RegionalCooperationCouncil

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Unleashing the Potential for **Competitiveness:**

Trends in the Western Balkans

Enabling Environment

Markets

Human Capital

Innovation Ecosystem

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Title: Unleashing the Potential for Competitiveness: Trends in the Western Balkans

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1. Introduction

The aftershocks of the COVID-19 pandemic, a war raging in Ukraine, and volatile energy prices have had a major impact on competitiveness in the Western Balkans (WB) and will continue to do so in the years to come. Local companies are hence scanning the horizon for trends that will impact their competition domestically, in the region and in collaboration with partners in the European Union (EU) so they can adequately prepare for what's to come.

The Regional Cooperation Council (RCC) Foresight study "Unleashing the Potential for Competitiveness: Trends in the Western Balkans" presents trends that are expected to have implications on the region's competitiveness until 2035 and provides examples for the respective WB economies. It also outlines potential implications that these trends could have on future challenges and opportunities to inclusive growth in the Western Balkan region. Based on the method of Strategic Foresight, the study provides a sound evidence base for preparing affected actors for future developments and supports them in designing respective policy options and strategies.

In order to provide a comprehensive picture of competitiveness, four areas of action have been taken into consideration, defined by the World Economic Forum's (WEF) Global Competitiveness Report (WEF 2020), i.e. an enabling environment, human capital, markets and the innovation ecosystem (Figure 1). For each pillar, several trends have been identified, resulting from in-depth desk research, qualitative interviews and a trend workshop conducted with experts from the

Figure 1. Four pillars of Competitiveness

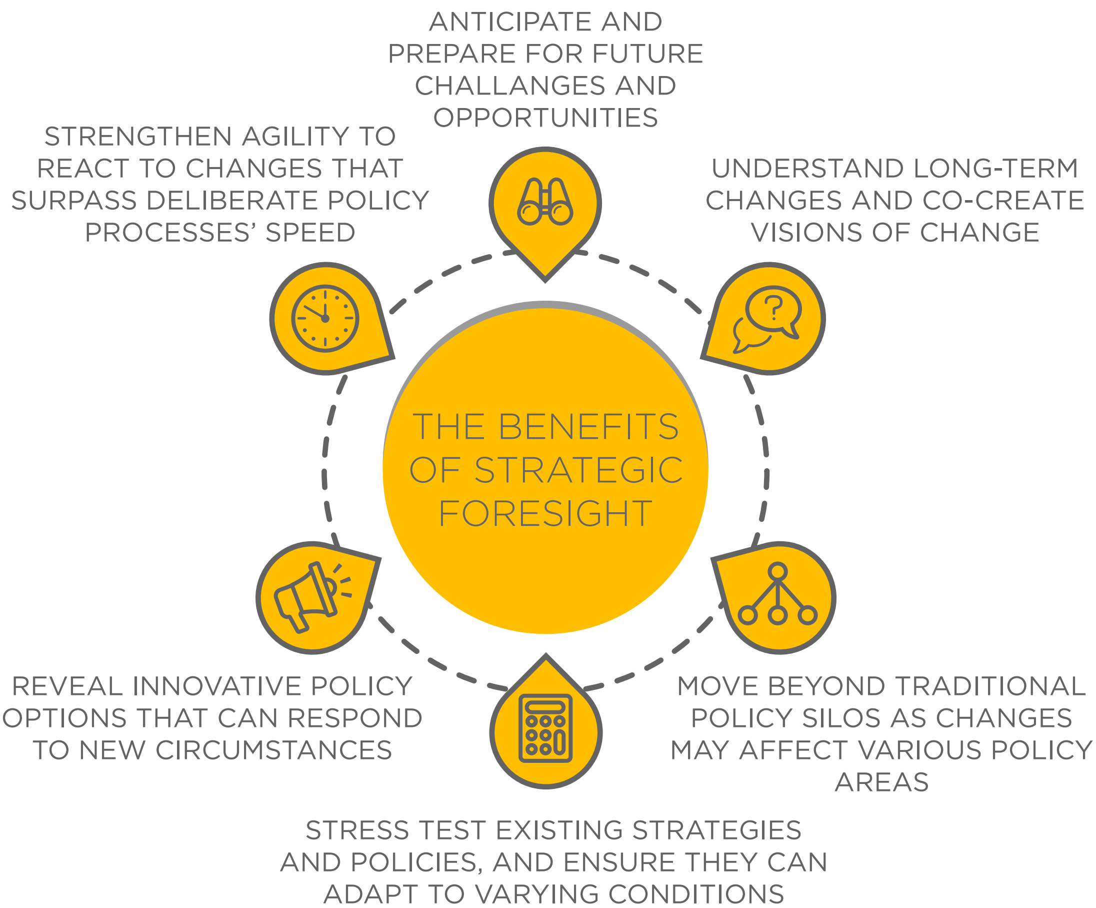
region and international organisations. Based on the observations visible today, these trends provide a comprehensive overview of the expected evolution of competitiveness over the next 12 years, serving as a valuable tool for policy makers to prepare for the future.

The following chapters will provide a brief overview of the methodology applied, i.e. Strategic Foresight, and then give a detailed account of the trends identified within the four pillars. The study concludes with a short summary of the findings and some suggestions regarding the next steps to take.

2. The merits of Strategic Foresight

According to the OECD, Strategic Foresight is defined as the "structured and explicit exploration of multiple futures in order to inform decision-making. Strategic foresight typically involves scanning the horizon for signs of emerging change, developing and exploring a diversity of possible future scenarios, and identifying potential implications for the strategies and policies being developed in the present" (OECD 2021b: 4). In complex and uncertain environments, Strategic Foresight can serve as a robust basis for formulating forward-looking public policies and ensuring that current policies are adaptable to future needs (ibid; see Figure 2).

Figure 2. The benefits of Strategic Foresight (European Commission 2021)



Navigating change through the analysis of trends

At the core of the initial phase in a Strategic Foresight cycle is the identification and analysis of signals of change and trends. Governments, (international) organisations, academia as well as public and private institutions have embraced the potential that trends can have to embrace change and prepare accordingly for potential developments in the future.

Identifying trends and emerging innovations is critical for institutions and companies seeking to gain a competitive advantage in their industry. By anticipating change, they can position themselves to respond effectively and efficiently to the evolving needs of their customers, the marketplace and the broader socio-economic environment. Actors that proactively monitor trends are better equipped to manage risks and take preventative action to minimise their impact. This approach not only improves risk management, but can also lead to increased innovation.

By analysing emerging trends, new opportunities can be identified, and products, services and business models developed that meet changing needs and preferences. Strategic planning is also essential for organisations that want to succeed in today's dynamic environment. By incorporating trends into their long-term planning, they can better align their vision and mission with the changing needs of the marketplace and broader environment. This enables them to develop more effective strategies and allocate resources more wisely.

The quest for competitiveness trends in the Western Balkans

The collection of trends signalling the different potential futures of competitiveness in the WB is based on a firm evidence base. An extensive literature review on the current ecosystem for competitiveness in Europe and the WB was complemented with in-depths interviews with competitiveness experts on the region itself and the single WB economies. The resulting 23 trends were then discussed, refined, substantiated and prioritised in an expert online workshop (see Figure 3) and subsequently backed with an additional research phase. Hereby, the different implications of these trends for the region as a whole, yet in cases also for some of the WB economies, were defined. Overall, a total of 20 regional competitiveness experts contributed to the report (see Acknowledgements).

