the potential of digital transformation for companies, especially SMEs, requires holistic policies that encompass a broad range of aspects to help businesses navigate this transition effectively (OECD, 2020[28]).

Western Balkan economies have acknowledged the importance of helping SMEs embrace digital technologies. This commitment is reflected in strategic documents targeting information society development or digital transformation that have been published since the CO 2021 assessment, for example the promotion of ICT adoption by SMEs through e-commerce and e-business development (in Albania, Montenegro and Serbia), alongside digital innovation and entrepreneurship (in all WB economies to some extent).

Inadequate financial resources are allocated to raise awareness of digitalisation benefits among SMEs and effectively support their digital transformation

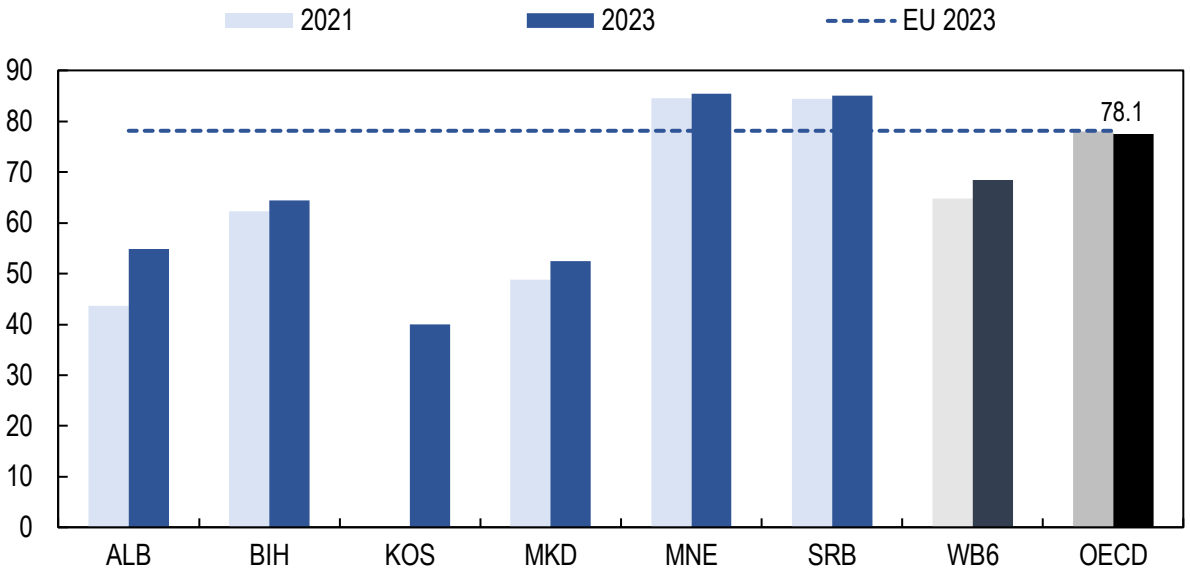
Improving productivity and competitiveness through the digitalisation of business models, processes and products depends on the successful dissemination of digital tools, which is significantly influenced by awareness campaigns and business investment in ICT. Since the CO 2021 assessment, most WB6 economies have intensified efforts to promote ICT investment through programmes providing monetary support to buy ICT equipment or services, and through non-financial support such as digital transformation consulting and mentoring services. However, these business digitalisation programmes have yielded limited results in terms of ICT adoption by SMEs. This can be attributed primarily to the insufficient allocation of funds to co-finance digital transformation projects, coupled with the lack of awareness regarding the availability of these programmes or how digital tools can support business growth.

The percentage of businesses with a website serves as an indicator of ICT adoption. In 2023, this indicator remained significantly lower than averages for the EU (78.1%) and OECD (77.5%) in Albania, Bosnia and Herzegovina, Kosovo, and North Macedonia (Figure 5.5). Additionally, while the use of social media for business purposes in the WB6 was roughly on par with the EU average (60.9%) in 2023 (Eurostat, 2023[29]), the adoption of more advanced digital tools such as cloud computing was below the EU average (45.2%) across all WB economies. For instance, in 2023 cloud computing was used by 20.7% of companies in Bosnia and Herzegovina, 31.7% in Montenegro and 37% in Serbia (Eurostat, 2023[30]).

The low percentage of businesses engaging in online sales in Albania, Kosovo and North Macedonia underscores a deficiency in effectively investing in programmes promoting e-commerce adoption among companies (Figure 5.6). These economies primarily rely on EU and donor-funded programmes to help businesses embrace e-commerce and e-business practices.[17] In Montenegro, only one-third of businesses are aware of the dedicated portal for digitalisation support, according to analysis conducted by the Montenegrin Chamber of Commerce in 2023 (KOMORA, 2023[31]). Additionally, even in Serbia, where annual dedicated programmes for SME digital transformation have been implemented since 2021, allocated funds have failed to meet industry demand: in 2022, only 272 companies received support from a total of 447 SMEs that applied for digital transformation consulting services.

Figure 5.5. Enterprises with a website in the WB6 economies, the EU and the OECD (2021,2023)

Percentage of enterprises

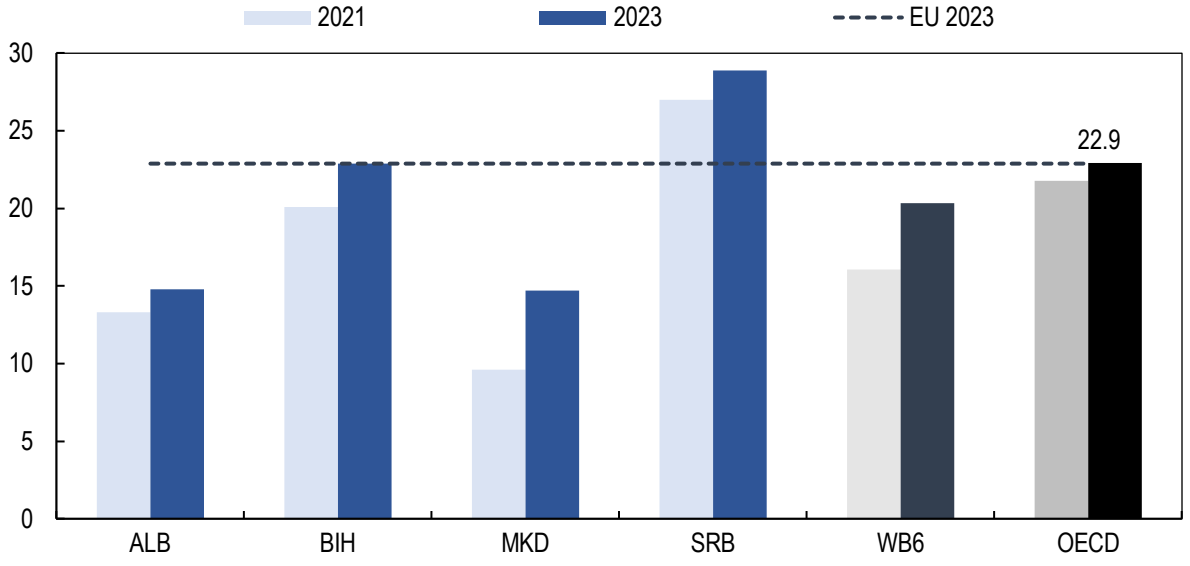


Sources: Eurostat (2024[32]); data received from ALB (INSTAT), KOS (KAS) data only for 2022, MKD (MAKSTAT), MNE (MONSTAT); OECD (2024[3]).

StatLink https://stat.link/qadp3k

Figure 5.6. Enterprises doing e-sales in the WB6 economies, the EU and the OECD (2021,2023)

Percentage of enterprises



Note: No data available for Montenegro.
Sources: Eurostat (2024[33]); data received from ALB (INSTAT), KOS (KAS) data for 2021, MKD (MAKSTAT), OECD (2024[3]).

StatLink https://stat.link/ba4fsx

The unavailability of digital skills in the workforce and the scarcity of ICT talent hinders the digital transformation of businesses

Digital innovation and entrepreneurship policies aimed at nurturing startups, facilitating access to finance, and fostering collaboration between industry and research institutions can play a crucial role in cultivating a vibrant digital ecosystem. Since the CO 2021 assessment, Western Balkan economies have made strides in enhancing the legal framework for entrepreneurship and startups, while also fostering initiatives to support innovation. The economies have invested in establishing dedicated innovation and startup funds, alongside initiatives to develop digital innovation hubs, technology parks, business accelerators, startup centres and IT clusters. However, the effectiveness of these initiatives is impeded by the scarcity of ICT talent and the digital skills deficit prevalent in the workforce throughout the region.

The digital skills deficit in the workforce (see Chapter 3) and the shortage of IT professionals, compounded by brain drain, hinder the ability of WB6 economies to harness the innovation potential of SMEs and startups. WB6 governments have yet to prioritise the development of comprehensive initiatives to address these challenges.

Digital upskilling activities have fallen behind in the majority of WB6 economies, with the notable exception of Serbia, where the Digital Academy of the Centre for Digital Transformation of the Chamber of Commerce and Industry offers free training on the fundamentals of digital transformation. IT (re-)training programmes have already trained 2 200 participants, with plans in place to address the digital skills gap by increasing the capacities of technical faculties in universities and enhancing programming classes in high schools.

Supporting effective and cutting-edge technological innovations

Due to the rapid development of emerging technologies, policy makers around the world, including those in the Western Balkans, are facing challenges in keeping pace and implementing policies that can harness the potential of these technologies, while minimising the associated risks (OECD, 2022[34]). The Western Balkans is still in the early stages of policy and regulation development at the economy level, which implies the need for overarching strategies and regional co-ordination, as this is not solely a national issue.

The region is pooling efforts to design frameworks governing emerging technologies, with each economy at different levels of readiness

The WB6 economies, with the exception of Serbia, have yet to implement comprehensive regulations for emerging digital technologies such as artificial intelligence (AI), blockchain and the IoT. While measures for AI are progressing, with each economy having at least one digital, development or reform strategy incorporating measures related to AI technologies, those for blockchain and IoT are lagging behind.

Among WB6 economies, Serbia and North Macedonia show more advanced AI development. Serbia's National Strategy for Development of AI aligns with the European AI Initiative and addresses several OECD AI principles (Box 5.2). It has established the Research and Development Institute for Artificial Intelligence to foster collaboration between public and private sector entities and serve as an incubator for AI startups. Serbia was also elected Chair of the OECD's Global Partnership on Artificial Intelligence (GPAI) for 2025. In parallel, North Macedonia is in the process of establishing a Coalition for Responsible Artificial Intelligence, positioning itself to become the second economy in the region (besides Serbia) to propose ethical guidelines regarding AI technology usage.

Box 5.2. OECD Recommendation of the Council on Artificial Intelligence

Adopted in 2019, revised in 2023 and amended in 2024, the OECD Recommendation of the Council on Artificial Intelligence (AI) builds upon existing OECD standards, including those on privacy and data protection, digital security risk management, and responsible business conduct.

The OECD's AI standards were established with the ethos that the technology's rapid development, use and implementation at the national level across the world requires a stable policy environment that supports a human-centric approach and fosters research, preserves economic incentives to innovate and applies to all stakeholders. The recommendation is aligned with the United Nations Sustainable Development Goals and the UN Declaration on Human Rights.

The recommendation is separated into two sections that encompass principles to ensure good practice and offer recommendations for OECD member and non-member states:

- Section one covers principles for responsible stewardship of trustworthy AI, including inclusive growth, sustainable development and well-being, human-centred values and fairness, transparency and explainability, robustness, security and safety, and accountability.
- Section two addresses national policies and international co-operation for trustworthy AI, including recommendations on investing in AI research and development, fostering a digital ecosystem for AI, shaping and enabling the policy environment for AI, building human capacity and preparing for labour market transformation, and international co-operation for trustworthy AI.

Given the evolving landscape of AI adoption, the Western Balkans is in a unique position where aligning AI initiatives and governmental frameworks with the OECD recommendation will foster responsible innovation and significantly contribute to regional economic convergence efforts. By embracing these guidelines, the Western Balkans can build upon an established foundation for AI governance that prioritises ethical considerations, fosters trust and leads with a human-centric approach, thereby facilitating sustainable growth and prosperity in the region.

Source: OECD (2024[35]).

Although it remains to be broadly adopted, governments across the WB6 are initiating the integration of blockchain technology as part of their wider digitalisation strategies, marking progress in their adoption of emerging technologies beyond AI. Albania is implementing blockchain technology into its governmental services through the Digital Agenda Strategy 2022-26, and Serbia is laying the groundwork for national-level blockchain integration with its 2020 Law on Digital Assets, which legally recognises virtual currencies and digital tokens as digital assets. These proactive digital initiatives signify progress towards the broader integration of emerging technologies beyond AI, underscoring the commitment of WB6 economies to aligning with EU and OECD standards.

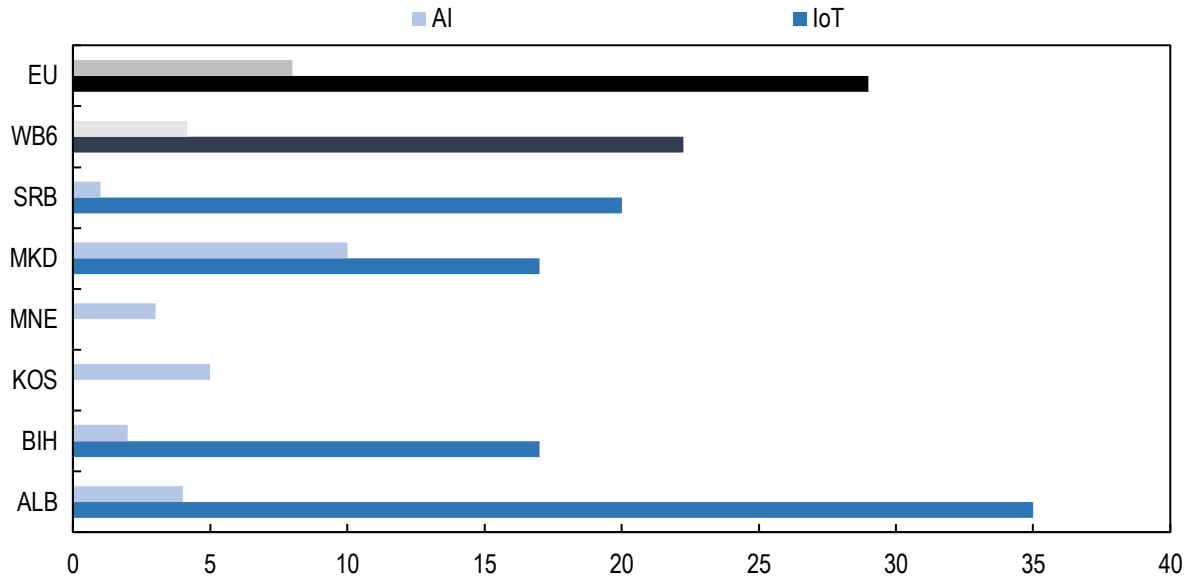
The prevalence of IoT adoption in enterprises across the region surpasses that of AI, with notable variances in adoption rates compared to EU peers

The prevalence of AI policies exceeds those of IoT and blockchain, although data reveal that enterprises across the Western Balkans rely more on IoT in their daily operations. IoT enabled products and services can automate processes and optimise resource utilisation, leading to increased efficiency and cost savings. Within the region, AI adoption stands at 4%, while 22% of enterprises have embraced IoT. Notably, North Macedonia exceeds the EU average of AI adoption in enterprises by 2 percentage points, and Albania surpasses the EU average of IoT adoption by 6 percentage points (Figure 5.7).

However, a more comprehensive review underscores that despite these outliers, WB6 economies generally lag behind the EU average in enterprise adoption rates of both AI and IoT. Across the EU and Bosnia and Herzegovina, North Macedonia, and Serbia (no data available for Albania, Kosovo and Montenegro), the use of IoT is largely for premises' security, such as smart-alarm systems, smoke detectors, door locks and security cameras, with an EU enterprise adoption average of 72%. IoT is also employed for energy consumption management (30% adoption rate among enterprises in the EU) and logistics management (24%), showcasing how the Western Balkans can learn from the evolving dynamics of the EU market and consider areas where significant gaps persist.

Figure 5.7. Enterprises usage of Artificial Intelligence and Internet of Things in the WB6 economies and the EU (2022)

Percentage of enterprises



Note: Data on AI for Kosovo and North Macedonia are from 2022 and sourced from the Regional Cooperation Council, DESI.
Sources: Eurostat (2021[36]; 2023[37]); RCC (2023[38]).

StatLink https://stat.link/z3ojwr

Recommendations for encouraging the uptake of digital technologies

- **Improve regional interoperability and advance towards European interoperability to achieve full integration into the European Digital Single Market**. Western Balkan economies face challenges in achieving regional interoperability for cross-border services due to the lack of mutual recognition of electronic identification (eID) systems and trust services. This hampers the region's aspirations of facilitating the free movement of workers and citizens across the Western Balkans. To overcome this obstacle, the region should prioritise efforts to enhance regional interoperability, aligning with the revised European Interoperability Framework. Such alignment will enable Western Balkan economies to seamlessly connect with European digital governments, fostering the development of effective cross-border digital public services. In pursuit of this goal, Western Balkan governments should actively consider aligning with the European Interoperable Act, which aims to establish a new co-operation framework for EU public administrations to ensure the smooth delivery of public services across borders.

- **Enhance user-centricity by consolidating digital public services into a single online point of entry, and adopt an omnichannel approach for digital service delivery**. Western Balkan economies are gradually consolidating all government websites into a single domain. These efforts should be intensified to further simplify user journeys and foster better understanding of data flows within the public sector. To meet the evolving needs of citizens in an increasingly digital environment, regional governments should provide seamless and cohesive service experiences across multiple channels, including online platforms, mobile applications and physical service centres. Governments should invest in modernising their service delivery infrastructure, ensuring interoperability and integration among various channels, and adopting user-centric design principles to enhance accessibility and usability. By embracing the omnichannel approach, Western Balkan economies can improve citizen engagement, streamline service delivery, and foster greater trust and satisfaction in government services (Box 5.3).

Box 5.3. Designing and delivering public services in the digital age: The omnichannel strategy

The evolution from analogue to digital government has left a large footprint. The processes, data flows and channels for delivering public services follow from strategies developed by different organisations at different times. Moreover, public services can be provided by central, regional or local governments and involve crossing nuanced organisational boundaries that may not be clear to the citizens or businesses trying to access services from "government". The result of this patchwork are user journeys that might involve switching among phone calls, face-to-face exchanges or online transactions. Although citizens might be able to access public services via this "multi-channel" approach, the websites, call centres, self-service kiosks or physical locations often behave as separate siloes, and interactions begun online often cannot be completed in person and vice versa.

A clear omnichannel strategy is therefore vital for addressing the confusion and competition between multiple entry points into government services. The omnichannel model of public service provision ensures that no matter the channel someone chooses, they will always be able to seamlessly access a consistent, joined-up and high-quality service. The clarity of this strategy and the leadership to support it is vital for ensuring that service teams can concentrate on meeting the needs of their users, not developing new channels of their own.

Several countries have consolidated all government websites into a single domain, which simplifies access for users. Such an approach simplifies access and the entire landscape of service provision, including the consolidation of user journeys and a better understanding of data flows within the public sector. These ambitions rely on government leaders cutting through organisational siloes, fostering horizontal integration and disrupting historic policy domain specific practices. Without these efforts it will prove very hard to ensure a consistent and seamless experience for the public.

Source: Welby and Tan (2022[39]).

- **Accelerate digital transformation among SMEs by increasing awareness of the benefits of digitalisation and supporting their journey towards digital maturity**. Governments should allocate sufficient funds to co-finance digital transformation projects, ensuring that SMEs have access to subsidised digital transformation consulting and mentoring services. They should raise awareness among SMEs about the benefits of digitalisation and the availability of digital tools capable of supporting business growth. Moreover, Western Balkan economies should prioritise the establishment of digital innovation hubs and ensure that SMEs seize the opportunities presented by the Digital Europe Programme, including access to funding support for digital innovation projects, advanced digital infrastructure (such as high-performance computing, AI and

cybersecurity capabilities), innovation partnerships and increased market opportunities within the EU. By implementing these measures, WB6 economies can empower SMEs to embrace digitalisation, enhance competitiveness and unlock new opportunities for sustainable growth in the digital economy.

Embracing digital sustainability

Building an inclusive and sustainable digital future for all

Enhancing Internet accessibility and digital literacy is paramount to ensure digital inclusivity. The strategic frameworks adopted in the WB6 economies incorporate measures on improving the quality of government digital services, enhancing digital literacy among disadvantaged groups, and ensuring Internet access to every household and public institution across the economy. They identify various challenges to overcome, such as underdeveloped or low-quality network infrastructure, particularly in rural areas; low levels of digital skills among vulnerable groups; and a considerable urban-rural divide due to significant rural populations.