Figure 3. The workflow at a glance

THE QUEST FOR COMPETITIVENESS TRENDS IN THE WESTERN BALKANS →

1. **SIGNAL SCANNING & TREND SCOUTING**
   Extensive desk research
2. **SUBSTANTIATING THE TRENDS**
   In-depth interviews with competitiveness experts
3. **DISCUSSION, VALIDATION & PRIORIZATION OF TRENDS**
   Expert trend workshop on competitiveness in the Western Balkans (online)
4. **COMPILATION OF TRENDS IN FACT SHEETS**
   Showcasing the identified trends at a glance
5. **DRAFTING**
   RCC study on Competitiveness Trends in the Western Balkans

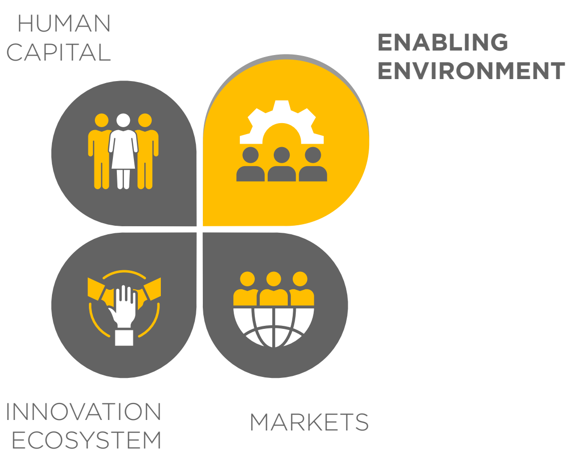
3. Trends that will shape competitiveness in the Western Balkans in the years to come

In the following, the trends identified will be presented. For each of the four pillars – i.e. enabling environment, markets, human capital and innovation ecosystem – the trends and their respective signals of change will be explained and their implications for the region's competitiveness clarified.

3.1 Enabling Environment

For competitiveness to flourish in the WB, formal and informal institutions are crucial to create an enabling environment for businesses. According to the World Economic Forum's Global Competitiveness Report, "utilities and infrastructure such as transport, energy, water and telecommunications; as well as the framework conditions set by monetary and fiscal policy, and more broadly, public finances" are equally important (WEF 2020: 12). Trends in (geo)politics, society and institutional frameworks will influence the region's competitiveness up to 2035 and beyond. Potential developments in the respective EU accession processes of the WB will have the biggest impact on competitiveness.

Figure 4. Enabling Environment Trends



- RISING UNCERTAINTY ABOUT EU ACCESSION
- GROWING SCEPTICISM VIS-À-VIS RUSSIAN AND CHINESE INVESTMENTS
- CONTINUOUS POLITICAL VOLATILITY
- CULTURE OF COMPLIANCE REMAINS FRAGILE
- DECLINING POPULATION WITH A HIGHER PROPORTION OF WORKING-AGE POPULATION

Trend: Rising uncertainty about EU accession

Explanation:

All WB economies aspire to join the EU. The formal applications for EU membership by Ukraine, Moldova and Georgia have opened discussions on preferential fast-track procedures that could potentially accelerate accession also for the WB until 2030, as announced in August 2023 at the Bled Strategic Forum by European Council President Charles Michel (European Council 2023), the three new candidates will now compete with the WB economies to join the EU. Reluctant member states of the EU contribute to an accession fatigue, which the WB are expected to counter with demonstrated reform progress. A recently published paper of Franco-German experts on EU institutional reform underlines that "the EU should set the goal to be ready for enlargement by 2030 and accession candidates should work to fulfil the criteria to accede to the EU on this earliest entry date" (Report 2023). Experts interviewed for this study underline the possibility that alternative approaches to full accession of the WB economies could take a more prominent role in the European discourse in the future.

Implications:

The implications for competitiveness of a full EU membership of some (or all) Western Balkan economies are manifold and all aspects cannot be outlined here. Noteworthy initiatives such as the Berlin Process or the Western Balkans Common Regional Market underline the commitment by the region and the EU to work towards closer economic cooperation (Berlin process, n.d.; European Commission, n.d.a). Exemplary, full access to the EU Single Market would facilitate access to over 450 million consumers and could thereby create new opportunities for businesses in the region. An enhanced regulatory environment would further strengthen a predictable and enabling environment for businesses from the region, as well as offer the potential to further enhance the quality of the goods produced. Additional foreign investment would boost growth, create jobs and allow for technology transfer. Yet, it is expected that most of the WB economies will continue to push for full membership in the EU.

Trend: Growing scepticism vis-à-vis Russian and Chinese investments

Explanation:

The COVID-19 pandemic and the resulting bottlenecks in supply chains highlighted the need for SMEs in the WB to diversify their suppliers (see "The WB are becoming a favoured destination for nearshoring by European companies"). Before the war in Ukraine in 2021, Russia accounted for 2.7% of exports from the WB economies, whereas imports from Russia accounted for 3.9%. China's figures amount to 11,6% and the EU accounted for 57,9% of imports (EPRS, 2023). According to experts interviewed for this study, the war in Ukraine demonstrated the agility of SMEs in adapting their supply chains and avoiding the risk of sanctions. It is expected that the economic toll of the war on the Russian economy will limit the scale of its investments in the region.

China aims to present itself as a strategic investor that refrains from intervening in the WB' internal politics and is ready to turn a blind eye to certain issues like state aid, corruption, or labour regulations (EPRS 2022). China's economic influence in the area is being expanded primarily through the Belt and Road Initiative, which also gives China access to vital land and sea routes. An early emphasis on transportation infrastructure has extended to include energy, industry and communications / IT (ibid).

The European Parliament Research Service (2022) projects that an "increasing number of Balkan [economies] now perceive the limits of China's presence, and are concerned regarding public procurement, environmental protection, human rights violations, and promotion of the authoritarian model, which all limit cooperation and impact EU accession prospects" (ibid).

Implications:
The growing scepticism vis-à-vis Russian and Chinese investments will contribute to the trend that the EU is and will continue to be the top economic partner for the WB. Today it is accounting for 81% of exports and 70% of all foreign direct investment (FDI), notwithstanding capital inflows from China, Russia and the United States of America (ibid).

Trend: Continuous political volatility

Explanation:
A regional market with close economic ties across boundaries creates a favourable environment for businesses to thrive. The efforts by the EU Special Representative for the Belgrade-Pristina Dialogue and other Western Balkan regional issues have led to a verbal – though fragile – agreement on a path to normalisation of relations between Kosovo* and Serbia (EEAS 2023a, EEAS 2023b). Bosnia and Herzegovina continues to search for a sustainable stability. According to experts interviewed for this study, current trends point to continued political volatility as no quick solutions are expected to ease the deep-rooted tensions in the region.

Implications:
Foreign investment may be discouraged by uncertainty and unpredictability, and enterprises in the WB may find it challenging to plan and make long-term investments. A potential decline in the confidence in political institutions to ensure political stability can moreover contribute to a decreased reputation for investing in the WB. While the Common Regional Market and the Central European Free Trade Agreement (CEFTA) are widely regarded as main instruments in regional integration, the uncertain political situation in the coming years hinders a deeper level of collaboration between the WB economies.

* 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.

Trend: Culture of compliance remains fragile

Explanation:

The development of anti-corruption strategies by all WB economies and growing endeavours to align with EU standards and regulations signals a gradual shift towards a "culture of compliance" in the WB. Policy-makers however need to show that they can move beyond lip service in order to turn around the perception of corruption in the region (see Table 1). This trend towards an emerging culture of compliance will remain fragile as it is closely linked to still uncertain EU accession prospects (see "Rising uncertainty about EU accession". Until then, a weak institutional set-up to enforce and check the compliance with rules and regulations (OECD 2021:73) will continue to negatively impact fair conditions for competition in the region.

Implications:

The OECD's conclusion that "[n]one of the [WB] economies have yet achieved a sound and sustainable independent judiciary [...]" will continue to impede competitiveness in the WB (OECD 2021:73). Irrespectively of the EU accession process, without an independent judiciary in the WB, businesses could be exposed to arbitrary and inconsistent decisions, which could undermine confidence in the legal system and deter investment. A fair and impartial judicial system is moreover essential for ensuring a level playing field for businesses, protecting property rights, and enforcing contracts.