Policy initiatives to enhance digital literacy among vulnerable groups and efforts to redesign e-services and websites to promote e-accessibility are not sufficiently prioritised

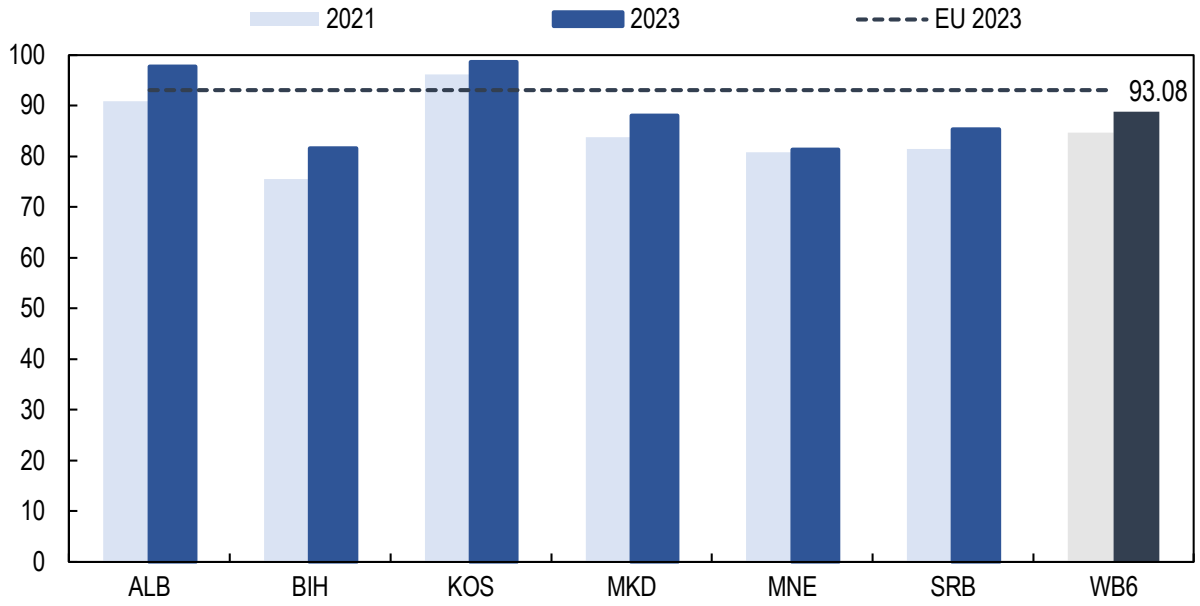
Digital sector policies implemented in the Western Balkans since the CO 2021 assessment have begun to address digital inclusion challenges such as digital literacy and the accessibility of digital technologies for vulnerable groups. However, the region still faces limitations in implementing initiatives to develop digital skills among vulnerable populations, often relying on EU and international donor funding. Moreover, despite commitments to EU accession, progress in addressing e-accessibility issues for people with disability in public sector websites and online applications has been minimal across Western Balkan economies. This is due to the non-binding nature of accessibility rules for public sector websites in some economies, and the low prioritisation of necessary redesign activities to align with EU and international e-accessibility standards.

While Serbia and Montenegro have adopted relevant legal obligations and rules on **e-accessibility**, implementation has been sluggish. The central government websites in these two economies and state-level institution websites in Bosnia and Herzegovina comply with the Web Content Accessibility Guidelines (WCAG 2.0) standard,[18] but other public bodies and local governments have yet to redesign their websites accordingly. Albania and North Macedonia plan to align with the EU *acquis* in 2024. The integration of accessibility requirements for ICT products and services in public procurement processes has also yet to be realised in Western Balkan economies.

While most WB6 economies are advancing **digital government services** by prioritising digital channels for accessing government services and promoting efficiency, accessibility and convenience, they have yet to adequately provide alternative channels for individuals lacking digital access or skills, or those who prefer non-digital methods. Additionally, although some economies are gradually adopting the one-stop shop approach in digital government, enhancing user-friendliness and engagement, progress in implementing the “once only” principle to reduce the need for in-person transactions remains insufficient. Regarding **Internet access** in households, regional economies have made strides since 2021, with Kosovo leading at 98.60% of households having some form of Internet access, surpassing the EU average of 93.08% in 2023 (Figure 5.8). This progress is attributed to achievements in network coverage through initiatives such as the Kosovo Digital Economy (KODE) project.[19] Albania is also surpassing the EU average, while the other WB6 economies slightly lag behind, with Montenegro ranking last at 81.28%.

Figure 5.8. Internet access in households in the WB6 economies and the EU (2021, 2023)

Percentage of the population aged 16-74



Source: Eurostat (2024[2]).

StatLink https://stat.link/5v8wki

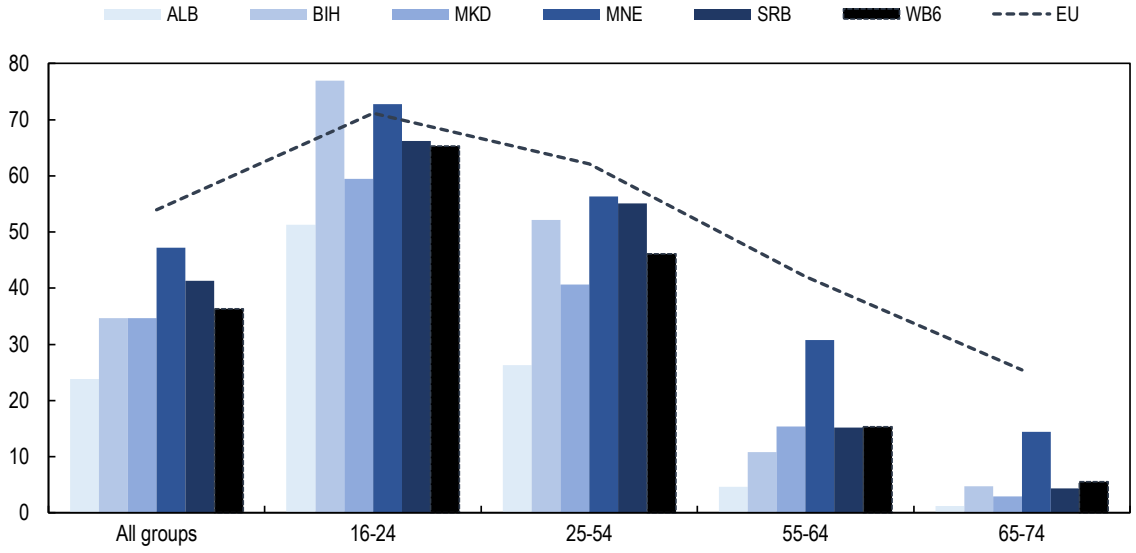
While Internet access is becoming widespread across the region, equitable participation in the digital economy is hindered by skills gaps among certain demographic groups (Figure 5.9). While young individuals (aged 16-24) in Bosnia and Herzegovina, Montenegro, and Serbia exhibit similar digital skills to those in EU member states, young people in Albania and North Macedonia slightly trail behind. As age increases, the skills gap widens, with Montenegro the only WB6 economy maintaining a relatively smaller gap in the 55-64 and 65-74 age groups compared to the EU average, while the rest significantly lag behind. Albania faces the lowest percentage of digitally skilled individuals in the region, with only 4.7% and 1.2% of individuals aged 55-64 and 65-74, respectively, possessing digital skills, indicating significant exclusion from the digital transformation process among these age groups.

Challenges in **digital literacy** extend to other vulnerable groups, exacerbating marginalisation. However, regional economies inadequately monitor digital inclusion indicators for groups such as people with disability and Roma or Egyptian populations. The implementation of digital literacy activities outlined in digital sector strategies in Albania, Montenegro, North Macedonia and Serbia is slow. In Montenegro, the Digital Academy has yet to offer digital skills training to vulnerable groups, while in Serbia, planned subsidies for these groups to purchase computer equipment and receive training are still pending. In Bosnia and Herzegovina, civil society initiatives play a crucial role in enhancing digital literacy, such as the IT Girls in BiH[20] that had trained 2 000 girls and young women by 2022.

Digital literacy is particularly critical in Albania, as the government has adopted a “digital-by-default” model in service delivery, with 95% of all services provided online, and is phasing out traditional service points. However, the government has yet to ensure that this approach does not exclude individuals facing barriers to digital access and that it provides support and alternatives for people to access services through other means.[21] Western Balkan economies have yet to prioritise the establishment of local service centres to assist citizens in using e-services. In North Macedonia, for instance, single point of service centres exist only in five cities, while plans for further expansion are pending.

Figure 5.9. Individuals with basic or above basic overall digital skills (all five component indicators are at basic or above basic level) by group age in the WB6 economies and the EU (2023)

Percentage of the population aged 16-74



Note: No data available for Kosovo.
Source: Eurostat (2024[40]).

StatLink https://stat.link/r18hp0

Limiting the environmental impact of digital technologies

Limiting the environmental impact of digital technologies is crucial for ensuring sustainable development and mitigating the ecological footprint of an increasingly digitalised world.

Western Balkan economies have not integrated environmental sustainability considerations into their digital transformation strategies and reform programmes

While heavily focusing on accelerating digitalisation, WB6 economies have largely overlooked its environmental impact. Albania stands out with its National Plan for the Development of Digital Infrastructure, which introduces measures to make high-speed communication networks environmentally friendly by implementing sustainable energy technologies such as solar installations at remote telecommunication stations. Similarly, Kosovo's Economic Reform Programme 2023-2025 outlines activities aimed at harnessing digital technologies to facilitate the green transition, although tangible outcomes have yet to materialise.

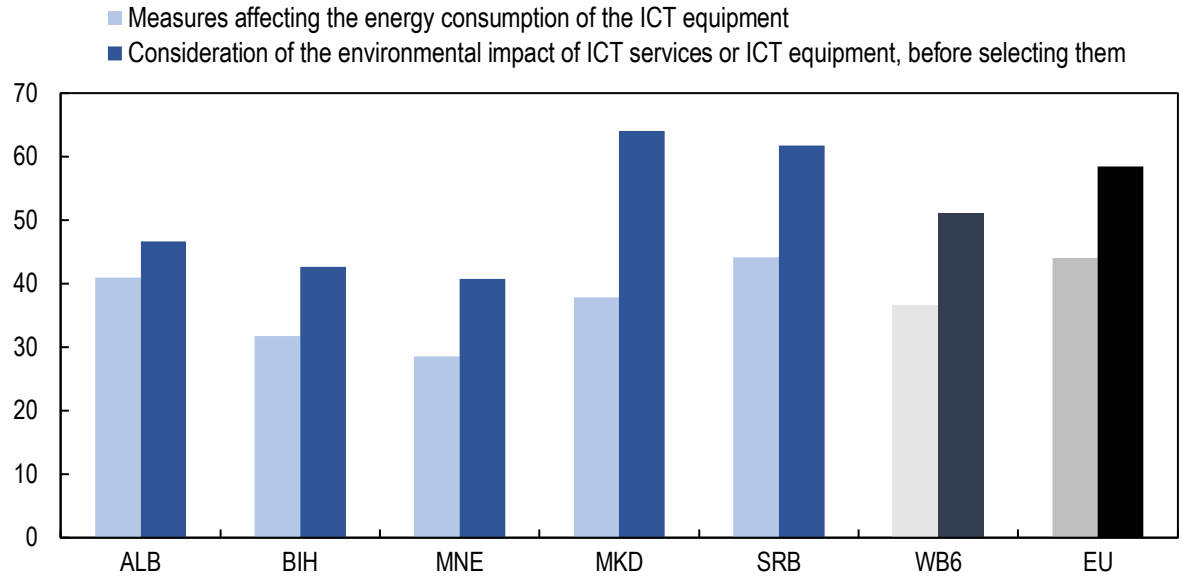
Western Balkan initiatives promoting environmental sustainability in digital technology use and awareness campaigns about the environmental footprint of digital technology are still in their infancy. While some EU and donor-funded projects attempt to address this issue, they have yet to take a strategic role for the region. For example, the Computing Power Goes Green project,[22] implemented by a partnership that includes the National Agency of Information Society in Albania and the Bureau for Regional Development in North Macedonia, aims to identify obstacles to green digitalisation and raise awareness about creating environmentally sustainable digital infrastructure. Initiatives under this project include tangible outcomes such as reducing the energy consumption of the Albanian government data centre by 20% (NAIS, 2023[41]).

On a positive note, WB6 economies are gradually integrating measures on waste electric and electronic equipment (e-waste) into their waste management policies. Over the past three years, Montenegro, North Macedonia, Serbia and FBiH have adopted or updated legal frameworks regulating e-waste management, and Albania and Kosovo have plans to establish relevant frameworks soon. These economies have also introduced extended producer responsibility (EPR) principles for e-waste management, although implementation is still in its early stages. EPR ensures that manufacturers consider the full lifecycle of their products, which promotes sustainability and environmental responsibility.

Furthermore, some economies have begun monitoring indicators measuring enterprises and individuals' environmental practices regarding the energy efficiency and e-waste disposal of ICT equipment. This monitoring will facilitate informed policy and decision-making processes that promote sustainable digitalisation (including potential greenhouse gas emissions and waste reduction). Data reveal that businesses in the Western Balkans are taking measures to reduce the energy consumption of ICT and to consider the environmental footprint of ICT services and equipment before making purchasing decisions (Figure 5.10). Serbia is on par with the EU average on both counts, while Montenegro lags behind the other regional economies in how its businesses consider ICT sustainability. On the contrary, citizens in the region appear to be unaware of the environmental impacts of ICT, as demonstrated by the low rates of recycling old smartphones, tablets and laptops (Figure 5.11). Although ICT recycling practices are more frequent in Montenegro than in Serbia and Albania, they still significantly lag behind the EU average.

Figure 5.10. Enterprises implementing green digital measures in the WB6 economies and the EU (2023)

Percentage of enterprises

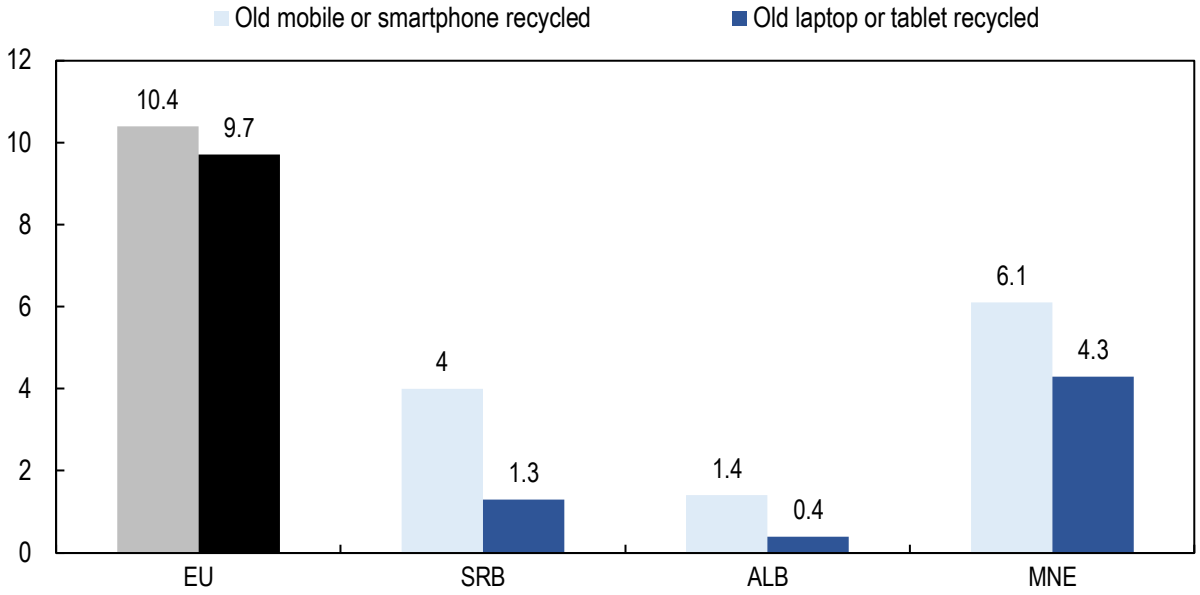


Note: No data available for Kosovo. Data for Albania not available on indicator "The enterprises considered the environmental impact of ICT services, or ICT equipment, before selecting them".
Source: Eurostat (2024[42]).

StatLink https://stat.link/o3m0dc

Figure 5.11. Old smartphones, tablets and laptops recycled by individuals in the WB6 economies and the EU (2022)

Percentages of devices



Note: No data available for Kosovo, Bosnia and Herzegovina, and North Macedonia.
Source: Eurostat (2024[43]).

Recommendations for embracing digital sustainability

- **Prioritise digital inclusion by enhancing digital literacy among vulnerable groups**. Western Balkan economies must design effective programmes targeting digital skills development for underprivileged groups in the population. Governments should tailor digital skills training to the specific needs and preferred delivery modes of marginalised individuals, including the elderly, people with disability, and Roma and Egyptian populations. To address the growing demand for digital literacy, regional economies should mobilise existing resources or establish new digital academies to provide free access to digital skills training. They should also leverage institutions such as public libraries or local cultural centres to offer relevant training, prioritising ease of access and user-friendly delivery methods to make them appealing to the individuals targeted.
- **Address persisting e-accessibility issues in public sector websites and integrate accessibility standards and requirements into the public procurement of ICT**. Western Balkan economies should accelerate public website redesign initiatives to ensure that they comply with international standards on e-accessibility (WCAG) and relevant EU legislation.[23] ICT products and services procured by public sector entities must comply with recognised accessibility standards, ensuring that they are inclusive and accessible to all users, including people with disability. Additionally, regional governments should invest in training programmes and capacity-building initiatives to raise awareness among public procurement officials and ICT vendors about the importance of e-accessibility and the specific requirements to be met.
- **Develop green digital policies and integrate green digital technology considerations into horizontal and sectoral policies**. To foster sustainable development and mitigate environmental impact, Western Balkan economies should prioritise the adoption of energy efficient ICT infrastructure, incentivising the use of renewable energy sources for digital operations and encouraging the development and deployment of green digital technologies such as smart grids,

energy efficient data centres and e-mobility solutions. Additionally, it is essential to address the greenhouse gas emissions and packaging waste associated with e-commerce as a part of both digital and sectoral policies. It is also important to invest in monitoring and evaluating the environmental footprint of the use of digital technologies in the public sector and in ICT-intensive firms. To further support these efforts, WB6 economies should establish certification schemes and standards to help ICT companies measure the environmental impact of their digital technologies. These standards can provide guidance on assessing energy consumption, carbon emissions and other environmental factors associated with digital products and services. By adhering to these standards, ICT companies can make informed decisions to minimise their environmental footprint and contribute to sustainability goals.

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Notes

[1] The WBIF is currently financing the Rural Broadband Rollout project (phase 2), which aims to enable Serbia to connect the existing fibre backbone to an additional 815 settlements, 305 schools and at least 128 000 households in rural areas without access to a broadband network.

[2] According to the Word Bank, in 2022 the percentage of rural population was 50% in Bosnia and Herzegovina, 43% in Serbia 43%, 41% in North Macedonia, 36% in Albania, and 31% in Montenegro, significantly higher than the EU average (25%) and the OECD average (19%) (World Bank, 2024[44]).

[3] The Balkans Digital Highway initiative, under preparation with lead financing by the World Bank, follows a WBIF technical assistance project for the preparation of the Feasibility Study, Cost Benefit Analysis and Preliminary Design of the Balkans Digital Highway network, completed in October 2023. For more

information see: https://wbif.eu/project-detail/PRJ-MULTI-DII-006 and https://www.wbif.eu/technicalassistancegrants//WB22-REG-DII-02.

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[9] Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation), see: http://data.europa.eu/eli/reg/2016/679/oj.

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[11] Staff count reported at the end of 2023 for the respective authorities for free access to public information and personal data protection in the Western Balkan economies: BiH (11), Kosovo (4), Montenegro (29) and North Macedonia (20), in contrast to Serbia (115) and Albania (60). This staff count includes personnel for both competences related to free access to information and personal data protection.

[12] Proposal for a Regulation of the European Parliament and of the Council on measures to reduce the cost of deploying gigabit electronic communications networks and repealing Directive 2014/61/EU (Gigabit Infrastructure Act), see: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52023PC0094.

[13] Data provided to the OECD by relevant institutions from WB6 economies.

[14] SIGMA-OECD monitoring reports based on the Methodological Framework for the Principles of Public Administration, see: https://www.sigmaweb.org/publications/monitoring-reports.htm.