Table 1: Corruption is perceived as a challenge by the population in the Western Balkans

	Corruption perception Index 2020	Corruption perception Index 2022	Rank 2022 (out of 180 economies)
Albania	36	36	101
Bosnia and Herzegovina	35	34	110
Montenegro	45	45	65
North Macedonia	35	40	40
Serbia	38	36	101
Kosovo*	36	41	84

Source: Transparency International (2022)

Note: A score is the perceived level of public sector corruption on a scale of 0-100, where 0 means highly corrupt and 100 means very clean. A rank is the position relative to the other WB and observed economies in the index. Ranks can change merely if the number of WB and observed economies included in the index changes.

Trend: Declining population with a higher proportion of working-age population

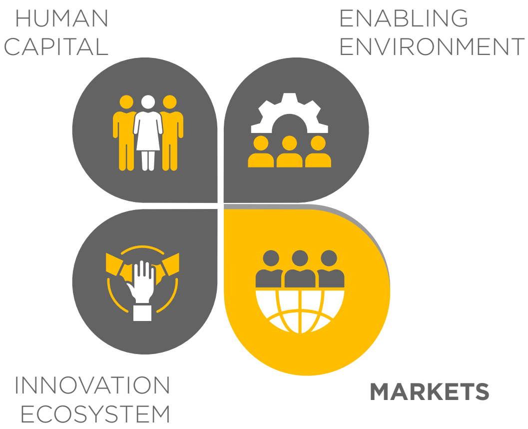
Explanation:
According to projections by the United Nations' 2022 Revision of World Population Prospects, Kosovo* will be the sole WB economy whose population is expected to have grown by 2.6% by 2035 (UN n.d.). All other Western Balkan economies will face the challenge of a declining population due to low birth rates that coincide with high emigration rates (see "Prevailing challenges posed by labour emigration"). Nevertheless, the United Nations project a significant increase in the percentage of the working-age population in all WB economies until 2035. On average, an additional six percent of the population will be of working-age in the WB (55.5% in 2035) (ibid).

Implications:
While the number of consumers will decline, businesses can draw from a larger pool of potential employees, which may lead to higher-quality hires, increased competition for jobs, and higher wages for workers.

3.2 Markets

Markets are an indispensable part of a functioning economy, providing the necessary foundation for economic activity. According to the World Economic Forum (2020: 28), "competitive markets often produce goods and services satisfying a large variety of human needs that are offered at the best possible prices". Market trends thus include any developments related to trade, access to finance, new demands or emerging priority sectors. Overall, the trends identified in this study highlight the need for greater regional cooperation to realise the full potential of the region's competitive advantage. As stated by the World Bank (2023: 49), "[t]rade facilitation and regional integration are crucial for the economic growth and competitiveness of the Western Balkan [economies], which currently face challenges due to fragmentation and their being small economies". Hereby, the Common Regional Market initiative plays a crucial role, as pinpointed by the World Bank (ibid.): "The Common Regional Market initiative, which covers the four freedoms (digital, investment, innovation, and industry policy) is an essential step towards integrating these economies with each other and with the EU economy".

Figure 5. Market trends



- THE WB ARE BECOMING A FAVOURED NEARSHORING DESTINATION FOR EUROPEAN COMPANIES
- FRIENDSHORING WILL BE BENEFITTING EU VALUE PARTNERS
- INCREASING INTRA-REGIONAL TRADE IN SERVICES
- MORE BACKWARD SPILLOVERS DUE TO INCREASING FDI IN HIGHER VALUE-ADDED ACTIVITIES
- FUTURE FDI POTENTIAL TO BE HAMPERED BY COMPETING INCENTIVE STRUCTURES
- POTENTIAL DIVERSION OF FDI INFLOWS FROM THE WESTERN BALKANS TOWARDS UKRAINE
- SURGING STRATEGIC IMPORTANCE OF NEW TECHNOLOGIES

Trend: The WB are becoming a favoured nearshoring destination for European companies

Explanation:
While a shift from globalisation towards more regionalisation was already underway, new strains on global supply chains resulting from, e.g., the COVID-19 pandemic are expected to intensify the trend of nearshoring. Companies around the globe are starting to reduce the risk of supply chain disturbances through supply diversification, shorter supply chains and geographically closer locations (Jovanović et al. 2021; UNCTAD 2020). The WB economies “appeal to Western European companies, not just because of their good geographical locations and competitive wage levels, but also because of ‘soft’ factors such as cultural proximity and the reputation of their workers as skilled and hard-working” (Jovanović et al. 2021). The World Bank concludes: Overall, the sharper rebound in net FDI inflows since 2019 may give some credence to the argument of nearshoring benefiting the Western Balkans, but also relocation of businesses from Ukraine and Russia.” (World Bank 2023: 44).

Implications:
Nearshoring creates new business opportunities, generates employment, and can help to attract foreign investment in the region. By offering a skilled and affordable labour force, as well as favourable business conditions and incentive structures for foreign investment, the Western

Balkans can become an attractive destination for companies looking to outsource business processes or services: "Even if it turns out to be on a smaller scale, it can still have a major impact on the Western Balkan economies due to their small sizes" (Jovanović et al. 2021). However, in order to seize the benefits of nearshoring, it is essential that the WB increase their efforts to be an attractive destination for FDI, i.e. by "improving their infrastructure, nurturing high-quality human capital, eliminating corruption at all levels, and building up institutional capacities" (Zavarska 2022). Moreover, in order to benefit in the long-term, the WB economies need to ensure to create backward spillovers into their local economies (see "More backward spillovers due to increasing FDI in higher value-added activities").

Trend: Friendshoring will be benefitting EU value partners

Explanation:
Whereas the pandemic-induced strains on global supply chains are likely to lead to a rise in nearshoring practices (see "The WB are becoming a favoured nearshoring destination for European companies"), the war in Ukraine has shifted the focus away from nearshoring and triggered discussions about a new trend called "friendshoring". According to the World Economic Forum (Ellerbeck 2023), friendshoring refers to "a growing trade practice where supply chain networks are focused on [places] regarded as political and economic allies". It follows that foreign investments from the EU are expected to shift to economies that are not only geographically close but also share the same values.

Implications:
The expected rise in friendshoring practices will have different implications for the Western Balkans – favouring EU investment in some WB economies while discouraging investment in those WB economies that continue to adopt a more pro-Russian stance. These, however, will potentially experience a boost in FDI from more Russian-friendly economies such as China.

Friendshoring and the case of Serbia: Nearshoring and friendshoring are expected to increase FDI inflows into the Western Balkan region in the years to come. Already today, an increase in foreign investment into the WB economies is visible (World Bank 2023: 44). The only exception appears to be Serbia, which refused to impose sanctions on Russia. Experts interviewed for this study hinted at a potential signal of change and noted the implications of friendshoring as opposed to nearshoring: According to data by the Vienna Institute for International Economic Studies (WIIW), the amount of investment from the EU to Serbia decreased significantly in 2022, making up only around one-third of the total compared to the previous years when it was about 60%. Conversely, FDI from China increased significantly, overtaking the EU as largest investor in Serbia for the first time (Nuttall 2023). According to data by the WIIW, figures from the first three quarters of 2022 show Chinese FDI at around €1bn, accounting for 36% of the total, while EU Member States account for around €900m, or 32% (ibid).