[15] Pillar 1 of the new Growth Plan underlines the importance of the integration of the region into EU trust services once national legislation is compliant with eIDAS. Currently, only Albania, Montenegro and Serbia are aligned.

[16] Regulation (EU) 2024/903 of the European Parliament and of the Council of 13 March 2024 laying down measures for a high level of public sector interoperability across the Union (Interoperable Europe Act), see: http://data.europa.eu/eli/reg/2024/903/oj.

[17] In Albania, the donor funded programmes “CoSolve-19” and “ConnectIT 2.0” supported 300 and 75 SMEs, respectively, in their digitalisation endeavours. In Bosnia and Herzegovina, the EU and donor funded “Go Digital in BiH” programme co-financed SME digitalisation. In Kosovo, the donor-funded “Access” programme supported 62 businesses in the period 2019-2022.

[18] Web Content Accessibility Guidelines (WCAG) 2.0 provide recommendations for making web content more accessible to people with disability. Adhering to these guidelines also enhances the usability of web content for all users.

[19] The development objective of the Kosovo Digital Economy (KODE) project is to improve access to better quality and high-speed broadband services in project areas and to online knowledge sources, services and labour markets among citizens, and public and academic institutions.

[20] Four UN agencies (UNDP, UNICEF, UN Women and UNFPA) launched the IT Girls initiative in BiH aimed at bridging the digital gender gap and promoting equal opportunities in the marketplace, workplace and community through high-quality digital skills training.

[21] Albania is currently establishing the Omni-Channel Contact Centre to provide support through various channels, including the virtual assistant, a reshaped helpdesk support, phone calls and face-to-face interactions as the very last resource. In addition, Youth Innovation Centers should offer face-to-face guidance on using e-Albania, host ICT training courses to boost digital skills and provide basic digital skills training.

[22] The Computing Power Goes Green project (GO_GREEN) is under the Transnational Cooperation Programme Interreg V-B "Balkan-Mediterranean 2014-2020", co-funded by the European Union, see: http://www.interreg-balkanmed.eu/approved-project/51/.

[23] Directive (EU) 2016/2102 of the European Parliament and of the Council of 26 October 2016 on the accessibility of the websites and mobile applications of public sector bodies (Text with EEA relevance), see: http://data.europa.eu/eli/dir/2016/2102/oj.

6 Greening cluster

This chapter aims to assess progress of the six Western Balkan (WB6) economies towards the green transition, focusing on the economy-environment nexus and evaluating the social and societal impacts of transitioning to a more environmentally sustainable economic model. It first analyses the pace at which WB6 economies are reducing carbon emissions by shifting away from fossil fuels, particularly within the energy and transportation sectors. The chapter then delves into the efficacy of policies aimed at adaptation and safeguarding fragile ecosystems and vulnerable communities. The final section addresses the economic and environmental hurdles stemming from the increasing demand for raw materials and linear supply chains within the region. Recommendations outline pathways for the region to advance towards becoming greener and more sustainable, all the while preserving economic competitiveness.

Key findings

The six Western Balkan (WB6) economies have made some progress in developing regulations and policies to facilitate the green transition in recent years, gradually aligning with the developments outlined in the Green Agenda for the Western Balkans. Some **key achievements** include:

- In acknowledgement of the increasing impact of climate change on their competitive landscapes, all WB6 economies have developed regulatory and policy frameworks setting targets for decarbonisation, aligning with the regional goal of achieving climate neutrality by 2050. These frameworks, in line with the COP28 agreement on phasing out fossil fuels, lay the groundwork for future actions, and prioritise sustainability and resilience.
- While reliance on fossil fuels in key emitting sectors persists, WB6 economies are actively expanding the adoption of renewable energy sources by implementing de-risking mechanisms and renewable support schemes. Efforts to enhance energy efficiency have also been strengthened.
- Depollution initiatives are underway, with substantial investments earmarked for water supply and sanitation infrastructure across all WB6 economies in response to escalating water and soil pollution levels. The Western Balkans Soil Partnership has also made a regional commitment to safeguard soils from contaminants.
- Amidst the current economic backdrop emphasising the risks of depending on globalised linear supply chains and low-cost virgin raw materials, the Western Balkans has witnessed a notable shift towards transitioning to a circular economy. Driven by whole-of-society initiatives, policy frameworks have been developed that provide clear guidance on priority sectors for maximising economic and environmental benefits, as well as fostering value creation in circular production and consumption.

Although progress has been made, the region needs to further enhance the implementation and impact of greening policies to ensure sustainable economic opportunities. **Key challenges** lie in the following areas:

- While all WB6 economies have committed to achieving carbon neutrality, they are still in the early stages of addressing the socio-economic impact of decarbonisation on affected businesses, regions and populations. Notably, access to green finance and training for the private sector on compliance with increasing mitigation measures remains limited, particularly in response to the European Union's (EU) Carbon Border Adjustment Mechanism.
- Despite recent policy improvements, the Western Balkans has seen limited initiatives to address air pollution, a crucial environmental and health concern, and there is a need to further improve air quality monitoring systems.
- The protection and restoration of ecosystems, which is essential for ensuring the sustainable economic development of the region, is advancing at slow pace. Overarching land-use management frameworks are lacking, hampering the effective planning, monitoring and use of land resources to maximise economic, social and environmental benefits. Moreover, economic activities such as tourism, mining and agriculture continue to threaten biodiversity conservation and ecosystem health.
- WB6 economies have witnessed a constant increase in waste generation per capita, and effective waste management remains a significant challenge throughout the region, placing substantial pressure on already strained resources, infrastructure and ecosystems. The

recycling rate of municipal waste among the economies (7.1% on average) remains over 40% lower than in the EU, leading to increased resource depletion.

Introduction

Environmental pressures and the impacts of climate change present significant challenges for the WB6 economies, jeopardising their ability to achieve sustainable growth and hindering competitiveness. The region faces threats from diminishing natural resources and the erosion of crucial environmental services, posing risks to both economic and social well-being.

By endorsing the Green Agenda for the Western Balkans at the 2020 Sofia Summit, the region committed to achieving carbon neutrality by 2050 and aligning with key elements of the European Green Deal. In addition to carbon neutrality, these include unlocking the potential of the circular economy; combatting air, water and soil pollution; promoting sustainable food production and supply methods; and ensuring biodiversity protection and ecosystem restoration.

The pace at which WB6 economies transition away from the use of fossil fuels towards renewable energy sources in its power sector and low-carbon transportation systems will be pivotal in ensuring long-term energy security and maintaining competitiveness in a progressively decarbonising global economy. As WB6 economies strive to achieve carbon neutrality, their ability to tackle the socio-economic impacts of decarbonisation on affected regions, industries and workers, ensuring a fair and inclusive transition, will indicate the region's preparedness for the future.

Moreover, the effectiveness of policies addressing adaptation and the protection of fragile ecosystems and vulnerable populations will determine the WB6's ability to withstand the adverse impacts of climate change and build equitable and resilient human-environment systems.

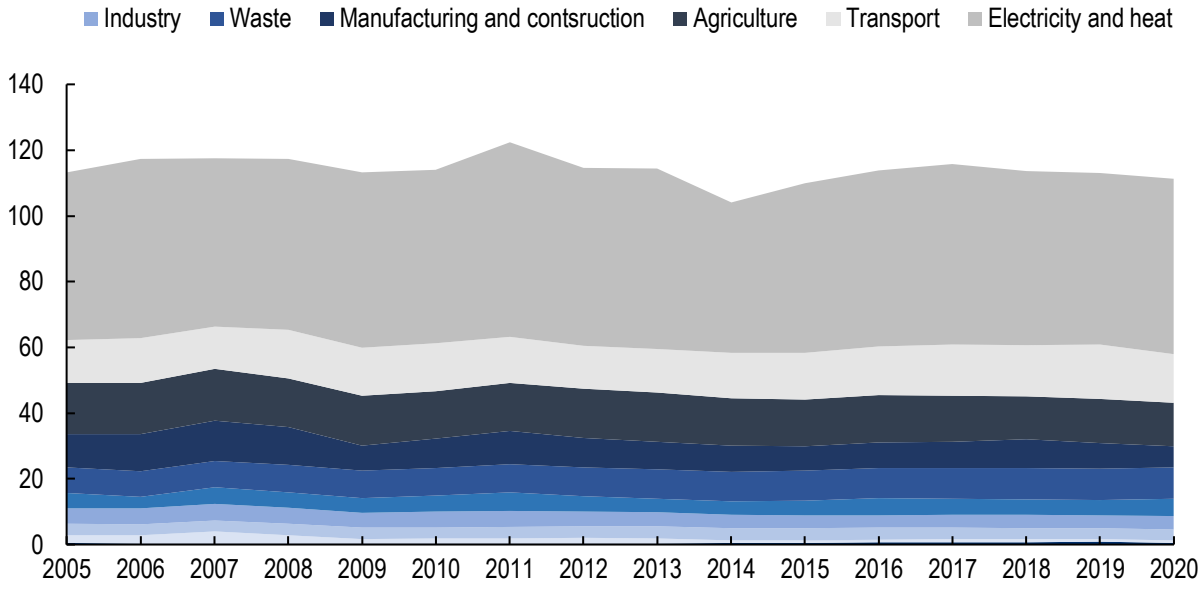
Addressing the region's economic and environmental challenges arising from the growing demand for raw materials and linear supply chains will be imperative to mitigate risks to economic stability and foster a more sustainable development path. WB6 economies' low waste recycling rate and high resource intensity continue to impose significant burdens on the environment. Embracing the circular economy has emerged as a viable solution to address these pressing environmental concerns and will allow the economies to foster sustainable and resilient economic growth, and unlock new business opportunities.

Decarbonising economies

The Western Balkans stands out as one of the regions in Europe most severely impacted by the effects of climate change. Projections indicate that this trend is expected to persist, with estimates suggesting temperature increases ranging from 1.7 to 4.0°C by the end of the century (RCC, 2018[1]). The energy sector represents the main greenhouse gas (GHG) emitter in the region (48% of total emissions) due to its reliance on energy production from burning lignite, a form of coal characterised by its low calorific value and significant pollution levels. The region hosts some of the most polluting power plants in Europe, which are responsible for tens of thousands of premature deaths annually due to air pollution, in addition to emitting substantial quantities of GHGs that exacerbate climate change (JRC, 2022[2]). The region also heavily relies on oil for the transport sector, which is the second most emitting sector, accounting for 13% of total GHG emissions (Figure 6.1).

Figure 6.1. Total annual greenhouse gas emissions in the WB6 economies by economic sector (2005-20)

In metric tons of carbon dioxide ($MtCO_2$) equivalent



Note: Data exclude land-use change and forestry emissions sources or sinks. No data for Kosovo.
Source: Climate Watch (2024[3]).

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In line with the EU ambition to become climate neutral by 2050 and to support the implementation of the EU *acquis*, the WB6 economies have committed to achieving carbon neutrality by 2050 by endorsing the Green Agenda for the Western Balkans and its action plan. Decarbonisation, involving the reduction of GHGs across various sectors, demands substantial changes throughout the economy. This includes altering how energy is generated, transforming production and delivery methods of goods and services, and implementing new approaches to land management. Decarbonisation not only serves to achieve net-zero objectives, but it also presents opportunities for new green economic ventures.

Gearing up to combat climate change

Climate change mitigation policies and regulatory frameworks are pivotal in shaping climate action efforts in the Western Balkans. As the region grapples with the impacts of climate change, the development and implementation of robust policies to reduce GHGs and limit further environmental degradation and climate-related risks are essential. A strong regulatory framework also ensures accountability, transparency and enforcement mechanisms to progress climate goals. By aligning their policies with international standards and commitments, the economies of the Western Balkans can support private sector competitiveness, attract investment, foster innovation and enhance regional co-operation in tackling climate change challenges.

Climate change mitigation policies are gaining momentum, increasingly targeting greater emissions reductions

In line with international commitments, all WB6 economies except Bosnia and Herzegovina, have established legal frameworks that enable regulatory mechanisms for low-carbon development and climate change resilience. Alongside Albania, Montenegro and Serbia, which already had a climate change legal framework in the Competitiveness Outlook assessment in 2021, Kosovo adopted its framework in 2024, while North Macedonia's Law on Climate Change awaits adoption. These laws are pivotal in transposing relevant EU directives[1] and establishing the necessary structures for monitoring, reporting and verifying GHGs.

Economy-wide targets for reducing GHG emissions until 2030 have been set in long-term climate change strategies in all economies, with projections until 2050 in most economies (Table 6.1). Climate change strategies provide a set of policies and measures spanning various sectors, each contributing to the overall achievement of national climate commitments. To ensure the mainstreaming of climate objectives across sectors, co-ordination among stakeholders responsible for climate change mitigation has been intensified in all economies, although there is a need to strengthen administrative capacities. Notable progress includes the re-establishment of National Climate Change Councils in Kosovo and Serbia, and the planned establishment of North Macedonia's climate change co-ordination bodies upon adopting the Law on Climate Change.[2]

Table 6.1. Climate change strategies in the WB6 economies

Economy		Strategy	Adoption year	Timeline
Albania		National Strategy for Climate Change	2019	2020-2030
Bosnia and Herzegovina	State level	Climate Change Adaptation and Low Emission Development Strategy	2023	2020-2030 with projections until 2050
	Federation of Bosnia and Herzegovina (FBiH)	Environment Strategy and Action Plan	2023	2023-2030
	Republika Srpska (RS)	Environment Strategy and Action Plan	2023	2023-2030
	Brčko District	Environment Strategy and Action Plan	2023	2023-2030
Kosovo		Climate Change Strategy	2019	2019-2028
Montenegro		National Climate Change Strategy	2015	2015-2030
		National Strategy and Action Plan for Low-Carbon Development	*To be adopted*	2030 with projections until 2050
North Macedonia		Long-Term Strategy on Climate Action and Action Plan	2021	2021-2030 with projections until 2050
Serbia		Low-Carbon Development Strategy	2023	2023-2030 with projections until 2050

As Non-Annex I signatories[3] to the UN Framework Convention on Climate Change (UNFCCC), and in line with recently adopted climate change strategies, all economies have increased their mitigation ambitions during the latest revision of their national climate pledges, also known as nationally determined contributions (NDCs) (Table 6.2). While Kosovo is not a party to the UNFCCC, it started to draft its voluntary NDCs in 2021 with the support of international partners.

Table 6.2. Emission reduction targets as part of nationally determined contributions (NDCs) in the WB6 economies

Economy	GHG emissions reduction target (first NDC)	GHG emissions reduction target (revised NDC)
Albania	11.5% below business-as-usual by 2030 (CO_2)	20.9% below business-as-usual by 2030
Bosnia and Herzegovina	15.2% by 2030 compared to 1990 levels	Conditional 36.8% below 1990 levels by 2030 (unconditional target of 33.2% by 2030 compared to 1990 levels)
Kosovo (voluntary)	n/a	16.3% compared to 2016 levels by 2030
Montenegro	30% below 1990 levels by 2030	35% below 1990 levels by 2030
North Macedonia	31% below 1990 levels by 2030	Net 82% by 2030 compared to 1990 by 2030
Serbia	9.8% below 1990 levels by 2030	33.3% compared to 1990 levels by 2030

Note: Kosovo's voluntary NDCs are yet to be adopted.

All WB6 economies are taking steps to address the critical decarbonisation of predominantly coal-based energy sectors alongside enhanced climate change strategies and revised NDCs. All have committed to implementing GHG emissions measurement, reporting and verification through National Energy and Climate Plans (NECPs) aligned with the Energy Community's 2030 targets. Albania and North Macedonia have adopted their NECPs within the deadline, which are to be updated following recommendations from the Energy Community, while others are drafting theirs with delays that could impede the concretisation of responses to the energy and climate crisis. NECPs are crucial for achieving 2030 decarbonisation goals in the region and include measures to develop adequate carbon pricing mechanisms to control emissions, alongside targets for renewables and energy efficiency. These efforts are key given limited economic instruments to discourage high-carbon behaviour and ongoing subsidies for coal-fired power. NECPs will also be a future vehicle to expand decarbonisation efforts to other emitting sectors such as transport and agriculture.

Implementation of planned mitigation measures is moving forward at a slow pace, impeding the region's competitiveness

Despite recent policy improvements, the enforcement of broader mitigation measures has been limited across economies during the assessment period. However, efforts to enhance enforcement are anticipated in the upcoming period with the development of NDC implementation roadmaps that delineate responsibilities, timeframes and funding sources, and include monitoring and evaluation frameworks. For instance, the roadmap for Bosnia and Herzegovina includes identified investment needs for each sector, with the highest priority given to energy generation, buildings and transportation.[4]

Economic instruments and incentives to achieve GHG emissions targets remain scarce throughout the region. A carbon tax for large industrial polluters, feebate or excise taxes on individual fuels, or an Emissions Trading System (ETS) have yet to be introduced in most of the region to discourage high-carbon activities. However, most WB6 economies' climate change strategies foresee continuous alignment with the EU ETS and consider the introduction of appropriate carbon pricing instruments over upcoming years. Montenegro is the only economy that introduced an ETS in 2020,[5] with the first auction awarding emission credits and allocating collected funds announced in 2023. Nevertheless, there are identified issues with the conception of Montenegro's ETS scheme, such as the slow reduction in the cap until 2030, lack of clear rules for the end of free allowances and insufficient fines for non-compliance. In addition to being a key instrument in achieving climate goals, introducing a carbon pricing mechanism in all economies will be crucial to cope with the impacts of the EU's Carbon Border Adjustment Mechanism (CBAM) on high-carbon exports (Box 6.1).

Box 6.1. Carbon Border Adjustment Mechanism (CBAM)

What is the Carbon Border Adjustment Mechanism?

The EU's adoption of the CBAM in April 2023 is a significant step to address rising carbon prices under the European Emissions Trading System (EU ETS). The CBAM imposes financial obligations on covered goods, encouraging non-EU producers to adopt greener processes. It acts as an import duty, impacting countries exporting significant quantities of CBAM-covered goods such as electricity, aluminium, iron and steel, hydrogen, cement, and fertilisers.

The CBAM is meant to stimulate trading partners' industry and energy sector transformations. Mitigating measures include emission reduction initiatives by exporting entities, governmental support through incentives or financial aid, and introducing carbon pricing mechanisms.

CBAM requirements

CBAM will apply in its definitive regime from 2026. Until then, affected exporters must measure their emissions and send data to the importers' clients inside the EU, who report every quarter. From 2026, EU importers will declare the emissions embedded in their imports and surrender the corresponding number of certificates yearly. If importers can prove that a carbon price has already been paid during the production of the imported goods, the corresponding amount can be deducted. Furthermore, if an economy's electricity market is integrated with the EU's, its electricity sector will be exempt from any CBAM obligations, contingent upon meeting additional criteria. These criteria include a legislative commitment to achieve climate neutrality by 2050, an ETS for electricity until 2030 with a price equivalent to that of the EU ETS, or ambitious renewable energy targets, all aligned with the Energy Community obligations.

Impact on the Western Balkans

In 2022, exports of CBAM products to the EU accounted for 22% of all Western Balkan exports to the EU, although varied considerably across economies. Montenegro and Bosnia and Herzegovina, which are predominantly reliant on coal and aluminium exports, face heightened exposure. Serbia and North Macedonia, which are both reliant on coal-based electricity and iron and steel exports, anticipate similar repercussions. Conversely, Kosovo and Albania, which have different export structures, anticipate lesser impacts.

Sources: European Commission (2024[4]); Allert, Larina and Glaser (2023[5]); EBRD (2024[6]); World Bank (2023[7]).

Economies throughout the region remain underprepared for the CBAM, with limited efforts undertaken to organise training and prepare the private sector for adapting their operations to upcoming obligations, further creating trade barriers for exporters to the EU. Only Serbia, through its Chamber of Commerce and Industry, has taken initial steps by conducting sector-specific training sessions for industries affected by the CBAM. Additionally, FBiH has outlined plans for similar technical support in its Green Transition Programme (2024). Furthermore, the absence of comprehensive strategies to tackle climate and environmental risks, coupled with the lack of green taxonomies and disclosure requirements, compound the challenges faced by businesses in the region. As a result, businesses encounter difficulties in accessing green finance opportunities, limiting their ability to invest in sustainable initiatives and remain competitive in the global market. Notably, the introduction of disclosure requirements for large corporates and other economic agents is lacking, hindering transparent reporting on environmental impacts.

Green taxonomies, which serve as a key enabler for the establishment of a green loan and bond market, have yet to be developed in most economies. Nonetheless, interest in such a market exists. For instance, Serbia, as the first economy to issue sovereign green bonds in 2021, experienced high investor interest, leading to subsequent projects aimed at reducing GHG emissions by about 150 000 tCO_2 per year (Government of the Republic of Serbia, 2024[8]). Similarly, North Macedonia's inaugural green bond auction in 2023 saw demand surpass supply nearly threefold, indicating a growing interest in sustainable investments (Ministry of Finance North Macedonia, 2023[9]).