Trend: Increasing intra-regional trade in services

Explanation:

Over the past decade, the WB have made significant efforts to improve trade relations within the region. As part of the European integration process, they have worked to harmonise their trade policies and regulations, reduce trade and non-tariff barriers, and to improve an intra-regional infrastructure. In this context, the adoption of the Central European Free Trade Agreement (CEFTA, 2006), the Regional Economic Area (2017-2020) and, more recently, the Common Regional Market Action Plan (2021-2024) are particularly important to mention. With the adoption of Additional Protocol 6 to CEFTA in December 2019 and its ratification by all WB economies, "significant improvements have been made in opening up trade in services" (OECD 2021a: 118). While the "extent of liberalisation depends on the economy and the sector analysed" (ibid), it is expected that subsequent efforts will considerably enhance trade in services within the region. Moreover, the signing of the Agreement on Recognition of Professional Qualifications for Doctors of Medicine, Dental Doctors and Architects in CEFTA context at the Berlin Process Summits (Berlin, 3 November 2022) and the Agreement on Recognition of Professional Qualifications for Nurses, Midwives, Pharmacists, and Veterinary Surgeons Mutual Recognition Agreement (Tirana, 16 October 2023) has increased further the potentials for the mobility of professionals in the respective professions within the region. In a 2023 report, the World Bank praised the Common Regional Market initiative, which is coordinated by the RCC, as "an essential step towards integrating these economies with each other and with the EU economy (...) leveraging deep trade agreements within the region and with the EU" (p.49).

Implications:

While early studies differed in their assessment of the impact that the reduction of trade and non-tariff barriers would have on intra-regional trade (Bartlett 2023: 5), more recent studies found that CEFTA membership have increased trade flows within the region by 74% between 2006-2015 (Petreski 2018; Grieveson et al. 2021; Matkovski et al. 2022). Accordingly, a significant increase in intra-regional trade in services is expected to further boost the efficiency of resource allocation, be cost-reducing and quality-improving, support regional infrastructures, create new business opportunities, generate employment, and promote economic growth through the benefits of economies of scale (Bartlett 2023; Sanfey and Zeh, 2012). Recent initiatives that were facilitated or propelled by the RCC has eased intra-regional trade in services. The introduction of "Roam Like at Home" regime facilitated by RCC eliminated all roaming costs within the region from 1 July 2021 (RCC, 2021d) while the Roaming Declaration facilitated by the RCC and the EC enabled the reduction of data roaming charges between the EU and the WB economies as of 1 October 2023. Intra-regional trade in services will also be easier ever since the signing of three mobility agreements at the Berlin Process Summit in November 2022. These new Common Regional Market agreements facilitate free movement and employment across the region. The agreements cover ID travel within the region, recognition of academic qualifications and recognition of qualifications for certain professions (European Commission, 2021a). However, stepping up intra-regional trade collaboration could be particularly favourable to attracting FDI, as the region will be viewed as a single investment destination, thereby improving its competitive advantage over other investment destinations.

A club worth joining: Kosovo's* profits due to its CEFTA membership. CEFTA has played a pivotal role in enhancing the competitiveness of Kosovo's* economy, with intra-regional trade cooperation contributing significantly to its growth. Recent data reveal that since joining CEFTA in 2007, over 43% of Kosovo's* exports were sold to CEFTA markets, compared to just 36% to EU markets by 2019 (OECD 2021a; Bartlett 2023: 5). And since Kosovo's* "main strength in the export market lies in services rather than in goods" (ibid.), it can be expected that the adoption of Additional Protocol 6 will further boost Kosovo's* trade within the region.

Trend: More backward spillovers due to increasing FDI in higher value-added activities

Explanation:
While FDI has played an important role in the economic development of many economies in the WB, the extent to which it has generated positive spillover effects on local firms and suppliers has been limited (Krasniqi et al. 2022: 12-13). According to experts interviewed, this is partly due to the fact that many foreign firms operating in the region have been focused on low value-added activities, such as assembly, basic manufacturing or real estate, which do not require a high degree of technology or knowledge transfer (Vujanović et al, 2022:11. Yet, interviews with experts from the region also indicate that there has been a recent shift towards investment into more knowledge-intensive industries such as information technology, software development, and research and development (R&D). This rise in foreign investment in higher-value activities may increase the potential for more linkages to the local economy in the future and hence generate more backward spillovers.

Implications:
An increase in backward spillovers is likely to increase competitiveness by improving productivity and innovation capabilities within the affected companies or sectors. Backward spillovers occur when the knowledge and technology developed by one industry or firm spills over to other industries or firms, e.g. by developing new skills of the labour force, facilitating integration with local firms, increasing technology and knowledge transfers, or by creating new jobs, especially for youth, for whom regional unemployment rates remain high (see "Elevated youth unemployment") (Krasniqi et al. 2022: 18; for more information, see Vujanović et al, 2022).

Trend: Future FDI potential to be hampered by competing incentive structures

Explanation:

Overcoming the ramifications of the eurozone crisis (Bartlett & Prica 2013) as well as the so-called "Balkan effect"[1] (Estrin and Uvalic 2014), several WB economies have managed to enhance the inflows of FDI within the last decade (Krasniqi et al. 2022). This was mainly due to the initiation of dedicated policies to attract FDI, such as special economic zones, tax breaks, subsidies or easy processing, which have been particularly successful in North Macedonia, Serbia and to a lesser extent in Bosnia and Herzegovina (Bartlett et al. 2019: 3). Yet, aggregated data for the WB suggests that there have been only minor effects on FDI as a proportion of regional GDP (Bartlett 2023: 8). This indicates that the competing incentive structures introduced on an individual-economy level "have only succeeded in diverting FDI within the region from one economy to another", while from a regional perspective little progress has been made in attracting foreign investments (ibid.). Unless regional cooperation intensifies further, this trend is likely to continue.

Implications:

The competing incentive structures introduced at individual-WB-economy level "have only succeeded in diverting FDI within the region from one economy to another", while from a regional perspective little progress has been made in attracting foreign investments (Bartlett 2023: 8). These competing incentive structures introduced at the economy-wide level are not only a potential barrier to further FDI inflows into the Western Balkan region, thereby hampering competitiveness. They might also lead to a "race to the bottom, with the result that corporate tax rates are low or non-existent" (Bartlett 2023: 7). This underlines the importance already suggested by the Common Regional Market, to widen the idea of regional cooperation to encompass the creation of a coordinated approach to investment promotion.

Trend: Potential diversion of FDI inflows from the Western Balkans towards Ukraine

Explanation:

When the war in Ukraine eventually comes to an end, the economy's reconstruction is likely to become a top priority for Western policymakers and businesses. As Ukraine offers a larger market – especially when compared to the small and rather fragmented Western Balkan region – a large workforce and relatively low labour costs, it might become challenging for the WB to compete with Ukraine in attracting FDI from European economies. Moreover, the significant amounts of reconstruction funds likely to flow into Ukraine could further enhance its attractiveness to foreign investors looking for opportunities to participate in rebuilding the economy's infrastructure and industries. In addition, Ukraine's geographical location makes it a good partner for Europe's nearshoring activities (see "The WB are becoming a favoured nearshoring destination for European companies"); and its political and economic ties with other

1 The "Balkan effect", a term coined by Estrin and Uvalic in 2014, attributes the lower-than-expected level of FDI, despite the region's strong economic fundamentals, to the legacy of political risk factors in the region.