Transitioning to clean energy

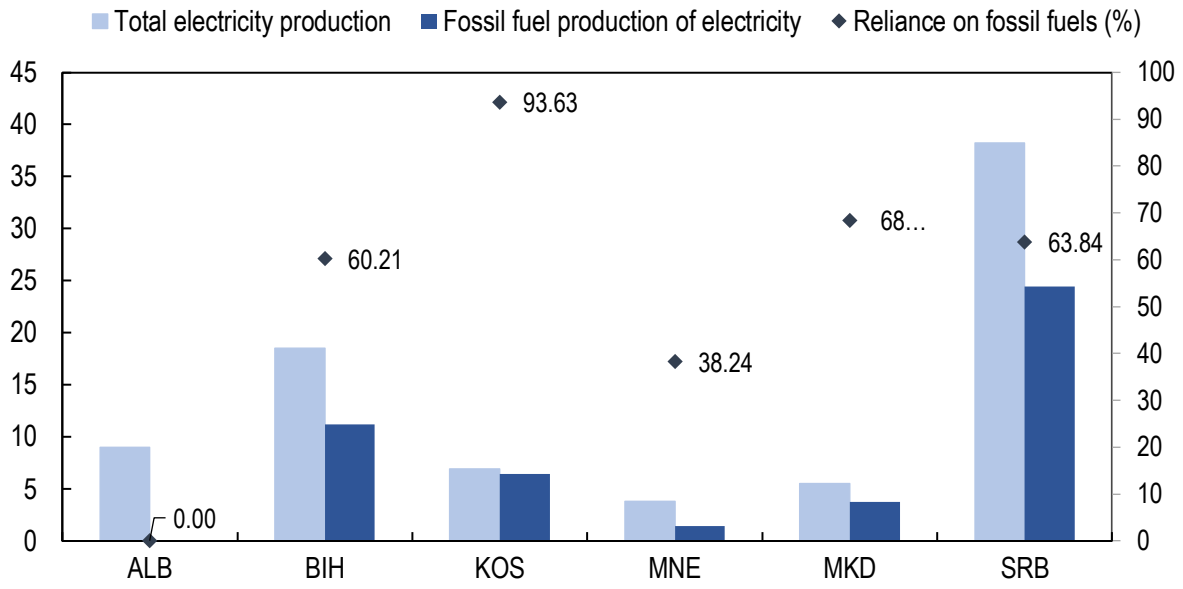
Transitioning to clean energy[6] is crucial for limiting climate change and reducing air pollution, which has long plagued the region due to its reliance on outdated coal-fired power plants. Embracing renewables addresses environmental concerns and positions the region for sustainable economic growth, attracting investment, stimulating job creation and fostering regional co-operation in achieving shared energy goals. Moreover, energy efficiency, or an economy's "hidden fuel", is a prerequisite for decarbonisation at the lowest possible cost. To undertake necessary energy efficiency investments, economies need competitive energy efficiency markets, a clear policy direction, strong legislation and modern building codes.

Reliance on fossil fuels remains high, and there are limited efforts to ensure a just and fair phase out

The energy sector accounts for most GHG emissions in the Western Balkans, with diversification low and dependence on fossil fuels (coal in particular) very high. In 2021, the region still relied on fossil fuels for more than 50% of its electricity production, although this differs significantly between economies: Albania did not rely on fossil fuels at all, whilst Kosovo almost exclusively sourced its electricity from fossil fuels (Figure 6.2).

Figure 6.2. Reliance on fossil fuels for electricity generation in the WB6 economies (2021)

In GWh and % of generated electricity



Source: Eurostat (2023[10]).

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The subsidisation of coal-fired power generation across most of the region distorts the energy market by artificially increasing the economic viability of coal-fired generation and lowering energy prices, hence making economies more vulnerable to rising energy import prices. Subsidies to coal-fired generation between 2018 and 2022 amounted to more than EUR 400 million in the WB6 region, with Serbia and Bosnia and Herzegovina making up 90% of these subsidies (Energy Community, 2023[11]).

While phasing out fossil fuels and their subsidisation will be key to fulfilling the region's aim of reducing carbon emissions and supporting the uptake of renewable energy and energy efficiency, it will bring about multifaceted impacts on both coal-dependent regions and populations. As phase out efforts will directly impact the estimated 138 000 jobs tied to coal mining and coal-based power generation in the region (Ruiz Castello et al., 2021[12]), ensuring adequate social protection policies, including labour market programmes to equip workforces and enhance skills for the green transition, will be of utmost importance (see Chapter 3). Some economies have adopted strategic documents to ensure that the benefits and associated costs of transitioning to a low-carbon economy are distributed equally across society, without exacerbating inequalities and economic downturns. In addition to Serbia's 2019 Roadmap for a Just Transition, North Macedonia adopted the Roadmap for a Just Transition in 2023 and Bosnia and Herzegovina developed a draft Roadmap for the Transition of Coal-Rich Regions in 2023. These documents outline options for energy conversion, recommendations for retraining and labour mobility, and strategies for repurposing land previously used for mining and related facilities. In Bosnia and Herzegovina, four local self-government units will act as pilot areas for a just transition towards decarbonisation through identifying strategies to reduce emissions and promoting innovative technologies and practices.[7]

Renewable energy remains underutilised, but measures to promote its uptake and diversification are gaining momentum

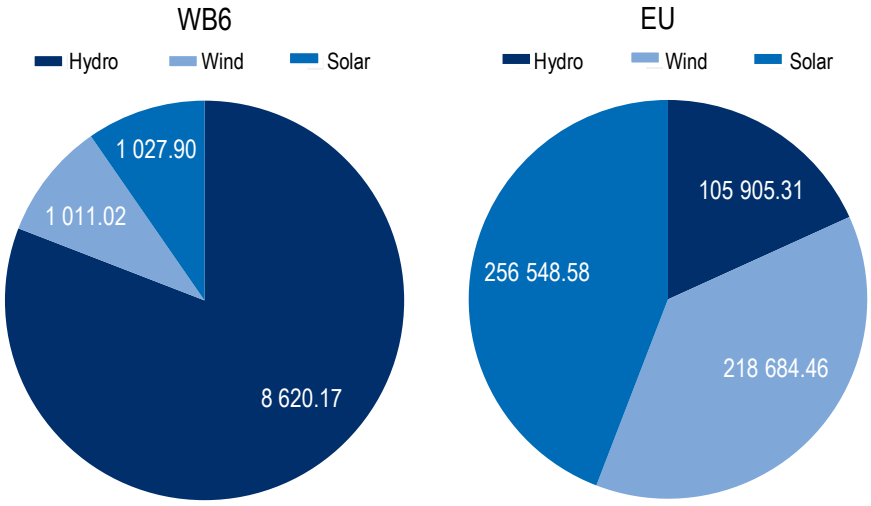
While renewable energy capacity has increased across the WB6 region since the last assessment, diversification remains low compared to the EU. Wind has emerged as the EU's primary energy source, surpassing hydro and solar in recent years. The share of hydro remains the primary renewable energy source in the Western Balkans, although it has seen a decline in the EU since 2021 and now represents the smallest share of installed capacity among wind, solar and hydro (Figure 6.3).

The potential for non-hydro renewables, especially solar and wind, remains largely untapped in the Western Balkans. While the region is endowed with abundant technical potential[8] for the deployment of these energy sources (Figure 6.4), the growth in their installed capacity has been continuing at a slow pace compared to the rate seen in EU member states, showing room for improvement in policies and incentives to accelerate their development. Underdeveloped electricity grid coverage and capacity are another challenge for integrating renewables into the energy system (see Chapter 2).

To support this development, a general trend observed in renewable energy policies among WB6 economies is enhanced alignment with the EU's Clean Energy Package, characterised by adopting laws to boost renewable energy sources (RES). New RES laws have been developed across the region, although Montenegro and North Macedonia are currently lagging behind in this regard. These laws have a stronger focus on competitive auctions for the procurement of additional RES capacities (Box 6.2).

Figure 6.3. Installed capacities of renewable energy by sources in the WB6 economies and the EU (2021)

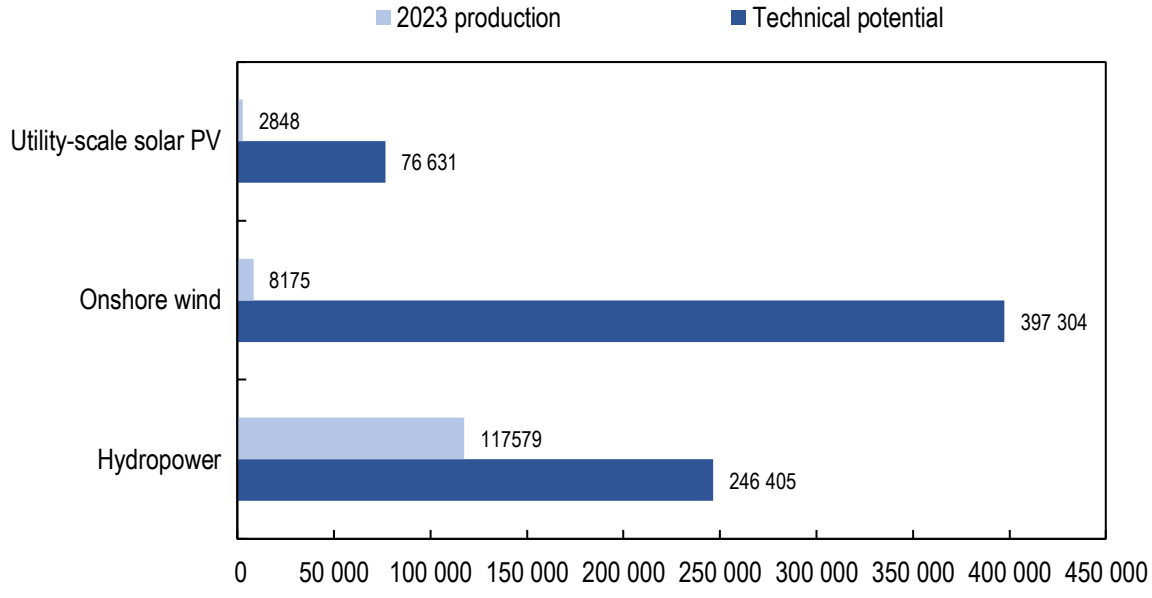
% of total installed renewable energy



Source: IRENA (2023[13]).

Figure 6.4. Electricity generation and technical potential for hydropower, wind and utility-scale solar in the power sector in the WB6 economies (2023)

In terajoules



Source: IRENA (2024[14]).

Box 6.2. Competitive auctions to promote the uptake and diversification of additional RES capacities

Following the implementation of essential regulations for the RES auction process, Serbia initiated its inaugural auctions for RES in June 2023, offering 50 MW of solar power and 400 MW of wind power. Serbia chose the Contract for Difference approach to secure these renewable energies. For wind energy, all 400 MW were auctioned off successfully, with winning bids falling between 64.5 EUR and 79.0 EUR per MWh. Additionally, four solar energy projects received allocations totalling 25.2 MW, with the successful bids ranging from 88.7 EUR to 98.8 EUR per MWh.

Albania has also successfully used competitive auctions: the third renewable energy auction, and the first dedicated to onshore wind, took place in 2023, with three bidders granted a total capacity of 222 MW. The winning bids were between 44.88 EUR and 74.95 EUR per MWh. Albania reached another important milestone in 2023 as the Karavasta PV project, with a capacity of 140 MW, became operational at the end of the year.

Sources: Energy Community (2023[11]); Balkan Green Energy News (2023[15]).

Feed in tariffs are increasingly being phased out or discontinued altogether in the Western Balkans. However, despite recognising the value of competitive mechanisms for renewable projects, some economies' legal frameworks still underutilise these tools, thus not unlocking the full potential of a green transition. Throughout the WB6 a common challenge in the further update of RES generation capacities is the insufficient involvement of the private sector and the insufficient utilisation of existing RES potential that focuses on a diversified RES generation mix. Improving and streamlining licensing procedures could further accelerate the deployment of additional RES generation projects and support the WB6 to better diversify their RES portfolios, which currently display a strong overreliance on hydro.

Support for energy efficiency is reinforced throughout the region

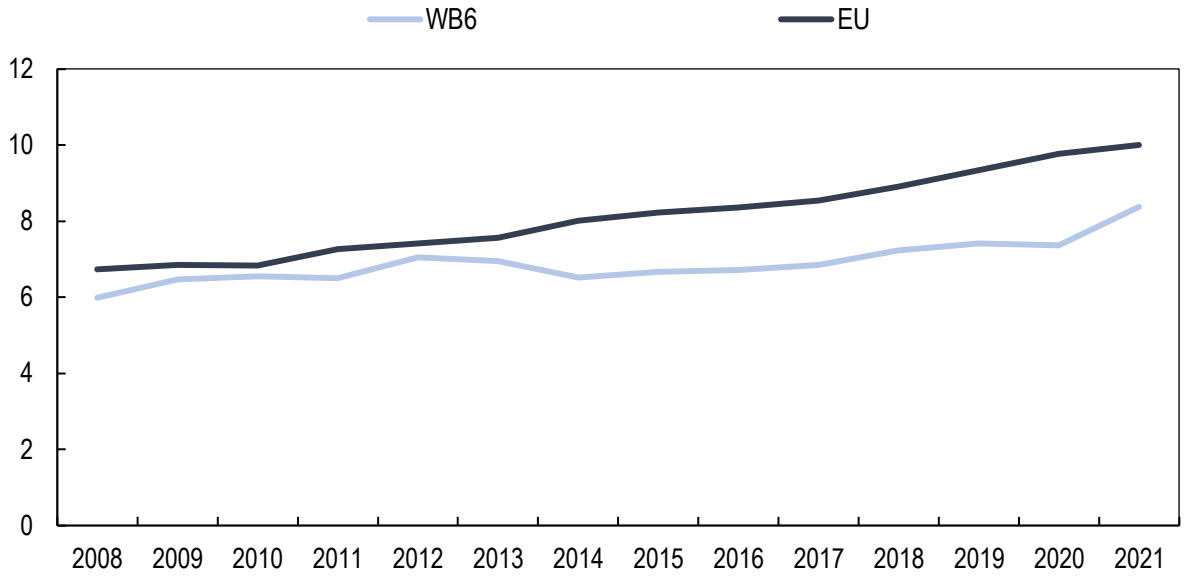
The region's energy productivity – one indicator of energy efficiency that measures economic output per unit of gross available energy in a specific area – remains about 20% lower than the EU average, with this gap persisting and having increased over the past decade (The WB6 economies are increasingly implementing energy efficiency policies and tools to enhance energy efficiency, with new related laws in the drafting process or adopted. Support schemes for energy efficiency are being deployed across all economies, albeit with Bosnia and Herzegovina notably lagging in implementation efforts. There is consensus on the need to strengthen legal frameworks for energy efficiency, particularly by adopting additional secondary legislation, to fully align with the EU and Energy Community *acquis* and to ensure that commitments are implemented.

Figure 6.5). Between 2008 and 2020, energy productivity in the region increased but then plateaued and started a declining trend, likely due to economic contraction post-COVID-19 and the Ukraine war.

The WB6 economies are increasingly implementing energy efficiency policies and tools to enhance energy efficiency, with new related laws in the drafting process or adopted. Support schemes for energy efficiency are being deployed across all economies, albeit with Bosnia and Herzegovina notably lagging in implementation efforts. There is consensus on the need to strengthen legal frameworks for energy efficiency, particularly by adopting additional secondary legislation, to fully align with the EU and Energy Community *acquis* and to ensure that commitments are implemented.

Figure 6.5. Energy productivity in the WB6 economies and the EU (2008-21)

Gross domestic product (2010 EUR in PPP) per kilogram of oil equivalent consumption



Notes: No data for Kosovo in 2021. PPP: purchasing power parity.
Source: Eurostat (2024[16]).

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In this regard, a common trend is the focus on enhancing audit and certification schemes for the energy performance of buildings. Long-term building renovation strategies are also increasingly being drafted as a long-term strategic tool to enhance energy efficiency both in the private and public building sector. Serbia has already adopted such a strategy, and all other WB6 economies are working on draft versions. Kosovo successfully makes use of a dedicated energy efficiency fund as a financing vehicle to support investments in energy efficiency. Montenegro is implementing energy efficiency and environmental projects through an Eco Fund, and North Macedonia is preparing a dedicated energy efficiency fund. All WB6 economies should consider establishing such funds, as sometimes institutional capacities and financing means for energy efficiency are limited.

Promoting low-carbon mobility

The transport sector in the Western Balkans is still heavily reliant on fossil fuels and lacks sustainable and innovative solutions. Transport represents the second largest source of GHG emissions and a significant source of local pollution. The promotion of a greener and more sustainable transport network, combined with cleaner fuels and higher fuel efficiency, can help reduce the environmental and health impacts of transport in the region.

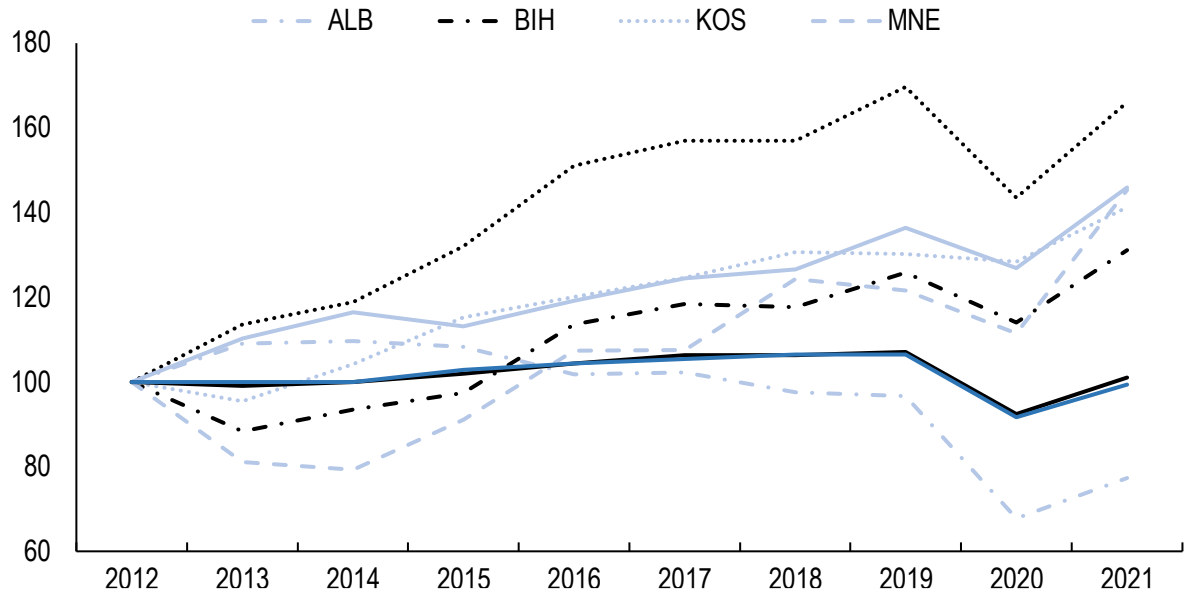
The environmental sustainability of the transport sector is increasingly featuring in strategic plans, combined with on-the-ground measures

WB6 economies are gradually implementing policies aimed at promoting the shift towards less carbon-intensive and more environmentally sustainable transport systems, albeit at varying paces and with distinct focuses. Overall, the region is grappling with the challenge of reducing the environmental footprint of its transport sector, which significantly contributes to overall GHG emissions (Figure 6.6). While each

economy has its unique policy framework for environmentally sustainable transport, there is evidence of increased alignment with the Smart and Sustainable Mobility Strategy for the Western Balkans, developed by the Transport Community in 2021 (Transport Community, 2024[17]).

Figure 6.6. Transport related greenhouse gas emissions in the WB6 economies, the EU and the OECD (2012-21)

2012 Index = 100



Sources: ITF Transport Related GHG Emissions questionnaire filled by respective economies; IEA (2023[18]).

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Several economies have made significant strides in advancing their policy frameworks towards decarbonised transport. Albania's Transport Sector Strategy 2023-30 and Kosovo's Multimodal Transport Strategy 2023-30 are notable examples as they integrate sustainable transport considerations and establish specific emission reduction targets across different modes of transportation. Comprehensive policies to support the sustainability of the transport sector have yet to be adopted in Bosnia and Herzegovina and North Macedonia.

Measures aimed at promoting the adoption of low- and zero-emission vehicles have been implemented throughout the region. In Albania, FBiH, Montenegro and Serbia, incentives for electric vehicles are available, with plans to introduce them in Kosovo. Serbia also offers tax exemptions for electric and hybrid vehicles owners. Initiatives such as the deployment of charging infrastructure in Albania and North Macedonia, as well as Serbia's issuance of a green bond[9] for environmentally friendly transport projects, underline enhanced commitment to sustainable mobility. Investments in upgrading transport infrastructure, such as electrifying railway lines in Albania and modernising the ports of Durres in Albania and Bar in Montenegro with a focus on clean energy, signify a regional trend towards greener transportation modes.

While there has been progress in implementing low-carbon mobility measures, it is often hindered by bureaucratic delays, inadequate funding and infrastructural constraints. The transposition of EU directives, such as the Alternative Fuel Infrastructure Directive, remains incomplete in some economies, affecting the

deployment of alternative fuel infrastructure. Data collection on sustainable transport indicators faces hurdles, with inconsistencies in reporting and limited transparency posing challenges for monitoring progress effectively.

Despite these challenges, the region showcases pockets of innovation and collaboration. Initiatives such as the deployment of e-charging stations along the Trans-European Transport Network (TEN-T) corridors and regional projects funded by international organisations demonstrate a collective effort towards sustainable mobility.

Recommendations for decarbonising economies

- **Consider introducing carbon pricing alongside a set of supporting policies, including those protecting vulnerable populations**. Carbon pricing can take two main forms: a carbon tax or an emissions trading system (ETS). A carbon tax provides investment security for companies by offering a predefined price path and ensuring relatively predictable government revenues. Conversely, an ETS, with its emissions cap, provides greater precision and certainty in achieving specific emission reduction targets. While a carbon price can send a financial signal, it is only effective if low-carbon substitutes are available and affordable. In the case of electricity, additional policies will be needed to incentivise the adoption of renewables in the region. Potential impacts on vulnerable groups should also be assessed, in particular regarding retail electricity prices and coal phase out. Carbon pricing can be applied to the whole economy or only to the sectors covered by the CBAM. The latter will offset the CBAM fee, thereby alleviating the overall burden imposed by the mechanism. Additionally, it serves as a potent incentive for producers to actively reduce the emissions intensity of their products. Montenegro is the only economy in the Western Balkans to have implemented carbon pricing in 2020, and the challenges and subsequent lessons learned can offer valuable insights for other WB6 economies.
- **Prioritise comprehensive capacity building and financial support for the private sector to address new obligations related to climate change mitigation measures and the CBAM**. This includes tailored assistance and guidance to ensure understanding and compliance with upcoming requirements, such as measuring emissions and collecting relevant data. Additionally, implementing targeted awareness campaigns and providing financial incentives and technical support for businesses to transition towards low-carbon and sustainable production methods and business models can bolster competitiveness and resilience in the face of evolving regulatory frameworks. Such support and incentives could be financed by revenues generated by the carbon tax or the auctioning of emissions allowances in the case of an ETS. The issuance of green bonds, which remain nascent in the region, could also help mobilise private capital towards climate mitigation.
- **Ensure the efficacy of climate change mitigation efforts through collaborative multilateral co-operation**. To bolster the design and implementation of climate change policies, inter-institutional working groups in the Western Balkans should consider engaging in multilateral co-operation opportunities. Joining platforms such as the OECD's Inclusive Forum on Carbon Mitigation Approaches (IFCMA) would enable the WB6 to learn from global peers and gain insights into the effectiveness of various carbon mitigation approaches worldwide (Box 6.3).

Box 6.3. OECD Inclusive Forum on Carbon Mitigation Approaches (IFCMA)

What is the IFCMA?

The IFCMA, an initiative spearheaded by the OECD, is designed to enhance global efforts to reduce carbon emissions. It achieves this through fostering the exchange of data and information on different emission reduction approaches used by countries around the world. It facilitates learning among countries about different approaches and encourages inclusive dialogue to help countries work together more effectively.

Why is the IFCMA important?

Countries use a variety of policies to mitigate emissions, but grasping the comprehensive impact of these efforts can be challenging. The IFCMA provides a clear view of what different countries are doing and how effective their policies are so that countries can:

- Learn from each other's successes and challenges.
- Develop more effective policies.
- Work together more effectively to reduce global emissions.

What are the IFCMA's key activities?

- Taking stock of different carbon mitigation approaches: This involves collecting information on the policies that countries are using to reduce emissions.
- Mapping policies to emissions: This entails determining which emissions reductions are attributable to different policies.
- Estimating the effects of policies on emissions: This encompasses efforts to quantify the emissions reductions achieved by each policy.
- Exploring methodologies for computing carbon intensity: This involves developing methods for measuring the carbon footprint of products and sectors.
- Facilitating inclusive multilateral dialogue: This entails providing a platform for countries to discuss climate change issues in a non-confrontational setting.

With over 55 countries collaborating, the IFCMA's Steering Group sets the agenda and ensures continuity. Recent activities include reporting to the G20 finance ministers and leaders on the work of the IFCMA, the publication of a paper on carbon intensity metrics, and high-level events at COP28.

Source: OECD (2024[19]).

- **Ensure diversification when expanding RES generation capacities.** Diversification is crucial for enhancing energy security as it ensures a stable and reliable energy supply by spreading the risk across various energy sources, which can be particularly beneficial given the variable nature of some renewables such as solar and wind power. Diversification also stimulates technological innovation and economic development as investments can flow into a broader range of technologies and sectors, fostering competition and reducing costs. Focusing on diversification from the outset also reduces the risk that the potential of certain RES technologies is overlooked. WB6 economies should ensure that their policy frameworks, permitting processes and investment incentives are conducive to the deployment of a varied mix of renewable energy sources to ensure that the overwhelming share of hydropower is gradually accompanied with increases in wind and solar capacity.

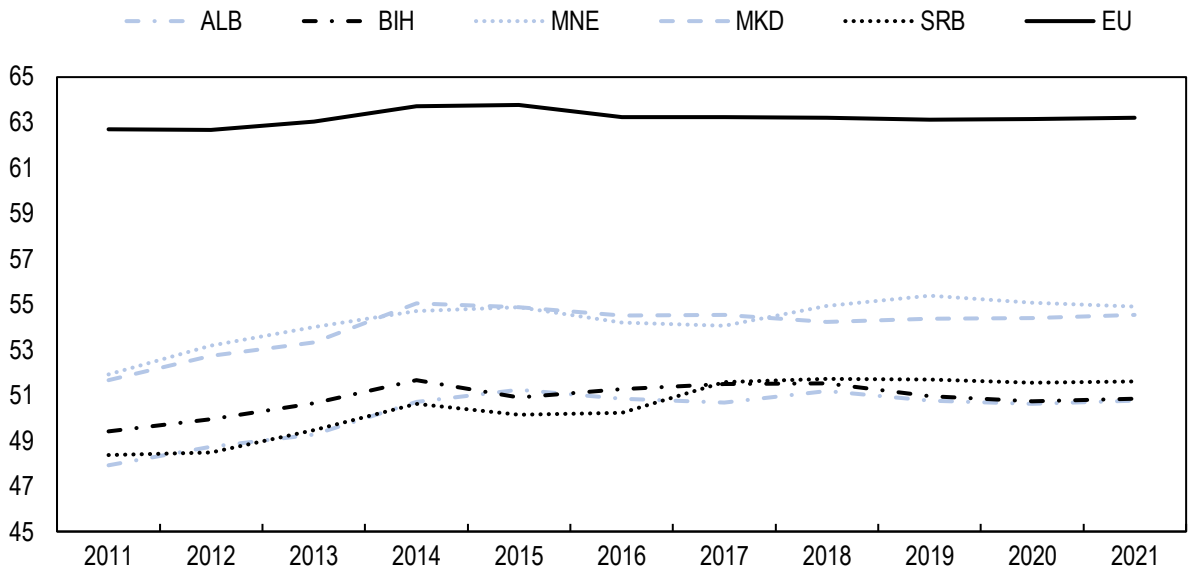
- **Increase financial resources for the implementation of energy efficiency projects.** To make full use of the potential of energy efficiency, the public and private sector must have adequate financing means at their disposal. Particularly in the early stages of enhanced focus on climate change mitigation and energy efficiency, dedicated support programmes are crucial for allocating financial resources to priority areas, where success can showcase the advantages and long-term savings of investments into energy efficiency. In this regard, dedicated capacity building and awareness-raising campaigns should also be implemented to promote energy efficiency among consumers and develop the required expertise in the public and private sectors.
- **Prioritise the alignment and implementation of national policies with the Smart and Sustainable Mobility Strategy for the Western Balkans.** To enhance the environmental sustainability of the transport sector, WB6 economies must focus on measures such as accelerating the adoption of low- and zero-emission vehicles, expanding charging infrastructure, and upgrading transport infrastructure with a focus on clean energy sources. Additionally, addressing bureaucratic delays, securing adequate funding, and improving data collection and reporting mechanisms will be essential for effective policy implementation and the monitoring of progress towards decarbonisation goals. Collaboration with international organisations and leveraging technical assistance and funding opportunities can further support the region's transition towards greener transportation modes.
- **Strengthen regional collaboration to promote low-carbon mobility**. WB6 economies should enhance collaboration and knowledge sharing to leverage best practices and overcome shared challenges. Establishing regional working groups or fora focused on sustainable mobility can facilitate the exchange of experience, promote joint initiatives and foster a sense of collective responsibility towards achieving environmental goals. The region can accelerate progress towards sustainable transport solutions that benefit all stakeholders by pooling resources and expertise.

Protecting ecosystems and citizens' well-being

Communities worldwide rely on intact ecosystems for their economic and social well-being. Diverse habitats provide indispensable resources and services such as clean air, water and food. Across the Western Balkans, marine, terrestrial and freshwater ecosystems are crucial for climate regulation and disaster mitigation. Forests and wetlands, for instance, act as natural carbon sinks and flood barriers. However, human-induced land-use changes, pollution and climate change are accelerating species extinction and habitat loss in the region. This disruption affects plants, animals and human settlements, leading to declining ecosystem services such as food and medicine, impacting citizens' livelihoods.

The Western Balkans is one of Europe's biodiversity hotspot regions and is renowned for its pristine landscapes and rich endemic flora and fauna; however, climate change continues to pose significant challenges in the region (IPCC, 2022[20]). The Western Balkans is more vulnerable and less equipped to address the impacts of climate change than the EU (Figure 6.7). Rising temperatures and more frequent extreme weather events in the future (floods and droughts in particular) would threaten vital ecosystems and human well-being, exacerbating land degradation and biodiversity loss and consequently impacting economic growth. Despite these challenges, current approaches to climate adaptation, nature conservation and disaster risk management often overlook integrating nature-based solutions. Except for air and freshwater quality, there appears to be a pervasive lack of awareness regarding the need for environmental protection, which is often perceived as costly and therefore clashes with other development goals in sectors such as infrastructure, energy, agriculture and tourism.

Figure 6.7. Notre Dame Global Adaptation Initiative (ND-GAIN) Country Index in the WB6 economies and the EU (2011-21)



Notes: The Notre Dame Global Adaptation Initiative (ND-GAIN) Index scores countries (0-100) on their climate vulnerability and readiness to adapt, with higher scores indicating better preparedness and resilience to climate change impacts. Data for Kosovo are not available.
Source: ND-GAIN (2024[21]).

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Adapting to climate change

The Western Balkans is particularly vulnerable to climate change due to its geographical location, socio-economic characteristics and existing environmental pressures. Some of the key vulnerabilities include water scarcity and drought, loss of biodiversity and related economic disruptions (such as agriculture, tourism and energy production). Water scarcity issues in North Macedonia and Serbia, though moderate according to the water exploitation index,[10] highlight the importance of managing water resources effectively to prevent future stress and ensure sustainable water availability (EEA, 2023[22]).

Freshwater also represents an important energy generation source in the region, as almost 20% of energy production is derived from hydropower (Eurostat, 2023[23]). This is particularly relevant for Albania, as almost all of its electricity production is derived from hydropower, making it highly vulnerable to the changing climate and annual fluctuations in precipitation.

Climate change adaptation policies are gaining momentum across the region

While climate change adaptation considerations are covered to a lesser extent than mitigation measures in all WB6 economies' climate change strategies, adaptation-specific frameworks are gaining momentum. Expect for North Macedonia, all revised NDCs (and the voluntary NDC for Kosovo) include specific adaptation measures for the most vulnerable sectors (Table 6.3). At the time of writing, Bosnia and Herzegovina and Serbia had adopted national adaptation plans/strategies, and all other economies were in the process of developing such a document with the support of the Green Climate Fund.

As adaptation policy frameworks have only recently emerged in the region, the implementation of measures remains limited. Serbia is a leader in this regard, having implemented adaptation measures since the 2014 floods. These efforts have been undertaken by a consortium of international organisations, such as the Making Cities Resilient 2030 programme, conducted in collaboration with the Ministry of Interior, which primarily focuses on awareness-raising and preparedness activities. Similarly, Montenegro has made significant progress in implementing adaptation measures, bolstered by capacity-building initiatives and training sessions for policy makers during 2021-22 that covered topics such as resilient infrastructure, urban adaptation, and the risk of flash flooding and forest fires.

Table 6.3. Most vulnerable sectors targeted as part of adaptation measures in the WB6 economies' NDCs

	ALB	BIH	KOS	MNE	MKD	SRB
Agriculture	✓	✓	✓	✓		✓
Biodiversity		✓	✓			
Energy		✓				
Forestry	✓	✓	✓	✓		✓
Infrastructure				✓		
Health		✓	✓	✓		
Other land use	✓		✓			
Population	✓					
Settlements	✓					
Tourism	✓	✓		✓		
Transport				✓		
Water		✓	✓	✓		✓

Notes: North Macedonia's NDC does not include adaptation measures. Kosovo's voluntary NDC is yet to be adopted.
Sources: Nationally Determined Contributions of respective WB6 economies; UNFCCC (2024[24]).

Vulnerability mapping has advanced, but ecosystem and community resilience to climate change remains constrained

To facilitate effective policy making and the implementation of climate change adaptation measures, Albania, Montenegro and Serbia have undertaken natural disaster risk assessments. These assessments play a crucial role in mapping vulnerabilities and provide valuable insights that inform targeted strategies for mitigating risks and enhancing resilience in the face of climate-related challenges. Significant progress is observable in almost all economies in evaluating flood risks, an increasingly occurring climate-related hazard in a highly exposed and vulnerable region. Moreover, regional co-operation on flood risks has also been enhanced with the Flood Risk Management Plan Updates, adopted in 2022 under the Montenegrin presidency of the International Commission for the Protection of the Danube River.

Progress on cross-institutional data collection has also commenced in all economies to further support the mapping of vulnerabilities, in alignment with the development of national adaptation plans (NAPs). The establishment of the Digital Climate Atlas of Serbia in 2022, which includes climate datasets and regional and local-level climate model projections, represents a good practice in this regard (Box 6.4).

Box 6.4. Digital Climate Atlas of Serbia

The Digital Climate Atlas of Serbia, inaugurated in October 2022, is an online and freely accessible platform utilising meteorological and geospatial data to offer insights into present and future climate changes. It is a significant advancement in climate data accessibility and analysis in Serbia.

The Atlas enables users, ranging from government bodies to the public, to access detailed climate information, promoting informed policy and decision-making processes. The tool is instrumental in understanding climate change impacts through easily interpretable data on temperature, precipitation and extreme weather events, at various administrative levels.

The Atlas supports climate adaptation strategies and vulnerability assessments, fostering resilience across vital areas such as agriculture, energy and infrastructure. Developed through a collaboration between the Ministry of Agriculture, the Ministry of Environmental Protection, the Faculty of Physics at Belgrade University and the United Nations Development Programme (UNDP) Serbia, and funded by the Green Climate Fund, it represents a strategic move towards standardised, data-based climate action planning.

Workshops have been organised, with more planned, to enable interested parties, including scientists, business leaders and representatives of local governments, to become familiar with the Atlas so that they can use the data for planning climate change adaptation at either the local or national level.

Sources: Ministry of Environmental Protection of the Republic of Serbia (2023[25]).

While most economies have laid the groundwork for adaptation, including the assessment of climate change risks, vulnerabilities and the identification of adaptation options, early warning capacities to assist communities in preparing for future risks remain limited. Only Albania, Montenegro and Serbia concretely plan to strengthen early warning measures. Emergency responses for climate change induced hazards are rarely defined, and compensation schemes are lacking for households, businesses and local governments. In Kosovo, some municipalities affected by the floods in 2023 are in the process of formulating emergency response plans, but they face challenges related to competencies and capacities. This underscores the need for further action to address gaps in hazard management and response mechanisms across the region.

The incorporation of strategies that encompass ecosystems and nature more expansively within climate change adaptation and disaster risk reduction measures remains insufficient and fragmented across all WB6 economies. ADAPT (2019-2024), a regional project implemented by the International Union for Conservation of Nature, aims to enhance ecosystem and community resilience to climate change and environmental degradation through the application of nature-based solutions for disaster risk reduction.[11] The key sectors identified for future interventions include agriculture, forestry and water resources.

Preserving landscapes and biodiversity

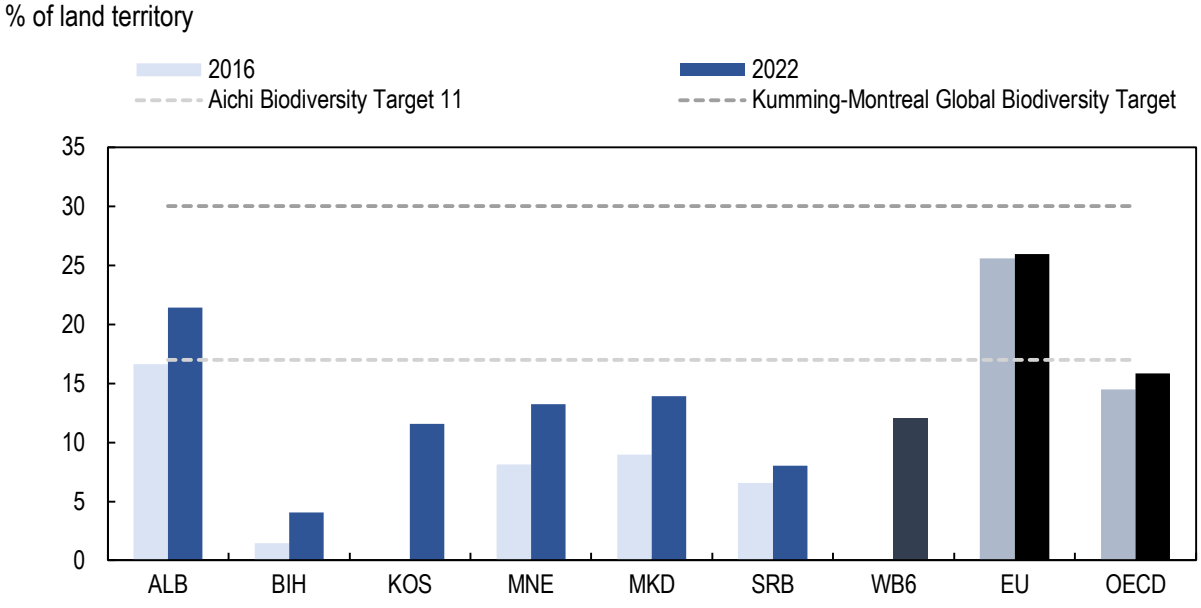
Protecting and restoring precious, fragile ecosystems is essential for ensuring the sustainable economic development of the region. Some critical economic sectors, including agriculture and tourism, are particularly sensitive to the disruption of ecosystem services. For centuries, farmers have used the region's high natural potential for agricultural activities, which is one of the most important branches of the economy in many Western Balkan territories (contributing to around 10% of gross domestic product [GDP] and 25% of employment in the region). Nevertheless, pressures due to conversion of habitats, overexploitation of resources, increased pollution and climate change directly impact biodiversity.

Preservation of biodiversity and forestry resources has increased, but the management of protected areas needs to be scaled up

Post-2020 Biodiversity Global Framework objectives, which include halting biodiversity loss, promoting sustainable use and enhancing ecosystem services, are increasingly being integrated into revised biodiversity strategies and laws in the Western Balkans. Increased commitments to preserve forestry resources and combat illegal logging is also visible through policy and regulatory changes, despite few prevention and punitive measures implemented in the assessed period. Moreover, recently adopted agriculture policies and strategies incorporate sustainable resource management and food production as novel objectives, including measures for afforestation, combatting erosion, addressing illegal construction and enhancing food security. IPARD programmes[12] also increasingly focus on sustainable farming practices to ensure landscape and biodiversity preservation. Nevertheless, the effective planning, regulation and use of land resources in a way that maximises economic, social and environmental benefits is hampered by the lack of overarching land-use management frameworks. North Macedonia and Serbia's National Spatial Plans, once adopted, could serve as such guiding documents.