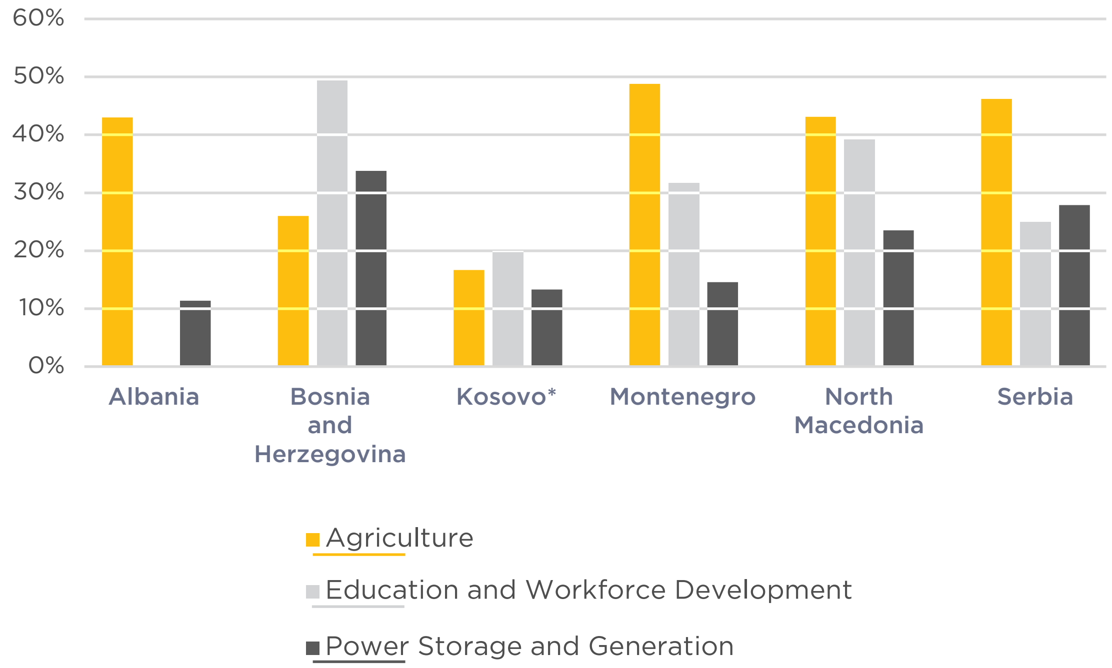
European economies could make it a more appealing partner for foreign investors compared to some Western Balkan economies (see "Friendshoring will be benefitting EU value-partners").

Implications:
As the EU is a central investor in the WB accounting for the majority of FDI inflows, its potential redirection to Ukraine might considerably hamper the WB region's competitiveness. In order to remain an attractive investment destination, the WB could focus on factors beyond proximity and labour costs. Instead, the WB economies could, for instance, focus on the quality of labour or a better infrastructure. In addition, it appears crucial that the WB further enhance intra-regional collaboration. The introduction of the Green Lanes during the pandemic and their current extension to EU Member States such as Italy, Croatia and Greece (and soon possibly Hungary), are a promising and effective sign of regional cooperation. The initiative helped to reduce waiting times at crossing points and speed up the transport of goods (RCC, 2020). However, unless governments and businesses step up regional cooperation the noteworthy initiatives, the region's attractiveness compared to other markets could diminish. By working together, the economies of the region can pool their resources, expertise, and market access to offer a more attractive investment destination for foreign investors. For example, by creating a common market or implementing harmonised regulatory frameworks, the region can provide a larger and more integrated market for investors, which can lead to economies of scale and increased efficiency.

Trend: Surging strategic importance of new technologies

Explanation:
The Fourth Industrial Revolution has created far-reaching opportunities for businesses and governments around the world (WEF 2023: 3). According to the "Markets of Tomorrow"-Report by the World Economic Forum that has been published in 2023 and reflects the expectations of more than 12,000 responses to the WEF Executive Opinion Survey carried out in more than 120 economies, three technologies in particular are likely to become strategically important in the Western Balkans (Figure 6).

Figure 6. Which technologies are the strategic priority in the next 10 years? (WEF 2023)



First, there appears to be a need for greater use of agricultural technologies, including basic techniques such as "mechanization and irrigation, [...] through to more cutting-edge developments, such as precision agriculture or the use of agricultural drones" (WEF 2023: 7). This trend ranks particularly high in all WB economies, being the number one priority in Serbia, North Macedonia and Montenegro, ranking second in Albania, third in Kosovo* and fourth in Bosnia and Herzegovina. Second and accelerated by COVID-19, WEF experts consider education and workforce development technologies to become a strategic priority for all Western Balkan economies (except for Albania). This entails ubiquitous computing, collaboration technologies, extended reality, artificial intelligence and blockchain (WEF 2023: 7). The importance of this trend is seen especially by experts in Bosnia and Herzegovina, North Macedonia and Montenegro, while it is considered somewhat important in Kosovo* and Serbia. Third, technologies related to power storage and generation are expected to become strategically important. While this trend has been reinforced by the war in Ukraine, "technologies for storage and flexibility are key to the global energy transition because they are the limiting factor for integrating renewables into the energy grid" (WEF 2023: 7). While the importance of this trend varies between the six WB economies (number two priority in Bosnia and Herzegovina and number ten priority in Kosovo*), it makes it in the top-ten list in all of them.

E-commerce and digital trade in Albania: Particularly striking is the importance attached to technologies related to e-commerce and digital trade in Albania, with three-quarters of respondents indicating that e-commerce and digital trade will become a strategic priority. While it has also been rated promising by the other WB economies, especially Kosovo*, the high level of agreement among the experts highlights the importance of this trend.

Implications:
Overall, companies that invest in new technologies can gain a competitive edge by improving their innovation, efficiency, sustainability, market access, and collaboration. Yet, the implications for competitiveness will depend on several factors, such as the level of adoption and investment in the technology, and the capacity of the region to adapt and implement the technology effectively. They also need to be accompanied by education and training programmes to ensure that the workforce is equipped with the skills and knowledge needed to adopt and implement new technologies effectively (see "Growing skills mismatch between labour supply and demand"). When implemented successfully though, new technologies are likely to generate new markets.

3.3 Human Capital

Human capital refers to "the capabilities and skills of individuals and populations" and is considered indispensable for fostering economic productivity and thus prosperity (WEF 2020: 8). To seize the value of human capital, the workforce needs to be equipped with relevant and up-to-date skills and capabilities that reflect the respective Zeitgeist. For the merits of human capital to be realised, adequate education and training possibilities as well as a favourable employment environment should be provided. In the Western Balkans, human capital continues to suffer from talent shortages and skills mismatches, exacerbated by both emigration and outdated education systems. These trends reinforce each other, resulting in a persistent and likely even growing trend towards increased youth unemployment. While most WB have made significant progress in analysing these shortcomings and even started to set up strategies to address them, the situation remains challenging. Continuous investments and collaborative efforts between the governments, academia and the private sector are needed to update education systems and to develop the skills needed for tomorrow.

Figure 7. Human capital trends

- ACCELERATING ADOPTION OF DIGITAL TECHNOLOGIES
- WIDENING SKILLS GAP
- GROWING SKILLS MISMATCH BETWEEN LABOUR SUPPLY AND DEMAND
- PREVAILING CHALLENGES POSED BY LABOUR EMIGRATION
- HIGH POTENTIAL OF DIASPORA REMAINS UNSEIZED
- ELEVATED YOUTH UNEMPLOYMENT

Trend: Accelerating adoption of digital technologies

Explanation:

The digitalisation of the labour market refers to the growing use of digital technologies and platforms to manage and perform work, and is fundamentally transforming labour processes. Despite lagging behind some other parts of Europe, the WB have made significant strides in recent years to foster digitalisation in the labour market and develop a digital infrastructure. This trend is anticipated to further accelerate, with the Markets of Tomorrow Report (WEF 2023) identifying "education and workforce technologies" (see "Surging strategic importance of new technologies") to become a top strategic priority for the region's future (including automation, artificial intelligence and machine learning, as well as digital platforms such as online job boards or remote work tools).