Despite increased monitoring mechanisms with additional management plans and conservation instruments, the management of protected areas remains weak across the region. While increasing, the share of protected areas is well below international targets in most economies (Figure 6.8). Only Albania has achieved the Aichi Target[13] of 17% for protected terrestrial areas by 2020, and has committed strategic objectives to achieve the Kunming-Montreal Target[14] of 30% in 2030. All economies with access to the sea have fallen short of the 10% target for marine areas (2.9% in Albania, 1.8% in Montenegro and 0% in Bosnia and Herzegovina[15]). Effective management of protected areas and prevention of illegal actions such as construction, hunting and logging must be addressed. Responsible institutions lack the capacity for proper management and monitoring, mainly relying on external financial and technical support.

Figure 6.8. Share of protected terrestrial areas in the WB6 economies (2019)



Notes: The data point for Kosovo is from the last available year, 2019. Aichi Biodiversity Target 11: Protect 17% of terrestrial and inland water area by 2020. Kumming-Montreal Global Diversity Framework's Target 3: Protect 30% of terrestrial and marine areas by 2030.
Sources: For ALB, MNE, MKD and SRB, data from the quantitative questionnaires for the Competitiveness Outlook 2024. For BIH, EU and OECD: Protected Planet (2023[26]).

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Economic activities continue to threaten biodiversity and ecosystems

Tourism, mining and agriculture are significant contributors to environmental degradation in the Western Balkans. From habitat destruction to pollution, these industries challenge biodiversity conservation and ecosystem health.

As tourism grows in the region, its impact on biodiversity and landscapes is becoming increasingly evident. High seasonality, concentration in coastal areas and the construction of associated infrastructure such as roads, hotels and resorts can disturb natural habitats and permanently change landscapes. Additionally, the rise in human activity linked to tourism, leading to pollution, waste production and habitat disturbance, could worsen environmental degradation if not properly controlled and managed sustainably. This holds particularly true for Albania and Montenegro, where tourism has rapidly grown over recent years, now representing 21.6% and 24.5% of GDP, respectively (WTTC, 2023[27]; 2023[28]). However, environmental considerations in tourism frameworks are advancing at a slow pace. Only Montenegro has fully integrated natural valorisation, sustainable resource management and sustainability considerations into its economic development framework, including its Tourism Development Strategy, Programme for Economic Reforms and Smart Specialisation Strategy. Kosovo has also taken steps by adopting a new Law on Tourism in 2022, focusing on the promotion and development of sustainable tourism.

Positive initiatives are underway to promote sustainability in tourism practices in the region. Albania has supported projects such as developing the Butrint National Park, designated as the first carbon-free park, and offers tax incentives for agritourism structures.[16] International partners have also provided support to Kosovo in developing the NaturKosovo project to promote tourism along the Via Dinarica. In Montenegro, the Blue Flag Programme encourages municipalities to maintain high environmental protection standards and ensure quality sanitary and safety conditions on beaches and marinas. Despite these efforts, comprehensive initiatives to monitor and address the environmental impact of tourism are lacking across the region. This is further compounded by insufficient resources in respective ministries, hindering effective responses to the challenges posed by tourism growth.

In recent years, mining activities in the Western Balkans have expanded significantly, driven by rising global demand for minerals and metals and supported by substantial foreign direct investments, which are facilitated by lower restrictions on procedures for issuing permits and concessions. However, this expansion raises concerns about environmental impacts on land-use management, including deforestation, water contamination, habitat destruction and threats to regional biodiversity. The lack of environmental impact assessments for many mining operations has worsened these environmental consequences. Such activities have led citizens in North Macedonia and Serbia to voice their discontent through protests against the government's rapid issuance of mining concessions. While mining plays a vital role in the economy, it is crucial to conduct exploration activities responsibly, considering key spatial planning principles and environmental concerns. In response to these challenges, the Ministry of Economy in North Macedonia is developing a new Strategy for Geological Research and Sustainable Use and Exploitation of Mineral Resources for 2025-2045.

Agriculture continues to play a crucial role in all WB6 economies, but also significantly impacts the region’s biodiversity and ecosystems. The expansion of agricultural land over the past decade in WB6 economies such as Bosnia and Herzegovina, Kosovo, Montenegro and North Macedonia (Eurostat, 2023[29]) has often resulted in the fragmentation and loss of natural habitats, leading to the displacement and endangerment of endemic species. To date, the adoption of organic agriculture and polycropping practices remains low, despite their important role in protecting ecosystems and biodiversity by minimising chemical inputs, and preserving soil health, habitat diversity and water resources, while supporting wildlife and pollinators through sustainable land management practices. Although legislation exists in WB6 economies regarding organic agriculture, it is still a very small proportion of overall farming: Montenegro leads the region with only 1.7% of agricultural land dedicated to organic farming, well below the EU average of 10% (Eurostat, 2023[30]).

Minimising pollution

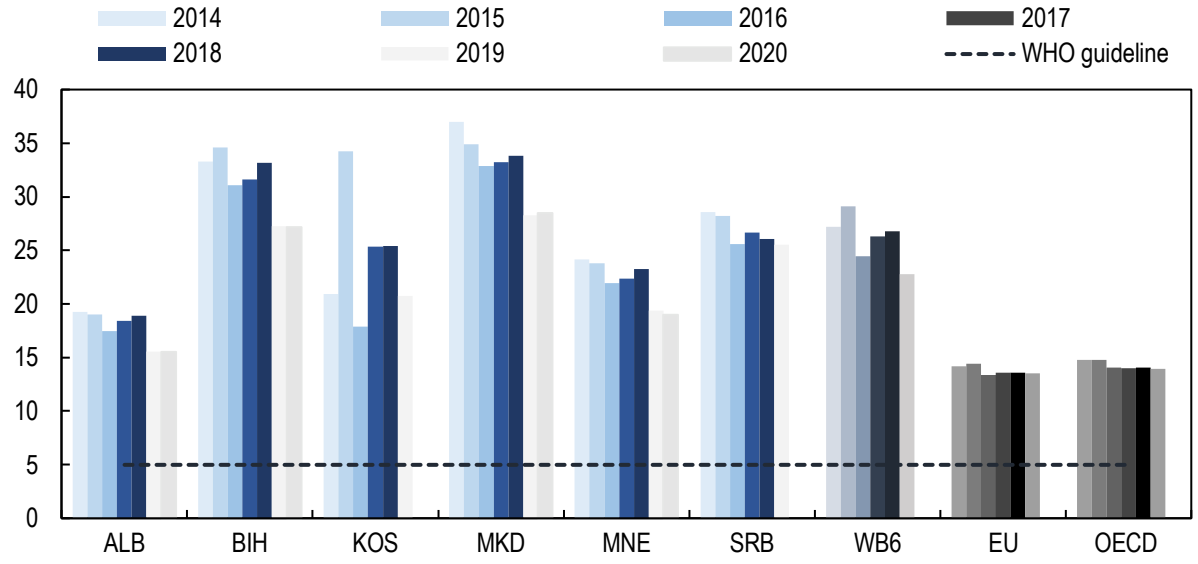
Minimising pollution is paramount for safeguarding planetary health. Pollution not only degrades air, water and soil quality, it also poses significant risks to human health and wildlife. Pollution through fine particulate matter ($PM_{2.5}$), wastewater and unsustainable agricultural practices in the Western Balkans are some of the many causes of increased biodiversity loss, environmental degradation, and heightened cost of public health. The air quality across the Western Balkans is among the lowest in the world, the status of waterbodies is largely unsatisfactory, and soil degradation is prevalent and extensive throughout the region (JRC, 2022[2]).

Exposure to air pollutants remains a major health threat in the region, despite recent policy improvements

While air quality in the Western Balkans has shown improvements over the past decade (Figure 6.9), annual average concentrations of $PM_{2.5}$ remain on average almost four times higher than World Health Organization recommended levels of 5 $\mu g/m^3$ (micrograms per cubic metre) (EEA, 2023[31]). This persistent issue is primarily attributed to significant pollution stemming from the energy and transportation sectors in the region. Nevertheless, since the Competitiveness Outlook assessment in 2021, efforts to address this issue have been made by revising frameworks aimed at enhancing air quality. Revised or new frameworks throughout the region's economies focus on similar objectives, including clarifying institutional capacities and responsibilities to manage air quality better, raising awareness among citizens about improving air quality, and expanding air monitoring and reporting mechanisms.

Figure 6.9. Annual mean population exposure to PM2.5 air pollution in the WB6 economies, the EU and the OECD (2014-20)

In micrograms per cubic metre (µg/m3)



Notes: $PM_{2.5}$ is fine particulate matter. Data for EU-28, OECD, Albania, Bosnia and Herzegovina, Montenegro, and North Macedonia are OECD estimates. Data for EU-28, OECD, and Serbia are only available until 2019. Data for Kosovo come from the Kosovo Environmental Protection Agency, only available until 2019.
Sources: OECD (2022[32]); for Kosovo: Kosovo Environmental Protection Agency (2020[33]).

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Weak co-ordination between national and local government still hampers the tailored implementation of air quality frameworks across all levels of government. Improvements have only been achieved in Albania with the planned establishment of a National Commission for Clean Air, and in North Macedonia with training support provided to local governments. Despite being prescribed in air management legal frameworks, the development of local air quality plans has been delayed in Albania and Montenegro, but municipalities in other economies have adopted new plans. For example, Pristina is implementing its Air Quality Plan (2023-28), emphasising cleaner vehicles, public transport, walking, cycling, a low emission zone and cleaner heating.

Air pollution from industrial installations such as manufacturing, power generation and resource extraction also remains a significant issue in the region. Alignment with the EU's Industrial Emissions Directive[17] is incomplete across economies, with progress made in North Macedonia with the preparation of the Law on Industrial Emissions and in Serbia with the preparation of the revised draft Law on Integrated Pollution Prevention and Control (IPPC), both pending adoption. However, most economies lack legally binding emission limit values in environmental permits for industrial installations. Frameworks in Serbia and Bosnia and Herzegovina foresee the introduction of best available techniques (BATs) to decrease air pollutants and heavy metals from industrial processes. Developments to address air pollution from thermal power plants are also ongoing, notably the desulphurisation process at the Kostolac B thermal power plant in Serbia and the ecological reconstruction of the Pljevlja thermal power plant in Montenegro.

A network of air quality stations is in place in all economies, largely covering atmospheric pollutants in line with EU requirements (NO_x, NMVOCs, So_x, NH_3, $PM_{2.5}$, PM_{10}), with information promptly made available online. Nevertheless, continuous monitoring at major industrial installations is not guaranteed for all types of pollutants, monitoring stations rarely cover the whole territory of all economies and maintenance of measuring devices is often challenging.

Efforts are ongoing to reduce water pollution and preserve related ecosystems

Most economies of the Western Balkans have significant freshwater resources. In Albania and Bosnia and Herzegovina in particular the amount of freshwater is three times higher than the EU average of 3 037 m^3 (World Bank, 2023[34]). Nevertheless, beyond issues of overexploitation and impacts of climate change, escalating pollution levels, particularly from untreated wastewater, exacerbate the already compromised water quality in the region.

Revised legal and policy frameworks in most WB6 economies put stronger emphasis on freshwater management preservation, particularly regarding reducing groundwater pollution and the restoration of degraded ecosystems. Advancements in adopting river basin management plans to safeguard water resources and related ecosystems at the local level have also been observed in Albania, Bosnia and Herzegovina, Montenegro and Serbia. However, the delayed development of river basin management plans in Kosovo and North Macedonia poses challenges for freshwater management, particularly for establishing water protection zones, which are necessary to address the cumulative and pollution impacts of economic activities and infrastructure, such as the development of hydropower plants, on freshwater resources.

Improvements in water quality are anticipated through ongoing and planned investments in water supply and sanitation infrastructure across all WB6 economies, primarily financed by international partners. However, common challenges persist in the region, including limited human and financial resources for implementing water supply and sanitation measures, and inadequate water tariffs that fail to cover operating costs and necessary infrastructure upgrades. Efforts to tackle these challenges are underway through various initiatives, such as the reorganisation of water supply and sewerage services in Albania, Bosnia and Herzegovina and Serbia. In order to ensure water quantity and quality, these reforms seek to regulate competencies at local self-government and utilities levels, including regulating water supplies, setting water tariffs and facilitating contracts for the provision of water services.

Despite progress in strengthening freshwater frameworks and increasing investments in water infrastructure, there is an absence of systematic collection or compilation of water quality and quantity data from various institutions across the region, which impedes informed policy decisions regarding competitive uses of water and the trade-offs among sectors. Furthermore, monitoring to identify emerging contaminants is widely lacking across all economies. However, Montenegro and North Macedonia (as part of the National Environmental System managed by the Macedonian Information Centre and groundwater cadastre) plan to improve their water monitoring by establishing national water information systems.

Activities to safeguard soils from pollutants remain limited, despite the significant impact of industrial and agricultural activities

The Western Balkans must dedicate more effort to safeguarding soils from pollutants to maintain ecosystem health, agricultural productivity and human well-being. Limited progress has been achieved in enhancing food safety and quality in the region, with agricultural practices contributing to soil degradation and water pollution. While maximum residue levels have been defined in all economies (expect for the FBiH), in line with EU regulations, the increasing use of pesticides and insecticides risks exacerbating soil and water pollution. The use of pesticides has been steadily rising in Albania, Bosnia and Herzegovina and Montenegro, contributing to a 10% increase in regional use over the past decade (FAO, 2023[35]). Moreover, Bosnia and Herzegovina, Montenegro and Serbia have increased their insecticide use, with both Bosnia and Herzegovina and Montenegro reaching record high levels of use in 2021 (FAO, 2023[35]). Nevertheless, some measures on sustainable food production and soil organic carbon will be integrated into a regional project under the Western Balkans Soil Partnership (Box 6.5). Establishing a regional soil map is also planned to strengthen data sharing on soil management at the regional level.

Box 6.5. Western Balkans Soil Partnership

The Western Balkans Soil Partnership, initiated under the Green Agenda for the Western Balkans and co-ordinated by the Standing Working Group for Regional Rural Development (SWG RRD), was established in 2022 to address soil degradation by enhancing soil health, water retention and nutrient cycling, thereby reducing the need for chemical inputs and mitigating environmental contamination.

In the same year, the SWG RRD published the region's first integrated assessment on soil management, identifying critical gaps and offering strategic recommendations. This publication was one of several outcomes from the seven interim meetings conducted between 2022 and 2024. The group's efforts also encompass administrative and technical preparations to establish functional sub-regional partnerships and initiate work on soil maps, specifically focusing on mapping contaminated sites.

This initiative remains committed to bringing together regional stakeholders to improve soil health, which is essential for agriculture, ecosystem services and climate adaptation.

Sources: RCC (2023[36]); SWG RRD (2024[37]).

Industrial risk management and measures to safeguard soils from industrial pollutants vary across economies, and there are gaps with EU legislation on risk management, environmental permitting and compliance. While no WB6 economy fully aligns with the EU Seveso-III Directive on preventing major industrial accidents, most economies have progressed by delineating specific obligations for industrial operators handling hazardous substances. A Pollutant Release and Transfer Register (PRTR) system, which aims to track the release and transfer of pollutants from industrial facilities into the environment, is currently operational in Albania, North Macedonia and Serbia, and is set to be established in all other economies with the support of an international project aimed at their development.[18] Some progress has

also been made in managing chemicals and their impact on soils, and in further aligning with the EU regulation on the registration, evaluation, authorisation and restriction of chemicals (REACH).

There has been little effort made to restore degraded land and ensure the systemic clean-up of industrial contaminated sites. Disposal facilities for hazardous waste remain minimal across the Western Balkans, and most industrial waste is illegally landfilled, posing significant threats to soil. Apart from a few ad hoc projects financed by international co-operation partners, efforts to clean up industrial sites remain limited. Most economies do not have a policy basis for systemic soil monitoring and cleaning, apart from Serbia, which has a Cadastre of Contaminated Sites Information System, and where the Serbian Environmental Protection Agency (SEPA) regularly collects soil monitoring data at the operational, post-operational and remediation stage to identify potential health risks.

Recommendations for protecting ecosystems and citizens' well-being

- **Mainstream biodiversity considerations into relevant policy frameworks and elevate commitment to safeguarding natural heritage by significantly expanding the coverage of protected areas.** A global vision for 2050 exists under the Convention on Biological Diversity, which WB6 economies can adopt or tailor to their national circumstances. WB6 economies should ensure that biodiversity is mainstreamed across relevant strategies and programmes (e.g. national economic plans, climate change and low emission development strategies, tourism, and agriculture) and strengthen inter-institutional co-ordination by setting clear roles and responsibilities. In particular, biodiversity loss and climate change must be addressed together, considering that terrestrial ecosystems are natural carbon sinks that have an annual gross sequestration level equivalent to about 60% of global anthropogenic emissions, and that biodiversity also enhances climate change adaptation through nature-based solutions (IPBES, 2019[38]). Given the region's vulnerability to climate-related hazards, investing in nature can be a crucial means to protect the population from threats such as floods, droughts and storms (OECD, 2021[39]).

  Most economies need to significantly expand the coverage of protected areas to ensure the effective enforcement of biodiversity measures. While established protected areas ensure the preservation of biodiversity, safeguard critical habitats, and support climate resilience, they fall short of international targets in most WB6 economies. Costa Rica's Payment for Environmental Services programme stands out as a successful model for expanding protected areas (Box 6.6).
- **Ensure the preservation of forestry resources by reducing illegal logging, notably by strengthening stakeholder collaboration.** Taking inspiration from Indonesia's effective Illegal Logging Monitoring and Environmental Protection Programme, WB6 economies should prioritise empowering local communities through alternative livelihood opportunities, such as agroforestry, eco-tourism and non-timber forest products. This approach not only reduces dependence on logging but also fosters a sense of ownership and stewardship over forest resources. To implement its programme, the Indonesian government provided training, technical assistance and resources to support initiatives (JPIK, 2020[40]).
- **Develop an all-inclusive land-use policy framework and strengthen institutional co-ordination between different ministries responsible for land-use issues related to climate, biodiversity and agriculture**. This should take place both horizontally (at the national level) and vertically (between different levels of government) to achieve a more holistic governance of land use. The land-use nexus involves multiple issues and affects multiple actors from both the public and private sectors; it therefore requires a whole-of-government approach to co-ordinate policies across all relevant stakeholders, which most WB6 economies currently lack. A comprehensive land-use framework should integrate the systematic use of Strategic Environmental Assessment (SEA) early in the planning process to ensure transparent, informed and sustainable decision making based on evidence and stakeholder involvement.

Box 6.6. Costa Rica's Payment for Environmental Services programme

Costa Rica's Payment for Environmental Services programme was introduced in 1997 as a pioneering initiative aimed at incentivising landowners through financial compensation to conserve and restore forests, protect watersheds and promote biodiversity conservation.

Through this initiative, landowners receive financial incentives for maintaining or restoring ecosystems on their land, effectively discouraging deforestation. This approach has expanded protected areas and fostered biodiversity conservation by creating biological corridors and engaging local communities in sustainable land management practices. The programme's success is attributed to a robust institutional framework, effective governance, and collaboration between the government, non-governmental organisations and communities.

Currently, Costa Rica has expanded its officially protected areas to cover 25% of land and 30% of marine areas, well above OECD averages.

Sources: OECD (2023[41]).

- **Adopt a comprehensive and integrated water management framework in light of the pressing challenges posed by water pollution and the impacts of climate change**. An integrated framework will require enhanced collaboration among various government departments and agencies involved in water management, pollution control and climate resilience. In addressing the integration of climate change impacts into water management, entities could adopt a similar approach to the Netherlands' Room for the River programme, a large-scale, integrated water management initiative aimed at mitigating flood risks and enhancing overall river management. The initiative involves creating additional space for the river to expand during floods, along with measures such as constructing floodplains, removing barriers and promoting sustainable land use to enhance overall water resilience. Moreover, it emphasises community involvement to create awareness, garner support, and incorporate local knowledge into the planning and implementation process (Rijkswaterstaat, 2024[42]).
- **Improve air quality by decreasing emissions from energy production and industrial processes.** Air pollution remains a significant environmental concern in all WB6 economies. While the problem is multifaceted, industrial activities and energy production (in particular metallurgy, mining, manufacturing and energy production from coal-fired power plants) are some of the main sources of pollution in the region, releasing large amounts of pollutants into the air. To ensure adequate pollution control measures in industries and powerplants, to reduce levels of harmful substances, and in addition to measures proposed to mitigate the effects of climate change, WB6 economies could refer to the EU's Best Available Techniques Reference Documents to ensure effective enforcement and regulatory compliance (Box 6.7).

Box 6.7. EU's Best Available Techniques Reference Documents

The EU's BREFs, or Best Available Techniques Reference Documents, are a series of guidance documents developed by the European Integrated Pollution Prevention and Control Bureau (EIPPCB). These documents provide detailed information on best available techniques (BATs) in various industrial sectors to prevent or reduce emissions and the impact of industrial activities on the environment. BREFs are an integral part of EU efforts to regulate industrial emissions and ensure environmental protection.

Key points about EU BREF documents:

- **Best available techniques (BATs):** BATs represent the most effective and advanced methods and processes to achieve a high level of environmental protection. They consider the costs and benefits of different techniques for preventing or controlling emissions.
- **Sector-specific guidance:** BREFs are sector-specific, covering industries such as energy, chemicals, metals and waste management. Each BREF focuses on a particular industrial sector and provides comprehensive information on the best practices within that sector.
- **Legal framework**: BREFs are crucial in implementing the Industrial Emissions Directive (2010/75/EU), formerly the Integrated Pollution Prevention and Control (IPPC) Directive. This directive sets the legal framework for controlling industrial emissions across the EU.
- **Reviewing and updating:** BREFs undergo regular reviews and updates to incorporate new technological advancements, changes in regulations and improvements in best practice. The process involves consultations with industry stakeholders, environmental non-governmental organisations and experts.

Source : European Commission (2024[43]).

Enhancing resource efficiency and circularity

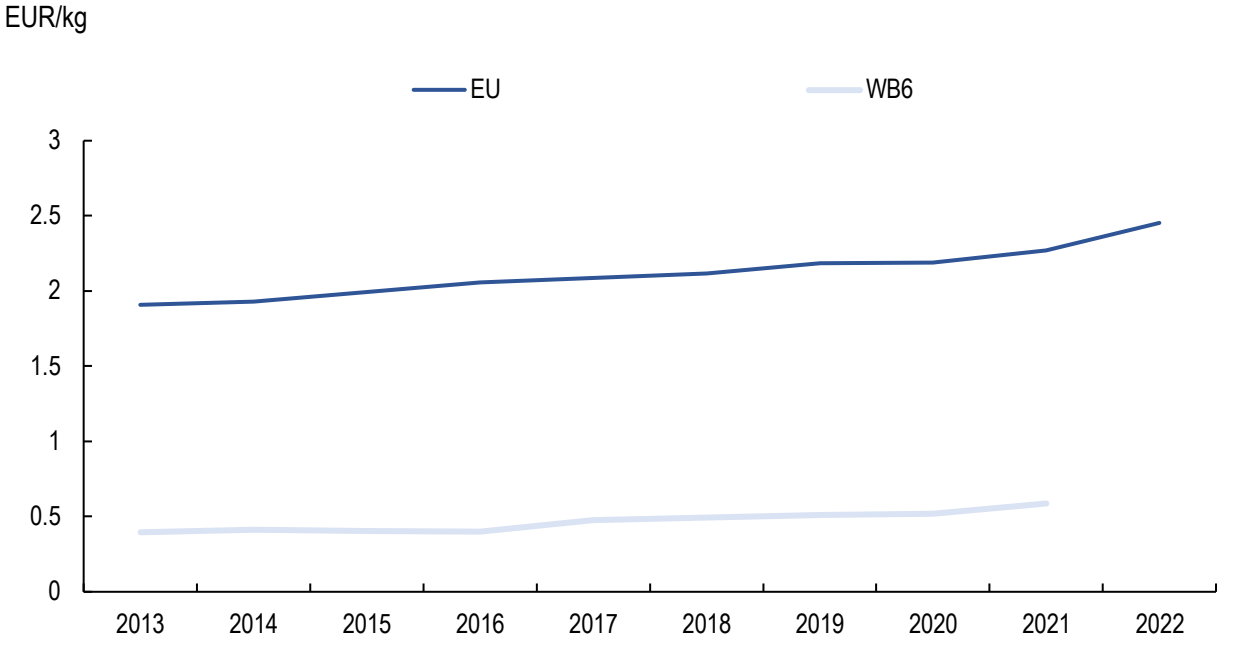
Resource intensity, which measures the amount of resources needed to generate value added, remains notably high in the WB6 economies compared to OECD and EU member states (OECD, 2024[44]). Additionally, despite increasing waste generation across these economies in recent years, waste prevention and treatment practices, especially recycling efforts for municipal waste, have failed to keep pace. These trends negatively impact the long-term security of non-renewable resource supply, which is a concern for sustaining regional economic growth, and creates environmental pressures due to unsustainable production and consumption practices.

As outlined in the Green Agenda for the Western Balkans, and underscored by vulnerabilities exposed during the COVID-19 pandemic, the region must reduce its reliance on globalised linear supply chains and inexpensive virgin raw materials. Such a strategic shift is crucial for mitigating economic risks (e.g. production disruptions and revenue losses) and environmental degradation. The promotion of circularity and resource efficiency is, therefore, imperative to future-proofing regional economies. It is an approach that stands to enhance competitiveness and job creation, but also drive innovation, ensure resource supply security and foster equitable growth across the Western Balkans. Additionally, reducing the emissions intensity of goods is crucial for protecting exports to the EU from decreased competitiveness due to higher prices resulting from carbon levies under the EU's CBAM.

Regionally, the potential for improved resource efficiency and the circular economy transition remains largely untapped. This could also be problematic for the green transition, as ensuring a sustainable supply of raw materials, particularly critical materials, is a fundamental requirement. Economies must diversify

sources of both primary and secondary materials, improve resource productivity, and prolong material use to maximise the efficient use of domestically extracted resources and minimise waste generation. Resource productivity in the WB6 economies rose from 0.4 EUR/kg in 2013 to 0.59 EUR/kg in 2021 (Eurostat, 2023[45]), but was still more than three times below the EU average (2.27 EUR/kg) (Figure 6.10).

Figure 6.10. Resource productivity in the WB6 economies and the EU (2013-21)



Note: No data available for Kosovo and no data for Bosnia and Herzegovina before 2015.
Source: Eurostat (2023[45]).

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Laying the foundations for sustainable production and consumption

The Green Agenda for the Western Balkans highlights the necessity of pursuing economic development and new business opportunities within frameworks for sustainable production and consumption. A key pillar of this is the transition towards a circular economy, which will require policies focused on promoting circular design, production and consumption practices, as well as waste prevention, reuse and recycling.

The circular economy is gaining traction as a model for sustainable production and consumption

Driven by a combination of environmental concerns, economic demands, and aspirations for regional and EU integration, the adoption of strategic documents related to the circular economy is gaining momentum in the Western Balkans (Table 6.4). Serbia and Montenegro have paved the way by adopting circular economy roadmaps in 2020 and 2022, respectively, followed by the introduction of related programmes, strategies and action plans. Kosovo published its circular economy roadmap in 2023, and Albania and North Macedonia finalised their circular economy roadmaps in early 2024, with the support of the OECD. Bosnia and Herzegovina is currently preparing a similar document.

Although all WB6 economies have policies and legislation in place that are directly or indirectly related to the circular economy, frameworks for sustainable production and consumption are still in their nascent stages throughout the region. Alignment with EU directives and policies on the circular economy also

remains limited, affecting the competitiveness of WB6 products and services within EU value chains. The focus in the region has primarily been on developing or updating waste management plans and programmes, and therefore addressing the end-of-life phase of products (see further details in the section Strengthening waste management and material recovery). This is consistent with the prevalent urgent need to address waste management more adequately across the region, as recycling rates remain low and extensive landfilling is the primary mode of waste treatment. However, to transition to a circular economy, the region will need to shift its focus from waste management to policies that also target more circular production and consumption.

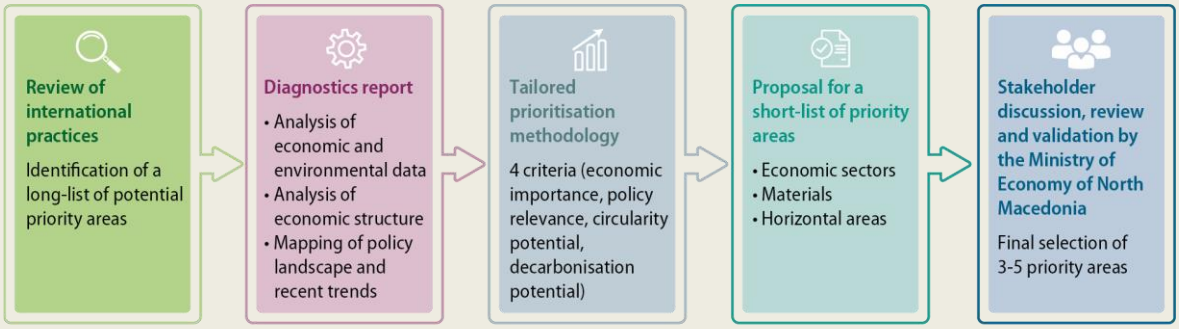
Table 6.4. Circular economy strategic and policy documents in WB6 economies

Economy	Document name	Adoption year	Timeline	Key priority areas	Co-ordinating ministry
Albania	A Roadmap towards Circular Economy of Albania	2024	n/a	- Economic instruments across sectors - Circular business models for small and medium-sized enterprises (SMEs) - Plastics - Horizontal areas: waste management, tourism and awareness raising	Ministry of Tourism and Environment (Directorate of Circular Economy)
Bosnia and Herzegovina	n/a	Under development	2021-2027	n/a	Ministry of Foreign Trade and Economic Relations (state level)
Kosovo	Circular Economy Roadmap of Kosovo	2023	n/a	- Food system - Forest system - Creative sector - Retail - Built environment - Manufacturing	Ministry of Environment, Spatial Planning and Infrastructure
Montenegro	Roadmap Towards the Circular Economy in Montenegro	2022	n/a	- Food system - Forest system - Built environment - Tourism - Manufacturing	Ministry of Economic Development
	National Circular Transition Strategy until 2030 and action plan for 2023-2024	2022	2023-2024	- Agriculture - Forestry - Construction - Tourism - Horizontal areas: economic instruments, circular business models, awareness raising, waste management	
North Macedonia	A Roadmap towards Circular Economy of North Macedonia	2024	n/a	- Circular business models for SMEs - Construction - Biomass and food - Textiles - Mining and metallurgy	Ministry of Economy
Serbia	Roadmap for Circular Economy	2020	n/a	- Manufacturing industry - Agriculture and food - Plastics and packaging - Construction	Ministry of Environmental Protection (Department for Circular Economy and Sustainable Development)
	Circular Economy Development Programme	2022	2022-2024	- Industry - Agriculture - Construction - Horizontal areas: circular business models, local self-governments: circular communities, waste management, economic instruments, awareness raising	

Box 6.8. Selecting priority areas for the circular economy

A review of international practice shows that countries follow customised methodologies to select specific priority areas for the circular economy. Albania and North Macedonia, for instance, developed their circular economy roadmaps in collaboration with and under the guidance of the OECD. The approach outlined in Figure 6.11 (example of North Macedonia) was adopted to define priority areas.

Figure 6.11. Approach for circular economy roadmaps, example of North Macedonia



Source: OECD (2024[46]).

The applied prioritisation methodology uses four criteria and their related indicators to help the selection of (potential) priority areas:

1. **Economic importance**: This involves a data-driven assessment, including indicators such as value added, employment, trade in sectors and industries, and position in the global value chain.
2. **Policy relevance**: Qualitative analysis determines if an area is included in national strategic documents and action plans. Consideration is also given to policy gaps identified in the area. Given that Albania and North Macedonia are EU candidates, the relevance to EU targets and obligations was also assessed for their roadmaps.
3. **Circularity potential**: Quantitative indicators such as material productivity or intensity, resource use, waste generation and recycling rates can be used to evaluate circularity potential. These indicators can be compared against peers, EU averages or specific targets to assess the potential for increasing circularity in specific areas.
4. **Decarbonisation**: This measures the level of greenhouse gas emissions in specific sectors/industries to identify those with the highest potential for emissions reduction.

A comprehensive diagnostic of the circular economy served as the primary source of data and information for the prioritisation exercises in Albania and North Macedonia. The OECD compiled a long list of potential priority areas and preliminary policy recommendations, which were discussed at stakeholder meetings in both economies. The working groups were then tasked with selecting three to five final priority areas.

Sources: OECD (2024[44]; 2024[46]).

The WB6 economies have varied approaches to circular economy policies, each tailored to their unique economic landscapes and priorities. Although methodologies for identifying priority areas vary across the WB6, they predominantly rely on comprehensive analyses of economic structures and challenges present within sectors, value chains and material or product life cycles. These analyses aim to pinpoint areas where transitioning to a circular economy would yield the greatest benefits, considering the economic importance

of the area in terms of value creation, overall policy relevance and emissions reduction potential, as well as opportunities such as new product and labour markets. Box 6.8 describes the OECD's prioritisation methodology applied when developing Albania's and North Macedonia's circular economy roadmaps.

Most WB6 economies prioritise the construction and food and agriculture sectors in their circular economy policies. These sectors tend to be associated with high consumption of natural resources, significant emissions and high levels of waste generation, yet also hold high economic relevance. Several circular economy policies also recognise the opportunity of integrating circular bioeconomy principles into agriculture restructuring, with the aim to future proof primary production, food processing and consumption sectors against various challenges (as outlined in the section, Economic activities continue to threaten biodiversity and ecosystems). Regional economies with smart specialisation strategies (S3), such as Montenegro, North Macedonia and Serbia,[19] also acknowledge the importance of agriculture for research and innovation-driven economic growth, with links to the circular bioeconomy.

New measures are being put in place across different sectors and value chains to incentivise more circular production and consumption

The WB6 economies have started to adopt measures to advance circular economy policies and promote circular production and consumption. These measures include green public procurement (GPP), private sector engagement, financial and technical support, and multi-stakeholder collaborations.The OECD and the EU's 2020 Circular Economy Action Plan identify GPP as a priority tool for promoting the circular economy. The use of GPP is mentioned in all strategic and policy documents identified in Table 6.4. For example, circular economy policy documents in Montenegro and Serbia entail objectives related to increasing the application of GPP to further the transition to a circular economy in different sectors. On average across all WB6 economies, public procurement accounted for about 8.9% of GDP in 2022 (European Commission, 2023[47]), and public procurement laws in the region already include provisions for environmental and climate-related criteria in GPP, making this a good avenue for increasing the supply of more environmentally friendly products and services. The use of GPP can have particular impact in the construction sector, a priority area in most WB6 economies. While this sector accounted for around 12.7% of gross value added and 400 000 jobs regionally in 2019 (WB6 CIF, 2021[48]), it also has a significant environmental impact: in 2020, manufacturing and construction accounted for around 6.4% of regional GHG emissions (Climate Watch, 2024[3]), and construction and demolition waste (CDW) are estimated to have comprised 5% of regional waste generation[20] (Eurostat, 2023[49]). However, this is likely a significant underestimation of CDW due to underreporting and illegal dumping (Nadazdi, Naunovic and Ivanisevic, 2022[50]). The circular economy presents opportunities to significantly reduce CDW and GHG emissions in the sector, thereby contributing to the decarbonisation of WB6 economies.

WB6 economies recognise the crucial role of the private sector in driving the circular transition and have begun devising both technical and financial support measures through targeted business support programmes and financial incentives. For instance, Serbia has introduced specific criteria for allocating grants within existing support programmes to support the application of circular economy principles. Serbia also promotes collaboration between scientific research organisations and companies through dedicated financial support programmes for innovation and production optimisation. However, at the regional level, progress in offering green financial incentives to businesses, including for circular economy projects, has been uneven. WB6 economies often rely on external funding from international development co-operation partners and lack sufficient business guidance and advice (OECD, 2022[51]). While some economies have established green funds targeting SMEs – constituting the vast majority of businesses in the region – and offer reduced interest loans and grants for SME greening initiatives, these efforts remain relatively small-scale, and green criteria are rarely integrated into existing credit schemes (OECD, 2022[51]). Non-financial tools to support environmental practices have remained scarce even when financial support is offered.

Promisingly, information-based tools have been scaled up, and chambers of commerce actively engage not only in promoting circular economy principles among businesses, but also in enhancing stakeholder engagement and collaboration. Organised stakeholder platforms are emerging across the region, with the Chamber of Commerce and Industry of Serbia pioneering a Digital Platform for Circular Economy since 2021. The Chamber of Economy of Montenegro launched its own circular economy stakeholder platform in 2023 (Box 6.9). The involvement of stakeholders is a key pillar for initiating the transition to the circular economy as it brings together different decision makers from the government and non-governmental sectors. Collaborative efforts among these stakeholder groups facilitate the mapping of opportunities, raising awareness and putting more focus on critical areas for a circular transition. Multi-stakeholder partnerships streamline co-operation and guide the overall strategic direction, helping to secure funding, fostering capacity building and facilitating knowledge exchange. Within such partnerships, sub-groups can also address sector-specific challenges relevant to priority areas.

Box 6.9. Circular Economy HUB Montenegro

In 2023, the Chamber of Economy of Montenegro established the Circular Economy HUB (CE HUB) as a unique focal point for circular initiatives and solutions. It is a digital open information platform intended to disseminate data and promote resource efficiency through circular value systems.

Mission and goal of the CE HUB

The CE HUB's mission is to "strengthen the capacity of Montenegrin economy on the circular transition path and to promote systemic changes towards the creation of circular business models". Its primary goal is the creation of a "framework for the integration of circular business models and practices based on identified priority areas in the Roadmap by establishing strong and continuous collaboration between institutional actors, business and academic community".

Empowering exchange

The CE HUB offers comprehensive insights and resources on the focus areas of Montenegro's circular economy roadmap. It provides valuable information and tools promoting circular practices across different key sectors, including manufacturing, the food system, tourism, the forest system and the built environment. Users can access case studies, reports and guidelines supporting Montenegro's transition toward a circular and resource-efficient economy. The hub also organises webinars covering various topics. In December 2023, the CE Hub convened industry experts and thought leaders to discuss the impact of innovation in the circular economy.

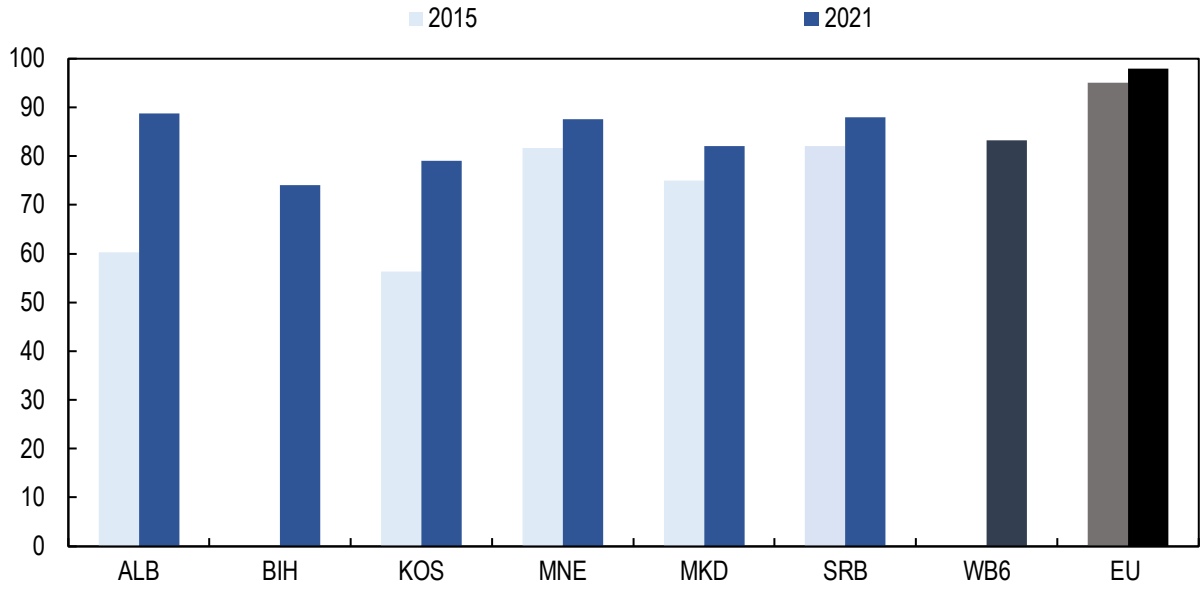
Source: CE HUB (2024[52]).

Strengthening waste management and material recovery

Effective waste management is key to a circular economy as it can help conserve resources, reduce environmental impact, save energy, create economic opportunities and facilitate the closing of material loops. In the Western Balkans, rapid urbanisation, industrialisation and economic development have increased waste generation over the past two decades, placing substantial pressure on already strained resources, infrastructure and ecosystems. Nonetheless, progress has been made with revised waste management laws and strategies across economies that have led to strengthened waste treatment and collection practices (Figure 6.12). However, the share of the population covered by waste collection services varies, particularly in rural areas where it can be as low as 40%.