Implications:

The implications of digitalisation on the labour market are complex and multifaceted. While it presents opportunities for enhanced productivity, efficiency, and innovation, it could also lead to job displacement and exacerbate existing inequalities. The COVID-19 pandemic has accelerated the adoption of digital technologies, resulting in a growing demand for workers with digital skills such as coding, data analysis, and digital marketing. This trend may create new job opportunities, including remote work, gig work and other freelance opportunities, but also require workers to acquire new skills to remain competitive (see "Growing skills mismatch between supply and demand"). However, as digital literacy rates remain low, the increasing diffusion of digital tools may further exacerbate the consequences of the skills gap (see "Widening skills gap") and increase existing inequalities. The RCC Digital Economy Society Index Report 2022 reveals that "[i]n the integration of digital technology, WB region underperformed compared to the EU. Montenegro is best positioned in the Integration of digital technology dimension, followed by

Kosovo*, Albania and Serbia with scores above the WB average" (RCC, 2022:27). Especially in such context, increasing digitalisation and artificial intelligence tools may raise concerns about the potential for automation to displace certain types of jobs or negatively impact the region's wage cost advantage.

Trend: Widening skills gap

Explanation:

The twin transition (see "The twin transition will foster competitiveness") is accompanied by the need for new knowledge and skills. However, "Europe is already facing shortages of skilled labour" (European Commission 2023: 14). Accordingly, the EU puts a strong focus on ensuring that the supply of education and training opportunities is revised to meet present and especially future needs (e.g. 2020 European Skills Agenda, 2023 European Year of Skills). Similarly, the WB suffer from a significant skills gap, which is likely to widen in the upcoming years. As indicated by Bartlett (2023: 8), "low levels of public expenditure on education have led to skills deficits, especially in rural areas" that will be difficult to overcome in the near future. According to an OECD study (2022b: 23), poor teaching quality, inadequate educational infrastructure and weak vocational training systems are the most pressing problems. But also, the ongoing emigration of medium- and high-skilled labour (see "Prevailing challenges posed by labour emigration") is anticipated to contribute to a widening skills gap.

Implications:

As noted by the European Commission (2023: 14), "a workforce with the requisite skills is essential for succeeding in the twin transitions, enabling companies to expand in growth sectors". According to the 2022 RCC's Western Balkans Digital Economy Society Index, only 35,3% of people in the Western Balkans possessed at least basic digital skills in 2021, compared to 53.9% in the EU. Only 2.6% of employed persons in the WB region were ICT specialists in 2021 (RCC, 2022). Similarly, only 8.7–19.8% of individuals aged 25-64 participate in adult education and training in the Western Balkans, compared to 43.7% in the EU (Eurostat, 2022). The growing skills gap in the WB can result in limited innovation, reduced productivity and competitiveness, and a loss of tax revenues. This in turn has the potential to discourage foreign investment as companies seek specific skills (Bartlett 2023: 8). Instead, they might rely on low-skilled industries (Bartlett 2009: 33), undermining the upgrading of the workforce and weakening competitiveness. Better education and more competencies are needed to raise productivity, create jobs, encourage civic participation, and make the region an attractive investment destination (OECD 2022b: 23).

Trend: Growing skills mismatch between labour supply and demand

Explanation:
While the region has made significant progress in improving access to education in recent years (OECD 2021a: 285), recent surveys among both employers (World Bank 2021) and employees (RCC 2021a) reveal that the education system may not be adequately preparing students for the job market (OECD 2022b: 160). This leads to a mismatch between the skills that employers are looking for and the skills that students are acquiring through their education (Bartlett and Uvalic 2018; Badescu 2021). On the one hand, young people transitioning to the labour market tend to accept jobs they are over-qualified for (vertical mismatch). In 2019, at least one-third of the population aged 15-24 have held jobs they were formally overqualified for; in Albania this was close to 50%, two-thirds in Serbia and three-quarters in Kosovo* (Badescu 2021: 5; Kriechel and Vetter 2022). On the other hand, the Western Balkan economies tend to see an oversupply in certain areas of study while several fields that would be relevant for the labour market remain considerably undersupplied (horizontal mismatch). For instance, and with the exception of Serbia, "regional economies have a relatively low share of graduates from engineering, manufacturing and construction programmes" (OECD 2022b: 82). While the problem is acknowledged and strategies have been set up in most WB economies, "overall, the education system is failing to produce the skills employers need [and] participation in upskilling and skills adaptation activities among both the employed and unemployed is low" (OECD 2021a: 319).

Implications:
A growing mismatch of the skills acquired by the workforce and the skills required by the labour market has three major implications for competitiveness. First, it will tighten the shortage of skills in certain (key) industries and sectors (see "Widening skills gap"). Second, it could make it more difficult for businesses to operate effectively in the region, incentivising them to relocate to other regions with a workforce more adequately skilled for their demands. Third, the skills mismatch might not only lead graduates to take jobs they are severely over-qualified for or to seek job opportunities elsewhere (see "Prevailing challenges posed by labour emigration"), it might also contribute to youth unemployment (see "Elevated youth unemployment"). Further initiatives are needed that require close collaboration between the education system, the private sector, and the government to ensure that students are acquiring the skills and knowledge needed to succeed in the job market.

Serbia as digital skills pioneer: Digital skills are a fundamental aspect of the digital economy, which has been even reinforced by the COVID-19 pandemic (see "Accelerating adoption of digital technologies"). In this environment, it is crucial for students to possess basic digital skills upon leaving school, and that employees get the chance to upskill. While all WB economies have set-up basic frameworks that recognise digital skills as a key competence, Serbia is the only economy to have adopted a Digital Skills Strategy (OECD 2021a: 390). The strategy aims at "improving digital competences in the education system, acquiring and developing basic and advanced digital skills for all citizens, raising digital skills in relation to the needs of the labor market and implementing programs intended for ICT experts to monitor development and progress in technology" (Government of Serbia 2023).

Trend: Prevailing challenges posed by labour emigration

Explanation:
All Western Balkan economies have adopted structural reforms to stimulate economic growth, increase employment rates and bring living standards closer to those in the EU. However, while some progress has been made in recent years in improving socio-economic prospects, convergence with EU standards remains slow. This continues to encourage emigration of (high- and low-skilled) labour from the Western Balkans to the EU. According to the OECD report on Labour Migration in the Western Balkans (2022: 25), "between 2015 and 2020, the number of migrants from the [WB] worldwide increased by 461 000, or about 10%". The major push factors for labour emigration include comparatively low wage levels, a lack of job opportunities (see "Growing skills mismatch between supply and demand"), and continuously high levels of corruption (see "Culture of compliance remains fragile"). While all WB governments have adopted migration strategies, "policies to actively attract migrants back are lacking" (OECD 2022a: 14) and "North Macedonia and Serbia are the only economies that focus on reducing the push factors of emigration" (OECD 2022a: 13).

Implications:
Persisting labour emigration means that the Western Balkans are losing their most valuable asset – highly skilled workers – which in turn can have serious consequences for competitiveness. In particular, it can contribute to labour market imbalances, aggravate talent shortages (see "Widening skills gap") and accelerate brain drain.

Brain drain from Serbia not supported by the facts: Labour migration is one of the long-standing defining features of Serbia's economy. According to UN statistics, the total number of migrants from Serbia is around 14% of the economy's total resident population (Arandarenko 2021: 8). The debate surrounding migration often focuses on the loss of highly educated and talented individuals, which raises concerns about the future of a declining and aging population. However, contrary to widespread perceptions, recent data suggests that "there is net immigration of the highly educated, i.e. those with college and university degrees, and thus no evidence of a brain drain" (Arandarenko 2021: 16). Arguably, this is due to the return of highly educated individuals coming home to Serbia after studying abroad, as well as students from neighbouring economies choosing to study in Serbian universities. Additionally, Serbia is becoming an increasingly attractive destination for high-skilled immigrants from the region due to its status as the largest economy in the Western Balkans and the presence of Belgrade, the region's largest city (ibid). While Serbia does face emigration challenges like other Western Balkan economies, it is likely in a better position than its neighbours in the region and should address this issue strategically.

Trend: High potential of diaspora remains unseized

Explanation:
Today, 4.8 million people or about one-fifth of the population born in one of the WB economies live outside of the region (OECD 2022a). While this development contributes to a "Widening skills gap", the resulting diaspora can also be seen as an opportunity for the WB economies. Recognising this, the migration strategies of all WB economies emphasise the need to promote the transfer of knowledge and skills from their diasporas, to map their diasporas more thoroughly, to build (e.g., research) partnerships with the diaspora, to increase collaboration with diaspora businesses and to facilitate investment (OECD 2022a: 14). However, while these initiatives are a step in the right direction, more often than not there is a lack of adequate frameworks and mechanisms to fully exploit their potential, and a lack of trust in public institutions is expected to remain a key barrier to diaspora engagement and investment in the coming years (OECD 2022a: 14). "Working together with chambers of commerce and non-governmental organisations has proved key to mobilising diaspora resources in Albania and Serbia" (OECD 2022a:14) and could be adopted by the other four WB economies, as well.

Implications:
While the diaspora could provide access to valuable skills, knowledge, and networks that can enhance the region's economic competitiveness, this potential is not yet sufficiently exploited by the WB. The lack of adequate support mechanisms means that the negative effects of labour emigration – i.e. labour market imbalances and skills gaps – still outweigh the positive ones. Policymakers in the Western Balkans hence revise (or ensure the implementation of) their strategies to fully seize the potential of the valuable diaspora.

Trend: Elevated youth unemployment

Explanation:
In 2021, the region's average youth unemployment rate as percentage of the labour force (age 15-24) averaged 33.9%, reaching 36.2% in Bosnia andHerzegovina (in 2022) and 32.6% in North Macedonia (2022) (Employment and Social Affairs Platform 2, n.d.). Even though the effects cannot be clearly isolated yet, it is expected that this trend will be reinforced by the pandemic (Badescu 2021: 4). Especially in the fourth quarter of 2020, youth unemployment "reached as high as 46.5% in Montenegro with sharp increases also in North Macedonia (to 39.2%) and Serbia (to 32.4%)" (RCC 2021b: 10). Interestingly, data show that "youth employment rates vary strongly with the level of education, averaging just 7.2% for young people with a low level of education compared

to 41.4% for those with a high level of education" (RCC 2021b: 10; OECD 2021a: 285). Besides the aforementioned shortcomings in preparing graduates for the demands of the labour market (see "Growing skills mismatch between supply and demand"), there are several other obstacles to addressing youth unemployment that are likely to keep it elevated for the foreseeable future. These challenges include "inefficiencies in the job search process [...]; the prevalence of temporary work contracts in some economies; the scarcity of available jobs for young people; a shortage of child-care facilities to support women returners to work; and the high level of informality" (RCC 2021b: 11).

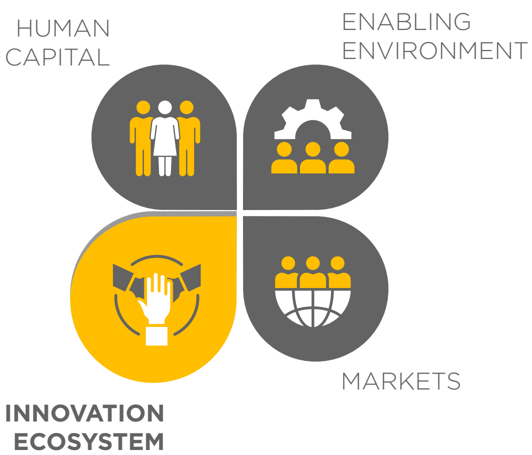
Implications:
High youth unemployment reduces economic growth and may foster social and political instability as young people become frustrated when they do not find an adequate job or are forced to take jobs they are over-qualified for (see "Growing skills mismatch between supply and demand"). It may also make young people leave the region and seek better opportunities elsewhere, resulting in a loss of talent (see "Prevailing challenges posed by labour emigration"), further exacerbating the skills shortage (see "Growing skills mismatch between supply and demand"). While "a wide range of employment promotion policies have been adopted in the [WB] economies" (RCC 2021b: 11), only few of them have been targeted at the youth. Only recently, there have been improvements to support young people to gain work experience (OECD 2021a: 319; OECD 2022b: 124).

North Macedonia's Youth Guarantee successfully tackles unemployment rates: In 2020, the EU Member States strengthened their commitment to the Youth Guarantee, which aims to provide all young people under the age of 30 with employment, education, apprenticeships, or traineeships within four months of leaving education or becoming unemployed. The success of the program is reflected in the record-low youth unemployment rate of 14.9% just before the pandemic. (ETF 2021). Following this example, in 2018 North Macedonia became the first WB economy to introduce a form of Youth Guarantee, which allows unemployed individuals under the age of 29 who are not in education or training to receive a job offer or participate in employment programs within four months of registering with the Employment Service Agency (Employment Service Agency of North Macedonia, n.d.). While an improving macroeconomic context has certainly played a role, the scheme has contributed to "an almost 8.9% reduction in the share of long-term youth unemployment between 2017 and 2019" (RCC 2021c). While the COVID-19 pandemic caused a slight setback, the high number of registrations (ETF 2021) suggests that the program will continue to combat youth unemployment in the North Macedonia.

3.4 Innovation Ecosystems

According to the World Economic Forum (2020), competitiveness requires innovation ecosystems that enable the creation of ideas, their transformation into innovative products and, ultimately, their widespread commercialisation. A variety of factors influence innovation ecosystem trends, including a supportive business culture that allows risk-taking and encourages entrepreneurship, and norms and regulations that incentivise this culture. A robust sector for the development of knowledge and cooperation between these knowledge centres and enterprises are other cornerstones of a supportive innovation ecosystem.

Figure 8. Innovation Ecosystem Trends



- THE TWIN TRANSITION WILL FOSTER COMPETITIVENESS
- HIGHER DEMAND FOR PRIVATE INVESTMENT
- R&D REMAINS SYSTEMATICALLY UNDERFUNDED
- SCATTERED COLLABORATIONS BETWEEN ACADEMIA AND BUSINESS
- PROPERLY IMPLEMENTED SMART SPECIALISATION STRATEGIES WILL ENHANCE COMPETITIVENESS

Trend: The twin transition will foster competitiveness

Explanation:
The twin transition refers to the simultaneous transformation towards a greener and more digital economy. This trend is driven by the increasing global demand for sustainable and innovative solutions, as well as the need to comply with the EU's environmental and digital standards, which the WB aspire to join. The COVID-19 pandemic has accelerated the digital transformation, as more businesses and public services have moved online to adapt to social distancing measures, while the tangible effects of climate change in the Western Balkans have moved the topic up the political priority list.

According to the 12,000 respondents to the World Economic Forum's Executive Opinion Survey (WEF 2023), e-commerce and digital trade, agricultural technologies, and education and workforce development technologies are expected to be the top strategic priorities over the next decade. While agriculture plays an important role in some WEF economies, new markets are expected to emerge in agriculture, forestry and fisheries over the next decade, according to the survey (WEF 2023).

Implications:

Companies that can successfully navigate the twin transition will have a competitive advantage in the European and global marketplace. Depending on the progress of EU accession, compliance with the EU's environmental and digital standards will become increasingly important for businesses and governments wishing to access the EU market. In addition, new markets are expected to emerge in the agriculture, forestry and fisheries sectors, creating opportunities for businesses that can provide innovative solutions in these sectors.