Figure 6.12. Population covered by waste collection services in the WB6 economies and the EU (2015, 2021)

% of total population



Note: No data available for BIH in 2015.
Sources: Respective Statistical Offices of WB6 economies; for Bosnia and Herzegovina, EEA (2021[53]).

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Sustained improper waste management practices lead to environmental pollution in the region

In the Western Balkans, more than 83% of waste is disposed of in landfills, with only a small amount recycled (Figure 6.13). This disparity can be largely attributed to inadequate infrastructure for waste sorting, collection and recycling, limited financial resources at the local level, and a lack of public awareness and engagement. Despite a legal obligation to separate waste at its source, implementation of this obligation remains marginal, and there is no organised system for separate waste collection in place. Some small-scale pilot projects for waste separation at source have been initiated in municipalities across the region, but their effectiveness remains uncertain.

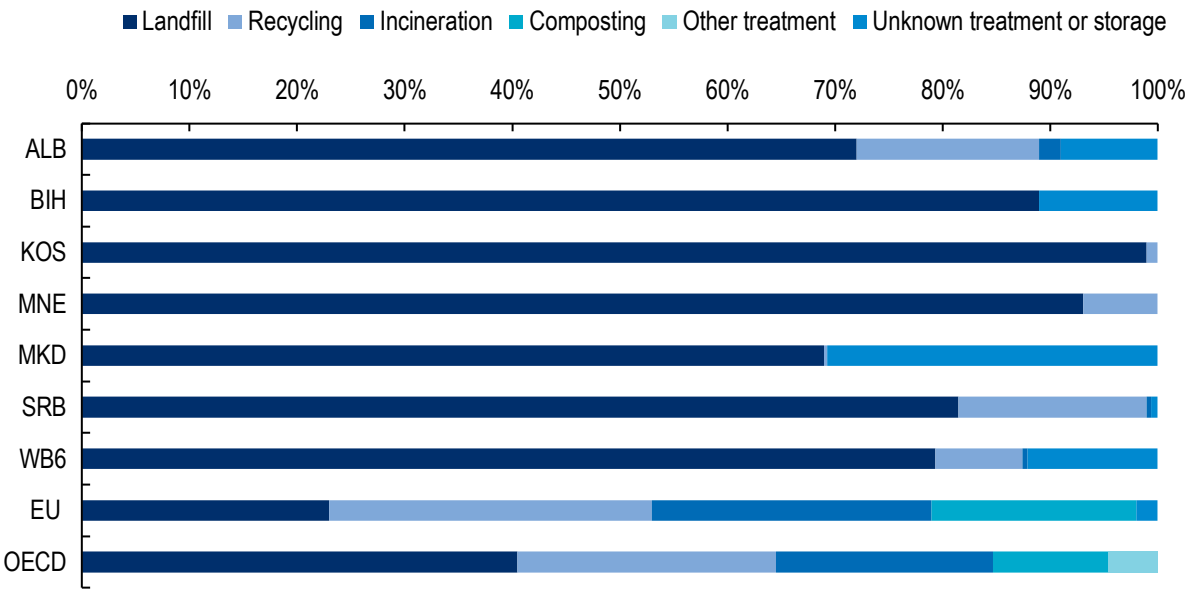
Illegal waste disposal in dumpsites or unsanitary landfills, where no fees are required, remains widespread across the region. For example, only one-third of landfilled waste in Bosnia and Herzegovina and one-quarter in Serbia is treated in sanitary landfills. Additionally, the frequent open burning of waste worsens environmental pollution and disrupts the operation of existing sanitary landfills. While there are efforts to close and remediate dumpsites and illegal landfills in Kosovo, North Macedonia and Serbia, progress overall is slow. Despite this, Kosovo has seen a significant decrease of nearly half in the number of illegal landfills recorded across all municipalities from 2020 to 2022. Some progress on managing plastic waste is also planned at the regional level through a joint statement on combatting plastic pollution issued in 2023 and the development of a regional action plan for plastic waste.

In all WB6 economies, the collection of recyclable waste, though minimal, is predominantly carried out by the informal sector. However, there is a lack of proper equipment and training, leading to health and environmental hazards. Despite its prevalence, this activity is not systematically addressed across all WB6

economies, with no plans for formalisation, which hinders the adequate funding and functioning of legal waste management infrastructure and impedes its gradual improvement.

Figure 6.13. Municipal waste treatment in the WB6 economies, the EU and the OECD (2021)

% of municipal waste



Note: Data for BIH are from 2019, and data for the OECD are from 2020.
Sources: Respective Statistical Offices of WB6 economies; for Bosnia and Herzegovina, EEA (2022[54]); for OECD, OECD (2023[55]).

StatLink https://stat.link/d31sez

Efforts to increase recycling rates continue through extended producer responsibility schemes and new investments in waste treatment facilities

While recycling and recovery rates remain very low in the region, revised legal and policy frameworks are incrementally being implemented to ensure proper waste management.

Waste management infrastructure is being improved in some economies with the construction of new recycling plants and sanitary landfills in Albania and Serbia, and the establishment of composting facilities in Albania and Kosovo. Albania has also invested in new incineration plants. Nevertheless, the region will need to ensure that incineration does not come at the expense of recycling, and that policies are aligned with the EU *acquis* waste hierarchy principle, recycling targets and a circular model.

Extended producer responsibility (EPR) schemes, which aim to shift the burden of paying for product management costs from the public sector to producers and consumers, and which has been successful in increasing the collection, sorting and recycling rates of the products these schemes cover, are planned to be introduced or further implemented across the region. EPR schemes also offer an opportunity to integrate the informal waste sector into more formalised types of employment (Prevent Waste Alliance, 2024[56]). EPR schemes for different product groups are already established in Bosnia and Herzegovina, North Macedonia and Serbia, but further enforcement efforts are required to ensure their effectiveness; Kosovo and Albania's revised waste laws include plans for the establishment of EPR schemes. Kosovo is also working on a business case for the introduction of a deposit refund system for bottles and cans to strengthen recycling activities.

While efforts are ongoing to implement waste management policies, the suboptimal availability and reliability of waste data remain a common challenge across the region. High-quality data are necessary to facilitate waste management planning, including the implementation of EPR schemes, and guide investments in necessary infrastructure. Nevertheless, the quantities of waste generated are often approximations that rely on factors such as the population of a municipality. While statistical surveys are conducted, their accuracy and response rates frequently fall short. Moreover, the absence of weighing equipment in many landfill sites contributes to uncertainty regarding data on the volume of waste treated at these sites. Advancements in this area have only been undertaken with the support of international co-operation partners in Albania, where a weighing exercise was undertaken across all 61 municipalities from 2020 to 2022, and in Kosovo, where waste reporting has been digitalised.

Recommendations for enhancing resource efficiency and circularity

- **Strengthen collaboration among stakeholders and foster public and private partnerships to advance the transition to a circular economy**. While Serbia and Montenegro have already introduced circular economy platforms, all other economies need to strengthen collaboration, information sharing and the exchange of good practices. Besides enabling collaboration and networking opportunities between the public and private sectors, such platforms may also facilitate synergies and knowledge sharing across the different parts of the value chain. Most OECD members have established national circular economy stakeholder platforms or hubs that serve as fora for information exchange, peer learning and multi-stakeholder co-operation, as well as a depository of information, data and other relevant material (see Box 6.10 for some examples).

Box 6.10. Examples of circular economy platforms/hubs

- **Circular Glasgow (United Kingdom)**: Hosted since 2015 by the Glasgow Chamber of Commerce, Zero Waste Scotland and Glasgow City Council, Circular Glasgow aims to build best practices and capacity on the circular economy across Glasgow businesses, helping them identify opportunities to support and implement circular ideas. This is done through workshops and events, including a series of knowledge-sharing business-to-business networking events; a circle assessment, a tool that helps businesses understand opportunities to become more circular; and the Circle Lab, an online hackathon event to find a circular solution to local challenges.
- **Turkey Circular Economy Platform**: Established in 2020 by the Business Council for Sustainable Development of Türkiye, this platform aims to provide practical solutions, incentives, news and opportunities in the field of circular economy. It includes a knowledge hub, an e-commerce platform for industrial symbiosis (as part of Türkiye Materials Marketplace – established in 2016) and measurement tools, and offers training, financial opportunities and consultancy services for companies looking to accelerate their circular transition.

Sources: OECD (2021[57]); BCSD (2024[58]).

- **Mainstream greening into existing funding mechanisms to better support circularity and the greening of SMEs.** To channel the full potential of the private sector in the transition to circular modes of production and consumption, WB6 economies must de-risk investments into circular and green projects and business models. Possible avenues for the government and national development banks include enlarging existing green funds, developing sustainability linked loans, and offering lower cost loans to SMEs by adapting existing credit guarantee schemes for green projects. Additionally, comprehensive training must be provided for both financial institutions and SMEs to enhance their understanding and capability to develop and implement circular economy projects.

- **Improve regulatory frameworks to provide incentives for circular production and consumption practices.** This can be achieved by implementing eco-design requirements to enhance product durability and reparability, such as establishing minimum recycling content standards, and promoting green certification and environmental labelling. Additionally, fiscal incentives such as reduced or exempt VAT on repair services and food donations can motivate businesses and consumers to adopt sustainable practices. These measures will ensure that products entering the regional market adhere to EU regulatory standards, facilitating compliance and fostering a transition to a circular economy.
- **Ensure implementation of revised waste management strategies, with a focus on achieving higher recycling rates and on waste prevention.** To improve recycling rates, the roll-out of extended producer responsibility (EPR) take-back schemes is advancing in the Western Balkans; however, full participation from both producers and consumers has not been realised. To help implement EPR schemes more effectively, WB6 economies could follow the guiding EPR principles laid out in Box 6.11.

Box 6.11. Guidance on implementing extended producer responsibility take-back schemes

OECD EPR Guidance

To effectively implement extended producer responsibility (EPR) take-back schemes to shift the end-of-life management costs of products from the public sector to producers and consumers, and to increase the collection and recycling rates of these waste streams, economies should ensure the application of the following principles (a selection based on the OECD EPR Guidance):

- **Clear legal framework**: The legislation needs to be clear on the definitions and responsibilities of all actors involved in EPR, with a legal framework for producer responsibility organisations to operate under. EPR targets need to be periodically reviewed.
- **Transparency**: The governance of EPR systems needs to be transparent to provide more effective means for assessing the performance of the actors involved and holding them accountable for their activities. This will require collecting both technical and financial data and setting up registers of producers, the accreditation of producer responsibility organisations, and appropriate sanctions.
- **Sufficient existing waste management capacity**: For EPRs to work effectively, adequate waste infrastructure needs to be in place across the country, including infrastructure for waste separation at source, collection and treatment (ideally recycling).
- **Administrative oversight capacity for better enforcement**: There needs to be sufficient enforcement capacity to prevent unauthorised facilities and collection points from operation. This should also minimise free-riding and non-compliance.
- **Stakeholder engagement**: Platforms for dialogue among stakeholders need to be established.

Prevent Waste Alliance EPR Toolbox

To facilitate the adoption of general good practices and OECD guidance on EPR, authorities and other relevant actors could use the EPR Toolbox developed by the Prevent Waste Alliance. This toolkit allows users to consult other international practices and participate in knowledge exchange to enhance the functioning of the domestic EPR system. The EPR Toolbox contains three modules that span the general aspects of an EPR, including the monitoring of financial flows, and also focuses on concrete actions such as the integration of the informal sector or the creation of a market for recycled plastics.

Sources: OECD (2016[59]); Prevent Waste Alliance (2024[56]); Tuscano et al. (2022[60]).

- **Improve the quality of waste data.** WB6 economies need to consolidate internal waste data and improve data sharing between all stakeholders. Particular attention needs to be paid to the quantities of waste generated across different waste streams, including industrial waste and CDW, as well as their classification as hazardous or non-hazardous, and the related recovery and recycling efforts. The current reporting methodology should be reviewed to enhance future waste management operations. This review should include definitions and surveying methods, breaks in time series, waste collection methods, and waste prevention measures. The city of Antwerp in Belgium and the Czech Republic can offer good practice examples of how to improve waste data collection and monitoring (Box 6.12).

Box 6.12. Managing waste data in Antwerp, Belgium, and in the Czech Republic

Waste dashboard in Antwerp, Belgium

Before 2016, the Waste Department of the City of Antwerp collected data using old-fashioned methods (handwritten notes, insufficient use of Excel, PDF, etc.), and standardised guidelines on collecting data did not exist. Fragmented internal data, limited access to waste data and limited data sharing between systems triggered the department's introduction of a data warehouse. The objectives were to increase insight into waste management practices to drive and support policy decisions eventually, and to disclose waste management data to different stakeholders as automatically as possible to increase transparency.

To achieve these objectives, the Waste Department collected all types of data (real-time such as sensor data; and static, historical and geographical such as track and trace) and involved all relevant stakeholders (local policy makers, local administration, waste processing companies, citizens and researchers). New technologies, including geographical information system (GIS), were used to optimise systems and improve the visualisation and analysis of data. Approximately EUR 100 000 were spent consulting expert analysts and on software licences (which consist of a business intelligence tool and a dashboard creator).

Waste data from different sources are now automatically uploaded to the data warehouse. The warehouse delivers added value to Antwerp's various stakeholders through increased transparency, time efficiency, cost efficiency, a reliable source for researchers, and synergies between different programmes. Policy makers can now use these data to allocate costs more accurately and introduce more targeted policy instruments towards sustainable waste management.

Data collection and processing for EPR schemes – Example of the Czech Republic

While certain technical requirements must be met, the first step towards ensuring transparency of EPR schemes is effective co-ordination and compliance with reporting obligations under applicable legislation. The Czech Republic's electronic registry for waste is an exemplary model for a successful national waste information database. It employs two distinct systems, recently rated as the best European system for waste data management and evaluation by the European Topic Centre on Circular Economy and Resource Use. One handles the mandatory data reported by entities subject to relevant legal acts (Information System for Reporting Obligations), while the other manages the subsequent verification, processing and evaluation of the reported data (Information System for Waste Management). This streamlined process is further enhanced by extending verification authority to municipal and regional authorities, with the Environmental Information Agency functioning as the central data hub. By engaging an array of stakeholders, including the statistical office, the information system becomes a catalyst for developing and implementing evidence-based waste management policies.

Sources: Interreg Europe (2021[61]); Tuscano et al. (2022[60]); Prevent Waste Alliance (2024[56]).

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Notes

[1] More information on these can be found at: https://climate.ec.europa.eu/eu-action/eu-emissions-trading-system-eu-ets/monitoring-reporting-and-verification-eu-ets-emissions_en.

[2] The National Co-ordinating Council, the National Council for Sustainable Development and the Scientific Advisory Body.

[3] Annex I countries in the context of the UNFCCC are often referred to as developed or industrialised nations, whereas Non-Annex I countries include a diverse group of nations, primarily developing countries, with varying levels of industrialisation and economic development. These countries are not bound by the same mandatory emission reduction targets as Annex I countries. Instead, they are encouraged to take

voluntary actions to address climate change and may receive support, including financial assistance and technology transfer, from Annex I countries.

[4] Key measures encompass various initiatives, such as evaluating the contributions of private sector endeavours, forecasting GHG emissions and removals, monitoring and evaluating NDCs, engaging in policy dialogues with the participation of all segments of society, and conducting training and capacity building activities.

[5] Free emissions allowances were granted to three plants: Pljevlja coal plant, KAP aluminium plant and Tosčelik steel mill. Funds raised from the scheme are to be transferred into the Environmental Protection Fund and used for renewable energy sources (EUR 4.1 million), protection of the environment (EUR 2.67 million) and to promote innovation following the Smart Specialisation Strategy (EUR 1.1 million).

[6] In this section, the clean energy transition refers mainly to energy supply and transformations, i.e. the generation of electricity and the necessary transformation of power systems to increase the use of renewable energy over fossil fuels for electricity production. It also examines how energy efficiency can reduce the overall demand for electricity and decrease fossil fuel consumption. It does not analyse the different uses of energy in sectors such as transport, buildings or industry.

[7] The Sustainable Transition of Bosnia and Herzegovina programme was launched in 2023 and is implemented by the Stockholm Environment Institute (SEI), in collaboration with the Ministry of Foreign Trade and Economic Relations of Bosnia and Herzegovina (MOFTER), the Swedish International Development Cooperation Agency (Sida) and four local self-government units: Banovići, Breza, Ugljevik and Živinice.

[8] Technical potential reflects the capacity for deployment of a renewable energy source based on available natural resources (wind currents, solar exposure, hydrometeorology and water resources), as well as the topographic limits and technological constraints related to deploying such a technology (size of installations, land available for use, etc).

[9] The funds raised from this bond are primarily dedicated to transport projects that prioritise environmentally friendly modes such as railways and inland waterways. The issuance of the green bond facilitated the acquisition of three trains and the reconstruction of 79.4 kilometres of railway

[10] The water exploitation index is a measure used to assess the level of water use relative to the available water resources in a specific region or area, indicating the degree of pressure on water resources due to human activities such as agriculture, industry and domestic use. It helps policy makers and water resource managers understand and manage water scarcity and sustainability issues.

[11] Its three main objectives include raising awareness and knowledge of nature-based disaster risk reduction solutions among decision makers, natural resource managers and local communities; integrating nature-based solutions and equitable climate-smart planning into adaptation and disaster reduction policy; and implementing and scaling up nature-based solutions for disaster risk reduction.

[12] The instrument for pre-accession assistance (IPA) includes support for IPA rural development programmes (IPARD). IPARD focuses specifically on rural areas and agri-food sectors of countries in the process of joining the EU. The IPARD III programmes cover the 2021-27 period.

[13] The Aichi Biodiversity Targets are a set of 20 goals set out by the Convention on Biological Diversity (CBD) to halt biodiversity loss by 2020. Specifically, Aichi Target 11 aims to conserve at least 17% of terrestrial and inland water areas by 2020 through effectively and equitably managed, ecologically representative, and well-connected systems of protected areas and other effective area-based conservation measures.

[14] The Kunming-Montreal Target, also known as the Post-2020 Global Biodiversity Framework, builds upon the Aichi Biodiversity Targets. Specifically, it aims to ensure that by 2030, at least 30% of land and sea areas are conserved through effectively managed, ecologically representative, and well-connected systems of protected areas and other effective area-based conservation measures.

[15] Bosnia and Herzegovina is a specific case as it only has access to the sea through a narrow strip of land near the town of Neum, which gives it a small coastline along the Adriatic Sea.

[16] In particular, a reduced VAT rate of 6% applies to accommodation and catering services, as well as an exemption from the infrastructure levy for facilities that operate certified agritourism. In addition, certified agritourism structures benefit from a reduced profit tax rate of 5%. To date, around 50 establishments have received provisional and final certificates recognising their commitment to these standards.

[17] Directive 2010/75/EU of the European Parliament and of the Council of 24 November 2010 on industrial emissions (integrated pollution prevention and control) (recast).

[18] “Improvement of registers of discharge and transfer of polluting substances (PRTR) in the countries of the Western Balkans and the Republic of Moldova’’, implemented from 2021 to 2023 by the Umwelt Bundesamt (UBA), Germany's main environmental protection agency.

[19] The three other economies, Albania, Bosnia and Herzegovina and Kosovo, are currently in the process of drafting their S3.

[20] No data available for Albania and Kosovo.

Competitiveness and Private Sector Development

Western Balkans Competitiveness Outlook 2024: Regional Profile

Inclusive and sustainable economic growth in the six Western Balkan (WB6) economies depends on greater economic competitiveness. Although the gap is closing gradually, the standards of living in WB6 are well below those of the OECD and EU. Accelerating the rate of socio-economic convergence will require a holistic and growth oriented approach to policy making.

This is the fourth study of the region (formerly under the title 'Competitiveness in South East Europe') and it comprehensively assesses policy reforms in the WB6 economies across 15 policy areas key to strengthening their competitiveness. It enables WB6 economies to compare economic performance against regional peers, as well as EU-OECD good practices and standards, and to design future policies based on rich evidence and actionable policy recommendations.

The regional profile presents assessment findings across five policy clusters crucial to accelerating socio-economic convergence of the WB6 by fostering regional co-operation: business environment, skills, infrastructure and connectivity, digital transformation and greening. Economy-specific profiles complement the regional assessment, offering each WB6 economy an in-depth analysis of their policies supporting competitiveness. They also track the implementation of the previous 2021 study's recommendations and provide additional ones tailored to the economies' evolving challenges. These recommendations aim to inform structural economic reforms and facilitate the region's socio-economic convergence towards the standards of the EU and OECD.

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