The 2022 RCC's Western Balkans Digital Economy Society Index finds that "[p]olicymakers in the WB region rapidly implement programmes and strategies that support digitalisation of business, including e-commerce. Montenegro recorded the best performance in the Integration of digital technology dimension, followed by Kosovo*, Albania and Serbia" (p.10). Yet, "[t]he adoption of digital technologies by SMEs remains notably below the EU average (35% in the WB region compared to the EU average of 55%). On average, only 7% of WB enterprises used big data, 16% cloud and 3% artificial intelligence in 2021, compared to 14%, 34% and 8% in the EU, respectively" (ibid.). These figures underline the urge to harness the opportunities that the twin transition yields for businesses in the region.

Trend: Higher demand for private investment

Explanation:

Access to finance plays a crucial role in ensuring an economy's competitiveness. While public support can facilitate investment, the substantial financing necessary to sustain it, requires a significant contribution from the private sector. Although access to finance in the EU has improved in recent years (European Commission 2023: 5), the shortage of risk capital will hold back companies that seek to grow and scale up. This highlights a trend towards an increasing need for private financing options that can complement the role of public support in stimulating investment and economic growth. The European Commission acknowledges that "[t]he EU venture capital industry is 20 times smaller than that of the US and most venture capital investments are concentrated in few EU Member States" (ibid).

The RCC finds that "[t]he WB region lacks venture capital on the level of individual economies as well as on the macro-regional level" (2022: 11). There is moreover a lack of sufficient private equity investment in the WB because the market size is too small for large equity investments, there is insufficient knowledge of the local market, and the political and economic situation is unstable. As a result, there are unexplored investment opportunities in the WB that have the potential to generate substantial returns on investment (RCC 2022: 62).

Implication:

A lack of private investment limits the ability of companies to invest in new technology and innovation, which are crucial to improving productivity and remaining competitive. This lack of investment can lead to the underdevelopment of new industries and the inability to attract foreign investment. In the WB, the few large companies may further extent their concentration of economic power, which limits a diverse, competitive market. Eventually, the SMEs in the WB will have limited resources to innovate and retain talented staff.

Trend: R&D remains systematically underfunded

Explanation:

Innovation funds are being or have been established by some of the WB economies. However, investment in R&D remains low compared to EU levels. Eurostat data reveals that in North Macedonia, Gross Expenditures on R&D represented 0.38% of GDP, while in Montenegro it was 0.49% and in Serbia it was 0.9% (RCC 2022: 16). Unfortunately, there is no official data available for other economies. For the EU, the figure is 2.3%. The OECD moreover finds that public research in the region is systematically underfunded and does not lead to optimal outputs of the research conducted (OECD 2021a: 66).

Implications:

The trend of persistently low investment in R&D will slow down technological progress, hamper the development of new products or services and weaken the capacity to innovate. This trend has a strong impact across the WB where 99% of enterprises are SMEs and account for 75% of employment in the region (OECD 2022c: 35). Additionally, the expected underfunding of R&D in all WB economies will perpetuate the non-competitiveness of research infrastructures and hinder their integration into large pan-European infrastructures (RCC 2022: 115). Adequate funding alongside the implementation of the research infrastructure roadmaps adopted by all WB economies would bring existing infrastructures up to date and expand their use for research purposes.

Trend: Scattered collaborations between academia and business

Explanation:

The links between academic research and industry are expected to remain limited and characterised by siloed approaches, according to the experts interviewed. The lack of strategic policies to promote collaboration between the two leaves unused potential to foster innovation. Although many economies have tried to provide financial incentives for such partnerships, non-financial incentives continue to be rare (OECD 2021a: 66). While institutional support for collaboration has grown, it often lacks a comprehensive approach and sometimes conflicts with larger policy initiatives aimed at creating an innovation ecosystem that prioritises start-ups (ibid).

Implications:

By increasing funding for public sector research and promoting scientific research as an attractive career choice to nurture human talent and prevent brain drain (see "Prevailing challenges posed by labour emigration"), innovation systems could become an important catalyst for economic growth in the future (OECD 2021a: 29). The growing number of science and technology parks and research laboratories will not be sufficient to overcome the prevailing mutual scepticism and initiate a cultural change, but they will provide the basis for sporadic collaborations.

Trend: Properly implemented Smart Specialisation Strategies will enhance competitiveness

Explanation:

All WB economies recognise the potential of Smart Specialisation Strategies (S3) to promote innovation-driven sustainable growth. Montenegro and Serbia have their S3's in place, while Albania and North Macedonia have identified S3 priorities. Bosnia and Herzegovina and Kosovo* are in the process of preparing their S3. The RCC's (2022) mapping of priority areas of the respective WB's S3 demonstrates the decision-makers' shared vision of future areas that will become crucial for competitiveness: Sustainable or smart agriculture and food is prioritised by Montenegro, Serbia and North Macedonia; Energy is included in the S3 in Montenegro and Albania; Tourism in the case of Montenegro, Albania; Future machines and manufacturing systems will become a priority in Serbia and North Macedonia, according to their S3 (RCC 2022: 118).

Implications:

If adopted, properly implemented and financed, these strategies will promote and support sectors and regions with comparative advantages. They will also promote innovation and technology transfer, as well as regional research (Bartlett et al. 2019). The development of S3 involves the identification of priority areas for the future and the mapping of R&I infrastructures, which serves as a framework for analysing research potential and determining how domestic infrastructures can contribute to strengthening R&I. In Albania, Montenegro, North Macedonia and Serbia, the identified commonalities in the S3 priorities highlight significant scientific potential that can contribute to the achievement of the S3 objectives in the region in the future. This underlines the crucial role of R&I infrastructures in the overall development of the economy and society (RCC 2022: 122).

4. Future Outlook

The study scanned the horizon for signals of change and identified a total of 23 trends that are expected to influence the evolution of competitiveness in the Western Balkans region until 2035. Persistent challenges in the enabling environment, effective use of human capital, market structures and a supportive innovation ecosystem demonstrate the timeliness of new approaches needed to make WB competitiveness fit for 2035. The trends covered in this study are diverse, although various interlinkages between the different pillars became evident. This underlines the importance of moving beyond siloed thinking when considering the future.

The trends identified for the enabling environment reveal increasing unpredictability due to external sources such as geopolitical shifts or the rising uncertainty on the pathway to the EU, and underline the importance of stepping up efforts to reform the institutional system. Market trends underline the shift towards greater regionalisation and suggest that increased cooperation between WB economies, both in terms of trade and investment, is key to realising the full potential of the region's competitive advantage. Trends in human capital clearly show that overcoming skills gaps and mismatches will be a key requirement for future competitiveness, with central implications for all other areas. The innovation ecosystem in the Western Balkans can only thrive if proper funding for R&D and the Smart Specialisation Strategies will be provided. The Twin Transition – if embraced by the decision-makers – has the potential to boost competitiveness in the region.

Identifying signals and formulating trends are valuable steps in thinking about the future and embracing the changes visible on the horizon. However, it is important to note that trends only take into account the present and then extrapolate into the future. The trends identified in this study therefore only reflect what is visible today. How these trends will ultimately unfold and benefit businesses in the Western Balkans depends on many factors. Future geopolitical shifts, the outcome of EU accession negotiations and decisions by policymakers in the region could have far-reaching implications for today's observations and the directions in which the identified trends may develop. The mapping of trends should therefore be seen as only a first step in thinking about the future of competitiveness in the region.

The most relevant steps still lie ahead. The formulation of different scenarios, for instance, could help to explore alternative ways in which different trends might evolve, thereby considering potential developments that are not yet signals of change. Scenarios take into account the possibility of different possible futures and can therefore make strategic planning more informed and robust.

The trends identified in this study should not remain on paper. Ultimately, citizens and businesses in the Western Balkans will judge the success of competitiveness policies not by the trends identified, but by the tangible impact of reforms in the region, both today and in the run-up to 2035. The coming years until 2035 will test the commitment of today's decision-makers to initiate and implement forward-looking competitiveness policies in the Western Balkans.

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